

**Review of ASIC Regulatory Guide 97:**  
***Disclosing fees and costs in PDSs and periodic  
statements***

**Report to the Australian Securities and  
Investments Commission**

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**July 2018**

**For ASIC purposes, this is ASIC Report 581**

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# 1. Executive summary

## 1.1 Introduction

This report (**Report**) has been prepared at the request of the Australian Securities and Investments Commission (**ASIC**) following its announcement of an external expert review (**Review**) of Regulatory Guide 97: *Disclosing fees and costs in PDSs and periodic statements* (**RG 97**). As set out in the engagement documentation, the aim of the Review is:

‘to ensure that the legislative modifications and guidance issued by ASIC for fees and costs disclosure in relation to superannuation and managed investment products will best meet in practice the objective of greater transparency for consumers. While this review will consider RG 97, it may also lead to a consideration of the principles and law on which RG 97 is based.’

As requested by ASIC, the Report reviews the law, existing policy settings, business practices in the industry, international experience, interaction with the Australian Prudential Regulation Authority (**APRA**) data collection obligations and industry stakeholder concerns.

The scope of the Review and the processes undertaken are set out more fully in Chapter 2. The key considerations that I have been requested to analyse are:

1. the value of the information currently required to be provided in product disclosure statements (**PDSs**) and periodic statements in relation to fees and costs and whether this assists consumers in making an investment decision;
2. the extent to which the current fee and cost regime results in disclosure which assists consumers (including by contributing to market analysis) in comparing superannuation and managed investment products (**MIS**);
3. the practicalities of producing information required for disclosure of fees and costs under RG 97, including the cost to consumers of doing so, as well as whether it might lead to decisions adverse for the long term interests of consumers; and
4. how the legislative modifications and guidance outlined in RG 97 could be amended to improve clarity and ease of implementation.

Extensive stakeholder engagement was undertaken, the outcomes of which are set out more fully in Chapter 2.3 and Appendix 2. Many issues of concern were raised mostly related to technical issues such as what types of fees and costs should be included in the various defined fee types and where, or whether, these should be disclosed in PDSs. Some, although fewer, comments were made about the disclosure regime such as how the various disclosure tools can best assist consumer decision-making. There was commonality in many of the issues and concerns raised that crossed the boundaries of sector and product type although there were also many areas where different sectors or individual stakeholders disagreed on preferred directions.

The Report and this Executive Summary looks firstly to the context and background – the policy framework, international references, the current regulatory requirements and the historical development of those requirements. Chapter 6 considers the effectiveness of the disclosure tools (the Fee Template, the Fee Example, the Consumer Advisory Warning, the additional explanation of fees and costs (**AEFC**) and periodic statements) and Chapter 7 considers the

rather more technical points about fee definitions and how and where particular components are disclosed in the disclosure tools.

## 1.2 Policy framework

Chapter 3 considers the broader policy framework within which the value, relevance and objectives of fee and cost disclosure should be viewed.

The starting premise is that fees and costs matter, particularly in long-term savings vehicles where the effect of fees and costs compound and can have a substantial impact on consumer outcomes over time.

The importance of, and focus on, cost impacts leads to numerous policy strategies and responses designed to reduce these cost impacts on consumers of financial products (Chapter 3.4). At the broadest level, these include strategies to improve provider (sell-side) pricing efficiency, improve consumer (buy-side) pricing efficiency and if necessary to regulate or control prices. Whilst the focus of this Review is on the disclosure of cost impacts, it is acknowledged that this is just one of the sub-strategies available for improving consumer pricing efficiency.

Given that cost impacts matter, it necessarily follows that costs are a factor that should be taken into account when a consumer makes a decision about a financial product. Saying that costs are a factor that consumers should take into account in decision-making is not to suggest that other factors are not important.

Whilst it can readily be asserted that cost impacts matter for consumer decision-making, it becomes somewhat more challenging to set out with precision exactly how consumers should use cost information when making decisions about products such as MIS and superannuation. The importance of cost impacts in decision-making vis-à-vis other factors can only be viewed in the context of the different types of decisions that consumers make in managing their financial affairs.

Chapter 3.2 discusses a range of different types of decisions that a consumer might make in relation to a MIS or superannuation product. Of the types of decisions commonly made, cost comparison is most relevant when choosing between similar investments across Providers or within a product, of some relevance when choosing between funds or Providers, and of less relevance when making decisions between most investment options or types of investment products. Other factors will be more or less relevant depending on the decision being made. Even where costs are particularly important, different types of fees and costs may be more or less relevant depending on the type of decision being made.

This highlights the fundamental challenge facing both consumers and the disclosure regime itself: making comparative investment decisions is very complex. Fees and costs are only one of a complex set of variables that a consumer wanting to make an objective comparison would have to consider. This reinforces how important it is that information about cost impacts be as accessible, simple and comprehensible as is possible.

Within the policy framework set out above, the objectives of fee disclosure (Chapter 3.5) is assessed as having one primary and three secondary objectives:

1. the primary objective is providing consumers with information that they can use in making more confident and informed value-for-money decisions;

2. secondary objectives of:
  - a. framing the nature of the relationship between product Providers and consumers;
  - b. verifying how contributions and earnings will and have been used; and
  - c. the provision of data and information about fund operations in a manner that can support analysis and policy development.

These high-level policy objectives should not be controversial and frame the way that the disclosure toolset (the Fee Template, the Fee Example, the Consumer Advisory Warning, the AEFC and periodic statements) work. By contrast, the objectives that frame more detailed points about what should be disclosed as a particular type of fee in accordance with Schedule 10 to the Corporations Regulations (**Schedule 10**) and RG 97, are less obvious. ASIC has substantially modified Schedule 10 in a manner consistent with its interpretation of the intention of Schedule 10 and related legislative provisions, particularly the changes made under the Stronger Super Reforms in 2013. To the extent that the regulatory direction is constrained by the need to deliver the interpretation of the Stronger Super Reforms that ASIC has applied, then it is difficult to depart from the current approach or suggest any material changes to it. ASIC has worked diligently and thoroughly to implement and clarify what it understands to be the legislative intention in the areas identified.

The breadth and intensity of reactions received during industry engagement, and the very fact that ASIC has committed to this external Review, suggest that some directional change should be considered however, if this can be done in a manner that is consistent with the overall, higher level objectives of the disclosure regime.

Given the primary objective of providing consumers with better information with which they can make more confident and informed value-for-money decisions, parameters such as relevance, reliability and the extent to which the item is consistent with consumer expectations, can be more robustly adopted as a key part of re-considering existing requirements.

Further, noting the importance of cost impacts when making comparative decisions, complexity of the comparison task and the limitations of available comparison tools, emphasis is also placed on simplifying the available data where possible, improving its reliability as a forward-looking indicator and improving the tools in a way that can better support consumer decision-making.

### 1.3 International references

Chapter 4 reviews related developments in other jurisdictions by considering some limited, pre-existing cross jurisdictional research, and through a series of jurisdiction specific case studies. The selected jurisdictions are those with more developed pension and retail investment systems.

Some of the key points of comparison between Australia and the Case study jurisdictions are:

1. standardised terminology, fee tables and synthetic cost indicators are commonly used however there is much diversity in presentation and focus;
2. synthetic costs indicators in other jurisdictions tend to be more focused on producing a single percentage figure (“reduction in yield” or “ratio”) rather than a single dollar figure as is the case in the Australian Fee Example;
3. fee and cost disclosure in most jurisdictions tends to be less detailed for pension products than for retail investments (contrary to the position in Australia), although this observation is

less true for pension products that invest through generally available retail investment structures;

4. transaction costs data is not commonly included in simplified fee disclosure although the trend, particularly in Europe, is towards doing so;
5. operational costs relating to investments (e.g. property operating costs and borrowing costs in the Australian context) do not appear to be within the contemplation of consumer-level fee and cost disclosure regimes anywhere except in Australia;
6. uplifting of fee and cost impacts from underlying investment structures is commonly done in the Case Study jurisdictions (although it is less common across a broader group of jurisdictions), however all other jurisdictions adopt a simpler test for identifying which types of structures this applies to than the tests adopted in Australia; and
7. periodic or annual account disclosure to members is generally more inclusive in Australia than elsewhere, particularly in relation to including approximated, apportioned impacts of non-account level fees and charges.

#### 1.4 The disclosure regime

Chapter 6 reviews the key elements of the disclosure regime and the extent to which the disclosure tools are consistent with the policy objectives set out above. As described in more detail in Chapter 5, the legislated disclosure tools comprise:

1. the four key PDS elements (the Fee Template, the Fee Example, the AEFC and the Consumer Advisory Warning); and
2. the fee description/calculation and additional explanation of fees and costs in periodic statements.

The Fee Template and the Fee Example within the PDS are the primary comparison tools available to consumers. Their approach is consistent with international references and is a notable improvement over disclosure that pre-existed their implementation. Nevertheless, they suffer from numerous limitations that severely inhibit their ability to support effective cost comparison by consumers:

1. PDSs are product specific point-of-sale documents meaning that PDS fee disclosure is naturally best suited to entry level, product level, comparison;
2. PDS based comparison is a laborious and time-consuming exercise that most consumers would likely avoid or short-cut;
3. despite the standardisation required in Fee Templates, in practice there are substantial variations in presentation that limit the usability of the Fee Templates for effective comparison across products or Providers and particularly as between Platforms (such as wraps or IDPS) and superannuation products or MIS;
4. it can be very difficult to find Fee Template information, particularly for non-default investment options when incorporated by reference;
5. there is much diversity in practice in the way that information is presented in documents incorporated by reference that makes the comparison task for consumers even more challenging;

6. there are various differences, both as to layout and underlying data, between superannuation and MIS disclosure that effectively prevents cost comparison between those products;
7. the sequencing and content of Fee Templates do not best support consumer comparison;
8. the overlap of the definitions for Indirect costs and Investment fees in the Fee Template for superannuation products would create confusion for consumers who are trying to make comparison across superannuation products;
9. the Fee Example is calculated only for a single MySuper product or investment option or a single balanced investment option in a MIS which represents only a small fraction of available options - whilst this may cover the most commonly used, default option, the rather perverse outcome of this is that, as a comparison tool, the Fee Example is most usable for those who do not make choices and does not well serve the needs of those who do make choices;
10. the Fee Example is based on a single account balance which whilst being a reasonably sized proxy to use, is relevant to very few consumers; and
11. the Fee Examples for MIS and superannuation products adopt different assumptions about contributions.

Although the disclosure tools were not the main focus of discussion with stakeholders, I consider it necessary and appropriate to suggest various improvements to the disclosure tools so that they can better meet the primary policy objective of providing consumers with information that they can use in making more confident and informed value-for-money decisions. Whilst some of these recommendations would require extra effort by product Providers, this is an appropriate and proportionate impost which can help justify reconsideration, on the same policy principles, of some of the problematic data issues discussed under the next heading. More details around, and qualifications to, individual recommendations are set out in the Chapters indicated. The list of recommendations also includes some designed to improve how the disclosure tools work for Platforms. Recommendation numbering is not fully sequential as the numbering reflects the fuller list in Chapter 8.

**Recommendation 1** (Chapter 6.4) ASIC undertake a feasibility study into whether it, or another government agency could provide, or sponsor, the development of:

1. a publicly accessible, consumer facing facility providing fee and cost information extracted from PDSs that can be searched and compared on a range of criteria; and/or
2. data about average “Cost of Product” figures for specific investment option types that can be included as a reference figure in Fee Examples.

**Recommendation 3** (Chapter 6.6) ASIC work with industry to improve consistency in the way that fee information is set out in Fee Templates.

**Recommendation 4** (Chapter 6.6) ASIC work with industry to improve consistency in the way that fee information is incorporated by reference into PDSs.

**Recommendation 5** (Chapter 6.6) When making future changes to the layout of the disclosure tools or the underlying data, including how and whether to implement other recommendations set out in this Report, ASIC should keep in mind a subsidiary objective of reducing or eliminating the differences between fee and cost disclosure appearing in PDSs of MIS and superannuation products.

**Recommendation 6** (Chapter 6.6) The superannuation Fee Template be modified to group together those fee and cost items that are ongoing separately from those that are dependent on member-initiated transactions or activities.

**Recommendation 8** (Chapter 6.6) The line item for “Advice fees” in the Fee Template for superannuation products be removed. Where the amount is not nil, the amount can be incorporated into the line “Administration fee”.

**Recommendation 9** (Chapter 6.6) The MIS Fee Template be modified to place “Management costs” at the top of the template.

**Recommendation 10** (Chapter 6.6) The MIS Fee Template be modified to include a line for “Buy-sell spread”.

**Recommendation 11** (Chapter 6.6) For superannuation products, the distinction between Investment fees and Indirect costs be removed from the Fee Template by merging the two items into a single line item (“Investment Fees and Costs”).

**Diagrams 6-1 and 6-2** set out modified versions of the superannuation and MIS Fee Templates that incorporate Recommendations 5, 6, 8, 9, 10 and 11 as well as other suggested textual changes. These Diagrams could be used as a basis for consultation or consumer testing.

**Recommendation 13** (Chapter 6.7) The Fee Example be extended to all investment options by the calculation and disclosure of an abbreviated “Cost of Product” figure.

**Recommendation 14** (Chapter 6.7) The Fee Example and the abbreviated “Cost of Product” calculation referred to in the preceding recommendation for superannuation products incorporate a contribution of \$5,000 on the last day of the period.

Many concerns were raised about how the fee disclosure tools apply for Platforms. Chapter 6.10 sets out the background and nature of concerns expressed. Many of the concerns are long-standing and this was one of the areas where there was a significant divergence of views between different industry sectors. In brief, disclosure challenges arise because of the multiple layers of products: fee and cost impacts occur at both the level of the Platform itself, and also within investment products (relevantly MIS) accessed through the Platform product. Consumers, or in most cases, their advisors, need to appreciate the double layer of fee impact and how to aggregate, or disaggregate, this disclosure depending on the comparison being made.

Because of their more complex structure, disclosure for Platforms is always going to be more complex than for non-Platform products. RG 97 includes various warning and safeguards that should assist in ensuring that consumers are aware of the need to aggregate the two levels of disclosure. Four recommendations are included that would, if implemented, assist in achieving fee and cost disclosure for Platforms that is functionally, substantially similar to that for MIS and superannuation products.

Fee Template differences would be moderated by showing key fees and costs of accessible MIS within the Platform’s investment menu documents in tabular format (**Recommendation 17**) and through greater consistency in the location and expression, in the Fee Template, of the warning that the fees and costs of the Platform relate to access to the investments on the list, not the costs within those investments (**Recommendation 20**). Extension of abbreviated Fee Examples (the “Cost of Product” calculation) to Platforms, including accessible MIS, would be important as

this is the most relevant comparison point for consumers and their advisors (**Recommendation 18**). For periodic statements, obligations should be extended to include the costs impacts of accessible investments in Platforms (**Recommendation 19**). In sum, these recommendations should result in functional alignment of fee and cost disclosure as between Platforms and other products.

Recognising however that some of these recommendations are dependent on how and whether other recommendations are implemented, **Recommendation 21** is that after implementation of other relevant changes set out in this Report, ASIC further review the disclosure of fees and charges for Platform products. Such review should focus on whether disclosure of fees and charges for Platform-based products is adequately meeting the objective of providing consumers with information that they can use in making more confident and informed value-for-money decisions when choosing investment options within Platforms and when making product level choices between Platforms, MIS and superannuation products.

### 1.5 Fee disclosure data

Notwithstanding the points discussed above about the challenges of the disclosure regime, the issues that were the primary focus of stakeholder comments were not the legislated disclosure tools but more technical questions and concerns about what data elements should go into the specific fees set out in the Fee Template, Fee Example and the AEFC. What goes into these fee and cost items raises many quite technical legal issues that are driven by Schedule 10, ASIC Class Order [CO 14/1252] (as amended by the various instruments) (**CO 14/1252**), RG 97 and the ASIC Q&A. The most debated areas relate to the meaning of defined terms such as Administration fees, Investment fees, Management costs and Indirect costs. Other problematic definitions feed into those definitions including Transactional and operational costs, Interposed vehicle, borrowing costs, property operating costs and performance fees.

The following is a listing of the major areas of concern raised by stakeholders, with more commonly raised issues listed higher in the list:

1. property operating costs - where and whether to disclose and calculation methodology;
2. borrowing costs - where and whether to disclose, separation of strategic from operational borrowings;
3. transactional costs generally - where and whether to disclose;
4. implicit transactional costs - where and whether to disclose, clarity of requirements and calculation methodology;
5. Interposed vehicle definition - in particular the appropriateness of the PDS test and the relative treatment of different investments;
6. performance fees - where and whether to disclose and calculation methodology;
7. performance-related fees - where and whether to disclose and calculation methodology;
8. OTC derivatives - treatment as part of Management costs; and
9. tax impacts - where and whether to disclose elements gross or net of tax.

It can be observed that a number of the areas of contention relate, to some extent, to the treatment of Transactional and operational costs.

Given the lengthy list of concerns and the likelihood that other points of concern will arise over time, the Report proposes a framework (Chapter 7.3) for ASIC to consider the issues rather than make specific recommendations on each and every issue. The framework for categorising where items should be disclosed is based on the existing segregation of fee and cost elements across the Fee Template, Fee Example, AEFC and outside of PDSs. The framework adopts approaches including minimising cross-over across different tools, limiting the need to constantly update the PDS and consistency with international approaches where possible.

The framework proposes that items that should be disclosed in the key comparative tools (the Fee Template and Fee Example) would have more of the following characteristics: they are significant, they are forward looking and objectively reliable, they are consistent with the public narrative and consumer expectations about the types of items that should be taken into account when comparing product cost impacts, the size of the item does not distort the narrative and disclosure treatment does not distort investment behaviour or create a gameable opportunity.

Other items or explanatory details may still be relevant but do not readily feed into comparative assessment across the relevant product universe because of their nature or how they need to be explained. These items should be disclosed in the AEFC rather than in the Fee Template or Fee Example.

Other items that are of limited interest or relevance to consumers or are disproportionately burdensome to identify, produce and/or maintain having regard to their relevance could be left to other explanatory documents, Provider websites or statistical returns.

Chapter 7.6 considers at some length how the suggested methodology might be applied to the various sub-components of Transactional and operational costs. The conclusion drawn is that some types of Transactional and operational costs are relevant to decision making, sufficiently reliable and consistent with reasonable expectations about what would be disclosed as part of fees and costs. These components (explicit transaction costs and counterparty spreads) could be included in the comparative tools for both superannuation products and MIS.

Other components (property operating costs, borrowing costs and implicit transactional costs (other than counterparty spreads)) do not meet the same criteria and need not be included in the comparative tools. Those items could be exempted from PDS disclosure completely, although ASIC could decide, after due consultation, that implicit transaction costs, for example, should remain in the AEFC or be disclosed elsewhere outside the PDS. Related recommendations and observations are set out below:

Based on the methodology set out in Chapter 7.3, ASIC could consider modifying RG 97 and Schedule 10 to achieve the following outcomes in relation to Transactional and operational costs:

1. explicit transaction costs and counterparty spreads (referred to as **Disclosed T&O costs**) be included, for both superannuation products and MIS as a separate line item in the Fee Template;
2. Disclosed T&O costs be excluded from other fee definitions including Investment fees;
3. Disclosed T&O costs be included in the Fee Example calculation;

4. property operating costs, borrowing costs and implicit transactional costs (other than counterparty spreads) (referred to as **Excluded T&O costs**) not be disclosed in the PDS and could be excluded from relevant definitions;
5. Disclosed T&O costs set out in the Fee Template be shown on a basis net of cost recoveries made via the buy/sell spread;
6. operational costs that are neither Disclosed T&O costs nor Excluded T&O costs (to the extent that any exist) be treated as a part of the Administration fee (for superannuation products) or Management costs (for MIS);
7. the gross figure of Disclosed T&O costs be set out in the AEFC as a part of the details required under clause 209(j)(iii); and
8. periodic statements need not show the impact of Excluded T&O costs.

Chapter 7.7 considers whether disclosure of performance fees can be enhanced to improve the reliability of associated disclosures. The main limitation on the reliability of performance fee disclosure is the challenge of estimating future performance fees and the volatility of performance fees year to year. Current requirements essentially rely on the use of the previous year figure. To reduce the scope for large variances between the disclosed figure and the outcome, the use of figures averaged over a five year period is suggested.

Based on the methodology set out in Chapter 7.3, ASIC could consider modifying RG 97 and related instruments to achieve the following outcomes in relation to performance fees and performance-related fees:

1. relevant definitions be amended such that the distinction between performance fees and those amounts described as performance related fees be removed (i.e. performance fee should include amounts calculated by reference to performance of a product, part of a product, an Interposed vehicle or part of an Interposed vehicle);
2. the amount of performance fees included in the Fee Template (as a component of Management costs, Investment costs, Indirect costs or a new measure such as a consolidated “Investment Fees and Costs”) be calculated by reference to the average of the performance fees that accrued in the fund and Interposed vehicles in each of the previous 5 years;
3. where a fund was not in operation for the previous 5 years or did not have a performance fee charging mechanism in place for the full 5 years, then the average be calculated by reference to the number of years in which the fund operated or had a performance fee charging mechanism in place;
4. transitional arrangements may need to accommodate data availability, particularly for Interposed vehicles, in the first 5 years of calculation;
5. the Fee Template contain an additional footnote referring to the AEFC (as illustrated in Diagrams 6-1 and 6-2); and
6. the AEFC set out the performance fees that accrued for each year used in the calculated average and may also set out further explanation in circumstances where the Provider believes that the 5-year figure is not representative for the coming period.

Chapter 7.8 and 7.9 discuss two other contentious fee data issues; the Interposed vehicle test and the treatment of third party payments and fee offsets. No substantive changes to the current approach are proposed at this stage.

## 1.6 Other recommendations

Chapter 8 sets out other recommendations related to ongoing supervision and enforcement, educational material for consumers, information for advisors and several drafting suggestions.

## 1.7 Conclusion

The recommendations and observations set out in this Report are quite broad in scope. They include a number of quite technical points about fee items and their definition, a number of suggested improvements to the disclosure tools, some suggestions for better support mechanisms for consumers and some observations about how fee disclosure might evolve going forward (Chapter 8.5). Given that most comments received from stakeholders were focussed on more technical details, some might not have expected recommendations to extend beyond the fee items and definitions. All of the observations and recommendations are directed at addressing the stated aim of the Review and the policy objective of achieving disclosure outcomes that can better support consumers in making more confident and informed value-for-money decisions. In addressing the more technical points it became apparent that the policy objective could not be met by merely responding on those technical issues and broader issues also warranted consideration in parallel.

Consequently, the recommendations and observations should be seen as a package rather than as a series of unconnected points. In some areas, such as how to disclose certain fee elements, application of that policy objective can, in my view, justify relaxation of current technical requirements in a manner that directly addresses some stakeholder concerns. Conversely, in some other areas, principally in relation to the presentation of the main comparative tools, the same policy objective suggests the need for enhancements that can better support consumer decision-making that will involve extra effort by product Providers.

Some in the industry will not agree with the overall approach and many will disagree with individual proposals based on their own circumstances. As the recommendations are structured as a package that provides some relaxation of requirements whilst delivering better overall outcomes for consumers, I would encourage ASIC not to allow cherry picking of individual recommendations, particularly those relating to the fee disclosure data. As just one example, proposals such as the relaxed disclosure of market impact costs are deliberately offset by giving consumers more usable disclosure of other transaction costs within the improved Fee Template and expanded Fee Examples.

Whilst the observations and recommendations should be considered as a package, the timing and/or development of individual elements may be affected by other developments. There are many concurrent initiatives affecting regulation of the sector, particularly superannuation, under consideration at the moment. It is impossible to forecast with any certainty the extent to which these developments, the scope of which are much wider than the issues considered in this Report, might impact on the directions or timing of recommendations. It is recognised that, at a minimum, these might affect sequencing or the timing of development of individual recommendations.

Hopefully, considered collectively and objectively, the proposed directions will be seen as an opportunity for different parts of the industry to work collaboratively amongst themselves, and with ASIC, in moving forward on an issue that has consumed excessive time and energy in recent years. For ASIC, the recommended directions, particularly in relation to fee data elements, would involve the robust use of ASIC discretionary powers in a manner that might, in some respects, depart from the more established use of those powers. I would accept that ASIC may be particularly uncomfortable in moving in the proposed directions in the face of substantial industry disagreement or cherry picking. Maintaining the substance of the current approach, which does represent a valid implementation of what ASIC considers to be the policy intent of the legislature, would be a justifiable, if less than ideal, fall-back position.

## 2. The Review

### 2.1 Engagement scope

ASIC has engaged me to conduct a review (**Review**) in relation to *Regulatory Guide 97: Disclosing fees and costs in PDSs and periodic statements (RG 97)* and provide a written report (**Report**) setting out findings and recommendations.

As set out in the engagement documentation, the aim of the Review is:

‘to ensure that the legislative modifications and guidance issued by ASIC for fees and costs disclosure in relation to superannuation and managed investment products will best meet in practice the objective of greater transparency for consumers. While this review will consider RG 97, it may also lead to a consideration of the principles and law on which RG 97 is based.’

The key considerations that I have been requested to analyse are:

1. the value of the information currently required to be provided in PDSs and periodic statements in relation to fees and costs and whether this assists consumers in making an investment decision;
2. the extent to which the current fee and cost regime results in disclosure which assists consumers (including by contributing to market analysis) in comparing superannuation and MIS products;
3. the practicalities of producing information required for disclosure of fees and costs under RG 97, including the cost to consumers of doing so, as well as whether it might lead to decisions adverse for the long-term interests of consumers; and
4. how the legislative modifications and guidance outlined in RG 97 could be amended to improve clarity and ease of implementation.

The engagement scope includes a consideration of the principles and law on which RG 97 is based. Observations and recommendations about the legislated disclosure regime are made under Policy Framework (Chapter 3) and Disclosure Regime (Chapter 6). Because the Review is focussed on RG 97 and not a rather more abstract review of fee disclosure generally, the Report does not, on the whole, extend into broader framework questions such as the extent to which disclosure can play an effective role in consumer decision-making and whether there are better approaches than segregated fee disclosure based on point-of-sale documentation. The accepted starting parameters, on which comments and observations are made, are a fee disclosure regime based on:

1. the PDS, as supported by periodic statements; and
2. a disclosure toolset comprising the standardised Consumer Advisory Warning, a standardised Fee Template, a Fee Example and an area for the AEFC.

### 2.2 Process

The engagement documentation states that the Review would require a consideration of the law, existing policy settings, business practices in the industry, international experience, interaction with APRA’s data collection obligations and industry stakeholder concerns.

In order to complete the Review and prepare this Report, I have:

1. reviewed the current legislative and regulatory settings;
2. reviewed the background and development of the current legislation and regulations;
3. reviewed related international practices;
4. corresponded, either directly, or through the assistance of ASIC, with regulators and industry bodies in other jurisdictions to clarify regulatory requirements in individual jurisdictions;
5. engaged with stakeholders via meetings and roundtables. A number of formal meetings with stakeholders (including industry, service providers, professional bodies and analysts) were conducted in Sydney, Melbourne and Brisbane and via teleconference. A list of stakeholders engaged in these meetings is set out at **Appendix 1**. In addition to formal meetings, I had numerous informal conversations and email exchanges with stakeholders;
6. met with ASIC's Behavioural Research & Policy Unit and Financial Capability Team to better understand related consumer behaviour and research;
7. reviewed and considered written submissions and material provided to me by stakeholders either directly or through the ASIC website (to facilitate broad engagement with stakeholders, ASIC maintained an email facility specifically for receiving comments and suggestions on the Review);
8. reviewed and considered written submissions previously provided to ASIC through the RG 97 development process;
9. reviewed published media and professional commentary of the Review topic; and
10. reviewed the Fee Template, Fee Example and AEFC of approximately 150 PDSs.

### 2.3 Engagement outcomes

A great many comments were received, particularly from industry participants, arising out of the engagement and submission processes set out above. On the whole, participants were enthusiastic in sharing their views. A general summary of the main points is set out in **Appendix 2**. As it is a summary, Appendix 2 does not set out every view expressed on the points made.

Whilst different groups of participants had some comments particular to their type of product, there was commonality in many of the issues and concerns that crossed the boundaries of sector and product type. Industry bodies representing a broad spectrum of affected industry stakeholders (retail funds, for member profit funds (**FMP Funds**), large and small funds, different asset types and differing structures) provided joint submissions in key areas identifying areas of common concern.

More details of the views expressed are extracted and discussed under individual issues where relevant.

### 2.4 Structure of this Report

The four key considerations that I have been requested to analyse are set out above under Chapter 2.1. The first two considerations, in conjunction, look to the threshold issue of the decisions that consumers make and the extent to which currently provided information about fees and costs supports the decision-making processes of consumers, including any necessary

comparison. In part, these two considerations look to the statutory disclosure regime and how that regime facilitates decision-making and comparison. Whilst these issues were not the major focus of the comments received, and may, in many respects, be outside of ASIC's control, they are an important aspect of the contextual framework within which more detailed questions need to be analysed and considered. These issues are considered in Chapter 6.

The third and fourth consideration and parts of the first, relate more to the detailed questions of data and information that go into the disclosure elements required under the regime; specifically, what goes into the defined fee elements that make up the fee and cost items in the Fee Template that feed into the Fee Example and ultimately the periodic statement. This is driven by Schedule 10, CO 14/1252 and RG 97. These issues are considered in Chapter 7.

Recommendations are included within the discussion of individual issues where relevant. Recommendations and observations are also summarised in Chapter 8.

## 2.5 Limitations and constraints

Given the Review has been undertaken at a stage where various implementation obligations were already in place, temporarily deferred or quickly approaching, and in order to provide certainty as to direction as quickly as possible, the engagement documentation has appropriately, abbreviated both the time and scope of the Review.

The development of RG 97 has been ongoing for many years and already represents a consensus approach in many respects. Many elements are already implemented. It was not intended that the Review undo those many years of work by both ASIC and affected stakeholders by adopting a "blank sheet of paper" approach.

The Review therefore, both as a matter of necessity and intention, has not revisited every one of the great many elements set out in RG 97 or the underlying legislative framework. A process has been undertaken, based on research and engagement with stakeholders, to identify key areas of concern, and these have been the focus of more detailed consideration and discussion in this Report.

Despite the extensive engagement set out above, it has not been possible to meet one-on-one with every stakeholder who might have had relevant views to express. Generally, representative views through industry bodies have been sought and obtained, although some individual stakeholder views have been obtained in relation to specific issues, where that stakeholder may have had some relevant individual perspective.

It is recognised that ASIC does not have a primary policy-making role in relation to the shape of the disclosure regime. Legislation has been enacted by the Australian Parliament, which ASIC has modified through the use of its powers under the Corporations Act and the Corporations Regulations. In addressing legislative gaps or stakeholder concerns about the Corporations Regulations, it is not possible for ASIC to just adopt an approach that implements a different policy direction from that contained in the legislation.

ASIC takes the position that the modifications to Schedule 10 made by CO 14/1252 provide clarification or fill in gaps in a manner that is consistent with the policy position explicit or implicit in the legislation. By extension, directions suggested by this Review are also constrained

by broad legislative policy directions. However, as expanded upon in Chapter 3.4 below, I have adopted a slightly different policy focus in some areas than that which ASIC has applied to date.

Most recommendations are drafted in a manner directed to ASIC without regard to the question of whether the recommendation could be achieved by use of ASIC powers. Where ASIC is of the view that a recommendation could not be delivered through the use of its own powers, then it should be read as a recommendation that ASIC raise the issue with the government for its policy consideration.

Many issues of detail were raised during discussions with stakeholders. It is not possible within the timeframe of this Review to consider, let alone resolve, every issue raised by several hundred enthusiastic contributors. This Report focusses on addressing key common areas of concern. The directions adopted in those areas will affect, and in many areas, address, the treatment of other issues of detail. Beyond that, the Report suggests a framework within which other, more detailed issues, can be addressed over time. In addition, ASIC will have its own processes to work through in considering and implementing the recommendations in this Report. These processes might involve consumer testing which has not been possible to undertake as a part of the Review. As such, this Review should not be seen as the end-point, but as a part of the ongoing process of addressing the issues raised.

The recommendations and observations set out in this Report have been made without regard to the details of changes that might flow from the government's "Protecting Your Super" Package<sup>1</sup> that was announced in the 2018-19 Budget. That package, and in particular the proposals to implement a fee cap for certain accounts and restrict exit fees would likely have impacts on the Fee Template, the Fee Example and periodic statements.

## 2.6 Acknowledgements

Whilst the Report and recommendations were developed by me, the support provided by ASIC staff is greatly appreciated. In particular, I record my appreciation for the tireless secretarial and logistical support provided by Kathy Neilson, Senior Lawyer (Acting), Investment Managers and Superannuation. I have also received full support from other members of the Investment Managers and Superannuation Team and policy staff, particularly in obtaining an understanding of the legislation, RG 97 and the policy background.

I also record my appreciation to those industry bodies and professional associations who have given freely of their time and opinions and coordinated contributions of industry participants. Finally, I thank the several hundred individuals who have attended engagement meetings and/or provided written material for my consideration. Initially I had feared that industry might be exhausted by the long developmental history of RG 97, however I found no lack of enthusiasm to engage and robustly share their views.

## 2.7 Terms and terminology

**Fees, costs and expenses:** Terminology used in the description of fees, charges and the deduction of other items that reduce investment returns of investment products is often used in

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<sup>1</sup> This package proposes a number of regulatory reforms including a cap on Administration and Investment fees charged on superannuation accounts with balances of \$6,000 or less at 3 per cent of the account balance, in addition to banning the charging of exit fees for any account: [see Treasury website](#).

different, and confusing, ways. This often means that conversations about fees and charges can be at cross purposes just because people are referring to different things. There is overlap, but also many differences between the technical and common understanding of terms such as fees, charges, costs, levies and expenses.

To a consumer, there might be no meaningful difference between a fee, cost or an expense. Considered somewhat more technically, a fee is a payment of an agreed amount for the provision of a service (which might or might not be closely related to the cost of providing the service), whereas an expense is a liability to a third party incurred by a trustee or responsible entity on behalf of a fund for which it can be reimbursed from the fund. Even this mildly technical understanding of a fee sits somewhat uncomfortably in the FMP Fund sector where what is usually described as a fee may be related to expenses or costs incurred by or on behalf of a fund.

Accounting treatment of expenses is a different concept again, although as noted in Chapter 4, some jurisdictions link disclosure to accounting treatment of expenses. Legal terminology is yet different again and can create confusion where definitions are used in a manner that departs from common understanding; a simple example being the way that fees (such as Administration fees and Investment fees) are defined in Schedule 10 as including elements of costs, and Management costs are defined in a way that includes some fees. Different treatment within the Corporations Act also means, for instance that fees and costs mean different things as between MIS and superannuation products.

The common meaning of terms can also vary depending on the perspective from which they are described; a trustee's fee, a contribution charge and an amount of brokerage on a share purchase are all costs from the consumer perspective but only the brokerage would be considered as a cost from the perspective of the trustee. To a retail Provider, staff salaries, accommodation, rental, and IT are all costs of providing the service, but these are generally not costs to a retail fund as they are paid out of the fee payable to the Provider rather than out of the fund. Some such items could however be treated as fund expenses if the constitutive documents provided accordingly. For a FMP Fund, the same types of costs might, in contrast, be directly deducted from the fund.

To minimise language confusion, this Report uses the broad terms “cost impact/s” or “fees and costs” where generic description of the impacts on a consumer of multiple items across the lifecycle of an investment is intended. Technical terminology and defined terms are used when discussing legislative provisions.

**Consumer:** For the purpose of this Report the term consumer is used to describe the end investor of relevant products instead of other terminology such as “investor”, “holder” or “member”, although these terms are often used in material quoted or referred to.

Other defined terms and abbreviations used in the Report are set out in the Defined terms and abbreviations section in **Chapter 10**.

## 3. Policy framework

Before looking to the details of the legislation and issues of concern, it is instructive to first consider the broader policy framework within which issues should be viewed. Most of the issues of concern raised by stakeholders relate to very narrow questions of detail, but some comments raised higher level questions about the value of fee disclosure and the objectives of disclosing information in the legislated manner. Some of these higher-level questions feed back into a consideration of the detail level questions as the technical treatment of certain fee items should be consistent with the overall objectives and framework.

In recent decades, there have been many, iterative, expansions in the way that cost impacts are disclosed to consumers of financial products both in Australia and in other jurisdictions. This trend is evident both within pension products and retail collective investment products. It is important to contextualise why disclosure of cost impacts is relevant and seen as important by policy-makers.

### 3.1 Fees and costs impacts matter

It is probably unnecessary to repeat to likely readers of this Report the mantra that costs matter. This is particularly true in long-term savings vehicles where the effect of fees and costs can be substantial over time. Cost impacts compound along with returns. Over time, seemingly small amounts of fees and costs can reduce net returns substantially. The standard Consumer Advisory Warning which is required to be included in PDSs states that 1% higher fees and costs could reduce final return by up to 20% over a 30-year period. Lowering return assumptions increases the impact of costs in such calculations and higher impacts of 30% and 40% are often quoted.

Chapter 3.4 considers, from a slightly higher level, the range of regulatory strategies that can be used to reduce cost impacts on end consumers of financial services. Most relevant for current purposes, provision of accurate and usable information about cost impacts at the level relevant to a decision being made is one sub-strategy.

Given that cost impacts matter, it necessarily follows that costs are a factor that should be taken into account when a consumer makes a decision about a financial product. This is not to suggest that other inputs should not be a part of the decision-making process. Expectations about investment returns and risks, services levels and other factors obviously matter as well. Expectations about investment returns, will, in particular, be important to some decisions, however the principal challenge with inputting investment returns into decision-making, is that future returns are highly unpredictable and past performance information is an unreliable indicator. If constructed in a manner that has regard to forward reliability, information about cost impacts can be relatively predictable.

### 3.2 Costs as a factor in decision-making

Whilst it can readily be asserted that cost impacts matter, it becomes somewhat more challenging to set out with precision exactly how consumers should use cost information when making decisions about products such as MIS and superannuation funds. Discussion and debate about disclosure of cost impacts is often generalised and does not have due regard to the range of investment decisions that consumers face. Throughout the course of the Review, comments have

been made to me by some, that there is too much of a focus on fees and costs and consumers should only be concerned about the net investment outcome. For some types of choices, this view possibly has some basis, but it overgeneralises the position to suggest a sole focus on one or the other. The real importance of cost impacts in decision-making can only be viewed in the context of the different types of decisions that consumers make in managing their financial affairs and how those decisions are made.

#### How decision-making is supported

Members of superannuation and MIS products face many choices and decisions. These can relate to joining, exiting, contributing, making investment selections, increasing or decreasing personal contributions, switching funds etc. In making these decisions they are supported by various safeguards and regulatory mechanisms.

Large parts of the regulatory framework are directed at ensuring that investment products and product Providers meet minimum standards across a spectrum of areas including organisational structure, governance, competency, compliance and financial resources. This part of the regulatory regime effectively removes from the decision-making process considerations in these areas (e.g. to a very great extent, a consumer should not have to factor into a decision about choice of Provider, a comparison of which one of them is more likely to steal money or go into liquidation).

The second support for member decision-making is that many decisions are not essential; there are rules or arrangements in place to deal with what happens if a consumer does not make a decision, whether they are disengaged or for some other reason. Taking employee superannuation as an example, employer contributions are mandatory (there are no choices about whether to participate or not), the law sets out how much and when contributions are made (there are no choices to be made about the amount or timing of mandatory contributions), the employee consumer does not have to choose the fund or investment option as there is a framework for determining what happens if the employee does not. There are also default arrangements about what happens on change of employment. Absent any decision to change, the contributions will continue to be invested in the same way until the employee meets withdrawal criteria where statutory processes deal with withdrawal arrangements.

Having good default arrangements that remove the burden of choice from consumers is an important and still developing area of regulation.

Next, decisions can also be supported by professional advice either within a whole of financial plan context or in relation to a specific decision.

Finally, disclosure of objective, usable information supported by tools and educational material is provided for the group of consumers who make some or all decisions by themselves. Both advisors, and consumers making decisions for themselves, rely on quality disclosure of information about relevant decision-making factors, including but not limited to, information about cost impacts.

It is difficult, or likely impossible, to ascertain with any accuracy the extent to which each support mechanism is relied upon by consumers. Different individuals might rely on default settings for some situations yet take responsibility for decision-making or seek advice in other situations. The Review of the Governance, Efficiency, Structure and Operation of Australia's

Superannuation System chaired by Jeremy Cooper (**Super System Review**) estimated that about 60% of superannuation members do not make active choices.<sup>2</sup> The ANZ Financial Literacy Survey in 2015 found that only 20% of those surveyed had accessed a financial planner in the previous 12 months.<sup>3</sup> ASIC survey data<sup>4</sup> shows that around one quarter of superannuation fund members did not know the balance of their superannuation account and another two fifths had “a rough idea”. Regardless of the statistical position, it must be accepted that there is a category of consumers who do make some or all of their own decisions relating to superannuation products and MIS. This category would likely grow in the future if the draft recommendations of the Productivity Commission that focus on increasing member engagement<sup>5</sup> are implemented. These consumers rely on quality disclosure of relevant information.

#### The relevance of cost impacts

There are multiple types of consumer choices relating to superannuation products and MIS. Different types of choices are made at different points in time and consumers can be making multiple decisions simultaneously. Not all decisions should necessarily have the same regard to cost impacts. To illustrate the point, a selected range of consumer choices, and the factors that might be relevant in making such choices, are expanded upon below:

**Choice 1 – choice of Provider:** some consumers might want to use a single Provider for a range of financial products or others might be wanting to make a new investment and start the decision-making process with a choice as between various known “brands” they are familiar with. In deciding which Provider, the cost impacts of using Provider A vs Provider B would be relevant as would relativities related to expected investment performance and service quality. Practically however, Provider fees and costs are generally only disclosed at the product level (a MIS PDS for instance does not give any indication about the cost efficiency of a particular Provider across its product range) and often fees and costs vary at the product and investment option level. As such, cost comparison loses some of its force in this type of choice, both because it is difficult to obtain aggregated Provider level data and because the eventual cost is dependent on product or investment level choices. Comparison of administration costs (as opposed to investment costs and transaction costs) might be particularly relevant where this is available in segregated form although even this could not be considered in isolation (it would be a poor cost-based decision to choose Provider A over Provider B because the disclosed Administration fee of some products is lower if the combined Investment Fees plus Administration fees of most investment options of Provider A were higher than Provider B).

**Choice 2 – choice of scheme or fund:** many consumers would make choices as between superannuation products at the fund level before considering individual investment choices within the fund. The most obvious example being choice of superannuation fund under contributions choice or portability rights.<sup>6</sup> Again, the cost impacts of choosing Superannuation Fund A vs Superannuation Fund B would be relevant as would relativities related to performance and service quality. Again however, the importance of cost comparison loses some of its force because the ultimate cost is dependent on investment level choices even where

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<sup>2</sup> Super System Review, Final Report: Part One at page 9.

<sup>3</sup> ANZ, May 2015 at page 83.

<sup>4</sup> ASIC Report 541 at page 29.

<sup>5</sup> Productivity Commission 2018, draft recommendations 1 to 3 at page 58 ff.

<sup>6</sup> \$47 billion moved under such rights for 1,974,000 accounts in 2017 APRA Annual Fund Level Superannuation Statistics, March 2018.

administration fees are separately disclosed for the same reasons expanded upon under Choice 1. An important aspect of service quality might, in this case, be the range of investment choice offered with the fund or scheme.

**Choice 3 - choice between employer and personal superannuation fund:** a subset of Choice 2 would be a choice as between the employer's chosen fund and the personal super product offered by the same Provider. Analysis suggests that around 22% of fund rollovers fall into this category.<sup>7</sup> Because services and many investment options are replicated across such products, service quality and performance might be less relevant for this choice than for Choice 2. Cost differences would be correspondingly of more relevance.

**Choice 4 - managed investment or superannuation:** another choice open to many consumers for discretionary investment is as between a superannuation Provider/product and a MIS Provider/product. In this case, taxation implications are likely to be the most relevant factor although under current taxation settings this becomes less relevant for higher account balances that are close to contribution caps and for low account balances where taxation impacts are less material. Cost differences would therefore be more or less relevant depending on personal circumstances. Cost comparison between MIS and superannuation is currently compromised because of disclosure differences (see Chapter 6.6 under "Differences between superannuation and MIS").

**Choice 5 - similar investment across Providers or funds:** some consumers might have a firm idea about the type of investment that they want to make (e.g. an Australian equities fund, or a 50:50 balanced fund) and want to make a choice across the superannuation funds, or across MIS or across both types that offer such an investment option. Consultation with financial planners suggest that this type of decision is the most relevant decision in the advisory context. Financial planning analysis will suggest the type of fund or risk appetite that should be accessed, and the advisor's resultant task is, in part, to identify funds that deliver that outcome.

This choice brings in some of the product to product comparison points under Choice 2 above but is narrowed because of the chosen investment option. Again, comparison as between all of costs, services and performance are relevant, however it could be argued that costs are particularly relevant in this context. Relative performance expectations would still be relevant, however, for a given investment strategy, it is much harder for a consumer, or even an advisor, to make informed judgements about relative future performance. There may be information available about past performance outcomes however there is much debate about the value of past performance information in this context. It could be argued that it is almost impossible for a consumer to make a decision about likely relative outperformance for a functionally similar investment across Providers or products. Absent any real ability for the consumer to make choices on the basis of likely investment performance, the cost impacts (which are relatively more predictable) would be a far more compelling comparison basis for this type of choice. Amongst cost impacts, investment costs and transaction costs might be more relevant in this type of decision.

**Choice 6 - investment choices within a fund or scheme:** a common choice for members of superannuation products and Platforms is the choice of investment option from the range offered. In contrast to Choice 5 above, it could be argued that cost impacts are relatively less important in making a choice as between investment options. A choice between investment options (e.g. Australian equities vs international equities, equities vs property securities,

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<sup>7</sup> "Member Switching", Rice Warner/Industry Super Australia, 12 September 2017 at page 28.

conservative vs growth, cash vs bonds etc) is essentially an asset allocation decision. The primary basis for such a decision should be expectations about risk/return trade-offs and how that fits with the individual's needs and risk profile. Cost differences as between the different asset allocation strategies would generally be of secondary consideration, except perhaps if a specific strategy carried such significant cost impacts that it materially affected the risk/return characteristics. A qualification to this would be a situation where there are functionally similar investment options within the product (e.g. an actively managed Australian equities fund vs a passively managed Australian equities fund). In such a case, there being no difference in services and if there were minimal difference in return expectations, costs differences (particularly investment costs and transaction costs) might be of paramount importance.

**Choice 7 – as between different types of investment products:** an extension of Choice 6 is that a consumer can make choices not just between investment options in a fund or scheme but across different types of investment structures and products (e.g. other MIS, banking deposit products, derivatives, listed securities, insurance policies, directly into real estate or equities). It is likely that in making such a decision, expectations about risk/return trade-offs would be even more relevant than in Choice 5 above. Cost impacts would still be relevant although that relevance may be correspondingly even less.

As set out above, the relevance and importance of cost comparison as a factor in decision-making is very much affected by the type of decision being considered. Without trying to attach too much science to the analysis above, it could be observed that cost comparison is most relevant when choosing between similar investments across Providers or within a product, of some relevance when choosing between fund or Provider, and of less relevance when making decisions between most investment options or across types of investment products.

#### Different costs – different relevance

Another dimension worth noting at this point is that different elements of fee and cost disclosure would be more or less relevant to different types of decisions. This is particularly the case for transaction costs, the relevance of which is very dependent on the type of decision being made. The impact and relevance of transaction costs can not be properly considered separately from the investment strategy, its risk and its returns; some elements are controllable, and some are not. As noted in a report to the FCA in the UK,<sup>8</sup> some consider it misleading to report transaction costs without the context of strategy, risk and return. Transaction costs might be most relevant in a choice between similar investment strategies across funds (Choice 5 above); the relative level of transaction costs would give an insight into trading efficiency and trading frequency (although even there it would be difficult for a consumer to draw inferences of value from the data – is higher trading frequency necessarily a good or a bad thing?). Comparing transaction costs at the fund level, or for different types of investment strategies, becomes relatively meaningless because it could be reflective of any number of variables (efficiency, turnover, active v passive management, asset class characteristics, trading strategies) and it becomes very difficult, if not impossible, to draw valuable inferences from simple data.

This point highlights tensions between the value of providing consumers with a single figure that aggregates data about various types of cost impacts and the value of segregating data elements that support more granular decision making. Different jurisdictions adopt different approaches.

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<sup>8</sup> See discussion in Chapter 7.5 “Transactional and operational costs”.

EU PRIIPS (see Case study 4 in Chapter 4.2) adopts a layout that is similar to Australia: a fee table that sets out segregated data which is then supported by an illustration that produces a single aggregated synthetic figure. The FCA suggests in its recent Asset Management Market Study<sup>9</sup> that it is minded to adopt a single “all-in figure” although details such as how this could be done (i.e. by regulating fee structures, through a fee table or through a synthetic figure are yet to emerge). An example of the alternate, segregated, approach is Dutch pension funds (Case study 5 in Chapter 4.2) where three different figures are used and deliberately presented in different ways reflecting their different nature. No aggregated single synthetic figure is produced.

The difference between administration costs and investment costs might also be of significance to some members. Administration costs do not add to retirement outcomes but might be reflected in service quality. Depending on the view taken about the value of active management, investment costs could be considered to contribute to improved retirement outcomes through enhanced investment results. Different consumers might have different motivations that are best met by being able to see segregated data about different cost impacts but this has to be balanced against the consequential complexity.

### 3.3 Comparison is difficult

As noted above, cost impacts are important in making investment decisions. The importance of costs as a factor is however dependent on the type of decision that is being made. Other factors will be more or less relevant depending on the decision being made. Even where costs are particularly important, different types of fees and costs may be more or less relevant depending on the type of decision being made.

This highlights the principle challenge for policy-makers and consumers: making comparative investment decisions is complex and difficult. Even where perfectly comparable information about cost impacts is available, the consumer needs to be able to:

1. access it readily when they need it;
2. understand and compare that information on a like-for-like basis;
3. consider the relative importance/weighting of this information; and
4. factor in relativities around even more complex issues like risk and return expectations, service levels, taxation impacts, investment strategies and other variables.

Fees and costs are only one of a complex set of variables that a consumer wanting to make an objective comparison would have to come to terms with. This emphasises how important it is that information about cost impacts be as accessible, simple and comprehensible as is possible.

### 3.4 Regulatory strategies and disclosure

The importance of, and focus on, cost impacts leads to numerous policy strategies designed to reduce the cost impacts on consumers of financial products. These can be broadly categorised as strategies to:

1. improve Provider (sell-side) pricing efficiency;

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<sup>9</sup> FCA, June 2017 at page 6.

2. improve consumer (buy-side) pricing efficiency; and
3. if necessary, intervene in, or control parts of the market, including directly controlling prices.

Whilst there are many regulatory strategies to consider in improving sell-side pricing efficiency, this Report focusses on disclosure as an element of consumer (buy-side) pricing efficiency.

There are, in turn, several policy sub-strategies to improve consumer pricing efficiency including:

1. removing obstacles to consumers moving invested funds between Providers or products;
2. providing accurate and usable information about cost impacts at the level relevant to a decision being made so that consumers (either directly or with the assistance of analysts and advisors) can more accurately and effectively make informed decisions incorporating cost impacts;
3. providing consumer education so that consumers can more effectively use information when making decisions incorporating cost impacts; and
4. providing consumers with support and facilities to make informed decisions incorporating cost impacts.

As such, when considering the disclosure of cost impacts, it is important to consider this within the context that such disclosure whilst being important, is only one sub-strategy for improving consumer pricing efficiency which is, in turn, just one element of managing cost impacts on consumers.

If ultimately, disclosure practices and other consumer support strategies are seen by policy-makers as being ineffective in supporting consumer decision-making in a manner that helps control cost impacts, then other policy strategies can be adopted. Provider-side cost efficiency is one option (supported in Australia by initiatives such as SuperStream which facilitates the transmission of money and information consistently across the superannuation system between employers, funds, service providers and the Australian Taxation Office) but market intervention remains as the ultimate tool where market forces can not achieve reasonable outcomes.<sup>10</sup>

### 3.5 Disclosure objectives

Within the policy framework set out above, it becomes apparent that the primary policy objective of improving transparency of cost impacts is to provide consumers with accurate and usable information about cost impacts at the level relevant to the decision being made so that they can (either directly or with the assistance of analysts and advisors) more accurately and effectively make informed decisions incorporating those cost impacts. Having accurate and consistent information from different Providers facilitates fair competition between Providers and supports better consumer decision-making. In short, the question for the consumer is “how much does this product cost”. In the Australian context, this is confirmed in section 760A of the Corporations Act which states:

‘The main object of this Chapter is to promote:

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<sup>10</sup> Various research reports suggest that disclosure can have a limited impact on consumers’ decision making. See for example Campbell, Jackson, Madrian, & Tufano (2011) and Financial Conduct Authority, “Now you see it: drawing attention to charges in the asset management industry”, OP32 April 2018.

- (a) confident and informed decision making by consumers of financial products and services while facilitating efficiency, flexibility and innovation in the provision of those products and services; ...’

Further, relevantly, the Explanatory Statement to the Corporations Amendment Regulations 2005 (No 1) when introducing enhanced disclosure of fees and charges noted that the PDS:

‘can be used to aid the consumer make a decision whether to purchase the product or not’.

The key to achieving this policy objective is the disclosure of usable information. Without repeating all of the elements already set out in ASIC Regulatory Guide 168: *Product Disclosure Statements (and other disclosure obligations)*, information will be more usable to consumers and their advisors where it is easy to read and understandable, where it is readily accessible and where it is produced in a manner that assists comparability of the type relevant to decisions they make. The recent Productivity Commission Draft Report referred to “good quality (salient and simple) information to inform their decisions”.<sup>11</sup>

Beyond this primary policy objective, fee disclosure is also designed to meet consumer’s general right to know information about their account and their investments, their rights and responsibilities. Transparency of itself can not be the objective as it should be seen as a strategy to achieve an objective rather than an end objective itself. Nevertheless, even in cases where consumers do not, or can not, make relevant decisions, it is appropriate that they be provided with information about how their invested moneys are being used, and relevantly, how much is used up before or during the process of producing investment gains. The objectives in this case are that the transparency supports verification of how contributions and earning are, or have been, used and plays a role in framing the nature of the relationship between Providers and consumers. Whilst, as a matter of law, other constitutive documents establish and define the legal relationship, it is the PDS that converts those documents into consumer level communication about the rights and responsibilities of the parties who operate and invest into the product. This assists in building trust between Providers and consumers.

Another, related objective is the provision of data and information about fund operations in a manner that can assist third party analysis and policy development. Third party analysis can be important in supporting the primary objective, for example, by converting raw data into more digestible information for consumers or advisors. Third party analysis would also include more sophisticated analysis about operational aspects such as trading and cost efficiency, that Providers and investment managers should be undertaking as a part of their own decision-making processes. As a secondary objective however, information presentation should not be focussed on the rather more technical and sophisticated needs of these parties.

Finally, data and information for analysis and policy development is important. In a sense this objective is a counter-point to the primary objective because it becomes more relevant the less that consumers are able to protect their own interests by making relevant choices. This objective is also more relevant in mandatory savings systems where at least some of the decision-making (for example whether to contribute and when to withdraw) is taken away from consumers. As noted above however, as a secondary objective, information presentation should not be focussed on the needs of policy analysis to the disadvantage of providing clear and simple information to

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<sup>11</sup> Productivity Commission 2018 at page 19.

consumers. If necessary, policy and third-party analysts can obtain information from other sources including direct approaches to Providers and statutory returns.

In summary, the objectives of fee and cost disclosure could be seen as having one primary objective and three secondary objectives:

1. the primary objective is providing consumers with information that they can use in making more confident and informed value-for-money decisions; and
2. secondary objectives of:
  - a. framing the nature of the relationship between product Providers and consumers;
  - b. verifying how contributions and earnings will and have been used; and
  - c. the provision of data and information about fund operations in a manner that can support benchmarking, analysis and policy development.

### 3.6 Disclosure strategies

Even where there are regulatory requirements to disclose relevant cost information, historically, absent further regulation, this has not been produced in a manner which is readily accessible or usable by consumers. Obstacles to accessibility and usability have been observed in many studies across many jurisdictions and include practices such as the use of complex and inconsistent terminology, setting out relevant information in different parts of documents, setting out information that is different in form or substance across different Providers or products, the use of complicated charging structures that make comparison difficult and the use of differing charging methodologies etc.<sup>12</sup>

The range of regulatory strategies adopted in Australia and elsewhere to deal with these observed practices (see discussion of international trends in Chapter 4) and the need to make information as usable as possible, varies from jurisdiction to jurisdiction, however the toolbox of available strategies can be broadly grouped as follows:

1. simplification and standardisation of terminology;
2. standardisation of layout and presentation (e.g. template fee tables);
3. standardising where disclosures appear within disclosure documents and elsewhere;
4. requiring the use of standardised/synthetic dollar or percentage-based summary information;
5. calculation and disclosure of a standardised synthetic indicator of overall impacts of costs or some elements of costs (these can be numeric - such as a percentage, dollar-based, or diagrammatic - such as stars or ticks);
6. mandating/regulating fee structures to simplify disclosure;
7. restricting the types of fees and charges that can be levied (and consequently reducing the diversity of disclosure);
8. using examples to show the prospective impacts of costs on account balances or sample size balances;

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<sup>12</sup> See for example the observations in the Ramsay Report Chapter 3 and the FCA Asset Management Market Interim Report Chapter 4.

9. expanding the range of cost impacts that are disclosed;
10. requiring that “after-the-event” disclosure in member reporting is consistent with “point-of-sale” disclosure;
11. standardising “after-the-event” disclosure in member reporting, including the reporting of transaction specific fees and the use of models or member specific calculations showing the impact of fund level fees and charges;
12. providing a centralised database or comparison facility; and
13. imposing fee controls (prescribed rates or caps) for products or elements of the fee chain for products.

As set out in Chapter 4, many jurisdictions considered have, over time, adopted more and more of these elements and different jurisdictions are further down the path of adopting these strategies than others. It should be observed at this early point in the Report, that the existing disclosure requirements for Australian superannuation funds and MIS appear to incorporate more of these elements than most jurisdictions, at least for those elements that relate to improving market forces rather than intervening in them.

### 3.7 Policy approach in Schedule 10 and RG 97

The relevant legislation and RG 97 are undoubtedly based on elements of the objectives and strategies set out above. During consultation and discussions, some have raised questions whether a regime focussed on the point-of-sale document (**the PDS**) can best serve the needs of consumers managing a long-term savings and income production strategy. Observations are made in Chapter 6 regarding the limitations of, and challenges for, a PDS-based regime and in Chapter 8.5 regarding alternate future approaches.

Most of the issues of concern raised by stakeholders, which are discussed in more detail in Chapters 6 and 7, were directed at issues of detail about defined fee elements and how they are dealt with in Schedule 10 and RG 97. Fewer comments were directed at the strategies and methods of disclosing cost impacts. Policy drivers for the methods of disclosure are relatively clear but are less obvious when considering questions of detail about defined fee elements at the Schedule 10 and RG 97 level.

ASIC would suggest that the approaches taken in RG 97 and related instruments are directed at implementing and clarifying the explicit or implicit legislative intention. ASIC’s view is that legislative changes to Schedule 10 made as part of the Stronger Super Reforms<sup>13</sup> in particular, suggest a much more expansive approach to cost disclosure for superannuation funds albeit within the existing disclosure tools. Even though ASIC’s modifications to the requirements have been extensive, this has been done within the framework of implementing what ASIC considers to be the legislative and policy intention of the relevant provisions including the adoption of certain approaches for superannuation products such as separation of different types of fee and cost elements, differing calculation methodology between fees and costs and including a wider range of impacts within the comparative tools (focussing for instance on the costs of operating a fund rather than simply how much it costs consumers more directly). Iterative changes in

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<sup>13</sup> The Superannuation Legislation Amendment (MySuper Measures) Regulation 2013 (Cth).

response to identified issues have led to finer and finer distinctions in the treatment of some items.

To the extent that the regulatory direction is constrained by the need to deliver the above interpretation of the Stronger Super Reforms, then it is difficult to depart from the current approach or suggest any material changes to it. ASIC has worked diligently and thoroughly to implement and clarify what it understands to be the legislative intention in the areas identified.

During engagement processes, some encouraged me to come to the view that the Stronger Super Reforms should not be interpreted in the expansive way that ASIC has. On the most benign view, the changes made to Schedule 10 related to definitional changes consequential to the Stronger Super Reforms (including the limitations to the types of fees that can be charged in a MySuper product) and related presentational changes such as splitting up Management costs. In their view nothing in the related Explanatory Statement suggests any ambition to dramatically change fee disclosure practices beyond those presentational changes. ASIC has however referred me to extensive collateral material suggesting more ambitious objectives in the Stronger Super Reforms which are supported by the literal terms of the provisions.

Ultimately, it is not necessary for me to express a view about the correct interpretation of the Stronger Super Reforms. The breadth and intensity of reactions received during industry engagement, and the very fact that ASIC has committed to this external Review, suggest that some directional change should be considered, if it can be done in a manner that is consistent with higher, overall, objectives of the fee disclosure regime. The types of comments received during consultation can be broadly categorised as concerns about:

1. complexity (the disclosure obligations are complex and detailed to such an extent that many Providers struggle to understand what they are required to do);
2. comparability (whilst technically justifiable, many requirements do not actually assist consumers in making comparisons);
3. compliance (Providers are not confident that others are complying with requirements giving them a competitive advantage);
4. cost (some issues/items are disproportionately costly to capture and calculate); and
5. consumer comprehension (the outcomes are not what consumers can readily use or would understand as being part of fee and cost disclosure).

One could adopt a cynical view that industry participants will always have objections to expanded fee disclosures, however many comments appeared to be genuine contributions at least in part directed to achieving improved disclosure outcomes for consumers.

The specific observations and recommendations about the disclosure regime (Chapter 6) and the fee elements (Chapter 7) are therefore approached from a slightly less technical starting point than ASIC has adopted to this point. Observations and recommendations are primarily directed at achieving outcomes consistent with the primary policy objective identified in Chapter 3.5 of providing consumers with information that they can use in making more confident and informed value-for-money decisions. Importantly, this approach is consistent with the engagement scope set out in Chapter 2.1 which focuses specifically on consumer decision-making and product comparison.

To the extent that the primary driver is providing consumers with better information with which they can make cross-product comparison, parameters such as relevance, reliability and the extent to which the item is consistent with consumer expectations, can be more robustly adopted as a key part of that framework.

Further, noting the importance of cost impacts when making comparative decisions, complexity of the comparison task and the limitations of available comparison tools, emphasis is also placed on simplifying the available data or tools in a way that can better support consumer decision-making.

## 4. International trends and precedents

As in Australia, fee and cost disclosure for managed funds and pension products has been a fertile developmental area in many other jurisdictions. It is useful to consider developments in other jurisdictions to observe how similar issues have been addressed elsewhere. Cross jurisdiction comparison, particularly for pension products, is notoriously difficult however, because of significant differences, country-to-country, in pension system structure (including the relationship between private and public systems), system choice architecture (including the extent to which consumers can choose providers and investments) and pension product design. The first part of this Chapter looks to some limited, pre-existing cross jurisdictional research, and the second part of this Chapter looks at a series of jurisdiction specific case studies, focussing on points of difference from, and similarities to, the approach adopted in Australia.

### 4.1 International benchmarking studies

In the investment fund area, there are numerous studies of the quantification of investment fund fees across countries (which generally rely on surveys or provider published expense ratios) but very little cross-jurisdictional comparison of how cost impacts are disclosed.

#### IOSCO

In August 2016, the International Organisation of Securities Commissions (**IOSCO**) published a report on “*Good practice for fees and expenses of collective investment schemes (CIS)*” (**IOSCO Report**). The aim of this report was to identify common international examples of good practice that can be applied to CIS fees and expenses. A number of these good practices (**GP**) related to disclosure of fees and expenses and these GPs are summarised below:

1. GP5: Investors should be adequately informed of the existence of performance fees and of the potential impact on returns;
2. GP6: Information should be disclosed to both prospective and current investors in a way that allows them to make informed decisions about whether they wish to invest in a CIS and thereby accept a particular level of costs. Investors should be provided with summarised information on the key elements of fees and expenses. More detailed information should be signposted;
3. GP7: To enable investors to understand what fees and expenses are charged:
  - a. information should be simple, concise, set out in clear and not misleading language;
  - b. information could distinguish between fees paid directly by an investor out of his/her account, and other fees and expenses that are deducted from the assets of the CIS;
  - c. information should avoid overloading investors with details that are irrelevant to them;
  - d. use should be made of a standardised fee table that discloses the total expenses ratio (**TER**) of the CIS or a comparable calculation based on the ongoing charges; and
  - e. the TER or comparable calculation should be disclosed in a standardised way, by means of a standardised fee table or financial highlights;
4. GP8: The information should describe the cost structure of the CIS: e.g. the management fee, and operational costs such as custody fees;

5. GP9: Information should describe the fees and expenses actually paid on an historical basis and may also describe the fees and expenses likely to be paid on an anticipated basis. Information on fees and expenses should be kept up to date and the updating frequency should be specified;
6. GP10: Information on fees and expenses should enable investors to compare the costs of different CIS;
7. GP11: Use of electronic media for disclosure of information on CIS fees and expenses should be encouraged;
8. GP13: Where transaction costs are deducted from CIS assets, this should be disclosed to investors before they invest. Documents should be provided or made available that:
  - a. contain, to the extent known, a detailed description of the CIS's fees and expenses; and
  - b. describe the types of cost that will be or may be charged as transaction costs. Where the actual amount of transaction costs is known to the CIS operator after the event, that amount (or the total of all such amounts charged in a specified period) could be disclosed to the CIS and its investors;
9. GP18: A CIS operator that uses hard or soft commission arrangements should disclose relevant information about them;
10. GP19: Information on fees and expenses should enable investors to understand that if there is a double fee structure, it will impact the performance of the CIS. When a CIS invests substantially in other vehicles, the management costs of the investing CIS and the underlying CIS should be disclosed to investors;
11. GP22: Regulators should require information disclosed to investors to be updated if an event occurs that changes the fees and expenses of a CIS. The way that this is done, and the urgency of the update, may depend on how material the change is; and
12. GP23: Requirements should aim to make current investors aware of changes to fees and expenses that have occurred.

As most of the GPs set out above are quite high level, the current Australian fee disclosure regime is broadly consistent with them. The IOSCO Report does not shed much light on preferred practices in areas of contention discussed later in this Report, although some comments relevant to specific issues are worthy of note, including:

1. the IOSCO Report discussed at length the policy and disclosure challenges related to performance fees. For disclosure, it suggested the use of concrete examples, but did not discuss the extent to which such figures should feature in tools such as expense ratios;
2. in view of the different approaches taken to using historical and forward-looking information, the IOSCO Report avoided proposing specific good practice suggesting the use of one or the other (it did however suggest the use of historical data in TER to facilitate international comparison);
3. given the challenges in calculating transaction costs (particularly implicit costs) the report noted that transaction costs are generally not included in expense ratios which focus on ongoing costs; and

4. no comments or references were made to the use of fee information in member level periodic reporting.

#### Pension systems and IOPS

For pension systems, there are numerous international studies that attempt to provide a framework and methodology for comparison of disclosed costs including Whitehouse in 2001<sup>14</sup> and Tapia and Yermo in 2008.<sup>15</sup> Comparison of cost levels is however not a focus of this Review which is more directed at how cost impacts are disclosed and what elements are disclosed.

The International Organisation of Pension Supervisors (**IOPS**) Working Paper 20 (2014) (**WP 20**), “*Update of IOPS Work on Fees and Charges*” gives an insight into the different approaches to cost disclosure taken in 20 pension jurisdictions (not including Australia), and the associated challenges in comparing cost disclosure across jurisdictions. WP 20 noted challenges created by the different types of charging mechanisms and that, even where a single cost indicator is used, it includes different components in different jurisdictions. Those findings are summarised in the Diagram 4-1 (which is based on Table 2 in WP 20). Jurisdictions with the most inclusive charge ratio calculations are listed first. Although not included, if Australia were included it would sit towards the very top of the Table.

The Table shows, for example, that all surveyed jurisdictions include the administration fee for the plan and investment management fees for the plan or primary fund. Only 5 of the 20 jurisdictions surveyed uplifted costs of underlying funds and only 9 of the 20 included any element of investment transaction costs.

Diagram 4-1 Cost and fee elements extracted from IOPS WP 20

Cost and fee elements incorporated in charge ratio (CR) calculation process

Jurisdiction	Plan scheme admin fees	Investment mgt fees - primary fund	Investment mgt fees - underlying funds	Custodian fees	Investment transaction costs	Guarantee fees	Other
Albania	yes	yes	yes	yes	yes	n/a	yes
Israel	yes	yes	yes	yes	yes	n/a	no
Hong Kong	yes	yes	yes	yes	no	yes	yes
Bulgaria	yes	yes	yes	yes	no	n/a	yes
Turkey	yes	yes	yes	no	no	n/a	no
Panama	yes	yes	n/a	yes	yes	n/a	no
Peru	yes	yes	no	yes	yes	yes	yes
Chile	yes	yes	no	yes	yes	yes	yes
Romania	yes	yes	no	yes	yes	yes	no
El Salvador	yes	yes	no	yes	yes	n/a	no
Czech Rep.	yes	yes	no	yes	yes	no	yes
Hungary	yes	yes	no	yes	no	yes	yes
Macedonia	yes	yes	no	yes	no	n/a	yes
Mexico	yes	yes	no	yes	no	n/a	yes
Colombia	yes	yes	no	yes	no	no	yes
Spain	yes	yes	no	yes	no	no	no
Croatia	yes	yes	no	no	no	n/a	yes

<sup>14</sup> Whitehouse, 2001.

<sup>15</sup> Tapia W. and Yermo J, 2008.

Jurisdiction	Plan scheme admin fees	Investment mgt fees - primary fund	Investment mgt fees - underlying funds	Custodian fees	Investment transaction costs	Guarantee fees	Other
Costa Rica	yes	yes	no	no	no	n/a	yes
India	yes	yes	no	no	no	n/a	yes
Poland	yes	yes	no	no	no	n/a	yes

Note for screen readers: A description of the information in the Diagram is set out in the paragraph above (accessible version).

WP 20 also noted that whilst improving disclosure (simplification, standardisation and the use of single synthetic indicators) was one strategy to reduce fees, some jurisdictions had had success using more interventionist strategies such as limiting the types of fees that can be charged (Chile, Mexico, Poland, Czech Republic and the Slovak Republic), auctioning default provider status (Chile) and imposing fee controls (Hungary, Macedonia, Poland, Turkey, Israel, Bulgaria, Croatia).

Another IOPS Working Paper worth noting is WP 15 (2011) (**WP 15**), “*Comparative Information Provided by Pension Supervisory Authorities*”. WP 15 identified that supervisory authorities frequently provide comparative fee information on their websites. Of 24 countries surveyed, 19 provided some level of comparison, even if this was more in the nature of statistical reports than a comparison facility like the one in Hong Kong (see Diagram 4-10 below). The paper noted that in many IOPS member countries the pension supervisory authority plays an important role as a provider of objective, comparative information, acting as a disinterested, comprehensive and authoritative source.

Another research paper by Turner and Witte,<sup>16</sup> now somewhat dated, provided a qualitative comparison of fee disclosure mechanisms across 6 selected countries. Table 8 of that review<sup>17</sup> (post the 2005 enhanced disclosure reforms in Australia) rated disclosure of Australian pension funds comparatively highly with a score of 3 as against Sweden with a score of 4 and Canada, the US and UK on a score of 1.

Diagram 4-2 Extract from Turner and Witte

#### Score Card for Fee Disclosure, Six Countries, 2008

Disclosure Item	Australia	Canada	Chile	Sweden	UK	US
Administrative expenses (amount)	yes	no	no	yes	no	no
Administrative expenses (%)	no	no	yes	yes	no	no
Investment mgt (amount)	no	no	no	yes	no	no
Investment mgt (%)	yes	yes	yes	yes	yes	yes
Investment transactions (amount)	no	no	no	no	no	no
Investment transactions (%)	no	no	no	no	no	no
Participant-initiated transactions (amount)	n/a	no	n/a	n/a	no	no
Participant education on importance of fees	yes	no	no	no	no	no
SCORE	3	1	2	4	1	1

<sup>16</sup> Turner J & Witte H, November 2008.

<sup>17</sup> Turner J & Witte H, November 2008 at page 22.

The score is the sum of the “yes” responses. The disclosure in Sweden refers to the mandatory individual account system. In Chile, the administrative expenses and the investment management costs are combined. Participant education refers to education or information provided in conjunction with fee disclosure.

Note for screen readers: A description of the information in the Diagram is set out in the paragraph above (accessible version).

## 4.2 International case studies

### Case study 1. UK occupational pension funds

Understanding regulation of pension funds and retail investment funds in the UK is complicated by the diversity of structures, differences from the Australian system and the overlay of European Directives and Regulations. For simplified comparison purposes, three different types of structures are considered:

1. occupational (or work based) pension funds: These are employer provided trust-based arrangements that are in some ways similar to FMP Funds in Australia. These can be defined benefit or defined contribution. These are regulated by the Department of Works and Pensions and supervised by The Pensions Regulator;
2. Workplace personal pension schemes (**WPPS**): These are a subset of contract-based pension schemes which are based on personal contracts between the individual and a pension provider (typically an insurance company or a platform)<sup>18</sup>. Despite being personal contracts, WPPS are often arranged by employers as group arrangements. WPPS can, in some respects, be compared to retail superannuation funds in the Australian context. Firms that sell WPPS are regulated by the FCA. Generally, the disclosure requirements explained under Case study 2 will apply to WPPS; and
3. retail investment funds: Generally similar in concept to MIS in Australia. Most investment funds available in the UK will be regulated under the EU Undertakings for collective investment in transferable securities (**UCITS**) directives. The FCA has issued or adopted rules for the disclosure of funds including UCITS. These are summarised under Case study 3 below. In due course, subject to Brexit consequences, the existing rule set for fee disclosure for UK investment funds will be largely overtaken by the EU PRIIPS Regulation which is discussed under Case study 4 below.

Current fee disclosure requirements for UK occupational pension funds are relatively basic. This is largely because occupational pension funds have traditionally been provided as an employment benefit that is not seen as being ‘purchased’ by retail investors or via a contract.

As such, occupational pension schemes are not required to provide a PDS-like, point-of-sale document to members upon joining. Trustees and managers of these schemes have a duty to request and report on the level of charges and, so far as they are able to do so, the level of transaction costs borne by scheme members for the default arrangement and the range of such charges and transaction costs for other arrangements via an annual document called “the Chair’s Statement”.<sup>19</sup> This statement is generally available 7 months after scheme year end, and is only available on request.<sup>20</sup>

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<sup>18</sup> The broader category of contract-based pension schemes include workplace and non-workplace personal pension schemes, self invested personal pensions, stakeholder pension plans and personal retirement annuity plans.

<sup>19</sup> Occupational Pension Schemes (Scheme Administration) Regulations 1996, Regulation 23.

<sup>20</sup> Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013, Regulation 12(1).

For the Chair’s Statement, “transaction costs” are defined<sup>21</sup> as the costs and charges incurred as a result of the buying, selling, lending or borrowing of investments. “Charges” principally consist of general scheme administration and investment administration costs. They are defined<sup>22</sup> broadly to be all costs and charges which are borne by the members other than transaction costs and those incurred as a result of the holding or maintenance of property, as well as a small number of other exemptions.

In recent years, the UK government and the UK regulators have worked to improve the disclosure of cost impacts to members of occupational pension funds and workplace personal pension schemes.

The first step in this was the introduction of requirements for financial institutions (essentially investment managers) to report relevant data to trustees of pension schemes. The FCA has recently made rules<sup>23</sup> (effective 3 January 2018) regarding reporting of transaction costs at the institutional level which will facilitate the reporting of fees and charges to and by trustees of occupational pension schemes. These transaction costs include both direct and indirect costs of buying and selling transactions. Specific rules are set out regarding how to calculate transaction costs for transferable securities, investment funds and real assets using a “slippage cost” methodology. This methodology calculates transaction costs as the difference between the price at which a transaction was executed, and the price when the order to transact was transmitted to a third-party (the arrival price). This is similar to the way that transaction costs are calculated for PRIIPS (below).

Even though there is now a framework for the provision of this type of information to trustees, this type of information is not currently provided to consumers. Both the Department for Work and Pensions and FCA have been looking to how costs and charges relating to occupational pension schemes and workplace personal pension schemes should be published and disclosed to scheme members.

In February 2018, the UK government finalised a consultation process<sup>24</sup> that improves the disclosure of “costs and charges” to scheme members of occupational pension funds from April 2019.<sup>25</sup> The key proposals adopted are:

1. a new requirement to publish charge and transaction cost information for defined contribution schemes and disclose this to members, beneficiaries of the scheme and others including recognised trade unions;
2. that both the Chair’s Statement and published cost and charge information should set out not just the costs and charges for each default arrangement but also each fund option which the member is able to select;
3. not to be prescriptive as to where costs and charges information is published as long as it is published on the internet for public consumption;

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<sup>21</sup> The Occupational Pension Schemes (Charges and Governance) Regulations 2015.

<sup>22</sup> The Occupational Pension Schemes (Charges and Governance) Regulations 2015.

<sup>23</sup> Financial Conduct Authority, Transaction Cost Disclosure in Workplace Pensions, PS17/20 September 2017.

<sup>24</sup> UK Government, Disclosure of costs, charges and investments in DC occupational pensions, Government response, February 2018.

<sup>25</sup> Regulation 1, Occupational Pension Schemes (Administration and Disclosure) (Amendment) Regulations 2018.

4. that trustees and managers should not only publish the cost and charge information, but also provide an illustration of the compounding effect of the costs and charges affecting their pensions savings;
5. that trustees and managers should, as a minimum, publish costs and charges on a similar annual cycle to the Chair's Statement, which must be produced alongside the scheme's annual reports and accounts; and
6. that each member who receives an annual benefit statement must also be provided at the same time with a web address where members can find the costs and charges for their scheme.

A few specific points of relevance to note are that:

1. generally, spreads are not disclosed as a part of charges or transaction costs, on the basis that entry and exit spreads tend to cancel out over time;<sup>26</sup> and
2. to increase reliability, disclosed transaction costs will be based on the average of the last 5 years.<sup>27</sup>

In terms of the UK policy approach, it should also be noted that since April 2015, default funds in occupational pension plans used for auto enrolment are subject to a cap on annual charges of 0.75% of funds under management (or an equivalent combination of flat fee or % based contribution charge plus annual funds under management charge). A similar restriction applies to default funds in personal pension schemes.

**Comparison points:** Even when the new requirements are implemented, it can be seen that requirements for disclosure of cost impacts for a member of a UK occupational scheme are significantly less than for an Australian superannuation fund, particularly in relation to how it is disclosed. There are policy reasons for the different position, but purely for comparative purposes the following differences are noted:

1. there is no PDS-like document setting out information about cost impacts;
2. no generic nor personalised cost impact information is required in annual benefit statements;
3. there are no disclosure templates nor standardised terminology;
4. there is no requirement to use a standardised synthetic indicator;
5. updating of information only occurs around 7 months after scheme year end; and
6. much more reliance is made on web based disclosure.

In terms of what is disclosed, it should also be noted that calculation of transaction costs does look through investments in ascertaining indirect transaction costs of underlying funds but does not appear to pick up any element of operational costs of a direct or indirect holding of investments (including real property).

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<sup>26</sup> UK Government, Disclosure of costs, charges and investments in DC occupational pensions, Government response, February 2018 at page 19.

<sup>27</sup> UK Government, Disclosure of costs, charges and investments in DC occupational pensions, Government response, February 2018 at page 32.

The only point in which the proposed position arguably exceeds current Australian requirements is in relation to the illustration of the compounding effect of fees and charges of the fund, although this is achieved to some extent in Australia by the use of fee calculators.

#### Case study 2. UK non-PRIIPS products

Notwithstanding the breadth of coverage of the EU PRIIPS Regulation discussed below, a number of pension and non-pension products in the UK will be out of scope of the PRIIPS Regulation and will continue to be regulated as retail financial products under the FCA.

Relevantly this includes:

1. some types of pension products;
2. UK UCITS that fall within the PRIIPS definition but benefit from an exemption until 31 December 2019. Those firms will need to continue to apply the existing Key Investor Information Document (**KIID**) until that time; and
3. some non UCITS retail investment schemes also benefit from the exemption until 31 December 2019. Those firms can use a slightly different document (a NURS KII document).

The FCA Conduct of Business Sourcebook (**COBS**) Chapter 13 sets out content requirements for key features information for non PRIIPS packaged products that are not regulated collective investment schemes.<sup>28</sup> Without unnecessarily repeating details this includes:

1. a description of the nature and amount of the charges a client may be expected to bear in relation to the product;
2. an “effect of charges” table which shows fee impact over various time periods;
3. “reduction in yield” information (effectively illustrating, as a percentage, the reduction in returns caused by charges); and
4. in relation to a personal pension scheme, the amounts of the charges, if any, which a personal pension scheme operator or pension scheme trustee will receive as retained interest (retained interest is the difference between the interest earned on cash accounts by operators and the interest actually paid to investors).

These requirements would not include performance fees or transaction costs. Although not mandatory, most UK funds also disclose an expense ratio, previously referred to as the TER but more recently as the Ongoing Charge Factor (**OCF**). Whilst this is broader than the previously used annual management charge (**AMC**), the OCF does not include transaction costs nor performance fees which are separately disclosed. Most funds distributed in the UK are UCITS which are subject to the EU Directives and Regulations set out in Case study 3 below.

#### Case study 3. EU UCITS

As a consequence of the UCITS Directive, UCITS distributed in the EU are required to provide a KIID. The KIID includes a short fee table, including a single figure ongoing charges ratio, as set out below.

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<sup>28</sup> Most regulated collective investment schemes are regulated as UCITS.

Diagram 4-3 UCITS KIID fee table

Charges for this Fund	
The charges you pay are used to pay the costs of running the fund, including the costs of marketing and distributing it. These charges reduce the potential growth of your investment.	
One-off charges taken before or after you invest	
Entry charge	[]%
Exit charge	[]%
This is the maximum that might be taken out of your money [before it is invested][before the proceeds of your investment are paid out].	
Charges taken from the fund over a year	
Ongoing charges	[]%
Charges taken from the fund under certain specific conditions	
Performance fee	[]% a year of any returns the fund achieves above the benchmark for these fees, [insert name of benchmark].

The **entry** and **exit charges** shown are maximum figures. In some cases you might pay less - you can find this out from your financial adviser.

The **ongoing charges** figure is based on expenses for the year ending []. This figure may vary from year to year. It excludes:

- Performance fees
- Portfolio transaction costs, except in the case of an entry/exit charge paid by the UCITS when buying or selling units in another collective investment undertaking

**For more information about charges, please see pages x to x of the fund's prospectus, which is available at [www.ucitsfund/](http://www.ucitsfund/)**

Note for screen readers: A description of the information in the Diagram is set out in the paragraph above (accessible version).

The Committee of European Securities Regulators (**CESR**) issued guidance in 2010<sup>29</sup> on the calculation of “Ongoing Charges”. Relevantly the ratio includes:

1. all payments to:
  - a. the management company of the UCITS;
  - b. directors of the UCITS if an investment company;
  - c. the depositary;
  - d. the custodian(s); and
  - e. any investment adviser; and
2. all payments to any person providing outsourced services to any of the above, including:
  - a. providers of valuation and fund accounting services;
  - b. shareholder service providers, such as the transfer agent and broker dealers;
  - c. registration fees, regulatory fees and similar charges;
  - d. audit fees;
  - e. payments to legal and professional advisers; and
  - f. any costs of distribution.

<sup>29</sup> Committee of European Securities Regulators, 1 July 2010, “Guidelines on the methodology for calculation of the ongoing charges figure in the Key Investor Information Document”.

Ongoing Charges also include the weighted Ongoing Charges of any funds in which the fund is invested. However Ongoing Charges specifically excludes:

1. entry/exit charges or commissions, or any other amount paid directly by the investor or deducted from a payment received from or due to the investor;
2. a performance-related fee payable to the management company or any investment adviser;
3. interest on borrowing;
4. payments to third parties to meet costs necessarily incurred in connection with the acquisition or disposal of any asset for the UCITS' portfolio, whether those costs are explicit (e.g. brokerage charges, taxes and linked charges) or implicit (e.g. costs of dealing in fixed interest securities, market impact costs);
5. payments incurred for the holding of financial derivative instruments (e.g. margin calls); and
6. the value of goods or services received by the management company or any connected person in exchange for placing of dealing orders (soft commissions or any similar arrangement).

**Comparison points:** The UCITS KIID provides fee disclosure that is broadly in line with MIS in Australia focussing on common fees and expenses. Transaction costs (explicit or implicit) are not included in the fee table nor elsewhere in the disclosure document. Other, minor differences include the exclusion of performance fees from the Ongoing Charges figure. The UCITS fee table separates performance fees from other charges and no single synthetic example figure (like the Australian Fee Example) is provided.

#### Case study 4. EU PRIIPS

On 1st January 2018, the European Regulation on PRIIPS<sup>30</sup> entered into force, obliging all fund managers who manufacture a product to be offered to retail investors to offer the investors a KIID detailing key information about risk, expected performance and costs of the product. Although UCITS funds are PRIIPS, the obligation to produce a KIID in respect of such funds will not apply until 31 December 2019. During the transitional period, UCITS funds are required to comply with the existing requirements to produce a KIID under the UCITS Directive.

The PRIIPS Regulation sets out various requirements in relation to the presentation of costs including two tables: one entitled “*Costs over time*”, and the other entitled “*Composition of costs*”. The format of these tables is set out in Annexure VII to the PRIIPS Regulation.

In the PRIIPS “*Costs over time*” table, a single figure is shown as the summary cost indicator of the total aggregated costs of the PRIIPS. It includes an aggregated figure of total costs for three different holding periods, assuming an investment of EUR10,000 and a figure showing the impact of total costs on investor returns as a percentage reduction in yield (**RIY**). The methodology for the calculation is set out in Annex VI to the PRIIPS Regulation. The figure is required to be expressed in both Euro and percentage terms. The table also includes a breakdown of one-off costs, recurring costs and incidental costs (see details below).

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<sup>30</sup> EU Regulation on Key Information Documents for Packaged Retail and Insurance-based Investment Products (EU1286/2014).

Diagram 4-4 The PRIIPS Cost over time table

Investment [EUR 10 000] Scenarios	If you cash in after [1] year	If you cash in after [recommend holding period/2]	If you cash in [at the end of the recommen- ded holding period]
Total costs	[...] %	[...] %	[...] %
Impact on return (RIY) per year	[...] %	[...] %	[...] %

Note for screen readers: A description of the information in the Diagram is set out in the paragraph above (accessible version).

The PRIIPS “*Composition of costs*” table includes a narrative explanation of each of the costs specified and shows the impact each year of the different types of costs on the investment return the fund might get at the end of the recommended holding period.

Diagram 4-5 The PRIIPS Composition of costs table

This table shows the impact on return per year			
One-off costs	Entry costs	[...] %	The impact of the costs you pay when entering your investment. [This is the most you will pay, and you could pay less]. [AND/OR where the costs are embedded in the price, for instance in the case of PRIIPs other than investment funds] The impact of the costs already included in the price. [This is the most you will pay, and you could pay less]. [Where distribution costs are included in entry costs] This includes the costs of distribution of your product.
	Exit costs	[...] %	The impact of the costs of exiting your investment when it matures.
Ongoing costs	Portfolio transaction costs	[...] %	The impact of the costs of us buying and selling underlying investments for the product.
	Other ongoing costs	[...] %	The impact of the costs that we take each year for managing your investments and the costs presented in Section II.
Incidental costs	Performance fees	[...] %	The impact of the performance fee. We take these from your investment if the product outperforms its benchmark [y by x%].
	Carried interests	[...] %	The impact of carried interests. We take these when the investment has [performed better than x%]. [A payment of y% of the final return will take place subsequently to the exit of the investment.]

Note for screen readers: A description of the information in the Diagram is set out in the paragraph above (accessible version).

The defined costs in the PRIIPS “*Composition of costs*” table include:

1. **One-off costs** (entry or exit costs which are either paid directly by the retail investor or deducted from a payment received from or due to the retail investor), such as distribution fee, constitution costs, marketing costs and subscription fees including taxes;
2. **Recurring costs** (payments deducted from the fund’s assets that represent expenses in the fund’s operation, including transaction costs), such as management fees, custody and depositary fees, audit and legal fees, distribution costs, financing costs related to borrowing, payments to third parties to meet costs incurred in connection with the acquisition or disposal of assets in the fund’s portfolio (transaction costs), the value of goods or services received by the manager in exchange for placing orders with dealers and earnings from efficient portfolio management techniques. Transaction costs must be calculated on an annualised basis, based on an average of the transaction costs incurred by the PRIIP over the previous three years;
3. **Transaction costs** (for any type of transferable security) are calculated as follows: for each purchase, subtract the net realised execution price from the price of the instrument at the time the purchase order is transmitted to another person for execution (the arrival price) and multiply by number of units purchased (vice versa for each sale). The net realised execution price is the price at which the transaction was executed, including all commissions and taxes. The arrival price is the mid-market price of the investment at the time when the order to transact is transmitted to another person. This may generate a negative figure. For private equity, the calculation could include the use of best estimates adopting, as proxies, either a comparable PRIIPS or a peer group. For new PRIIPSs that have been operating for less than 3 years, transaction costs are calculated either based on an estimate of the portfolio turnover in each asset class (using a methodology based on reference indices) or an average of the actual costs incurred during the period of operation; and
4. **Incidental costs** (performance related fee or carried interest). Performance fees are calculated based on a 5 year historical average.

Whilst the PRIIPS Regulation does not provide for ongoing investor reporting, annual reporting (including individualised cost calculations) is required under the related Article 50(9) of Directive 2014/65/EU (commonly referred to as “MiFID II”).

**Comparison points:** The PRIIPS disclosure regime adopts most of the available point-of-sale tools including standardised summary table/s. A synthetic summary cost indicator that sums up fee and cost impacts is also produced for consumers to assist comparison. Unlike the Fee Example used in Australia, this is not limited to default options and is shown for 3 periods (after 1 year and two other periods related to the recommended holding period). The summary cost indicator is expressed as a percentage (rather than a dollar figure as in the Australian Fee Example) and, following the UK example, is expressed as a reduction in yield (effectively showing consumers the extent to which performance has been reduced by fees and costs).

In terms of item detail, recurring costs would include most elements of Administration fees, Investment fees or Indirect costs used for superannuation funds. PRIIPS has a strong focus on transaction related costs and provides a detailed methodology for calculating these costs incorporating implicit costs (including market impact costs) which are included in general cost disclosure including the reduction in yield calculation. Borrowing costs, from related parties, are

treated in the same manner as other costs (meaning they are included in the summary cost indicator, reduction in yield calculation). These are two areas where PRIIPS goes further than Australian cost disclosure (particularly as compared to MIS). Costs of underlying investments are uplifted, as in RG 97, but the test appears to be entirely objective based on whether the underlying structure is an investment product or PRIIPS as defined. There is no test similar in effect to the PDS test in RG 97.<sup>31</sup> It is unclear whether multiple layers of investment products are uplifted in all circumstances. Operational costs associated with holding an asset (such as property operating costs) do not appear to be captured as a cost except for the specific inclusions of custodian costs and payments for property management services.

#### Case study 5. Netherlands pension funds

The framework for disclosure of fees and costs of pension funds in the Netherlands is often referred to positively by commentators.<sup>32</sup> Direct comparison with Australia is difficult because of structural differences and a different approach to communicating fee information; rather than relying on a point-of-sale document, in the Netherlands, fee and cost information is set out in the fund's annual accounts supported by legislated, layered digital communications.

The summary elements below refer to recommendations issued by The Federation of the Dutch Pension Funds first issued in 2011 and updated in February 2016.<sup>33</sup> Large parts of these recommendations have been given statutory force through the Pensions Act since 2015.

In essence, Dutch pension funds are required to report three key figures:

1. pension management costs (referred to as “administrative costs” in relevant legislation) in euros per participant;
2. asset management costs as a percentage of average assets under management (these include remuneration for fiduciary management; investment manager fees; custody fees; performance fees, and fees for services such as investment administration, valuation, accountancy etc); and
3. transaction costs (or estimated transaction costs) separately as, a percentage of average assets under management.

For pension management costs and asset management costs, the use of benchmark figures is also recommended to give the figures some context. It is recognised that providing benchmarks for transaction costs is not yet feasible.

Several principles, that are in most aspects reflective of the approach in RG 97, underlie the calculation of the key figures:

1. costs should not be offset against related income;
2. asset management and transaction costs (but not pension management costs) are calculated on a basis that looks through “investment funds”;

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<sup>31</sup> See clause 101B(4) of Schedule 10 and RG 97.60 – RG 97.67.

<sup>32</sup> See for instance “UK pension funds should copy ‘tried and tested’ Dutch model” IPE, 9 March 2016, “UK told to follow Dutch pension cost reporting example” European Pensions, 10 February 2016, Submission by the Local Government Association to the DWP Transparency Team, 1 May 2015.

<sup>33</sup> Federation of Dutch Pension Funds (Pensioenfederatie), 2016 “Recommendations on Administrative Costs”, revised version.

3. non recurrent costs are included;
4. estimates are used where costs can not be directly identified supported by external verification (e.g. accountant);
5. taxes related to a cost are treated as a part of that cost; and
6. costs paid by other parties are included as costs of the fund.

Management costs of listed entities (e.g. REITs) are not counted as pension management costs.

Transaction costs are calculated by reference to three categories:

1. subscription and redemption costs for investment funds;
2. buy and sell costs for direct holdings in investment funds (net after 1 above); and
3. acquisition costs for assets calculated by reference to invoiced charges (such as brokerage), the buy-sell spread (as recorded per transaction, averaged over a quarter, or based on standard market data), the cost of OTC swap agreements, plus, for illiquid assets, deal costs agency fees, transfer tax etc.

**Comparison points:** At the data level, many elements of the Dutch approach are similar to the Australian approach. Similar types of fees and costs are disclosed on a, simplified, “look through” basis. Differences worth noting are that, for a system that does engage extensively in direct property and infrastructure investment, operational costs of direct real estate investments (and presumably infrastructure investments) are specifically excluded from asset management costs. Management costs of an unlisted investment fund used for investment in real property or infrastructure assets would however be included as asset management costs. Management costs of listed entities (e.g. listed REITs) are not uplifted as pension management costs.

The approach to transaction costs is quite inclusive although somewhat simplified. No attempt is made to calculate implicit transaction costs except for spreads or their equivalent. OTC derivative costs are kept within transaction costs.

Beyond the data level, the regime is quite different to Australia however. Firstly, consumer cost disclosure is not based on a point-of sale document but on annual accounts. As such, there is no attempt to be forward looking (such as in the Fee Example). Importantly, the three key pieces of information (pension management costs, asset management costs and transaction costs) are deliberately separated and shown on a different basis – pension management costs being shown as euro per participant rather than as a percentage of assets. No attempt is made to provide a single synthetic figure by adding the three together for simplified comparative purposes (such as in the Fee Example). This is not an omission but a conscious recognition that the three key pieces of information should be used for different purposes (contrast the Australian approach which lumps the items together for comparative purposes). The approach also recognises the value of benchmarking the individual items.

#### Case study 6. US 401(k) pension plans

Like the UK, the retirement savings landscape in the United States is complicated by fragmented structures across public, workplace based and private pensions. This Case study considers commonly used 401(k) plans. These plans are tax-qualified, defined-contribution pension accounts defined in subsection 401(k) of the US Internal Revenue Code. Under individual work-

place arrangements, retirement savings contributions can be provided and/or matched by an employer. Employee contributions can be made before or after taxation which affects the subsequent taxation treatment.

The US Department of Labour (**DOL**) through its agency, the Employee Benefits Security Administration (**EBSA**), is the primary regulator of these plans.

In October 2010, EBSA issued a new rule to improve transparency of fees and expenses to workers in 401(k) type retirement plans.<sup>34</sup> The 2010 rule provides that when a plan allocates investment responsibilities to participants or beneficiaries, the plan administrator must ensure that such participants and beneficiaries, on a regular and periodic basis, are made aware of their rights and responsibilities with respect to the investment of assets and are provided sufficient information regarding the plan and the plan's investment options, including fee and expense information, to make informed decisions with regard to the management of their individual accounts.

A plan administrator must provide to each participant or beneficiary certain plan-related information and certain investment-related information including the following information relating to cost impacts:

1. **Administrative Expenses Information** - An explanation of any plan level fees and expenses for general plan administrative services that may be charged to or deducted from individual accounts, examples include fees and expenses for legal, accounting, and recordkeeping services;
2. **Individual Expenses Information** - An explanation of any plan level fees and expenses that may be charged to the individual account of a participant or beneficiary based on the actions taken by that person. Examples include fees and expenses for plan loans and for processing qualified domestic relations orders. (The information in these two subcategories must be given to participants on or before the date they can first direct their investments, and then again annually thereafter);
3. **Statements of Actual Charges or Deductions** - In addition to the plan-related information that must be furnished up front and annually, participants must receive statements, at least quarterly, showing the dollar amount of the plan-related fees and expenses (whether "administrative" or "individual") actually charged to or deducted from their individual accounts, along with a description of the services for which the charge or deduction was made. These specific disclosures may be included in quarterly benefit statements required under section 105 of the Employee Retirement Income Security Act of 1974 (**ERISA**); and
4. **Investment-Related Information**, including "Fee and Expense Information", must be furnished in a chart or similar format designed to facilitate a comparison of each investment option available under the plan. For investment options that do not have a fixed rate of return, the total annual operating expenses expressed as both a percentage of assets and as a dollar amount for each \$1,000 invested, and any shareholder-type fees or restrictions on the participant's ability to purchase or withdraw from the investment. The rule includes a model comparative chart, the part relating to fees and costs of which is extracted below:

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<sup>34</sup> Fiduciary Requirements for Disclosure in Participant-Directed Individual Account Plans, 75 FR 64910 (Oct. 20, 2010).

## Part II. Fee and Expense Information

Table 3 shows fee and expense information for the investment options listed in Table 1 and Table 2. Table 3 shows the Total Annual Operating Expenses of the options in Table 1. Total Annual Operating Expenses are expenses that reduce the rate of return of the investment option. Table 3 also shows Shareholder-type Fees. These fees are in addition to Total Annual Operating Expenses.

Table 3—Fees and Expenses		
Name / Type of Option	Total Annual Operating Expenses As a %      Per \$1000	Shareholder-Type Fees
<b>Equity Funds</b>		
A Index Fund/ S&P 500	0.18%    \$1.80	\$20 annual service charge subtracted from investments held in this option if valued at less than \$10,000.
B Fund/ Large Cap	2.45%    \$24.50	2.25% deferred sales charge subtracted from amounts withdrawn within 12 months of purchase.
C Fund/ International Stock	0.79%    \$7.90	5.75% sales charge subtracted from amounts invested.
D Fund/ Mid Cap ETF	0.20%    \$2.00	4.25% sales charge subtracted from amounts withdrawn.
<b>Bond Funds</b>		
E Fund/ Bond Index	0.50%    \$5.00	N/A
<b>Other</b>		
F Fund/ GICs	0.46%    \$4.60	10% charge subtracted from amounts withdrawn within 18 months of initial investment.
G Fund/ Stable Value	0.65%    \$6.50	Amounts withdrawn may not be transferred to a competing option for 90 days after withdrawal.

Generations 2020/ Lifecycle Fund	1.50%    \$15.00	Excessive trading restricts additional purchases (other than contributions and loan repayments) for 85 days.
<b>Fixed Return Investments</b>		
H 200X / GIC	N/A	12% charge subtracted from amounts withdrawn before maturity.
I LIBOR Plus/ Fixed-Type Invest Account	N/A	5% contingent deferred sales charge subtracted from amounts withdrawn; charge reduced by 1% on 12-month anniversary of each investment.
J Financial Serv Co. / Fixed Account Investment	N/A	90 days of interest subtracted from amounts withdrawn before maturity.

Note for screen readers: A description of the information in the Diagram is set out in alt text (accessible version).

The 2010 rule defines<sup>35</sup> the term “total annual operating expenses” for investment options that are mutual funds as the annual operating expenses and other asset-based charges (e.g. investment management fees, distribution fees, service fees, administrative expenses, separate account expenses, mortality and expense risk fees) that reduce the alternative’s rate of return, expressed as a percentage, calculated in accordance with the relevant Securities and Exchange Commission

<sup>35</sup> Paragraph (h)(5).

forms. For investment options other than mutual funds the term is defined as the sum of (i) management fees, (ii) distribution and/or servicing fees and (iii) other fees or expenses that “reduce the alternative's rate of return” but specifically excludes brokerage fees.

Each of “management fees”, “distribution and/or servicing fees” and “brokerage” are defined by reference to the Securities and Exchange Commission Form N-1A (which applies to, inter alia, mutual funds). The inclusion of “other fees or expenses that reduce the alternative's rate of return” is intended to pick up fees (such as externally negotiated investment management fees) associated with entities for which the Securities and Exchange Commission Form does not apply (such as bank collective investment funds).

Tracking through the Securities and Exchange Commission Form N-1A this would, in sum, capture traditional fee items including fees charged at underlying fund level but would not include transactional costs nor operational costs.

**Comparison points:** Fee disclosure requirements for members of 401(k) plans includes “point-of-sale” disclosure but this is separated between plan level administration expenses, individual expenses and investment option related expenses. There is no standardised or simplified disclosure of these items except for the latter.

Investment option level fee disclosure is standardised and includes a single comparative figure “total annual operating expenses” which is expressed both as a percentage and a dollar figure. Compared to Australian superannuation fund fee disclosure in the Fee Example, it does not include fund level administration costs, performance fees of underlying funds, transaction costs (explicit or implicit) nor operational costs. Fees of underlying investment structures are uplifted but only for companies commonly known as mutual funds<sup>36</sup> or an unregistered fund-of-funds structure.<sup>37</sup> Uplifting is not dependent on the investment strategy.

Members of 401(k) plans receive quarterly statements that include information about administrative and individual expenses. This does not include any element of cost impacts at the investment level. Practically, often no administrative costs are shown because they are absorbed under investment related fees.

#### Case study 7. US mutual funds

The Securities and Exchange Commission (**SEC**) regulates the disclosure of fees in mutual funds.

Fee disclosure is driven by the SEC Form N-1A. The form includes a standardised fee table template which is extracted below. Percentage amounts of fees are set out under three broad headings, “Fees and expenses of the fund”, “Shareholder fees” and “Annual fund operating expenses”:

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<sup>36</sup> See item 3(f)(i) to SEC Form N-1A.

<sup>37</sup> See EBSA Field Assistance Bulletin No. 2012-02 Q31.

Diagram 4-7 Extract of fee table from SEC N-1A

### Fees and expenses of the Fund

This table describes the fees and expenses that you may pay if you buy and hold shares of the Fund.

#### Shareholder Fees (fees paid directly from your investment)

Maximum Sales Charge (Load) Imposed on Purchases (as a percentage of offering price)	_____ %
Maximum Deferred Sales Charge (Load) (as a percentage of _____)	_____ %
Maximum Sales Charge (Load) Imposed on Reinvested Dividends [and other Distributions] (as a percentage of _____)	_____ %
Redemption Fee (as a percentage of amount redeemed, if applicable)	_____ %
Exchange Fee	_____ %
Maximum Account Fee	_____ %

#### Annual Fund Operating Expenses (expenses that are deducted from Fund assets)

Management Fees	_____ %
Distribution [and/or Service] (12b-1)	_____ %
Fees Other Expenses	_____ %
_____	_____ %
_____	_____ %
_____	_____ %
Total Annual Fund Operating Expenses	_____ %

Note for screen readers: A description of the information in the Diagram is set out in the paragraph above (accessible version).

The fee table is followed by a simplified fee example which uses the “Total Annual Fund Operating Expenses” to illustrate total costs of a \$10,000 investment over 1, 3 5 and 10 years.

Diagram 4-8 Extract of fee example from SEC N-1A

#### Example

This Example is intended to help you compare the cost of investing in the Fund with the cost of investing in other mutual funds. The Example assumes that you invest \$10,000 in the Fund for the time periods indicated and then redeem all of your shares at the end of those periods. The Example also assumes that your investment has a 5% return each year and that the Fund’s operating expenses remain the same.

	1 year	3 years	5 years	10 years
Although your actual costs may be higher or lower, based on these assumptions your costs would be:	\$ _____	\$ _____	\$ _____	\$ _____
You would pay the following expenses if you did not redeem your shares:	\$ _____	\$ _____	\$ _____	\$ _____

The Example does not reflect sales charges (loads) on reinvested dividends [and other distributions]. If these sales charges (loads) were included, your costs would be higher.

#### Portfolio Turnover

The Fund pays transaction costs, such as commissions, when it buys and sells securities (or “turns over” its portfolio). A higher portfolio turnover rate may indicate higher transaction costs and may result in higher taxes when Fund shares are held in a taxable account. These costs, which are not reflected in annual fund operating expenses or in the example, affect the Fund’s performance. During the most recent fiscal year, the Fund’s portfolio turnover rate was \_\_\_\_\_ % of the average value of its portfolio.

Note for screen readers: A description of the information in the Diagram is set out in the paragraph above (accessible version).

Mutual funds are required to disclose in their annual and semi-annual reports to shareholders fund expenses borne by shareholders during the reporting period. Mutual fund shareholder reports are required to include 2 examples: (1) the cost in dollars associated with an investment of \$1,000, based on the fund's actual expenses and return for the period; and (2) the cost in dollars associated with an investment of \$1,000, based on the fund's actual expenses for the period and an assumed return of 5 percent per year.

Diagram 4-9 Example of mutual fund annual and semi-annual reports fee examples

XYZ Fund			
Based on Actual Fund Return	Beginning Account Value 7/31/2012	Ending Account Value 1/31/2013	Expenses Paid During Period
ABC Shares	\$1,000	\$1,031.75	\$1.23
DEF Shares	1,000	1,032.25	0.51
Institutional Shares	1,000	1,032.55	0.41

XYZ Fund			
Based on Hypothetical 5% Yearly Return	Beginning Account Value 7/31/2012	Ending Account Value 1/31/2013	Expenses Paid During Period
ABC Shares	\$1,000	\$1,024.00	\$1.22
DEF Shares	1,000	1,024.70	0.51
Institutional Shares	1,000	1,024.80	0.41

Note for screen readers: A description of the information in the Diagram is set out in the paragraph above (accessible version).

In addition, plan participants must receive a “Summary of Material Modifications” whenever a change in the plan provisions with respect to fees, or other major changes in the plan, are made.

**Comparison points:** Fee disclosure requirements for members of US mutual funds bear substantial similarity to Australian MIS. The differences are substantially less than in the comparison between US 401(k) pension plans and Australian superannuation funds. A standardised fee table and fee example are used based on a combined single figure. This figure does not include transactional costs; an alternative approach of disclosing turnover rates is used instead.<sup>38</sup> Cost of underlying mutual funds are uplifted on a similar basis to the investing mutual fund, but do not include performance fees.<sup>39</sup> Uplifting is not dependent on the investment strategy.

Periodic shareholder reports include examples of the effect of fees on a standardised \$1,000 investment, based on the total fund operating expenses ratio, but are not personalised to reflect members individual transactions or balances.

<sup>38</sup> Some information about transaction costs is also included in the fund’s statement of Additional Information filed with the SEC. See SEC Form N-1A Item 21.

<sup>39</sup> SEC Form N-1A paragraph 3(f)(iv).

### Case study 8. Hong Kong mandatory pensions

Mandatory contributory retirement savings in Hong Kong are, in relevant respects, regulated under the Mandatory Provident Fund Schemes Ordinance (**MPFSO**) and the related Mandatory Provident Fund Schemes (General) Regulation (**MPFSR**). The structure of the mandatory provident fund (**MPF**) system is broadly similar to retail master trusts in Australia.

Obligations to disclose fees and charges in the legislation<sup>40</sup> at point-of-sale and subsequently, are quite general. These general obligations are supplemented by statutory guidance issued by the regulator, the Mandatory Provident Fund Schemes Authority (**MPFA**), in the Code on Disclosure for MPF Investment Funds (**Disclosure Code**). The Disclosure Code puts in place a fee disclosure regime that is broadly similar to that which applies to superannuation funds in Australia, the key elements being:

1. a standardised fee table divided into five parts:
  - a. Joining Fee and Annual Fee;
  - b. Fees and charges arising from account transactions;
  - c. Fund Operating Charges and Expenses;
  - d. Fees and Charges payable out of underlying funds; and
  - e. Additional Service Fees;
2. the Ongoing Cost Illustration (**OCI**) which illustrates the effect of fees on each \$1,000 invested in each investment option of a fund over 1, 3 and 5 years;
3. the inclusion of a Fund Expense Ratio (**FER**)<sup>41</sup> in periodic fund updates and other places; and
4. disclosure in Annual Benefit Statements of fees incurred for member transactions and a total of such fees.

The MPFA maintains a Comparative Platform on its website<sup>42</sup> which allows consumers to sort, search and compare various attributes of all investment options within the system (469 options across 32 funds).<sup>43</sup> These attributes include the latest FER, ongoing cost illustration figures, standardised risk indicator and returns. All information is extracted from documents prepared by trustees. The screenshot below shows a selection of mixed asset funds ranked by Fund Risk Indicator. The columns show the name of the trustee, the scheme and fund, the type of fund (standardised), the Latest FER, OCI for 1 and 5 year periods, risk and return data.

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<sup>40</sup> Sections 31(2) and 54 of the MPFSR.

<sup>41</sup> For calculation methodology see Chapter E2 of the Code on Disclosure for MPF Investment Funds.

<sup>42</sup> [Comparative Platform, MPFA website.](#)

<sup>43</sup> MPFA Statistical Digest March 2018 at page 2.

Diagram 4-10 MPFA fee comparative platform

248 funds selected / Average FER = 1.73% / Median risk indicator = 8.22%

MPF Trustee	Scheme	Constituent Fund	Fund Type	Latest FER	OCI 1 Year	OCI 5 Year	Fund Risk Indicator	Annualised Return 5 Year	Annualised Return 10 Year
BCT	BCT (MPF) Pro Choice	BCT (Pro) Absolute Return Fund	Mixed Assets Fund	1.39%	\$15	\$78	3.18%	+2.45%	+2.76%
BCT	BCT (MPF) Industry Choice	BCT (Industry) Absolute Return Fund	Mixed Assets Fund	1.73%	\$18	\$97	3.20%	+2.16%	+2.45%
BCT	AMTD MPF Scheme	AMTD Allianz Choice Dynamic Allocation Fund	Mixed Assets Fund	1.30%	\$14	\$73	3.22%	+2.48%	n.a.
UCT	Allianz Global Investors MPF Plan	Allianz Absolute Return Fund - Class T	Mixed Assets Fund	1.25%	\$13	\$71	3.23%	+2.66%	+2.94%
BCT	Allianz Global Investors MPF Plan	Allianz Absolute Return Fund - Class B	Mixed Assets Fund	1.28%	\$13	\$72	3.23%	+2.59%	+2.87%
BCT	Allianz Global Investors MPF Plan	Allianz Absolute Return Fund - Class A	Mixed Assets Fund	1.48%	\$16	\$83	3.23%	+2.45%	+2.69%
HSBC	Hang Seng Mandatory Provident Fund - SuperTrust Plus	Age 65 Plus Fund	Mixed Assets Fund	1.47%	\$15	\$83	3.30%	+2.27%	n.a.
HSBC	HSBC Mandatory Provident Fund - SuperTrust Plus	Age 65 Plus Fund	Mixed Assets Fund	1.48%	\$16	\$83	3.30%	+2.27%	n.a.
HSBC	Sun Life MPF Master Trust	Schroder MPF Capital Stable Portfolio - Class B	Mixed Assets Fund	1.59%	\$17	\$89	4.41%	+2.58%	+2.56%
SLPT	Sun Life MPF Comprehensive Scheme	Sun Life MPF Comprehensive Scheme Stable Portfolio	Mixed Assets Fund	1.94%	\$20	\$108	4.43%	+2.20%	+2.18%
HSBC	Sun Life MPF Master Trust	Schroder MPF Capital Stable Portfolio - Ordinary Class	Mixed Assets Fund	1.78%	\$19	\$99	4.44%	+2.35%	+2.22%
BCT	BCT (MPF) Pro Choice	BCT (Pro) E30 Mixed Asset Fund	Mixed Assets Fund	1.70%	\$18	\$95	4.50%	+2.59%	+2.23%
BOCIP	BOC-Prudential Easy-Choice Mandatory Provident Fund Scheme	BOC-Prudential Stable Fund	Mixed Assets Fund	1.87%	\$18	\$94	4.56%	+3.07%	+2.76%
BCT	Invesco Strategic MPF Scheme	Capital Stable Fund - Unit Class H	Mixed Assets Fund	1.16%	\$12	\$66	4.68%	+4.05%	+3.63%
BCT	Invesco Strategic MPF Scheme	Capital Stable Fund - Unit Class A	Mixed Assets Fund	1.28%	\$13	\$72	4.68%	+3.93%	+3.51%

Note for screen readers: A description of the information in the Diagram is set out in the paragraph above (accessible version).

The platform also provides basic analysis such as the most and least expensive funds by type and the trend of FER over time. Diagram 4-11 is a screenshot of the analysis page showing the average FER by fund type and also the details of the funds with the highest and lowest FER for each fund type.

Diagram 4-11 MPFA platform fee analysis

Analysis of FER (Fund Expense Ratio)								
Analysis of FER								
Fund Type	No. of Funds	Average FER	Highest FER	Constituent Fund / Scheme	MPF Trustee	Lowest FER	Constituent Fund / Scheme	MPF Trustee
Equity Fund	181	1.55%	2.64%	Manulife MPF North American Equity Fund / Manulife Global Select (MPF) Scheme	Manulife	0.65%	Eurasia Fund / AIA MPF - Prime Value Choice	AIA
Mixed Assets Fund	248	1.73%	2.15%	Manulife MPF 2040 Retirement Fund / Manulife Global Select (MPF) Scheme	Manulife	0.91%	SHKP MPF Fund / SHKP MPF Employer Sponsored Scheme *	HBC/IST
Bond Fund	50	1.31%	1.87%	BCT (Industry) Global Bond Fund / BCT (MPF) Industry Choice	BCT	0.78%	Asian Bond Fund / AIA MPF - Prime Value Choice	AIA
Guaranteed Fund	25	2.05%	3.37%	Guaranteed Fund / MASS Mandatory Provident Fund Scheme	MassMutual	1.29%	Global Bond Fund / Hang Seng Mandatory Provident Fund - SuperTrust Plus	HSBC
Money Market Fund - MPF Conservative Fund	36	0.60%	0.85%	Manulife MPF Conservative Fund / Manulife Global Select (MPF) Scheme	Manulife	0.36%	Principal Capital Guaranteed Fund - Class D / Principal MPF Scheme Series 600	PRIN
Money Market Fund - non MPF Conservative Fund	10	0.94%	1.34%	Sun Life MPF RMB and HKD Fund - Class A / Sun Life Rainbow MPF Scheme	Sun Life	0.43%	Sun Life MPF Comprehensive Scheme MPF Conservative Portfolio / Sun Life MPF Comprehensive Scheme	SLPT
Others	4	1.21%	1.29%	Principal HK Dollar Savings Fund - Class I / Principal MPF Scheme Series 800	PRIN	1.00%	My Choice RMB & HKD Money Market Fund / My Choice Mandatory Provident Fund Scheme	BOCIP
Overall	556	1.48%	3.37%			0.36%	Principal HK Dollar Savings Fund - Class D / Principal MPF Scheme Series 600	PRIN
Reduction in average FER since the launch of the platform in 2007: 24.27%								
No (%) of constituent funds in different ranges of FER								
	1% or below	1.01% to 1.25%	1.26% to 1.5%	1.51% to 1.75%	1.76% to 2%	2.01% to 2.25%	2.26% to 2.5%	
End 2015	72 (13.8%)	79 (15.1%)	85 (16.3%)	114 (21.6%)	105 (20.1%)	38 (7.3%)	18 (3.4%)	
End 2016	82 (17.1%)	66 (13.6%)	88 (16.3%)	112 (23.3%)	82 (17.1%)	33 (6.9%)	6 (1.3%)	
End 2017	89 (18.4%)	82 (12.8%)	100 (20.7%)	109 (22.5%)	80 (17.6%)	22 (4.5%)	8 (1.7%)	
28 Feb 2018	89 (18.4%)	82 (12.8%)	100 (20.7%)	109 (22.5%)	80 (17.6%)	22 (4.5%)	8 (1.7%)	

Note for screen readers: A description of the information in the Diagram is set out in the paragraph above (accessible version).

**Comparison points:** The Hong Kong fee table is rather more detailed than the Australian Fee Template as it seeks to set out all fees and charges rather than just the significant ones. In sum, with the AEFC, Australian fee disclosure would be substantially more detailed and lengthy however. Fees and charges incurred in a fund are disclosed in the Hong Kong fee table separately from those incurred by underlying vehicles.

The OCI applies to all investment options unlike the Fee Example in Australia. The Annual Benefit Statement adopts a broadly similar approach to periodic statements in Australia excepting that no attempt is made to estimate or attribute the total fee impact at the member level.

The most important differences would lie in the different approach taken to the data elements included in the Hong Kong fee table and FER which flows through to the OCI and Annual Benefit Statements. Fee disclosure does capture fees and expenses charged at underlying fund level<sup>44</sup> but, in the fee table, focusses only on fees and expenses incurred by intermediaries such as the trustee, custodian, administrator, investment manager and sponsor. Expenses, which are backward looking are not shown in the fee table but are disclosed as a part of the FER. The expenses part of the ratio is driven by whatever is shown as an expense in the financial statements of a fund or underlying fund. This would not include borrowing costs or operational costs (such as property operating costs) and a specific exclusion applies for transaction costs, foreign exchange losses, taxes and distributions. In sum, the Hong Kong disclosure regime stops at more traditional intermediation fees and expenses.

#### Case study 9. New Zealand

In New Zealand, managed funds, including Kiwi Saver products, are regulated under the Financial Markets Conduct Act 2013 (**FMC Act**) and the Financial Markets Conduct Regulations 2014 (**FMC Regulations**) and KiwiSaver Act 2006 (**KiwiSaver Act**). On the whole, New Zealand adopts a disclosure based approach to fees, although it is worth noting that the KiwiSaver Act contains a requirement that KiwiSaver fees must not be unreasonable.

Fee information for regulated offers must be disclosed in the fund's PDS and in the ongoing quarterly fund update. Members of funds do not generally receive an annual member statement but do receive transactional confirmation information. For KiwiSaver and other retirement savings vehicles, the confirmation information statement is provided to investors annually within 3 months of the end of the scheme's account period. The KiwiSaver confirmation information includes a figure showing the approximate total attributed fees charged at the fund level (including underlying fund charges) expressed as a dollar figure for each investor.

The FMC Regulations require that the PDS sets out information under 10 prescribed sections,<sup>45</sup> one of which is titled "What are the fees?" Fee information must include total annual fund charges as a percentage<sup>46</sup> and be set out in tables,<sup>47</sup> however the tables are not prescribed. The PDS includes a worked example of the impact of fees on a \$10,000 investment<sup>48</sup> as does the quarterly fund update.<sup>49</sup> Information in the PDS often includes an estimate of ongoing charges based on reasonable assumptions, and fees such as performance-based fees need to be described.

The annual fund update includes a breakdown of the total of actual fund charges including the fund's total "management and administration charges".<sup>50</sup> This is the cost of all fees and charges

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<sup>44</sup> The definition of underlying fund includes all collective investment schemes such as trusts and REITs.

<sup>45</sup> Clause 9, Schedule 4 FMC Regulations.

<sup>46</sup> Clause 32, Schedule 4 FMC Regulations.

<sup>47</sup> Clause 36, Schedule 4 FMC Regulations.

<sup>48</sup> Clause 38, Schedule 4 FMC Regulations.

<sup>49</sup> Clause 66, Schedule 4 FMC Regulations.

<sup>50</sup> Clause 63, Schedule 4 FMC Regulations.

which affect investors in proportion to their interest in the fund. This definition is quite broad and includes any fees or charges which affect the amount of income or capital distributions made to investors. “Management and administration charges” do include fees charged by an underlying fund in which the fund is invested, however they do not include performance-based fees or trading expenses.<sup>51</sup>

A fund’s total management and administration charges in the fund update (which are made up of management and administration charges plus performance-based fees) comprises a “manager’s basic fee” and “other management and administration charges”. The “manager’s basic fee” generally covers only those items charged directly by the manager in respect of management services. Generally, fees and charges paid by third parties or out of underlying funds are classified as “other management and administration charges”. A fund update must breakdown information about total management and administration fees, the manager’s basic fee and other fees.

Managers must separately disclose in the PDS any performance-based fees charged by the manager or the manager of related underlying funds. The PDS should also separately disclose individual action fees if any (such as contribution or withdrawal fees; and other charges that do not meet the definition of management and administration charges as they do not impact investors in proportion to their interest in the fund (e.g. \$3 per month administration fee)). Fund updates must also disclose other charges.

In addition to fees incurred or charged by the fund itself, the FMC Regulations also require managers to disclose to investors the fees and charges of underlying funds. These fees are not required to be disclosed separately. Instead they must be included within the fund’s overall fee disclosure, either as a “performance-based fee” or “management and administrative charges” (as appropriate).

The New Zealand Financial Markets Authority has issued guidance<sup>52</sup> in relation to what is an “underlying fund”. In broad terms, this adopts the approach taken in the definition of Interposed vehicle in RG 97 in that it looks firstly to the characteristics/business of the investment vehicle (whether it is fund-like), and secondly to the purpose of the investment (would investment reasonably be regarded as being made in the investment vehicle as the end investment or to gain access to assets the entity invests in). The definition is however narrower than the Interposed vehicle concept because it only applies to investment vehicles that are funds or fund like and generally, listed funds are not treated as an underlying fund.

**Comparison points:** Fee disclosure for managed funds in New Zealand is simpler and deliberately less inclusive than for Australian funds. The layout of fee disclosure is less prescriptive. Simplicity in regulation is facilitated, in part, because of comparatively limited product diversity (KiwiSaver products fit within the same regime with limited additional regulation). In contrast to the Australian position, fee and cost disclosure does not extend to including transactional and operational costs within management costs (direct or indirect). Underlying fund costs are uplifted in a manner similar to Australia although for fewer types of underlying investment vehicles and only to the extent that they are management costs. In this

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<sup>51</sup> Clause 2, Schedule 4 FMC Regulations.

<sup>52</sup> Financial Markets Authority (New Zealand) - Guidance Note Fee Disclosure for Managed Funds: May 2017 as amended July 2017.

latter respect, New Zealand requirements are somewhat similar to the requirement that existed before the Stronger Super Reforms made in Australia.

#### Summary of international case studies

Diagrams 4-12 and 4-13 below set out a summary of the Case Studies discussed above. Care needs to be taken in interpreting the summary as some points of comparison do not lend themselves to a simple yes or no answer.

Diagram 4-12 Summary of international reference points – point of sale documents

Feature	Aust Super Funds	Aust MIS	UK Occ. Pens Funds	UK non PRIIPS KIID	EU UCITS KIID	EU PRIIPS	Dutch Pens Funds	US 401(k)	US Mutual Funds	Hong Kong MPF Funds	NZ
Standardised Terminology	yes	yes	no	no	yes	yes	yes <sup>1</sup>	yes <sup>3</sup>	yes	yes	yes
Prescribed Fee Table	yes	yes	no	no	yes	yes	yes <sup>1</sup>	yes <sup>3</sup>	yes	yes	no
Prescribed Fee Example	yes	yes	yes <sup>2</sup>	yes	yes	yes	no	yes <sup>3</sup>	yes	yes	yes
Fee Example including transaction costs	yes	no	no	no	no	yes	n/a	no	no <sup>4</sup>	no	no
Transaction costs shown elsewhere	yes	yes	yes	n/a	no	n/a	n/a	n/a	yes <sup>5</sup>	no	n/a
Fee example multi period	no	no	no	yes	no	yes	n/a	no	yes	yes	no
Fee Example multi a/c size	no	no	no	no	no	no	n/a	no	no	no	no
Fees including property operating costs	yes	yes	no	no	no	n/a	no	no	no	no	n/a
Uplift lower fund costs	yes	yes	no	n/a	yes	yes	yes	yes	yes	yes	yes
Uplift includes subjective element	yes	yes	no	no	no	no	no	no	no	no	yes

n/a means not relevant, uncertain or not considered

#### Notes

- 1 Not in PDS-like document but contained in annual accounts
- 2 Not in PDS like document but contained in Chair's Statement
- 3 Only for one category of fees
- 4 Turnover figures shown in lieu
- 5 In statutory filings

Note for screen readers: A description of the trends in the Diagram is set out below Diagram 4-13 (accessible version).

Diagram 4-13 Summary of international reference points – periodic or annual statements

Feature	Aust Super Funds	Aust MIS	UK Occ. Pens Funds	UK non PRIIPS KIID	EU UCITS KIID	EU PRIIPS	Dutch Pens Funds	US 401(k)	US Mutual Funds	Hong Kong MPF Funds	NZ
Inc. member transaction fees	yes	yes	no	n/a	no	yes <sup>1</sup>	n/a	no	no	yes	yes
Inc attributed fund costs	yes	yes	no	n/a	no	yes <sup>1</sup>	n/a	no	no	no <sup>2</sup>	yes

n/a means not relevant, uncertain or not considered

1. Under the Directive commonly referred to as 'MiFID II'

2 Done only on example basis for \$1,000

Note for screen readers: A description of the trends in the Diagram is set out below (accessible version).

Specific comparison points are expanded upon under individual areas of discussion in the Chapters below, but a few key points of comparison between the jurisdictions discussed in the case studies above that stand out are:

1. standardised terminology, fee tables and synthetic cost indicators are commonly used however there is much diversity in presentation and focus;
2. synthetic costs indicators (like the Australian Fee Example) tend to be more focused on producing a single percentage figure ("reduction in yield" or "ratio") rather than a single dollar figure as is the case in Australia;
3. some synthetic cost indicators or examples in some other jurisdictions are expanded across multiple time periods to illustrate the impacts over time, but none of the jurisdictions reviewed expand this across multiple account sizes;
4. where backward looking fees and costs (e.g. transaction costs and performance fees) are included in disclosure documents, they are often averaged over a period of 5 years;
5. fee and cost disclosure tends to be less detailed for pension products, than for retail investments (contra the position in Australia), although this observation is less true for pension products that invest through generally available retail investment structures;
6. transaction costs data is not commonly included in simplified fee disclosure although the trend, particularly in Europe, is towards doing so;
7. operational costs relating to investments (e.g. property operating costs and borrowing costs in the Australian context) do not appear to be within the contemplation of fee and cost disclosure regimes anywhere except in Australia;
8. uplifting of fee and cost impacts from underlying investment structures is commonly done in the Case study jurisdictions (although the IOPS analysis in WP 15 and WP 20 suggests it is less common across a broader group of jurisdictions), although all jurisdictions other than Australia adopt a rather simpler test for identifying which types of structures this applies to; and

9. periodic or annual account disclosure to members is generally more inclusive in Australia than elsewhere, particularly in relation to including approximated, apportioned impacts of non-account level fees and charges.

A concluding observation on the international case studies is that the diversity of disclosure approaches identified highlights the challenges of making quantitative comparison across jurisdictions. Whilst it can be tempting to form simplistic views about the relative levels of fees and costs of different systems, it is dangerous to do so without a detailed understanding of where the data comes from, how it is calculated and what it includes. Beyond that, the effect of different charging mechanisms (e.g. the use of contribution-based or salary-based charging) and different cost recovery structures (e.g. the role of employers in occupational schemes) would need to be considered in making valid cross jurisdictional comparison of the levels of fees and costs.

## 5. Australian legislative and regulatory framework

### 5.1 Introduction

This Chapter sets out a summary of the Australian regulatory requirements relating to the disclosure of fees and costs in PDSs and periodic statements for MIS and superannuation products. After setting out the current requirements, parts of the historical development of these provisions are also summarised to assist in contextualising the objectives of the requirements.

### 5.2 Current requirements

The following is a summary of the legislative requirements in the Corporations Act and Corporations Regulations relating to the disclosure of cost impacts for superannuation funds and MIS. Only those parts related to disclosure of cost impacts are extracted where possible, although other provisions are also included where necessary for context. This summary focuses on issues relevant to this Review and is not intended to be a comprehensive analysis of the law. As a summary of quite technical provisions, it necessarily ignores many qualifications on the broad provisions not relevant to issues considered and should not be relied upon as legal advice.

In broad terms, the most relevant provisions for the purposes of this Report are the requirements under Schedules 10, 10D and 10E of the Corporations Regulations setting out:

1. the three PDS content requirements (the Fee Template, the AEFC and the Fee Example); and
2. the fee description/calculation and additional explanation of fees and costs in periodic statements.

#### General PDS disclosure requirements

Part 7.9 of the Corporations Act and related Corporations Regulations sets out the disclosure requirements for financial products (including relevantly superannuation products, RSA products and MIS).

Part 7.9 sets out, inter alia:

1. requirement that information in a PDS must be up to date (section 1012J);
2. when the obligation to provide a PDS applies (sections 1012A to 1012IA and 1012K);
3. who must prepare a PDS (section 1013A);
4. required content of a PDS (sections 1013B – 1013M);
5. circumstances in which a supplementary or replacement PDS is required and the content requirements of those documents (sections 1014A-1014L);
6. ongoing disclosure of material changes and significant events (section 1017B);
7. obligation to provide additional information to holders of superannuation and RSA products (sections 1017C);

8. periodic statements for retail clients for financial products that have an investment component (section 1017D);
9. regulation making power to specify additional obligations on trustees of superannuation entities to provide information (section 1017DA); and
10. miscellaneous provisions, including stop orders, exemptions and modifications by ASIC and by regulations (sections 1020A – 1020G).

#### Content requirements for PDSs

Most relevant to this Review, sections 1013C and 1013D set out the content requirements for a PDS. These sections have been substantially modified under the shorter PDS regime explained below:

##### ‘1013C Product Disclosure Statement content requirements

- (1) A Product Disclosure Statement:
  - (a) must include the following statements and information required by this Subdivision:
    - (i) the statements and information required by section 1013D; and
    - (ii) the information required by section 1013E; and
    - (iii) the information required by the other provisions of this Subdivision; and
  - (b) may also:
    - (i) include other information; or
    - (ii) refer to other information that is set out in another document ...
- (3) The information included in the Product Disclosure Statement must be worded and presented in a clear, concise and effective manner.

##### 1013D Product Disclosure Statement content – main requirements

- (1) Subject to this section, subsection 1013C(2) and sections 1013F and 1013FA, a Product Disclosure Statement must include the following statements, and such of the following information as a person would reasonably require for the purpose of making a decision, as a retail client, whether to acquire the financial product: ...
  - (d) information about:
    - (i) the cost of the product; and
    - (ii) any amounts that will or may be payable by a holder of the product in respect of the product after its acquisition, and the times at which those amounts will or may be payable; and
    - (iii) if the amounts paid in respect of the financial product and the amounts paid in respect of other financial products are paid into a common fund – any amounts that will or may be deducted from the fund by way of fees, expenses or charges; and
  - (e) if the product will or may generate a return to a holder of the product – information about any commission, or other similar payments, that will or may impact on the amount of such a return; and ...
  - (h) general information about any significant taxation implications of financial products of that kind; and ...
  - (k) any other statements or information required by the regulations; and ...
  - (m) unless in accordance with the regulations, for information to be disclosed in accordance with paragraphs (b), (d) and (e), any amounts are to be stated in dollars.’

The Corporations Regulations (particularly Part 7.9 Division 4C), in turn, set out specific requirements regarding fee disclosure for certain financial products.

Regulation 7.9.16J applies Division 4C to certain superannuation and MIS products:

‘This Division applies to:

(a) superannuation products other than:

- (i) self-managed superannuation funds; and
- (ii) superannuation products that have no investment component (also known as risk-only superannuation products); and
- (iii) annuities (except market-linked annuities); and
- (iv) non-investment or accumulation life insurance policies offered through a superannuation fund; and
- (v) pensions provided under the rules of a superannuation fund that meet the standards of subregulations 1.06(2), 1.06(6) or 1.06(7) of the SIS Regulations;<sup>53</sup> and

(b) managed investment products.’

Regulation 7.9.16J also had broader effect to exclude RSA products.

Regulation 7.9.16L then sets out additional requirements for information about fees and costs for some of the products captured by Regulation 7.9.16J:

‘(1) ... a Product Disclosure Statement must include the details of fees and costs set out in Part 2 of Schedule 10.

(2) This regulation does not apply if the Product Disclosure Statement is for:

- (a) a margin loan; or
- (b) a superannuation product to which Subdivision 4.2B of Division 4 of Part 7.9 applies; or
- (c) a simple managed investment scheme to which Subdivision 4.2C of Division 4 of Part 7.9 applies.’

Regulation 7.9.16N requires that the PDS include a single section headed “Fees and other costs” which must include:

- ‘(a) the Fees and Costs Template, comprising the template and the additional explanation of fees and costs set out in Part 2 of Schedule 10; and
- (b) an example of annual fees and costs and associated notes as set out in Part 2 of Schedule 10; and
- (c) the boxed Consumer Advisory Warning Statement set out in Part 2 of Schedule 10.’

For explanation of the exceptions related to Subdivision 4.2B and 4.2C of Division 4 of Part 7.9, see the discussion of the shorter PDS regime below.

Schedule 10 of the Corporations Regulations then sets out the substantive disclosure requirements for “Fees and Other Costs” which are the subject of this Review. These are discussed under a separate heading below.

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<sup>53</sup> Regulation 7.9.16J(a)(v) is inserted into Corporations Regulations by paragraph 5 of CO 14/1252.

### The shorter PDS regime

As referred to above, the requirements in Regulation 7.9.16L(1) do not apply to a PDS for a superannuation product to which Subdivision 4.2B of Division 4 of Part 7.9 of the Corporations Regulations applies; or a simple MIS<sup>54</sup> to which Subdivision 4.2C of Division 4 of Part 7.9 applies. For those products, the shorter PDS regime has applied since June 2010 (subject to transitional arrangements). This simplified regime deals mainly with the length, form and content of the PDS, and variation of certain PDS provisions that apply generally to a financial product PDS.

Relevant to the disclosure of fees and costs:

Regulation 7.9.11K sets out the application of Subdivision 4.2B for superannuation products:

- ‘(1) This Subdivision applies to:
  - (a) a superannuation trustee that is required to prepare a Product Disclosure Statement for a superannuation product; and
  - (b) a Product Disclosure Statement for a superannuation product.
- (2) However, this Subdivision does not apply to the following financial products:
  - (a) an interest in a superannuation product that is solely a defined benefit interest;
  - (b) a superannuation product that is solely a pension product;
  - (c) a superannuation product that has no investment component (also known as a risk-only superannuation product).’

Regulation 7.9.11O sets out that the form and contents for superannuation products to which Subdivision 4.2B of the Corporations Regulations applies are contained in Schedule 10D (rather than the general Schedule 10).

Regulation 7.9.11P prescribes requirements for incorporation of material by reference into a PDS of a superannuation product.

Regulation 7.9.11S sets out the application of Subdivision 4.2C for simple MIS:

- ‘(1) This Subdivision applies to:
  - (a) a person that is required to prepare a Product Disclosure Statement for a simple managed investment scheme; and
  - (b) a Product Disclosure Statement for a simple managed investment scheme.
- (2) This Subdivision does not apply to the extent that the simple managed investment scheme relates to a financial product (known as a "quoted product") which is, or is intended to be, traded on a prescribed financial market.
- (3) This Subdivision does not apply to the extent that the simple managed investment scheme relates to a financial product (known as a "stapled security") to which the following requirements apply:
  - (a) the product consists of interests in 2 or more financial products;
  - (b) the interests include at least 1 interest in a registered managed investment scheme;
  - (c) under the terms on which each of the interests is to be traded, the interests must be transferred together;

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<sup>54</sup> Defined in regulation 1.0.02(1). Also see CO 12/749.

- (d) there are no financial products in the same class as the interests which may be transferred separately.
- (4) This Subdivision does not apply to the extent that the simple managed investment scheme is a managed investment scheme that has a constitution that provides that:
  - (a) a member may direct that an amount of money corresponding to part or all of the amount invested by the member in the scheme be invested in accessible investments; and
  - (b) the distributions of capital and income from the scheme to the member in relation to the member's interests in the scheme will be determined by reference to amounts received by the responsible entity or a custodian in relation to the accessible investments acquired in accordance with the direction.<sup>55</sup>

Regulation 7.9.11W sets out that the form and contents of a PDS for a simple MIS is contained in Schedule 10E (rather than the general Schedule 10).

Regulation 7.9.11X permits the incorporation into a PDS of a simple MIS of matters by reference, and also sets out the method of incorporation and related liability.

Finally, it should also be noted that ASIC Class Order [CO 12/749] (**CO 12/749**) modifies Regulation 7.9.11K in a manner that permits Platform Providers to use the shorter PDS regime.

The form and content requirements in Schedules 10, 10D and 10E

The substantive disclosure requirements for “Fees and Other Costs”, which are relevant to this Review, are set out in:

1. Schedule 10 (for superannuation and MIS products to which Regulation 7.9.16L applies but which are not covered by the shorter PDS regime);
2. Schedule 10D (for superannuation products covered by the shorter PDS regime); and
3. Schedule 10E (for MIS covered by the shorter PDS regime).

Structurally, Schedules 10D and 10E differ from Schedule 10 in that they deal only with PDSs (and not periodic statements) and they are not limited to disclosure of fees and charges: they prescribe the length, sequence, section titles and numbering and some of the PDS content. For products to which Schedule 10 continues to apply - length, sequence and content continue to be regulated in a more general manner under section 1013D. Part 3 of Schedule 10, which deals with disclosure of fees and costs in periodic statements, continues to apply to superannuation and MIS products covered by the shorter PDS regime.

Clause 8 of Schedule 10D requires disclosure of fees and costs for each MySuper product<sup>55</sup> in the form of a template table that is, in all relevant respects, identical to the one required in Schedule 10. Relevant definitions are also carried over from Schedule 10.

Clause 8(7) and (7A) of Schedule 10D also require the PDS to include a worked example of annual fees and costs in the fees and costs section that is the same as the one required under Division 5 and 6 of Schedule 10.

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<sup>55</sup> Also including any investment option that has been described under section 5 of the PDS.

Clause 8(10) of Schedule 10D requires that fees and costs of all investment options<sup>56</sup> within a superannuation fund are to be provided in accordance with Schedule 10 and that this information can be incorporated by reference.

For simple MIS, clause 8 of Schedule 10E requires disclosure of fees and costs for specified investment options in the form of a template table that is a slightly cut down version of the one required in Schedule 10. Relevant definitions are also carried over from Schedule 10.

Clause 8(7) of Schedule 10E also requires a worked example of annual fees and costs that is the same as the one required under Division 5 and 6 of Schedule 10. Again, clause 8(10) requires that fees and costs of all investment options within a MIS are to be provided in accordance with Schedule 10 and can be incorporated by reference.

Accordingly, for most issues relevant to this Review, namely how fees and costs are disclosed in the PDS (the Fee Template, the AEFC, the Fee Example) and the disclosure of fees and costs in periodic statements, regard can be had to Schedule 10, and in particular, to the definitions applied in that Schedule.

The enacted form of Schedule 10 has been materially modified by CO 14/1252 which has been further modified by ASIC during the development process by ASIC Corporations (Amendment) Instrument 2015/876, ASIC Corporations (Amendment) Instrument 2016/1224, ASIC Corporations (Amendment and Repeal) Instrument 2017/65, ASIC Corporations (Amendment) Instrument 2017/664 and ASIC Corporations (Amendment) Instrument 2017/1138. These modifications are summarised below under Chapter 5.3. It can be challenging to interpret Schedule 10 as modified without the assistance of a consolidated version of these changes. ASIC has provided me with a consolidated version which is attached at **Appendix 3**. Schedule 10 without the amendments made by CO 14/1252 is attached at **Appendix 4**.

**Part 1 of Schedule 10** provides the definition of terms used in the disclosure regime including Administration fees, Investment fees, Indirect costs, Interposed vehicle, Management costs, Transactional and operational costs and Indirect cost ratio.

**Part 2 of Schedule 10** sets out main disclosure elements for fees and costs in the PDS which are as follows:

1. the Fee Template for superannuation products (Division 1);
2. the Fee Template for MIS (Division 2);
3. the requirement to include certain information under the heading “Additional explanation of fees and costs” in the fees section of PDSs (Division 4);
4. definitions of fees for superannuation products (Division 4A);
5. the requirement to include a prescribed Fee Example (Division 5); and
6. the requirement to include a prescribed Consumer Advisory Warning (Division 7).

**Part 3 of Schedule 10** then sets out requirements relating to how fees and costs are to be disclosed in periodic statements including disclosure of Indirect costs (Division 1), total fees (Division 2) and a requirement to include certain information under the heading “Additional explanation of fees and costs” (Division 3).

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<sup>56</sup> This includes MySuper products which are also subject to the other parts of Schedule 10D.

### The Fee Template and Fee Example - superannuation products

Except where indicated, this summary focusses on the main ongoing fees and costs rather than activity generated fees and costs (such as buy-sell spreads, switching fees, exit fees, advice fees and other activity fees) which have generated relatively little comment during the Review process.

The prescribed Fee Template shows “the fees and other costs that you may be charged”, and sets out three main ongoing fee elements: Investment fees, Administration fees and Indirect Cost Ratio (**ICR**) (representing the fee and cost impacts that are indirect). Each of these is defined in a manner that excludes the other although the trustee has some discretion to treat some Investment or Administration fees as Indirect costs<sup>57</sup> (in which case the Investment or Administration fees would be lower and the ICR correspondingly higher).

Investment fees are defined<sup>58</sup> as fees in payment for the exercise of care and expertise in the investment assets of a superannuation entity including investment management fees and costs relating to the investment of assets but excludes borrowing costs.

Administration fees are defined<sup>59</sup> as a fee that relates to the administration or operation of the superannuation entity including costs that relate to that administration or operation, but again, excludes borrowing costs.

The ICR is based on the definition of Indirect costs in clause 101A of Schedule 10. The definition of Indirect costs<sup>60</sup> adopts a top down, outcomes driven, drafting approach focussing on any amount that will reduce, directly or indirectly, the return or value of property of the product or an Interposed vehicle. The definition also includes, rather more technically, payments of costs by other persons.<sup>61</sup> Each of those definitional elements is however limited by an overriding provision that an amount is only an Indirect cost if it would be an Investment fee or an Administration fee if paid from the superannuation fund itself.<sup>62</sup>

The definition is specifically expanded to include transaction costs for acquiring derivatives.<sup>63</sup> Although not specifically included, transactional and operational costs for other investments would generally be included as Investment fees, or consequently, Indirect costs based on the general definitions.

The example of annual fees and costs of a specified MySuper product/option is also included in the PDS.<sup>64</sup> This Fee Example adds Investment fees to Administration fees plus the Indirect costs to show a total dollar amount that the member “will be charged”. This example assumes no flows into or out of the product/option over the 12 month illustrative year. The dollar calculation is based on an account balance of \$50,000.

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<sup>57</sup> Clause 209A of Schedule 10 (definition of Administration fee and Investment fee).

<sup>58</sup> Clause 209A of Schedule 10.

<sup>59</sup> Clause 209A of Schedule 10.

<sup>60</sup> Clause 101A of Schedule 10.

<sup>61</sup> Clause 101A(1)(a)(ii) of Schedule 10.

<sup>62</sup> Clause 101A(1)(d) of Schedule 10.

<sup>63</sup> The calculation of which could be based on the difference between actual and underlying return, the extent to which the acquisition cost exceeds the disposal price at the time of acquisition or 0.1% of the value of the derivative see clause 101A(3) of Schedule 10.

<sup>64</sup> Regulation 7.9.16N(2)(b).

## The Fee Template and Fee Example - managed investment schemes

The Fee Template and Fee Example for MIS are broadly similar to superannuation products however there are a few important differences.

First, Division 2 of Part 2 of Schedule 10 includes two tables for MIS; the difference relating to whether the product has a single or multiple fee structure. The difference between the two is not significant for current purposes.

Unlike the superannuation Fee Template, the MIS Fee Template is split into three headings: (a) Fees when your money moves in or out of the MIS, (b) Management costs and (c) service fees.<sup>65</sup> Except for the fact that some fees are not relevant to both products, the items under (a) and (c) are not materially different between the superannuation and MIS Fee Templates.

Management costs are included as a single item rather than being split between Investment fees and Administration fees as in the superannuation Fee Template. Most of the elements of the definitions of Investment fees or Administration fees are included in the definition of Management costs.<sup>66</sup> The following table maps the differences and similarities between the definitions.

Diagram 5-1 Management costs for MIS vs superannuation product fees

<b>Management costs definition</b>	<b>Superannuation product fees</b>
<b>Elements included</b>	<b>Treatment in superannuation fees</b>
an amount payable for administering the scheme	included in Administration fees
costs involved in gaining access to or participating in a custodial arrangement	not specifically mentioned but included in general definition of Investment fees
distribution costs	not specifically mentioned but included in general definition of Administration fees
other expenses and reimbursements	not specifically mentioned but included in general definition of Administration fees or Investment fees
amounts payable for investing assets	not specifically mentioned but included in general definition of Investment fees
amounts deducted from a common fund by way of fees, costs, charges or expenses	not specifically mentioned but included in general definition of Administration fees or Investment fees
estimated performance fees	specifically included in Investment fees
any other investment-related expenses and reimbursements,	specifically included in Investment fees although reimbursements not specifically mentioned
Indirect costs as defined in clause 101A of Schedule 10	not included in Investment or Administration fees – included in Indirect costs and ICR
<b>Elements excluded</b>	<b>Treatment in superannuation fees</b>
fees disclosed under other items	generally similar

<sup>65</sup> The layout and content of the Fee Template has not changed materially since it was introduced.

<sup>66</sup> Clause 102 of Schedule 10.

Management costs definition	Superannuation product fees
Elements excluded	Treatment in superannuation fees
Transaction costs and operational costs (other than costs of derivative products)	not excluded – included in Administration fees, Investment fees or ICR as appropriate
costs related to an asset or activity that the investor would incur if he/she invested directly in the asset	not excluded – included in Investment fees or ICR as appropriate
incidental fees	not excluded - included in Administration fees, Investment fees or ICR as appropriate

The Fee Example of annual fees and costs for a MIS includes only two items – Contribution fees plus Management costs (noting from the table above that Management costs incorporates most of the three fee elements included in the Fee Example for a specified MySuper product/option but not Transactional and operational costs and costs that a direct investor would incur). In the calculation, a year end contribution of \$5,000 and a balance of \$50,000 are used.

#### The Additional Explanation of Fees and Costs (AEFC)

Division 4 of Part 2 of Schedule 10 sets out information that must be included in the PDS under the heading “Additional Explanation of Fees and Costs”. The use of this separate area for some fee information can be traced back to the report by Professor Ian Ramsay, *Disclosure of Fees and Charges in Managed Investments: Review of Current Australian Requirements and Options for Reform* (identified for ASIC purposes as ASIC Report 16) (**Ramsay Report**) and the ASIC fee disclosure models released in 2003 and 2004. The Fee Template was originally intended to be a simple, at a glance, snapshot of “significant” fees<sup>67</sup> with other fee information being disclosed outside the table in an “important additional items” section. Originally in 2005 this section included only five items, none of which were otherwise included in the Fee Template: worked fee examples, transaction costs, incidental fees, advisor remuneration arrangements and how fees could be negotiated (if relevant).

The current requirements are substantially expanded by the Stronger Super Reforms and CO 14/1252 and comprise 15 items and 26 item subheadings. The worked Fee Example in the original 2005 version has been further prescribed and moved to its own section. The remaining four original items are all contained within the current requirements in an expanded form. Other items now included are as follows:<sup>68</sup>

1. any other service fees, advice fees, activity fees or special request fees;
2. information about performance fees;
3. a cross reference on tax issues;
4. insurance fees (if relevant);
5. whether the benefit of any tax deductions are passed on to an investor;
6. explanation of advice fees;

<sup>67</sup> ASIC Report 23 at paragraph 5.2.

<sup>68</sup> Clause 209 of Schedule 10.

7. information about fee changes;
8. information about flexible charging structures (if relevant);
9. details of borrowing costs (for superannuation products only); and
10. details of property operating costs (for superannuation products only and only until 30 September 2019).<sup>69</sup>

#### Periodic statements

The Fee Template, Fee Example and the AEFC are designed as point of sale disclosure that sets out how fees and charges may be, will be, or are being, charged. The periodic statement given to members of superannuation funds and MIS serves multiple purposes, including providing after-the-event confirmation of what fees and charges were actually incurred or paid by a member.<sup>70</sup>

Section 1017D sets out the key elements such as:

1. the circumstances in which a periodic statement must be given (to retail clients who holds or held, relevantly, a MIS, a superannuation product or an RSA product);<sup>71</sup>
2. when periodic statements must be given<sup>72</sup> (as soon as practicable and in any event within 6 months after the end of a reporting period;<sup>73</sup>)
3. content of the periodic statement:
  - ‘(4) **[Information required]** The periodic statement must give the holder the information that the issuer reasonably believes the holder needs to understand his or her investment in the financial product.
  - (5) **[Contents]** The periodic statement must include the following if they are relevant to the financial product:
    - (a) opening and closing balances for the reporting period;
    - (b) the termination value of the investment at the end of the reporting period (to the extent to which it is reasonably practicable to calculate that value for the investment or a component of the investment);
    - (c) details of transactions in relation to the product during the reporting period as required by regulations made for the purposes of this paragraph;
    - (d) any increases in contributions in relation to the financial product by the holder or another person during the reporting period;
    - (e) return on investment during the reporting period (on an individual basis if reasonably practicable to do so and otherwise on a fund basis);

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<sup>69</sup> After 30 September 2019, property operating costs for superannuation products should be disclosed as Investment fees or Indirect costs.

<sup>70</sup> “For periodic statements, it is essential that the actual amount charged or incurred by the member or product holder is indicated on the statement”. Explanatory Statement to the Corporations Amendment Regulations 2005 (No.1).

<sup>71</sup> Section 1017D(1).

<sup>72</sup> Section 1017D(3).

<sup>73</sup> Generally every 12 months or after a holder ceases to hold the product – section 1017D(2).

- (f) details of any change in circumstances affecting the investment that has not been notified since the previous periodic statement;
  - (g) details prescribed by regulations made for the purposes of this paragraph.’
4. requirements that most information be disclosed in dollars;<sup>74</sup> and
  5. how the statement can be given.

Regulation 7.9.60B(2) includes a requirement that a periodic statement must include a brief description of each transaction in relation to the product. Relevant to fee disclosure, Regulation 7.9.60B(6) provides:

‘For a superannuation product or a managed investment product, the only fees and costs that need to be itemised in a periodic statement are the fees and costs shown in the fees and costs template of a Product Disclosure Statement in Part 2 of Schedule 10.’

Regulation 7.9.75(1) sets out more details about how to show fees and costs and other information in periodic statements as follows:

- ‘(1) For paragraph 1017D(5)(g) of the Act, the prescribed details in relation to a financial product include:
  - (a) the amounts paid by the holder of the financial product in respect of the financial product during the period; and
  - (b) if the amounts paid in respect of the financial product, and the amounts paid in respect of other financial products, are paid into a common fund, and amounts are deducted from the common fund by way of expenses, fees and charges:
    - (i) a proportion of the amount deducted that is actually or notionally attributable to the product holder's interest; and
    - (ii) if applicable - a statement informing the product holder that the notional proportion of the amount may not give an accurate estimate of the effect of the deduction on the product holder's interest; and
  - (c) a statement informing the product holder:
    - (i) that there is a dispute resolution mechanism that covers complaints by holders of the product; and
    - (ii) of the means by which a product holder is able to gain access to that mechanism; and
  - (d) a statement that further information in relation to the financial product is available on request, and the means by which the product holder can gain access to that information; and
  - (e) in relation to a superannuation product (other than a self-managed superannuation fund) or a managed investment product - the details set out in Part 3 of Schedule 10.’

Subregulation 7.9.75(1)(b) is omitted by CO 14/1252 and replaced by provisions that apply for periods ending after 29 June 2019. Part 3 of Schedule 10, as modified by CO 14/1252, then sets

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<sup>74</sup> Section 1017D(5A).

out specific requirements regarding how Indirect costs and total fees are to be calculated and disclosed. Essentially, for a MySuper product or a superfund investment option (if relevant), the text and amounts of two indirect items are set out after the transactions itemisation:<sup>75</sup>

**‘Indirect costs of your investment**

This approximate amount has been deducted from your investment and covers amounts that have reduced the return on your investment but are not charged as a fee.

**Other fees of your investment**

This approximate amount or amounts have been deducted from your investment and covers fees that are not reflected as transactions on this statement.’

Similarly, for a MIS, the following text and amounts must be inserted after the transactions itemisation<sup>76</sup>:

**‘Indirect costs of your investment**

This approximate amount has been deducted from your investment and covers amounts that have reduced the return on your investment but are not charged directly to you as a fee.’

Clause 301(2) to (4) of Schedule 10 set out the rules for calculating the amounts to be inserted. Amounts must be shown as a single dollar and:

1. for a MySuper product or investment option, must include the Indirect costs; and
2. for a MIS must include all Management costs (including Indirect costs) not deducted directly from the holders account calculated by multiplying the ICR by the holders average account balance.

Clause 302 further requires the insertion of a total fee calculation including all fees and costs included in the statement:

**‘TOTAL FEES YOU PAID**

This approximate amount includes all the fees and costs which affected your investment during the period.’

Finally, as is the case for the PDS, the periodic statement also contains a separate statement outside of the key summary, under the heading “Additional Explanation of Fees and Costs”. For superannuation products, this includes details of: any activity fees, advice fees and insurance fees, a statement about whether the benefit of any tax deduction has been passed on to the investor, and for any reporting period ending after 29 June 2019, information about the impact of borrowing costs.

For MIS, this includes details of: any incidental fees, service fees, whether the benefit of any tax deduction has been passed on to the investor, and for any reporting period ending after 29 June 2019, information about transactional and operational costs.

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<sup>75</sup> Clause 301(1) of Schedule 10.

<sup>76</sup> Clause 301(1A) of Schedule 10.

### 5.3 Historical development

This section sets out key events in the development of the current regime for disclosure of fees and costs in PDSs and periodic statements. Diagram 5-2 is a brief chronology. More details are set out sequentially below.

Diagram 5-2 Brief chronology of development of the fee disclosure regulations

Date	Event
pre FSRA	Disclosure for MIS regulated under the prospectus regime in Chapter 6D of the Corporations Act.  Disclosure for superannuation products regulated under the SIS Act and RSA products under the RSA Act.
November 2001	ASIC Policy Statement 168 <i>Product Disclosure Statements (and other disclosure obligations)</i> issued which includes good disclosure principles: disclosure should (a) be timely, (b) be relevant and complete, (c) promote product understanding, (d) promote product comparison, (e) highlight important information, and (f) have regard to consumers' needs.
March 2002	Commencement of FSRA and related regulations. Broadly common disclosure regime created for superannuation and MIS products.
September 2002	Original Schedules 10 and 10B of the Corporations Regulations cease effect after Senate disallowance of key regulations.
September 2002	The Ramsay Report identified that fees were disclosed differently across and within products, terminology was used inconsistently, positioning of fee disclosure in PDSs varied and generally that comparison was not facilitated.
August 2003	ASIC Report 23: <i>A model for fee disclosure in product disclosure statements for investment products</i> is released ( <b>ASIC Report 23</b> ). This report set out a good practice model for fee disclosure in PDSs including the use of a Significant Fees Table, a Breakdown of Ongoing Fees Table and some degree of standardisation of terminology (for common significant fees).
June 2004	Corporations Amendment Regulations 2004 (No 6) (Cth) are gazetted. Known as the dollar disclosure regulations, these require product issuers to disclose various fees, benefits, costs and interests as amounts in dollars in PDSs.
June 2004	ASIC releases revision to the model for fee disclosure introducing a single table containing a reference to all fees and costs, both direct or indirect, and stated in dollars or translated to dollar terms.

Date	Event
March 2005	Corporations Amendment Regulation 2005 (No 1) (Cth) ( <b>Amendment Regulation</b> ) substituted Schedule 10 and gave statutory force to most elements of the ASIC model for fee disclosure, including Management costs and the indirect costs ratio.
March 2006	ASIC first publishes guidance in <i>Enhanced fee disclosure regulations: Questions and answers</i> , which was re-issued in May 2007 as RG 97.
June 2010	Corporations Amendment Regulations 2010 (No. 5) (Cth) introduced a short form PDS regime for most superannuation and simple MIS products. This did not materially change the content of fee disclosure although it did result in some fee disclosure being incorporated by reference into the PDS rather than appearing in the PDS itself.
June 2010	The Super System Review made several specific observations and recommendations regarding the disclosure of fees and charges for superannuation products. The Super System Review Final Report observed that “ <i>the superannuation system lacks transparency, comparability and accountability in relation to costs, fees and investment returns</i> ” and recommended the adoption of a new ratio to capture administration and investment expenses.
November 2011	ASIC re-issued RG 97.
July 2014	Disclosure changes under Stronger Super Reforms commence for superannuation and MIS.
July 2014	ASIC releases ASIC Report 398: <i>Fee and cost disclosure: Superannuation and managed investment products</i> ( <b>ASIC Report 398</b> ).
December 2014	CO 14/1252 and draft updated RG 97 released.
November 2015	ASIC makes amendments to CO 14/1252 by ASIC Corporations (Amendment and Repeal) Instrument 2015/876 and final version of RG 97 released.
December 2016	ASIC makes further amendments to previously modified CO 14/1252 by ASIC Corporations (Amendment) Instrument 2016/1224.
March 2017	ASIC issued updated RG 97 and makes further amendments to CO 14/1252 by ASIC Corporations (Amendment and Repeal) Instrument 2017/65.
September 2017	ASIC makes further amendments to CO 14/1252 by ASIC Corporations (Amendment) Instrument 2017/664.
November 2017	Review commences.
December 2017	ASIC makes further amendments to CO 14/1252 by ASIC Corporations (Amendment) Instrument 2017/1138 as a consequence of the Review.

## Financial Services Reform Act 2001 (Cth) (FSRA)

One of the objectives of the FSRA was to establish a consistent regulatory regime for licensing, disclosure and conduct for financial services. Prior to the FSRA, disclosure for MIS was regulated under the prospectus regime in Chapter 6D of the Corporations Act and disclosure for superannuation products was regulated under the SIS Act (in the Insurance and Superannuation Commission's section 153 Determination) and RSA products under the RSA Act.

One of the stated statutory objectives was, and remains, to:

‘promote confident and informed decision making by consumers of financial products and services while facilitating efficiency, flexibility and innovation in the provision of those products and services’.<sup>77</sup>

Without unnecessarily repeating all definitional provisions, the parts referred to below applied to both superannuation and MIS products (except where indicated).

The FSRA effectively replaced the whole of Chapter 7 of the Corporations Act. The new Part 7.9 dealt with disclosure and some other matters relating to the issue and sale of financial products. Although amended repeatedly, as summarised below, the basic structure of the relevant parts of Part 7.9 remain as originally enacted and cover issues such as: who issues a PDS, when it must be issued, content and amendment of a PDS, and issue and content of periodic statements.

Section 1013C(3) of the Corporations Act, in its original form and since, states that the information in the PDS:

‘must be worded and presented in a clear, concise and effective manner’.

The general content requirements for PDSs were, as now, set out in s1013D(1)(d) including the requirement to set out:

- ‘(i) the cost of the product; and
- (ii) any amounts that will or may be payable by a holder of the product in respect of the product after its acquisition, and the times at which those amounts will or may be payable; and
- (iii) if the amounts paid in respect of the financial product and the amounts paid in respect of other financial products are paid into a common fund—any amounts that will or may be deducted from the fund by way of fees, expenses or charges; ...’

Further details were set out in the Corporations Regulations. There was much legislative debate and activity about the Corporations Regulations including Senate disallowance of the superannuation disclosure regulations with effect from 16 September 2002. For the current purpose of noting key aspects of the development of regulation of fees and charges, there is little point in reciting the lengthy history of the political debate. The provisions mentioned below are as initially gazetted ignoring disallowances.

Regulation 7.9.01 defined many of the terms used in the subsequent Corporations Regulations including terms such as charge, contribution charge, death and disability insurance charge, direct account charge, exit charge, investment management charge, ongoing management charge, switching charge, and transaction cost.

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<sup>77</sup> Section 760A(a).

Other parts of the Corporations Regulations contained some specific requirements for fee disclosure of superannuation products based largely on the pre-existing requirements in the SIS Act.

Subregulation 7.9.01(1), defined OMC as being a charge that:

‘(a) is made against:

- (i) a product holder’s benefits in a fund or financial product; or
- (ii) the assets or investment earnings of the fund or financial product (as appropriate); or
- (iii) a product holder or another person (acting) on the product holder’s behalf; and

(b) is not:

- (i) a contribution charge, death and disability insurance charge, exit charge or switching charge; or
- (ii) a charge that:
  - (A) is made for a service requested by the product holder that the product holder could not reasonably expect to receive unless the product holder asked for it and paid a reasonable charge; and
  - (B) is provided by the provider; and
  - (C) is reasonable; and

(c) is worked out in accordance with Schedule 10.’

In 2002 Schedule 10 set out the workings of the OMC:

‘1. The ongoing management charge for a year of income is:

$$\frac{MC}{AV}$$

expressed as a percentage, where:

AV is the average value of the net assets of the fund or product during the year of income, worked out in the following way:

- (a) add each of the net asset valuations made during the year of income;
- (b) divide the result by the number of valuations added under paragraph (a).

MC is the total amount of ongoing management charges charged for the year of income, excluding, in relation to a fund, the amount of a charge paid or payable by a standard employer-sponsor of the fund.

2. For item 1, if:

- (a) underlying investments are managed by a person, persons or organisation other than the product issuer or an employee of the product issuer; and
- (b) a charge is deducted from the investment return before the amount of the return is worked out and paid to the fund or product issuer;

a charge must be included in MC in respect of the investments managed by the person, persons or organisation.

3. For item 2:

- (a) a direct investment by the fund in shares or other securities listed for quotation in the official list of a stock exchange in Australia or elsewhere is to be excluded; and
- (b) if the product issuer cannot determine the amount of charge, the product issuer must make a reasonable estimate of the amount.’

In 2002, Schedule 10B also set out some specific disclosure requirements for “Charges of the fund” for each investment option within a superannuation product:

‘7.1 For any contribution charge, direct account charge, investment management charge, exit charge or switching charge of the fund, a description of:

- (a) the charge; and
- (b) the amount of the charge:
  - (i) expressed as a fixed amount; or
  - (ii) if it is not practicable to express a fixed amount, expressed as a percentage of:
    - (A) the contributions made in respect of a member; or
    - (B) the member’s benefits in the fund; or
    - (C) the assets of the fund; and
- (c) against what, or to whom, the amount or percentage will be charged (for example, against contributions made in respect of the product holder to the fund or against the assets of the fund); and
- (d) if the amount or percentage varies for different classes of product holders, the minimum or maximum limit for each amount or percentage ...

7.3 A statement outlining:

- (a) the circumstances in which and the times when any charge may be increased or decreased; and
- (b) any maximum limit, for a charge, mentioned in the governing rules of the fund.

7.4 If a charge referred to in subitem 7.1 cannot be expressed as an amount or a percentage, the product issuer must explain how it will be determined.’

Clause 8 of Schedule 10B required inclusion of the OMC in the PDS. Disclosure varied depending on whether the financial product offered a single investment strategy or whether it offered a choice of investment strategies, but broadly the objective and calculation of the OMC was driven by the requirement<sup>78</sup> to disclose the following statement in the PDS:

‘Its purpose is to give a broad indication of the level of costs incurred by a particular fund or provider of an annuity as a percentage of the value of assets. Costs include all fees, charges and expenses except for [insert ‘switching costs, ‘entry and exit charges’ or other appropriate description]. The level of costs incurred by an individual product holder will depend on individual circumstances and as a percentage of value of the fund assets of the individual may be more or less than the ongoing management charge. The ongoing management charge should not be taken to be representative of the actual fees, charges and expenses that will be borne by an individual. Full details of fees, charges and expenses applicable to individual circumstances are set out in [section X] of this document.’

The content requirements for periodic statements for superannuation funds were set out in Regulations 7.9.20(1)(d) and 7.9.75 and included, relevantly, a requirement to include the cost of any transactions (including the amount payable and the amount of taxes and charges in relation to the transaction), the total amounts paid by the holder of the financial product in respect of the financial product during the period, and the times at which those amounts were paid; and amounts deducted from the common fund by way of fees, expenses or charges.

In summary, the FSRA imposed a generally common PDS format for superannuation and MIS products, although the disclosure requirements for fees and costs for superannuation funds were

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<sup>78</sup> Clause 8 of Schedule 10B of the Corporations Regulations.

somewhat more detailed. Whilst including specific PDS disclosure requirements for costs and other amounts payable by a holder or out of a common fund, there was no prescribed layout or format excepting the use of the OMC<sup>79</sup> for some superannuation products. It is notable that there was no requirement to use OMC or a similar measure for managed funds, although, the Investment and Financial Services Association (IFSA) had published IFSA Standard No 4.00 relating to the calculation and use of management expense ratios (MER) in MIS. The MER however, excluded some items that were included in the OMC.

It is not entirely clear whether the requirements in section 1013D relating to common funds could be read in a way that created an obligation to uplift costs of underlying investments.

To a greater extent than now applies, disclosure practices under the FSRA were driven by general requirements and duties on product Providers, and the overarching obligation that a PDS should be presented in a “clear, concise and effective” manner.

#### The Ramsay Report and ASIC Report 23

Early in the implementation of the FSRA, ASIC identified the need to do more work regarding the regulation of fee disclosure practices for investment products.

In September 2002, the Ramsay Report was published. The Ramsay Report identified that there were significant variations and inconsistencies in disclosure practices that would inhibit effective comparison: fees were disclosed differently across and within products, terminology was used inconsistently, positioning of fee disclosure in the PDS varied and was fragmented.

Recommendations included:

1. standardised descriptions and definitions of fees in the PDS;
2. the use of a standardised fee template for significant fees, setting out fees and their purpose;
3. separation of disclosure of administration and investment management fees;
4. the development/use of a standardised cost indicator (noting the differences between the OMC used for superannuation and the MER used for MIS at that time);
5. the use of dollar based disclosure (rather than percentages) to the extent possible; and
6. improvement to how cost impacts are disclosed in periodic statement including individualised member calculations or illustration of dollar amounts of fees based on a pre-set investment amount.

During 2003 and 2004, there was much political discussion and debate concerning the regulation of fee and cost disclosure. This included: the disallowance of certain aspects of the Corporations Regulations relating to fee disclosure for superannuation funds, the introduction and debate of regulations concerning the use of dollars, an enquiry and report by the Parliamentary Joint Committee on Corporations and Financial Services on various Corporations Amendment Regulations<sup>80</sup> and ongoing debates between industry bodies concerning a preferred model for fee disclosure.

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<sup>79</sup> Noting however that the OMC requirement was part of the disallowed part of the Corporations Regulations.

<sup>80</sup> Inquiry into the regulations and ASIC policy statements made under the FSRA, tabled 23 October 2002.

Against this background, in August 2003<sup>81</sup> and June 2004,<sup>82</sup> ASIC introduced a good practice model for fee disclosure in the PDS for investment products. This model included many elements recommended in the Ramsay Report including:

1. the use of a Significant Fees Table using three broad headings: (i) Fees when your money moves in or out of the fund, (ii) management costs, (iii) Additional service fees;
2. under management costs, separate disclosure of administration costs and investment costs (noting that investment costs specifically excluded transaction costs);
3. some degree of standardisation of terminology (for common significant fees);
4. the use of dollar-based disclosure where possible; and
5. the inclusion of “Important additional information” which set out a worked example (showing the effect of a range of fees on different investment amounts), transaction costs (such as brokerage and buy-sell spreads), advisor remuneration and how fees could be negotiated.

#### Corporations Amendment Regulation 2005 (No 1) (Cth)

Immediately after the release of ASIC’s final good practice model in June 2004, the government announced its intention to introduce reforms that would give statutory force to many of the elements of the model. The reforms were contained in the *Corporations Amendment Regulation 2005 (No 1) (Cth)* (**Amendment Regulation**). The key elements were:

1. a standardised fees and costs template (incorporating standardised definitions and descriptions);
2. a standardised “Additional explanation of fees and costs”;
3. an illustrative worked example of fees and charges in a balanced investment option; and
4. a standardised consumer advisory warning box.

Regulation 7.9.16J applied the relevant provisions to certain superannuation and MIS products.

The Amendment Regulation also introduced requirements that periodic statements include:

1. a standardised item showing the approximate amount, in dollars, of Management costs that were not paid directly out of a members account (“other management costs”); and
2. an item showing a single dollar amount that includes the total fees that a product holder paid during the period (“Total fees you paid”). This amount did not include transactional and operational costs.

The Amendment Regulation also overcame the problems associated with the differing application of OMC and MER by introducing the concept of an Indirect Cost Ratio (**ICR**)<sup>83</sup> to:

‘provide a consistent methodology for the calculation of “management costs” that were not deducted directly from a member’s or product holder’s account’.

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<sup>81</sup> ASIC Report 23.

<sup>82</sup> ASIC Report 23 at Appendix A.

<sup>83</sup> ICR was used instead of the previously announced Total Expense Ratio to “avoid confusion about the composition of the ratio and any possible misrepresentation to consumers”. See discussion under clause 104 of the Explanatory Statement to Select Legislative Instrument 2005 No. 31.

The ICR feeds into the calculation of “other management costs” in the periodic statement and the illustrative worked example of annual fees and costs in the PDS.

The Amendment Regulation introduced a new Schedule 10, which is the predecessor of the current version (modified as it is by CO 14/1252). A few points worth noting about its original form:

1. both for superannuation and MIS, the definition of Management costs excluded costs that an investor would necessarily incur if the investor invested directly in underlying assets (the focus of fee and cost disclosure was on the additional costs incurred in investing through the superannuation or MIS product);
2. the explanatory statement made it clear that layers of Management costs, including the costs of investing through an “interposed entity” were intended to be captured in Management costs although arguably this was not clear in the drafting (the term interposed entity for example was not mentioned); and
3. the Explanatory Statement made it clear that double counting of fees due to overlap of definitions was intended to be avoided.

#### Shorter PDS regime

For certain types of superannuation products and for a simple MIS (schemes investing predominantly in assets that are easily realisable), a shorter PDS regime applied from June 2010 (subject to transitional arrangements). This shorter PDS regime deals mainly with the length, form and content of the PDS, and variation of certain PDS provisions that apply generally to a financial product PDSs.

The shorter PDS regime did not materially change the manner or form of disclosure of fees and charges excepting that it facilitated greater use of incorporation by reference. Relevant provisions were subsequently amended by the Stronger Super Reforms and the resultant impacts are more fully set out under the description of the current law in Chapter 5.2 above.

Whilst these changes did not materially address how fees and charges are disclosed, it should be observed that these changes arose from ongoing concerns that disclosure practices, even under the enhancements noted above, did not facilitate consumer understanding and product comparability.<sup>84</sup>

#### Stronger Super

Notwithstanding all of the regulatory developments that were designed to enhance fee and cost transparency and comparability noted above, concerns continued to arise about fee disclosure. The Super System Review made several specific observations and recommendations regarding the disclosure of fees and charges for superannuation products. The Super System Review, Final Report observed that:

‘the superannuation system lacks transparency, comparability and accountability in relation to costs, fees and investment returns.’<sup>85</sup>

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<sup>84</sup> The stated intention of the shorter PDS regime in the Explanatory Statement to the Select Legislative Instrument 2010 No. 135 was “the development of the shorter, simpler and more readable PDSs”.

<sup>85</sup> Super System Review, Final Report: Part Two at page 100.

Specifically, relevant to disclosure of fees and charges, the Super System Review, Final Report made the following observations:

- ‘(a) there are not sufficiently strong incentives for trustees to be transparent about the various outcomes: fees, costs, investment returns, and other aspects that are important to members; ...
- (c) outsourcing of many functions has led to an inherent complexity, with fees and charges being incurred at multiple layers;
- (d) a cultural and attitudinal barrier to effective disclosure of costs and fees; a belief that it is only the net investment return that matters, without clarity around risk exposure;
- (e) disclosure requirements (for example, in PDSs have tended to mechanistically reflect existing complexities, which in turn has invited a ‘data dump’ approach to fee disclosure, quite commonly resulting in too many pages of fee disclosure in PDSs); ...
- (g) the language of debate around data and disclosure has been largely captured by those whom it has suited to characterise members as ‘investors’ and the purpose of data disclosure as limited to enabling investor choice of fund or investment option.’

In relation to the ICR (introduced under the Amendment Regulation as noted above), the Super System Review noted that there was a lack of standardisation and consistency in application.<sup>86</sup> The Super System Review Final Report referred to a submission stating that:

‘under current rules, investments could be arranged in such a way that the ICR for many superannuation funds could be legitimately disclosed as zero ...’<sup>87</sup>

Amongst its many recommendations, the Super System Review Final Report recommended that:

1. costs and fees should be disclosed gross of tax;
2. fees should feature in the newly proposed product dashboard through the use of a simple dollar sign graphic; and
3. the adoption of a new ratio called the Total Annual Expense Ratio that captures all the investment and administration expenses of a MySuper product or choice investment option to at least the first non-associated entity level, as calculated according to an outcomes reporting standard.

Following the Super System Review, changes to the fee and cost disclosure regime, mainly affecting superannuation, but also incidentally MIS, were introduced by the *Superannuation Legislation Amendment (Further MySuper and Transparency Measures) Act 2012* (Cth). Detailed requirements about the content and presentation of the information in the MySuper Product Dashboard were set out in the Corporations Regulations, as amended by the *Superannuation Legislation Amendment (MySuper Measures) Regulation 2013* (Cth). A number of key definitions were introduced, or amended, under Schedule 10 to the Corporations Regulations to reflect changes to fee and cost arrangements for superannuation trustees in the SIS Act. Key changes included the introduction of the Investment fees and Administration fees, as well as changes to the Indirect costs concept. The Indirect costs of a superannuation product was used as the basis of the amended definition of ICR for superannuation products. The term Indirect costs was defined as being any amount that a trustee of an entity knows, or reasonably should know, will reduce the return for a member that is not charged to that member as a fee.

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<sup>86</sup> Super System Review, Final Report: Part Two at page 128.

<sup>87</sup> Super System Review, Final Report: Part Two at page 128 referring to submission by ASFA.

The ICR changes were particularly relevant for the purposes of this Review. The 2013 amendments provided that the ICR for a MIS was based on Management costs, and these excluded costs that an investor would necessarily incur if the investor invested directly in underlying assets. The ICR changes under the Stronger Super Reforms adopted an outcomes based test of Indirect costs that looked to any amount that will reduce the return for a member and did not exclude costs that an investor would necessarily incur if the investor invested directly. Whilst achieving the objective of being a more inclusive and comprehensive definition, such a change had the effect of, once again, creating a difference in approach between how the single figure ratio worked for superannuation and MIS products.

The new fee and cost disclosure requirements were scheduled to start on 31 December 2013 for superannuation products and on 1 July 2014 for MIS. By class order, ASIC delayed the start date for superannuation products until 1 July 2014.<sup>88</sup> Any PDS given on or after 1 July 2014 must contain the new fee and cost disclosure for both superannuation and MIS products.

#### Post Stronger Super

In July 2014, ASIC released ASIC Report 398. The report describes how ASIC undertook the review in order to understand the practices used by the financial services industry and to identify any gaps which may lead to underreporting of fees and costs.

ASIC Report 398 made a number of observations about disclosure practices including:

1. inconsistency in the disclosure of Management costs associated with investing funds through external investment structures (e.g. fund-of-fund structures), in that some funds did not look beyond the first layer of fees in the underlying investment vehicle they invested through;
2. failure to fully disclose fees in a range of circumstances, including:
  - a. the underlying manager fees, performance fees and operating expenses of fund-of-funds;
  - b. hedge funds, where strategies are implemented through swap arrangements;
  - c. private equity funds;
  - d. listed property and infrastructure trusts; and
  - e. life companies that declare returns after fees and costs;
3. failure to include fees that were offset against other arrangements such as the use of securities lending revenue or splitting of dividend income;
4. differing practices for reporting of performance fees;
5. inconsistency in the disclosure of tax treatment of fees and costs; and
6. instances of Management costs being treated as Transaction and operational costs.

Following ASIC Report 398, ASIC consulted further with the industry on how to deal with the noted issues of concern. On 8 December 2014, ASIC released CO 14/1252:

‘to clarify the costs that must be disclosed consistently with the intended effect of Schedule 10 to the Regulations.’<sup>89</sup>

<sup>88</sup> ASIC Class Order [CO 13/1534] Deferral of Stronger Super amendments in relation to PDS and periodic statement disclosure.

<sup>89</sup> ASIC Class Order [CO 12/1452] Explanatory Statement.

CO 14/1252 modified Schedule 10 of the Corporations Regulations, including in the following respects:

1. modification of the definition of Indirect costs to:
  - a. clarify that Indirect costs include any amount that directly or indirectly reduces the return on, or value of, income or property attributable to an Interposed vehicle;
  - b. clarify that the costs imposed on vehicles downstream of an Interposed vehicle are included in Indirect costs;
  - c. clarify that Indirect costs includes buy-sell spreads for OTC derivatives (except in relation to managed investment schemes where the derivative is used for hedging); and
  - d. remove any doubt about double counting of Indirect costs by excluding any amount charged to a member as a fee as defined in the SIS Act; and
2. introduced a concept of Interposed vehicle that:
  - a. focussed on bodies, trusts or partnerships carrying on the business of investment in securities or financial products;
  - b. included listed investment companies and quoted and listed MIS, such as index funds that are exchange traded funds;
  - c. did not include a MIS that invests directly in property where the scheme is listed on a prescribed financial market, such as the ASX;
  - d. did not include vehicles that, having regard to the relevant PDS, could be regarded as the investment, rather than the means by which the benefit of investments is obtained (e.g. a property trust investment where the PDS makes it clear that the property trust is the investment, and that the value of the investment depends on how the trust is managed and does not refer to the real properties in a way that could result in the trust being viewed as a means of obtaining exposure to the properties); and
  - e. did not include investment options offered through a Platform type arrangement.<sup>90</sup>

In November 2015, after further industry engagement, ASIC amended CO 14/1252.<sup>91</sup> These amendments included the following:

1. to address concerns about potential double counting,<sup>92</sup> inserted a modified definition of Administration fees and Investment fees (for superannuation products) that allowed Indirect costs not paid out of the superannuation entity to be treated as Indirect costs (rather than fees), where the trustees had elected to do so in writing;
2. substituted the definition of Interposed vehicle to the effect that:
  - a. an entity that has more than 70% of its assets by value invested in securities or other financial products would be treated as an Interposed entity, subject to two exceptions: (a) the 70% does not count certain investments such as listed securities used as a means of investment in real property or an infrastructure entity and (b) the 70% does not count

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<sup>90</sup> Namely those custodial arrangements to which section 1012IA(1) of the Corporations Act apply.

<sup>91</sup> ASIC Corporations (Amendment and Repeal) Instrument 2015/876.

<sup>92</sup> See related discussion under Overlap of fee definitions in Chapter 6.6.

investments that confer control of another entity, unless the second entity has more than 70% of its assets invested in securities or other financial products);

- b. whether an entity was listed was no longer relevant; and
  - c. the PDS test became freestanding;
3. modified how to calculate the costs related to non option derivatives (based on the difference between the return for the derivative over the year and the return on the underlying assets); these costs would form part of Indirect costs; and
  4. clarified the timing relevant for data used in compiling Indirect costs, ICR and Transactional and operational costs.

In December 2016, ASIC made further amendments to CO 14/1252<sup>93</sup> including the following:

1. further modified the definition of Interposed vehicle so that:
  - a. the exception in the 70% test for investments such as listed securities used as a means of investment in real property or an infrastructure entity was changed so that the securities no longer had to be listed to be counted under the test; and
  - b. the PDS test was slightly modified to extend consideration beyond information within the PDS to other information issued as well;
2. modified the definition of Transactional and operational costs to:
  - a. clarify that Transactional and operational costs includes such costs incurred in an Interposed vehicle; and
  - b. remove borrowing costs for a superannuation product (which instead would now be disclosed under the AEFC).

In September 2017, ASIC made further amendments to CO 14/1252<sup>94</sup> including:

1. an option for superannuation trustees, until 30 September 2018, to disclose property operating costs under the AEFC in the PDS rather than as part of Investment fees or Indirect costs;
2. expanded the definition of Indirect costs to include amounts that are paid by persons who are paying returns that are retained by the issuer;
3. further modifying the definition of Interposed vehicle to clarify which entities through which exposure to property is obtained are treated as an Interposed vehicle;
4. clarifying that Transactional and operational costs includes property operating costs and implicit costs; and
5. providing some temporary relief regarding the reporting of borrowing costs, buy-sell spread fee, and property operating costs in periodic statements.

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<sup>93</sup> ASIC Corporations (Amendment) Instrument 2016/1224. A further amendment was made in March 2017 by ASIC Corporations (Amendment and Repeal) Instrument 2017/65 which made only minor drafting corrections.

<sup>94</sup> ASIC Corporations (Amendment) Instrument 2017/664.

Given the commencement of this Review, a further ASIC instrument in December 2017<sup>95</sup> extended by one year, certain temporary relief provided in the September 2017 Instrument.

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<sup>95</sup> ASIC Corporations (Amendment) Instrument 2017/1138.

## 6. Disclosure regime – discussion and recommendations

### 6.1 Methodology and approach

As outlined in Chapter 2, the key considerations that I have been requested to analyse are:

1. the value of the information currently required to be provided in PDSs and periodic statements in relation to fees and costs and the extent to which this assists consumers in making an investment decision;
2. the extent to which the current fee and cost regime results in disclosure which assists consumers (including by contributing to market analysis) in comparing superannuation and MIS products;
3. the practicalities of producing information required for disclosure of fees and costs under RG 97, including the cost of doing so, as well as whether it might lead to decisions adverse for the long-term interests of consumers; and
4. whether the legislative modifications and guidance outlined in RG 97 could be amended to improve clarity and ease of implementation.

The first two considerations, in conjunction, look to the threshold issue of the decisions that consumers make and the extent to which currently provided information about fees and costs supports the decision-making processes of consumers, including any necessary comparison. This focus is consistent with the analysis of policy objectives in Chapter 3. This Chapter looks largely to the statutory disclosure regime and how that regime facilitates decision-making and comparison.

This Chapter reviews the key elements of the disclosure regime and the extent to which they are consistent with the policy objectives set out in Chapter 3. The next Chapter, Chapter 7, considers the substantive, but detail level issue, about the data and information that goes into the key elements of the disclosure regime. There are many sub-issues about what should or should not be included in the fee and cost items and how this affects comparability.

Recommendations are included in the discussion of individual issues where relevant and are also summarised in Chapter 8.

### 6.2 Consumer decisions and the relevance of fees and costs

As set out in Chapter 3, costs matter when making decisions about long-term savings products like superannuation and MIS. Regulatory strategies to manage cost impacts include providing consumers with information that they can use to make more confident and informed decisions. There are multiple types of consumer choices relating to superannuation or MIS products and not all should necessarily have the same regard to cost impacts. Comparative decision-making about financial products is difficult. Fees and costs are only one of a complex set of variables that a consumer wanting to make an objective comparison would have to come to grips with. To facilitate this, disclosure of information about fees and costs needs to be as simple as possible.

### 6.3 How the disclosure regime supports decision-making

Chapter 5.2 identifies the key comparative tools for improving disclosure of fees and costs which are supported by general requirements that a PDS (other than a shorter PDS) must include all relevant information that a retail investor would require to make a decision as to whether or not to invest. The key components of the legislative regime for fee disclosure in Australia are:

1. the four key PDS content requirements (the Fee Template, the AEFC, the Fee Example<sup>96</sup> and the Consumer Advisory Warning<sup>97</sup>); and
2. the fee description/calculation and additional explanation of fees and costs in periodic statements.

These components, whilst all being part of the one disclosure regime serving the same overall objectives, can have slightly different focusses:

1. some are focussed on providing basic information about rights, obligations and the type of financial services product. The Consumer Advisory Warning and the preamble to the Fee Template meet this objective, as supported by other parts of the PDS and educational material;
2. other parts provide forward looking product specific information, whether for understanding rights and obligations (what can be charged), or as the base data for comparison. The Fee Template and the AEFC in the PDS would fall into this category;
3. other parts are focussed on making the task of comparison easier for consumers by providing a shortcut tool. The Fee Example and parts of the Fee Template are directed at this objective, as are comparison tools such as fee calculators; and
4. finally, some elements provide backward-looking information confirming or verifying what was actually charged. This is largely delivered through the fee disclosure in the periodic statement (member level), but also in some of the fund or option level historical information in the AEFC (e.g. transactional and operational costs, borrowing costs).

### 6.4 How PDS-based disclosure assists

The first observation is that, as a consequence of the PDS being a product specific document, it necessarily follows that the PDS-based disclosure regime is less helpful in decision-making about choices that are not product based (e.g. Choices 1, 4 and 7 set out in Chapter 3.2). A consumer who, for instance, wanted to do a comprehensive Provider level cost comparison would have to gather the PDSs for all or a selection of products issued by each Provider and do some data manipulation in order to compare Provider level costs. Possibly by design rather than coincidence, decision-making about choices that are not product based are, based on the analysis in Chapter 3.2, the choices for which cost impacts are less relevant.

The converse of this observation is that a PDS-based disclosure regime is of most assistance when making a comparison between investment options in a product and also, to a lesser extent, when comparing similar investment options in different funds/schemes. Again, perhaps as a matter of design rather than co-incidence, this is the right outcome: better cost disclosure is available for those decisions where costs are a more important comparison point.

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<sup>96</sup> The Fee Example figure is also used in the MySuper Product Dashboard.

<sup>97</sup> Required under Division 7 of Schedule 10.

An important principle level limitation on using the PDS as the basis for decision-making is that the PDS is, by design, primarily a point-of-sale document focussed on the entry level decision. It is somewhat less helpful for ongoing decision-making during the life of a holding in a fund.

A more practical limitation of a PDS-based cost disclosure regime is that, even for the most relevant types of choices, comparison is a laborious and time-consuming exercise. Taking Choice 6 in Chapter 3.2 as an example, a consumer wanting to find the costs of Australian equities investment options across superannuation funds, would firstly have to somehow identify which funds offer such an investment option, then obtain the PDS for those funds, then physically find the Fee Template information, Fee Example and AEFC (noting that for most funds, fee details about an Australian equities option will not be in the PDS but incorporated by reference from another document), then somehow record and compare the data for available investment choices. This process is made more challenging by the data and layout comparability challenges discussed further below, and the unavailability of Fee Examples for the majority of investment options (an Australian equities investment option, for example, would almost never appear in the Fee Example). In sum, this would be seen by most consumers as a time inefficient process, which they would likely shortcut or avoid. Advisors would often have access to some facility that makes the comparison task somewhat simpler.

In the MySuper context, cost information is simplified and combined with information about other relevant factors (risk and past returns) in the MySuper Product Dashboard. Legislation extending these requirements to all choice products is already in place although currently deferred until 1 July 2019. Even when these are available for all choice products, making use of them will still require significant manual effort by a consumer if a broad cross-product search is being undertaken.

Given the complexity of the task and the various limitations to the PDS disclosure tools discussed below, consumer decision-making needs to be better supported.

**Comparison Facilities:** One direction to consider is whether technology can be used to do some of the work for a consumer who wants to make a comparison. One possibility is the development of a web-based comparison facility that can bring data for many products and investment options into a single point. In some jurisdictions,<sup>98</sup> a supervisor or other government agency provides an online public facility that collects cost data from Providers and presents this in a format that makes comparison much easier. Often, these facilities are searchable and can be ranked or sorted by different criteria. Disclosure documentation and education material then signposts this resource for consumers.

In Australia, there are numerous commercial information providers who have developed databases that provide some of this functionality. Most are not publicly available and for various reasons might not be ideal for public comparison purposes. The content and presentation of the commercial providers is naturally focussed on the needs of customers they are seeking to market their product to. The existence of these facilities does however indicate that it is technically possible to obtain, update, store and disseminate such data in a manner that can be used to simplify the comparison task.

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<sup>98</sup> See international references in Chapter 4 above.

It is noted that in 2014 the Financial System Inquiry also posed as a policy option that consideration be given to placing:

‘more reliance on making financial product and service information more accessible to consumers, including information brought together by third-party providers through online tools and comparators.’<sup>99</sup>

The Productivity Commission draft report also suggested the use of online facilities to bring together product dashboards for all superannuation investment options<sup>100</sup> and to support the proposed “Best in show” default selection process.<sup>101</sup>

APRA fills some of the gap in the *Annual Fund-level Superannuation Statistics* report which contains amongst other data, entity level fee information for APRA-regulated superannuation funds with more than four members and eligible rollover funds, as well as profile and structure information for the trustees of these superannuation funds. Unfortunately for current purposes, this data does not extend, at the moment, to product or investment option level.

A database that is centrally provided by an agency such as a public body or an agent of a public body (for example such as ASIC’s MoneySmart website) would be preferred. Such a facility would be available to all members of the public, would provide the type of data and form of data agreed by consensus to be preferred comparison points and would likely have more credibility as an authoritative source of information than a commercially provided facility. A centrally provided facility would also overcome natural discomfort about educational material or PDSs sign-posting to a commercial database.

No doubt many issues would need to be worked through such as functionality, the breadth and categorisation of products covered, which fee and costs elements should be the focus, the extent to which data other than fees and costs should be included, data management, data input method, data integrity, ownership, maintenance, costs, liability and content limits. Broad stakeholder engagement would be required, and consumer testing may be considered necessary.

**Including Averages in PDSs:** Another possibility is to provide some context around data. When looking at any individual Fee Template or Fee Example it is impossible for a consumer to form a view whether the disclosed fees are high or low without some relative information for context. Comparison to other PDSs is best, but as noted above, this is a laborious process, perhaps even if supported by some comparison facility. Including within the PDS disclosure, information about relevant industry averages would help consumers come to a quicker view about the reasonableness of figures. As an example, the Fee Example could include a brief statement after the “Cost of Product” line showing the average figure for similar types of products. This would be a quite powerful disclosure tool that could materially assist the comparison process. Benchmarking in this manner is adopted, for example, for Dutch pension funds (see Case study 5 in Chapter 4.2).

Such a comparison indicator would be most useful where the “type” categorisation is as narrow as possible (given product diversity there would be little point in showing an average figure for all superannuation investment options or all MIS). Consistent and meaningful categorisation

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<sup>99</sup> Financial System Inquiry, Interim Report July 2014, Chapter 6 Consumer Outcomes.

<sup>100</sup> Productivity Commission 2018, Draft Recommendations 9 and 10 at page 61.

<sup>101</sup> Productivity Commission 2018, Draft Recommendations 1 and 2 at page 58.

would be one of the challenges with such an approach. Data collection, analysis, distribution and timing would also present challenges to work through.

**[Recommendation 1]** I recommend that ASIC undertake a feasibility study into whether it, or another government agency could provide, or sponsor, the development of:

1. a publicly accessible, consumer facing facility providing fee and cost information extracted from PDSs that can be searched and compared on a range of criteria; and/or
2. data about average “Cost of Product” figures for specific investment option types that can be included as a reference figure in Fee Examples in the manner suggested above.

I acknowledge that a decision to provide either would not be an open and shut case, given the need to balance the utility of such a facility against the effort and cost involved in providing this for the benefit of the perhaps narrow segment of consumers who do, or would, actively make their own investment decisions.

Whilst there is a natural alignment between PDS-based cost disclosure and the types of decisions that rely more on good cost disclosure, consumers would also be assisted in making Provider or product level comparisons if aggregated data were available at that level. This issue is rather more complex and of lower level importance however, depending on how a public comparison facility as recommended above could be structured, it might be possible for such a facility to do some amount of Provider level, or product level aggregation and/or averaging of cost data. At least some of this data could be based on existing APRA data collection processes.

**[Recommendation 2]** I recommend that the feasibility study referred to in the preceding recommendation also consider whether aggregated product or Provider level cost data can be provided, outside of PDSs to support consumers who make Provider or product level choices.

## 6.5 Are the elements the right ones?

A next question is, accepting that PDS based disclosure is the starting parameter, whether the Fee Template, the AEFC and the Fee Example in the PDS are the best ways of assisting consumers in making comparative decisions.

As set out in Chapter 5.3 of this Report, the Fee Template, the AEFC and the Fee Example in the PDS are the outcome of a long and well considered development process. The Fee Template is intended to provide an “at-a-glance” view of the most common and significant types of fees and costs. As noted above however, the Fee Template serves multiple purposes: partly educational, partly base data and partly comparison tool. The Fee Example is the tool that converts the, still largely text based, Fee Template into a single dollar figure which is, in principle, a simplified basis for comparison. More detailed information about fees and costs is then left for the AEFC.

As demonstrated in Chapter 4, these three elements are consistent with international thinking and development about how to present cost information to consumers, although there would be scope for debate as to whether the simplicity of a single dollar figure outweighs the benefit of segregation of different types of figures (e.g. transaction costs). As suggested above, the only other element that could be identified from international reference points, would be a public facility that brings the data of different products into one place and/or the inclusion of relevant benchmark figures for context.

## 6.6 Effectiveness of the Fee Template

This Chapter does not look to the data underlying the Fee Template but the format and layout of the Fee Template. For recommendations and observations about data refer to Chapter 7.

The Fee Template and the Fee Example sit at the heart of fee and cost comparison. These two tools need to be considered in conjunction.

The development history is set out in Chapter 5.3. Essentially the Fee Template is intended to be an at-a-glance summary of significant fees; the place to go to for a quick understanding. The Explanatory Statement to the Amendment Regulation that introduced the Fee Template indicates that the objective of the Fee Template was to improve comparability across products.<sup>102</sup> At the outset it should be acknowledged that the current Fee Template is a substantial improvement to the way that fees and costs were disclosed before 2005 in terms of consistency of layout, terminology and readability. The Fee Template makes it much easier for consumers and their advisors to find and understand information about fees and costs.

As a summary, the Fee Template necessarily represents a compromise at different levels. Most obviously, to keep the template short there is a necessary compromise between detail and simplicity. The layout also reflects judgements about what attributes of the fee and cost items are considered to be the most important for most readers: should it be presented by the types of fee or cost, sequentially by when they are incurred or separated by how they are paid? Currently, the superannuation Fee Template sets items out by types of fee although they are not well grouped by type. Grouping by type has advantages, however, as a consequence there is little apparent relationship between the Fee Template and the way that fees and costs are described in periodic statements<sup>103</sup> (where they are set out according to how they are paid: either out of the account or out of “your investment”, as “Indirect costs” or “other fees”). Inevitably, judgements about how to simplify and what is, for most readers, the best format, means that individual needs are often not best accommodated. Nevertheless, these are compromises necessary in improving readability and consistency for general purposes.

### Fee Templates are difficult to compare

Whilst Fee Templates have improved readability and consistency compared to pre-2005 disclosure, it is difficult to be confident that they provide consumers with a usable basis for simple comparison of information about fees and costs. Because of the complexity of the comparison task (noting that fees are just one of multiple variables and their relevance varies decision-to-decision), the effort involved, and the cognitive limitations of many consumers, fee information would need to be presented in a manner that is unqualified, simple and directly comparable to be usable by consumers. At the principle level, a Fee Template/Fee Example could best assist consumers if it produced a single figure. Given pre-existing consumer research supporting the dollar-based disclosure changes,<sup>104</sup> a single dollar figure would be the ultimate simplified comparison tool. Failing that, a single percentage-based figure would be the next most simple. Consumer usability becomes progressively more compromised the further data moves from these points of simplicity. Requiring the consumer to add multiple dollar figures presents

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<sup>102</sup> Explanatory Statement, Amendment Regulation (Select Legislative Instrument 2005 No.31) at page 2 and page 9 “the fee template that simplifies the disclosure of fees and costs and allows for more effective comparison across products” at page 10, “The simple table format allows for more effective comparison between like products”.

<sup>103</sup> See Chapter 6.9 for details.

<sup>104</sup> See also the references in the FCA Asset Management Market Study Interim Report at page 59.

challenges; the addition of multiple percentage figures creates more challenges; the addition of a percentage figure to a dollar figure starts to create serious comprehension challenges. Add to this, other variables (such as conditionality, different calculation bases, ranges, textual information, discounts or qualifications, different fee items) and it becomes unlikely that even a financially sophisticated consumer will be able to cross compare two otherwise identical options, let alone a universe of potential choices.

Unfortunately, there are many aspects about the way that Fee Templates are presented in practice that limits their use in effective comparison across products or Providers. A review of PDS Fee Templates of different products identifies many differences in approach that makes comparison across products or Providers extremely challenging. Some examples are set out below (actual examples are included in italics in quotation marks):

### **Superannuation funds**

1. some amounts are dollar based, some are percentage based, and some rely on textual description;
2. some amounts are expressed as a range rather than a single figure: “*administration fee up to 0.65%*”, “*Investment Fee 0.04% - 4.66% for other investment options*”;
3. different fee items are relevant: different items are shown as nil in different Fee Templates not just for transaction/activity fees but also Administration fees, Investment fees and ICR in some cases;
4. many items are expressed as an estimate, some in ranges; “*buy-sell spread estimated at 0.36%*”, “*estimated performance-related fees of 0.03 to 0.04%*”, “*Buy-sell spread estimated to be between 0.10% and 0.12%*”;
5. quite often items are compound: ICR, for example can include multiple elements such as “*Regulatory Change Expense Recovery*”, “*estimated performance related fees*”, “*other indirect costs*”, “*external fixed investment costs*”, “*trustee related costs*”;
6. quite often compound figures include a dollar-based amount and a percentage based amount “*administration fee 0.45% pa of your account balance plus \$6.50 per month*”, “*0.50% plus \$8.80 per month*”, “*\$97 per annum plus 0.41% of your account balance*”;
7. dollar based amounts can be expressed as a weekly, monthly or annual figure;
8. qualification by capping, the calculation method of which can vary: “*if administration fee exceeds \$1,000 in a financial year, you’ll get a refund of any amount you pay over the cap*”, “*Administration fee capped at \$2,500 p.a. plus an ORFR fee estimated at between 0.03-0.14% p.a.*”;
9. qualifications on nil amounts: “*Buy-sell spread – Nil however a transaction cost allowance will apply*”;
10. other qualifications: “*Up to 0.65% pa of your account balance less any applicable administration fee discounts*”;
11. some items, such as performance fees or performance-related fees require extensive textual explanation of the circumstances in which they apply;

12. some PDSs refer to fee discounts or rebates that do not need to be negotiated (not applicable to MySuper products), which are commonly related to account balance and vary from fund to fund;
13. applicable employer discounts are typically not disclosed in PDSs;
14. diversity in other, generally activity-based, fees: some examples “*Family Law information request*”, “*Family Law split fee*”, “*valuation fee*”, “*lost member search fee*”, “*contribution refund fee*”, “*No-TFN tax recovery fee*”, “*dishonoured payment fee*”; and
15. not infrequently, mixed messages about the disclosed information such as comments that the quoted fees should not be relied upon “*Investment fees may vary from year to year and cannot be precisely calculated in advance. Past costs are not a reliable indicator of future costs*”, “*Past costs are not a reliable indicator of future costs. Future costs may differ*”, “*a fund displaying high investment and operational fees and costs doesn’t necessarily charge members higher fees*”.

**Managed investment schemes:** being more diverse, MIS show even more variation in expression. In addition to many of the same points above, MIS PDSs include the following variations:

1. fees calculated by reference to factors other than contributions or NAV (gross asset value is often used in property funds): “*ongoing management fee of 7% of the net rental received by the Fund*”, “*fund management fee of 0.6% pa of the fund’s gross assets*”;
2. fees that vary depending on information or events that might not, in some cases, be readily ascertainable: “*Management Fee equal to: a. 0.65% per annum for so long as the GAV is up to \$750 million; and b. for so long as the GAV is more than \$750 million, the aggregate of: i. 0.65% per annum of \$750 million; and ii. 0.60% per annum by which GAV exceeds \$750 million*”;
3. numerous sector or asset specific fees or costs some of which are a fixed amount: “*Capital Works Fee to manage capital works. Equal to 5% of the value of all capital works undertaken by the Fund*”, “*Acquisition fee – \$350,000*”, “*Acquisition fee of up to 2.0% of the gross value of the asset*”, “*Equity Raising fee – \$320,000*”;
4. different interpretations of the requirement<sup>105</sup> to list components of a cost separately (even where for example the components are all percentage based and could be added together): “*Management costs include a management fee of 0.86%, recoverable expenses estimated to be 0.12%, estimated indirect costs of 0.00%*”;
5. for property or mortgage funds a variety of costs not paid by the member or out of the fund such as fees or costs paid by the borrower: “*loan application fee*”, “*loan administration fee*”, “*early repayment fee*”;
6. greater use of performance fees expressed as a formula: “*Performance fee of 20.5% (inclusive of the net effect of GST) of any returns in excess of an 8% Hurdle Rate*”; and
7. non-alignment of Fee Template and Fee Example: examples were noted where the Management costs in the Fee Template were different to the Management costs used in the Fee Example because the management fee had been reduced.

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<sup>105</sup> Clause 204(6) of Schedule 10.

**Platforms** can be either superannuation funds or MIS, however, because of their structure and regulatory arrangements, their Fee Template disclosure is quite different. General challenges associated with fee disclosure for Platforms is discussed below in Chapter 6.10, but for current purposes some of the differences in Fee Template expression are also noted:

1. they will usually have tiered administration fees;
2. often the tiered administration fees can be aggregated with other types of accounts or family members;
3. administration fees will often have a cap;
4. administration fees will occasionally have a minimum;
5. Indirect costs are often disclosed as nil (i.e. the Platform arrangement itself has no indirect costs) or as a range showing the investment costs of underlying MIS “*Estimated to be 0-6.23%*”, “*Estimated to be 0% - 7.59% p.a.*”;
6. special fee arrangements for cash held in the account; and
7. lengthy list of “other fees” (which in some PDSs are set out under the additional information rather than in the Fee Template) including brokerage, offline transaction fees, non-advised client fee, IPO fee, managed account transaction fee, non-accessible investment fee, negative cash account fee.

The differences commented on above are not intended as a criticism of the practice in all cases nor do they necessarily raise compliance concerns. The diversity in expression is in large part reflective of differences across a range of parameters such as product structure, business models, asset class, charging methodology, etc. There is also a natural, and to some extent unavoidable tension between showing a summary and drafting the Fee Template so that it accurately reflects the basis on which fees and costs can be deducted or levied in the particular product.

The point being made is simply that, as a consequence of this diversity, product-to-product comparison based on Fee Templates is very compromised. It is particularly difficult to make any relative cost assessment as between Platforms and superannuation funds or MIS.

This conclusion might suggest that Fee Templates are not able to deliver on the objective of comparability and should be re-considered as a tool. Practically however, there is no real alternative. Whilst Fee Templates might be a quite imperfect comparison tool, as shown in Chapter 4, they are still one of the primary regulatory strategies currently adopted internationally. Further, although the Fee Template does not provide a simple comparison point, it serves other purposes such as providing the base level information about fees and costs. This information is important in setting out in a comprehensible manner, what can be charged and, even if not a comparison basis in itself, the Fee Template provides data on which other more focussed comparison tools can be based.

If the ambition were to use the Fee Template as the primary basis for cross-product comparison, this issue would have to be addressed by regulating and simplifying fee charging mechanisms in all products (beyond even that done already for MySuper products). Whilst this approach might work in some jurisdictions, it would be difficult to make this work in Australia given the high degree of diversity across products and charging structures. Looking forward, there might be some scope for the “Best in show” default selection process outlined in the recent Productivity

Commission draft report<sup>106</sup> to require alignment of fee charging structures by including this within the relevant selection criteria.

The comparison challenge needs to be, in part, addressed by other disclosure tools discussed elsewhere in this Report. Nevertheless, to enhance the role that the Fee Template can play in comparison to the extent possible, suggestions are made below on simplifying the format.

**[Recommendation 3]** I recommend that ASIC work with industry to improve consistency in the way that fee information is set out in Fee Templates. It may be possible to develop industry standards or best practice statements that can deliver improved levels of consistency. If not ASIC may need to impose some regulatory requirements.

Many examples identified above could not be aligned, but there are some areas where greater consistency should be achievable in a way that can further assist comparability (e.g. dollar-based fees be expressed as an annual amount, compound figures be reduced to a single figure where possible, standardised sequencing and greater consistency about what types of fees appear in the Fee Template versus the AEFC).

#### Fee Templates can be difficult to find

A more basic challenge for the diligent consumer comes in finding Fee Template information, particularly for non-default investment options. Under the simplified disclosure regime, the Fee Template is only required to include one investment option (typically for superannuation, the MySuper option). Fee Template information for other options is required, but is usually incorporated by reference. In many instances, the only differences relate to investment costs in either Investment fees or ICR (for superannuation). Usually, Administration fees and other transaction or activity related fees do not vary between investment choices.

In some PDSs, the Fee Template sets out the information for all options because they are the same; for others, the fees for other investment options which vary, are also set out in the one Fee Template. More often, some or all fee information relating to other investment options are contained in another document that is incorporated by reference.

There is much diversity in practice in the way that information is presented in documents incorporated by reference. In some cases, the incorporated document refers to yet another document (e.g. periodic updates of investment fees for options). Sometimes information about required fee items is presented in a format that looks like a Fee Template but often it is not. In some documents, the fee information for different options is presented in one place, in others it is spread out under other information about each option. In some PDSs, the fee information for investment options is contained within the AEFC. On occasions, a difference was observed between ICR figures in the PDS and other incorporated documents, possibly explainable by timing differences. In some PDSs, there is no reference to incorporated information in the fee section itself (although that additional information may be incorporated by reference through a cross reference elsewhere in the PDS).

Depending on exactly what choice the consumer is considering, it can require some effort to even find the relevant document/s and find where in those documents the relevant information is located, whether in hard copy or electronic form.

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<sup>106</sup> Productivity Commission 2018 Draft Recommendations 1-3 at page 58-59.

**[Recommendation 4]** I recommend that ASIC work with industry to improve consistency in the way that fee information is incorporated by reference particularly as regards cross referencing in the Fee Template, location and format of presentation. As there may be multiple acceptable methods, this issue might not warrant regulatory control. It may be possible to develop industry standards or best practice statements that can deliver improved levels of consistency of practice.

At a minimum, the Fee Template of PDS issued under the shorter PDS regime should contain, at a standardised place or places, reference to the location of:

1. any other parts of the Fee Template or additional explanation (e.g. details about transactional costs or borrowing costs); and
2. fee information about investment options.

For electronic documents hyperlinks to incorporated information should be provided.

#### Differences between superannuation and MIS

Another limitation in using the Fee Template for comparison is the various differences, both as to layout and underlying data, between superannuation and MIS.

As noted under Historical Development in Chapter 5.3 above, the Fee Templates have changed over time. The layout of Fee Templates under the original ASIC best practice models and the Amendment Regulation were essentially the same for MIS and superannuation products. Partly due to changes in relevant definitions, the Fee Templates for superannuation products were changed under the Stronger Super Reforms in 2013. The major difference being the splitting of Management costs into three components: Administration fees, Investment fees and ICR. Not only did the layout change but because of definitional changes, the three fee components for superannuation included amounts not captured as Management costs for MIS.<sup>107</sup>

Clearly, these changes to Fee Templates make comparison across MIS and superannuation funds more difficult. As expanded on above in Chapter 3.2, there would be circumstances when such a comparison is made, and cost comparison becomes a relevant comparison point. Unfortunately, the changes to layout and data content make it almost impossible for consumers, or their advisors, to make this type of cost comparison.

There are also other negative practical consequences of the difference in approach between MIS and superannuation, such as the complications that arise where a superannuation fund invests into a MIS directly or indirectly. If the MIS is an Interposed vehicle as defined, then the superannuation type fees and costs of the MIS need to be included as Indirect costs for the superannuation fund disclosure. The PDS disclosure by the MIS will however be presented according to the content required for MIS. Industry have worked co-operatively to work around this problem, but industry members have advised me that it remains a serious and costly practical issue. Superannuation Platform Providers say that they are unable to present fee and cost information of accessible MIS products in accordance with superannuation level requirements in many instances (although noting that a reasonable estimate could be used in such cases). Even where they are able to do so, this raises inevitable differences between the primary fee disclosure which is provided in the MIS PDS and the adjusted superannuation-like figures provided elsewhere.

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<sup>107</sup> For details see Diagram 5-2 above.

There are also some overlaps between ICR and Investment fees (explained in more detail directly below) that also support the case for some revision to the layout of the fee components for superannuation products.

Whilst the layout and definitional changes affecting superannuation were a matter of government policy implemented by the Stronger Super Reforms, comparison will be facilitated materially if the differences (both as to layout and data content) between MIS and superannuation funds can be reduced or eliminated.

**[Recommendation 5]** I recommend that when making future changes to layout of the disclosure tools or the underlying data, including how and whether to implement other recommendations set out in this Report, ASIC should keep in view the subsidiary objective of reducing or eliminating the differences between fee and cost disclosure appearing in PDSs for MIS and superannuation products.

There will be some challenges in aligning data content; on the current understanding of the law, amounts included as fees and costs for MIS would need to be expanded or alternatively, amounts included as fees and costs for superannuation products would need to be reduced, however the scale of necessary realignment could be considered further once other recommendations in Chapter 7 of this Report relating to data content have been further considered and developed. The gap between the two might not ultimately be as wide as currently is the case. Depending on the resultant size of the gap, a solution might be within the scope of ASIC's modification powers, however this would be a matter for ASIC to consider.

#### Presentation issues

Industry representatives have raised a number of concerns about Fee Template presentation including the following:

1. the terminology confusion between “fees” and “costs”; the legal definitions in Schedule 10 “costs” and “fees” interchangeably and this flows through to the Fee Template for superannuation products. Items that are set out as fees (such as Administration fees and Investment fees) actually contain amounts commonly understood to be costs, and the ICR will often include amounts commonly understood to be fees. Whilst this is technically in order, it has been suggested that this mixing of concepts causes confusion to consumers. This point is addressed in recommended changes to the layout of Fee Templates below; and
2. some items are “double disclosed”; most amounts of Transactional and operational costs form part of Indirect costs (or potentially form part of Investment fees)<sup>108</sup> for superannuation products. These items are also set out in more detail in the AEFC. It has been suggested that some consumers and advisors are confused by this and have been adding the amounts appearing as Transactional and operational costs in the AEFC to amounts already disclosed in the Fee Template (which already include most of these amounts). It has been suggested that in some cases advisors are not confused but use the overlap selectively as a way of justifying a recommendation to move to another product. This point is addressed under the recommendations and observations in Chapter 7 about how the disclosure of Transactional and operational costs might be addressed more broadly.

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<sup>108</sup> There are minor exceptions for a cost that is a cost of the asset (e.g. implicit costs in acquisition), see note to the definition of investment fee in clause 209A of Schedule 10.

To these points I would add the following observations about Fee Template presentation:

1. the layout of the 8 line items of different fees in the superannuation Fee Template must raise questions in the minds of consumers about what to do with such information. Some may be tempted to try to add up all the items, which would be an unsound approach, given that some are ongoing and some are only incurred if a relevant transaction or activity is initiated. At the very least, grouping, or potentially aggregating the ongoing elements (Administration fees, Investment fees and Indirect costs) would be a better approach. The MIS Fee Template does a slightly better job of separating transaction/activity dependent fees and costs from ongoing fees and costs (which are aggregated as a single figure), although this too could be improved;

**[Recommendation 6]** I recommend that the superannuation Fee Template in clause 201 of Schedule 10 be modified to group together those fee and cost items that are ongoing separately from those that are dependent on member-initiated transactions or activities.

2. the inclusion of ICR as a line item in the superannuation Fee Template is also likely to confuse. Each of the other line items is expressed as a fee or cost, yet at the bottom of the list in the Fee Template an important item called a ratio is included. Consumers must be challenged with what to do with this ratio vis-à-vis the fees and costs set out above it; should it and can it be added to those items, does it include those items? If ultimately retained as a separate line item (see discussion under Overlap of Fee Definitions directly below) it would be simpler to refer to Indirect costs (rather than indirect cost ratio) in the Fee Template. Division 3 of Schedule 10 could still set out the mathematical method in determining what percentage figure to include as Indirect costs;

**[Recommendation 7]** I recommend that, if the line “Indirect cost ratio” is retained as a separate line item in the superannuation Fee Template, that the description of the line in clause 201 of Schedule 10 be modified to “Indirect costs”.

3. the line for “Advice fees” in the superannuation Fee Template includes additional text “relating to all members investing in a particular MySuper product or investment option”. As explained in RG 97.177, this item relates to costs paid out of a superannuation fund for what is generally referred to as “intra-fund advice” as opposed to individual advice fees (which would be included under “Other fees and costs”). Notwithstanding the explanation in RG 97, the meaning of this text would be unclear to a casual reader. It is also noted that the additional text referred to (which seeks to explain the nature of the item) gives undue prominence to the item vis-à-vis other fee items. I also note that some PDS include the additional text, but many do not, which would create some confusion between this item and any fees for individual advice fees. For all but one PDS that I reviewed, the amount for Advice fees was nil. Given the potential for confusion that the line item creates, the diversity of practice and the undue prominence for an item that is almost always nil, there is a strong case for deleting the item from the Fee Template which is intended to only include significant fee items. For the apparently limited number of funds where this amount is not nil, it would aid simplification of the Fee Template if the amount were incorporated within Administration fees;

**[Recommendation 8]** I recommend that the line item for “Advice fees” in the Fee Template for superannuation products be removed. Where the amount is not nil, the amount can be incorporated into the line Administration fees.

4. the sequencing of the MIS Fee Template arguably focusses on the wrong elements. In most MIS PDSs reviewed, all of the first 4 lines (Establishment fee, Contribution fee, Withdrawal fee and Exit fee) are nil. The most relevant fee is Management costs which appears towards the bottom of the Fee Template. As is the case for the superannuation Fee Template, it would be better if the more relevant, ongoing, fee items appeared first;

**[Recommendation 9]** I recommend that the MIS Fee Templates in clauses 202 and 202A of Schedule 10 be modified to place “Management costs” at the top of the template.

5. unlike the superannuation Fee Template, the Fee Templates for MIS in clauses 202 and 202A of Schedule 10 do not include a line for “Buy-sell spread”. Where it applies, this can be an important fee when considering some decisions. If a buy-sell spread applies, clause 209(j) of Schedule 10 requires that it be disclosed in the AEFC. Buy sell spread is commonly disclosed in MIS PDSs and appears to be at least as significant as “Contribution fee” and “Establishment fee” which are more commonly disclosed as “nil”. Both because of its significance and to further align disclosure between MIS and superannuation products, buy-sell spread should be included in the Fee Template for MIS.

**[Recommendation 10]** I recommend that the MIS Fee Templates in clauses 202 and 202A of Schedule 10 be modified to include a line for “Buy-sell spread”.

#### Overlap of fee definitions

An issue related to the presentation points noted above, that was raised repeatedly by industry, relates to the overlap of the definitions for Indirect costs in clause 101A of Schedule 10 and Investment fees in clause 209A of Schedule 10. Both items currently appear in the Fee Template for superannuation products.<sup>109</sup> This issue is not relevant to current MIS disclosure.

The starting problem was that the definition of Investment fees, in its enacted form which cross refers to section 29V(3) of the SIS Act, is potentially very broad, including as it does, all costs that relate to the investment of assets of the superannuation entity. This potentially includes costs incurred within underlying investment structures. Both cost and fee elements captured by the definition might also be captured by the broad definition of Indirect costs. This created a potential obligation to disclose the same amounts under each item and created uncertainty about how to deal with the overlap. ASIC responded by modifying the definitions in Schedule 10 to the effect that they are mutually exclusive. Part of the modification of the definition of Investment fees<sup>110</sup> allows the trustee to elect to treat amounts (not paid out of the superannuation entity) as Indirect costs. The definition of Indirect costs<sup>111</sup> in turn excludes, inter alia, Investment fees. The consequence of this drafting is that an amount should only fall within Investment fees or Indirect costs (as extended where relevant by the trustee election).

The modifications have overcome any double disclosure/counting concerns and clarified how trustees may act, however the discretion to treat amounts as Indirect costs has led to different practices across superannuation products. Comments were made during the Review that some

<sup>109</sup> Although not raised by industry it is noted that similar points could possibly apply in relation to Administration fee subject to whether practically, any Administration fees are categorised as Indirect costs. To the extent that this is the case then the discussion below would apply to the Administration fee as well.

<sup>110</sup> Sub-clause (b)(ii) of the definition of Investment fees in clause 209A of Schedule 10.

<sup>111</sup> Clause 101A(1)(c) of Schedule 10.

trustees were motivated to move as much as possible into Indirect costs as some consumers and analysts were more focussed on Investment fees.

Technically, it does not matter whether an amount is treated as Investment fees or Indirect costs as one offsets the other and does not affect the total amount of fees and costs disclosed in the Fee Template, nor the amount shown in the Fee Example. However, many comments were received that the difference is important because consumers or their advisors might focus on one figure in isolation and because trustees can cherry-pick information in marketing strategies (an example was provided to me of a superannuation product being advertised on the basis of having low Investment fees rather than by reference to the total of Investment fees plus Indirect costs). At the very least, it has to be acknowledged that different treatment of the amounts between products can make the information harder for consumers to understand or reconcile.

The current arrangements effectively illustrate that there is little point in drawing any distinction between Investment fees and Indirect costs. Given the cross over in meaning and the consequential discretion for trustees to shift amounts between the two, only the total figure has any real meaning. Even if an effective demarcation can be developed by appropriate drafting, it is unlikely to serve any real purpose as the difference between the two items will likely, in any event, reflect structural differences rather than fee or cost differences. The two items could best be disclosed as a single item in the Fee Template under the heading “Investment Fees and Costs”.

During consultation, some industry participants expressed a preference for keeping the distinction because it can serve to highlight whether the related amounts are paid to a trustee or some other party. Whilst on balance I do not support this view in general, it should be acceptable if the Fee Template disclosure additionally breaks out the single figure to explain the components in situations where a Provider considers that this is meaningful to consumers.

**[Recommendation 11]** I recommend that, for superannuation products, the distinction between Investment fees and Indirect costs be removed from the Fee Template by merging the two items into a single line item in the Fee Template titled “Investment Fees and Costs”.

The drafting approach to be adopted would require further consideration by ASIC and discussion with affected industry. Depending on the approach adopted amendments might not be needed to the definitions of Indirect costs and Investment fees but merely to how they are presented in the Fee Template (clause 201 and Division 3 of Schedule 10) and the Fee Example ((Divisions 5 and 6 of Schedule 10). To the extent that any Administration fees are incurred indirectly (in accordance with section 101A of Schedule 10) then similar consequential changes would be required.

#### Segregation of fee elements

Related to the above, is the issue of whether it is preferable to provide consumers with a single figure that aggregates data about various types of cost impacts or whether it is better to segregate data elements in a manner that supports more granular decision making.

There are some benefits in separation for information purposes, particularly where different pieces of information (e.g. Administration costs, Investment costs and transaction costs) support different types of decisions (see the discussion under Chapter 3.2 above).

There is, however, a question whether the separation of Administration fee from “Investment fees and costs” for superannuation products is of benefit. Whilst supporting more granular decision-making, separation does not facilitate comparison if it requires the consumer to add two fee items together, in a manner they find challenging (this might particularly be the case where one is percentage-based and the other partly dollar-based). This added challenge for consumers can be justified where separation gives consumers extra information that is valuable in the context of the decisions that they make.

In the superannuation context, aggregating Administration fees and Investment fees has the advantage of better aligning disclosure of superannuation products and MIS. Separating the Administration fee arguably does not help in choice of superannuation fund because administration services can only be “purchased” as part of an investment option along with the investment fees and costs. This might suggest that there may be no net benefit in separately disclosing Administration fees and Investment fees within a comparative tool like the Fee Template.

When consulted on this specific point, most respondents were of the view that the benefits of separating these two items outweighs the benefits of combining them. Administration fees might (as noted under Choice 1 in “Relevance of cost impacts” in Chapter 3.2) arguably have special relevance for some types of decisions. Accordingly, proposals below proceed on that basis, however if other elements of Fee Template presentation are to be consumer tested at some point, it would be helpful to also test consumer response to merging Administration fees with Investment fees.

**[Recommendation 12]** I recommend that if other elements of Fee Template presentation are to be consumer tested, consumer response to merging Administration fees with Investment fees (or “Investment Fees and Costs” as proposed in Recommendation 11) also be tested as an input into further consideration of whether the two line items should be merged.

The balance between segregation and aggregation also arises in other contexts discussed later in this Report: subject to how transaction costs are disclosed (see discussion in Chapter 7), a question arises as to whether they should be disclosed separately or whether they should be disclosed as a part of investment costs. A similar question could arise regarding performance fees given their volatility and unpredictability (see discussion in Chapter 7.7).

#### Fee Templates modification

The recommendations above suggest several possible changes to the Fee Templates in Part 2 of Schedule 10. If the layout and structure of the Fee Templates are to be reviewed generally, then it may be appropriate that there be consumer testing to identify the preferred direction, particularly in relation to Recommendations 6 to 10. As such, it is not appropriate for this Report to make untested recommendations, nevertheless, for the purpose of proposing a layout worth consumer testing, I would suggest the following amended version of the superannuation Fee Template in clause 201 of Schedule 10 (which is based, to the extent possible, on the existing Fee Template):

Diagram 6-1 – Modified version of superannuation Fee Template

<i>[Name of superannuation product]</i>		
Type of fee or cost	Amount	How and when paid
<b><i>Ongoing annual fees and costs</i></b>		
<i>Administration fees and costs</i>		
<i>Investment fees and costs<sup>1</sup></i>		
<i>Transaction costs (net)</i>		
<b><i>Member activity related fees and costs</i></b>		
<i>Buy-sell spread</i>		
<i>Switching fee</i>		
<i>Exit fee</i>		
<i>Other fees and cost<sup>2</sup></i>		
1.	<i>[If relevant insert a footnote Investment fees and costs includes an amount of x.xx% for performance fees. The calculation basis for this amount is set out under “Additional Explanation of Fees and Costs”.]</i>	
2.	<i>[If there are other fees and costs, such as activity fees, advice fees for personal advice or insurance fees, include a cross-reference to the “Additional Explanation of Fees and Costs”.]</i>	

The inclusion of the line for “Transaction costs (net)” and the footnote relating to performance fees are included for illustration, subject to the discussion in Chapter 7. It is also noted that, under the government’s “Protecting Your Super” Package<sup>112</sup> that was announced in the 2018-19 Budget, exit fees would be prohibited. If enacted this would mean that the related line could be removed from the template above.

Changes to affected definitions in Schedule 10 would be required.

A similar type of Fee Template could be tested for MIS adding different fee types and payment options as appropriate. Again, for the purpose of proposing a layout worth consumer testing, Diagram 6.2 set out an amended version of the MIS Fee Template in clause 202A of Schedule 10 (which is based, to the extent possible, on the existing Fee Template).

As for Diagram 6-1 the inclusion of the line for “Transaction costs (net)” and the footnote relating to performance fees are included for illustration, subject to the discussion in Chapter 7. The MIS Template is substantially longer than the one for superannuation products however this appears difficult to avoid having regard to the different regulatory requirements.

<sup>112</sup> This package proposes a number of regulatory reforms including a cap on Administration and Investment fees charged on superannuation accounts with balances of \$6,000 or less at 3 per cent of the account balance, in addition to banning the charging of exit fees for any account: [see Treasury website](#).

Diagram 6-2 – Modified version of MIS Fee Template

<i>[Name of managed investment product]</i>		
Type of fee or cost	Amount	How and when paid
<b>Ongoing annual fees and costs</b>		
<b>Management fees and costs<sup>1</sup></b> The fees and costs for managing your investment <sup>2, 3</sup>		
<b>Transaction costs (net)</b> The costs incurred by the product when buying or selling investments		
<b>Member activity related fees and costs (fees for services or when your money moves in or out of the product)</b>		
<b>Establishment fee</b> The fee to open your investment		
<b>Contribution fee<sup>3</sup></b> The fee on each amount contributed to your investment		
<b>Buy-sell spread</b> An amount deducted from your investments representing transaction costs incurred by the product		
<b>Withdrawal fee<sup>3</sup></b> The fee on each amount you take out of your investment		
<b>Exit fee<sup>3</sup></b> The fee to close your investment		
<b>Switching fee<sup>4</sup></b> The fee for changing investment options		

1. [If relevant insert a footnote *[Management fees and costs includes an amount of x.xx% for performance fees. The calculation basis for this amount is set out under “Additional Explanation of Fees and Costs”.]*]
2. [If relevant insert *The management fees and costs for specific investment options are shown at page [insert page number].*]
3. This fee includes an amount payable to an adviser. (See Division 4, “Adviser remuneration” under the heading “Additional Explanation of Fees and Costs”.)
4. [If there are other service fees, such as advice fees or special request fees, include a cross-reference to the “Additional Explanation of Fees and Costs”.]

#### Fee Template – summary points and recommendations

In summary, my observation is that while the Fee Template might be a necessary source of data about fees and costs, it is not a consumer-friendly basis for making meaningful cross product cost comparison. Some of the issues relating to variations in PDSs are less of an issue in investment option comparison within a product (there is generally minimal diversity of description within the one PDS) but some are still relevant. In short, there are too many variables across different Fee Templates for consumers to reconcile for them to play a stand-alone role in product-to-product comparison.

If there is a desire to see the Fee Template play a more effective role in helping consumers to make comparisons across products (mainly for investment option comparison) the Fee Template could be improved by:

1. greater standardisation in how fee information is set out;
2. greater standardisation in how fee information is incorporated by reference into a PDS;
3. aligning presentation and, if possible, underlying data as between MIS and superannuation products;
4. simplifying the layout of fee elements in the Fee Template to separate ongoing annual items from fees relating to member-initiated activity;
5. removing unnecessary lines from the Fee Templates;
6. better grouping of ongoing annual items particularly in the Fee Template for superannuation products;
7. merging ICR with Investment fees; and
8. clarifying that the explanation about Transaction and operational costs in the AEFC relates to amounts that are already included in the Fee Template.

Specific recommendations are outlined above.

### 6.7 Effectiveness of the Fee Example.

The Fee Example (based on a balance of \$50,000) is the working partner of the Fee Template. The objective of the Fee Example is to convert the, still somewhat compound, information in the Fee Template into a single, synthetic, figure for simple comparison purposes. Details of the regulatory requirements are set out under Chapter 5.2 above. Again, the analysis at this stage does not go to whether the outcome is truly comparable because of data issues but looks to the Fee Example as a disclosure tool.

If the objective is simplified comparison, then a single figure comparison is undoubtedly the best approach for facilitating consumer comparison. Some jurisdictions have tried to reach this theoretical end point by another route; by regulating fee charging structures in a way that only permits a single line fee that can be easily compared. An example would be the salary-based or contribution-based fee arrangements in Latin America. In Chile, El Salvador and Peru for example, fee comparison has historically been focussed on the single monthly percentage of salary charged by providers.<sup>113</sup>

The alternate route is to allow multiple fee and cost impacts, but to get to a single figure comparison by use of an illustrative synthetic figure that brings multiple fee or cost impacts into the single figure. Many jurisdictions have attempted such a solution adopting differing methodologies. Some examples are set out under Chapter 4 above. It is noted that the use of a percentage figure (such as a “Reduction in Yield” figure) is used more commonly than a dollar based figure as used in Australia. The use of a dollar figure assists consumer understanding relative size, although a percentage figure would better assist consumers in understanding the relevance in the context of overall returns.

Notwithstanding the presentational difference, the Fee Example shares most attributes of similar tools used elsewhere. The methodology for its production is consistent (subject to issues about underlying data comparability) and reasonably clear.

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<sup>113</sup> See IOPS Working Paper 20 Table 1 for an analysis of different types of charging structures.

There are however limitations in using the Fee Example for comparison purposes. These generally flow from the compromises necessary in ensuring that the PDS is kept to a manageable size and a readable format.

1. **Limited Coverage:** The most obvious limitation is that, for presentational simplicity, the Fee Example is calculated only for a single MySuper product or investment option or a single balanced investment option in MIS.<sup>114</sup> If the relevant MySuper product uses a lifecycle investment approach, Investment fees used in the calculation must be the highest Investment fees for a lifecycle stage of the product<sup>115</sup> (in effect only one part of that single investment approach). As such, the universe of investment options for which the Fee Example is calculated is quite limited. APRA statistics<sup>116</sup> suggest an average of 236 options per superannuation fund (however this would be skewed by the range of options provided under Platforms). PDS reviews suggest that industry superannuation funds typically offer around 10 options. Whatever the actual figure, it is clear that only a small proportion of investment choices within superannuation funds are set out in the Fee Example. This is less of an issue for MIS PDSs which typically comprise a single investment option.

The counter point to this concern is that, by design, the Fee Example covers the most commonly used options. In the case of superannuation, it is focussed on the MySuper product or option. This would typically cover members who do not make a choice. The rather perverse outcome of this is that, as a comparison tool, the Fee Example is therefore most usable for those who do not make choices and does not well serve the needs of those who do make choices except perhaps in illustrating the approach that a consumer should take in taking into account different fees for comparison purposes.

2. **Single account size:** Another limitation relates to the Fee Example being based on a single balance – usually \$50,000. Inevitably, this means the Fee Example is most useful for those members who have an account balance of around \$50,000. APRA data suggests that only 24% of accounts have a balance that falls within the broad range of \$25,000 to \$100,000. Sample data provided to me by the FSC suggests that only around 10% of accounts have a balance of between \$40,000 and \$60,000 and ASFA analysis suggests that only 2-3% of accounts fall within the \$45,000 to \$55,000 range. This suggests that, whilst \$50,000 might be a reasonable figure, it is of limited use in application because of the spread of account sizes.

This would not be a major obstacle if the Fee Example figures were easily capable of extrapolation; a member with a \$100,000 account balance could simply double the Fee Example figure. This can not however be done because many products, particularly within superannuation, have fees that are a combination of a fixed dollar amount and a percentage of balance based amount. Consequential extrapolation errors increase as account sizes increase. Some also have fee caps that cut in at different account sizes. Platforms often have minimum and maximum fee levels. Some funds have tiered fee structures. All of these variations make simple extrapolation unworkable.

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<sup>114</sup> Or another single investment option in accordance with clause 220 of Schedule 10.

<sup>115</sup> Clause 214A of Schedule 10.

<sup>116</sup> APRA Annual Fund level Superannuation Statistics 2017, at table 2.

Another aspect of this limitation is that Fee Examples do not work well for multiple holdings in a fund where there is a fixed administration fee.

3. **Time periods:** The Fee Example only illustrates impact over a 12 month period. Similar tools used in other jurisdictions extend the illustration over multiple time periods and, in the UK case, this is related to suggested holding periods.

Whilst inclusion of differing time periods would be of value, the benefits may be outweighed by the layout complexities involved particularly if different account sizes are to be included. Given local charging practices, I consider that including different account sizes would be of more value to consumers than multiple time periods.

4. **Assumptions about flows:** The Fee Example calculation for superannuation assumes no contribution, no withdrawal, no exit and no activity-based fees. The Fee Example calculation for MIS assumes a contribution of \$5,000 but no withdrawal or exit and no activity-based fees. The differences in approach are presumably derived from the fact that MySuper products have no contribution-based fees. This might not be relevant to other investment options in a superannuation fund. In this particular respect, comparison between superannuation and MIS products is compromised.
5. **Calculation qualifications:** Occasionally, PDSs contain lengthy footnotes or explanation after the Fee Example that limit its value as a simple point of comparison. Performance fee and other fees are, for example, sometimes qualified by comments that the figure used in the example should not be relied upon because e.g. *“performance fees may be higher or lower or not payable in the future”*, *“the amount will depend upon the Fund’s performance”*, *“fees and expenses ... fluctuate daily”*.

Limitations 1 and 2 above could be addressed if PDSs set out the Fee Example calculation for all investment options across a range of account sizes and time periods. The international comparison case studies in Chapter 4 show that such calculation across time periods is common, although comparison across different account sizes is not. Technically either or both would not be difficult for Providers to calculate. There would however be issues about including this additional information within a PDS, given existing concerns about readability and length, particularly for PDSs which are subject to the shorter PDS regime.

To reduce length, additional information could be limited to the single “Cost of Product” calculated figure rather than setting out the calculation of the elements as done in the existing example. The range of sample account sizes could be kept to perhaps four – one low figure directed to early year employees with low balances, an average figure and two higher balance figures directed to later career, higher balance fund members who may for example be adjusting investment strategies. Figures such as \$20,000, \$50,000, \$200,000 and \$500,000 could be considered. Even for 20 investment options this could be contained within a half-page table. For funds or schemes with many more investment options, such a table would be longer, but within the context of their, already lengthy, disclosure (some already contain up to 20 pages of fee disclosures) an additional page should not be too onerous or extra columns could be added to existing investment menu tabular information which is typically incorporated by reference.

Such calculations could also feed into any central comparison facility discussed in Chapter 6.4. These figures could also feed into any expansion of the product dashboard requirements, if or when these are extended for use beyond MySuper products.

**[Recommendation 13]** I recommend that the Fee Example be extended to all investment options by the calculation and disclosure of an abbreviated “Cost of Product” figure. Flexibility could be provided as to where the “Cost of Product” figure is to be disclosed (either in the PDS, incorporated by reference or in some other manner).

To further align disclosure between superannuation and MIS products, the same assumptions about flows should be used. This would affect the Fee Example and any abbreviated “Cost of Product” calculation, principally as impacted by any applicable buy-sell spread. The existing assumption used for MIS (a contribution of \$5,000 on the last day of the period) seems a reasonable basis.

**[Recommendation 14]** I recommend that, the Fee Example and the abbreviated “Cost of Product” calculation referred to in the preceding recommendation for superannuation products incorporate a contribution of \$5,000 on the last day of the period.

Again however, these observations and recommendations need to have regard to the observations above that the comparison task for a consumer would still be very challenging even if the Fee Example were extended to all investment options. Wide cross product comparison could only be done effectively with the support of some electronic tool or facility that brings data from Fee Examples across products into one point or the inclusion of some average “Cost of Product” figure. Related recommendations are set out in Recommendation 1 (Chapter 6.4).

#### 6.8 Effectiveness of the AEFC

As noted in Chapter 6.3, the AEFC does not primarily serve a comparative purpose but a base information provision purpose. It is most suited for information items that are not significant ongoing fees or costs (which are better placed in the Fee Template) and backward-looking data (which has limited forward looking reliability). The content requirement for the AEFC has grown substantially over time. From five items in the original 2005 version, current requirements comprise 15 items and 26 item subheadings.

Whilst initially well segregated from the Fee Template, the cross over of information has tended to increase over time. Some items, such as most transactional and operational costs for superannuation funds, are disclosed in both the Fee Template and the AEFC.

In reviewing PDSs as part of the Review, I observed that the format and layout of the AEFC varies substantially, particularly when contained within a document that is incorporated by reference. This is however not such a major concern given that the AEFC is not primarily a comparative tool (in contrast to the Fee Example and Fee Template).

Overall, few points of concern were raised regarding the AEFC except as a consequence of concerns about the treatment and positioning of specific items such as Transactional and operational costs (including property operating costs) and borrowing costs. Clearer messaging as to its purpose and use could be considered. Some confusion has been noted regarding exactly what use should be made of information and data in the AEFC.

No specific recommendations are made in this regard, although recommendations in Chapter 7 necessarily affect the AEFC. Appropriate messaging can be considered in light of any changes to position of data, particularly those relating to Transactional and operational costs.

One minor point that could be further considered, if other changes are to be consumer tested, is whether a more consumer friendly title should be used. Cross references to the Additional Explanation of Fees and Costs are something of a mouthful and rather awkward. If other potential changes are to be consumer tested a punchier title such as “Fees and Costs Details” could be tested at the same time. A corresponding change of the Fee Template to “Fees and Costs Summary” could also be consumer tested at the same time as a better companion to the “Fees and Costs Details”.

**[Recommendation 15]** I recommend that if other potential changes to Fee Templates are to be consumer tested, possible change of the name of the AEFC to “Fees and Costs Details” and change of the name of the Fee Template to “Fees and Costs Summary” be tested at the same time.

## 6.9 Periodic Statements

### Background

Periodic statements are issued to members in prescribed circumstances;<sup>117</sup> generally, either annually or on exit from a fund. Periodic statements are required to include three functionally different types of information:

1. a listing of transactions in a member account (including fees deducted directly from that account);
2. other figures that show the impact of various other fees and costs not directly deducted from the member’s account (these are shown as dollars in a manner that seeks to apportion investment level fund costs to an individual member account, based on average account balance); and
3. other figures or information that explain or expand upon other items of fee or cost.

As modified, Schedule 10 requires the following items in periodic statements (ignoring, for simplicity, transitional treatment):

#### **A - Superannuation products:**

1. a listing of transactions in the account including fee items deducted from the account (including for example switching fees, administration fees);
2. “Indirect costs of your investment” (meaning the apportioned amount of Indirect costs of the product as defined);
3. “Other fees of your investment” (meaning the apportioned amount of items listed as fees in the PDS (e.g. Administration fees, Investment fees, buy-sell spread) not recorded under (1));
4. “Total fees you paid” (this item adds up all fees and costs in (1) (2) and (3) above);
5. details of any activity fees, advice fees and insurance fees;
6. a note about whether the benefit of any tax deduction has been passed to the investor; and
7. the approximate amount of borrowing costs or the total of borrowing costs plus (4) above.

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<sup>117</sup> See section 1017D of the Corporations Act and Div 5 of Part 7.9 of the Corporations Regulations.

## **B - Managed investment schemes**

1. a listing of transactions in the account including fee items deducted from the account (e.g. contribution fees, establishment fees);
2. “Indirect costs of your investment” (meaning the apportioned amount of all Management costs borne by the holder (other than those recorded under (1)));
3. “Total fees you paid” (this item adds up all fees and costs in (1) and (2) above);
4. details of any incidental fees;
5. details of any service fees;
6. a note about whether the benefit of any tax deduction has been passed to the investor; and
7. the approximate total amount of transactional and operational costs affecting the holder (or that amount plus (3) above) excluding implicit transaction costs and the amount recovered by a buy-sell spread (in defined circumstances).

## **C - Platforms**

For Platforms, the above requirements apply, although there is no statutory obligation in Schedule 10 that a periodic statement for a Platform member should include costs attributable to chosen underlying investments. In relevant ASIC Q&As, ASIC state that periodic statements for Platforms should provide additional lines of information that include, and sum up, the costs of underlying investments in combination with the fees and costs of the Platform.<sup>118</sup> For a superannuation Platform, for example, this would suggest inclusion of an extra 2 lines:

1. a line showing the cost of chosen underlying investments; and
2. a line that sums (1) with “Total fees you paid”.

### **Observations**

Most should agree that the objective of including data (even if approximated) about the impact of investment level fees and costs in periodic statements is a sensible direction. It is noted however that this is not commonly done in the jurisdictions considered in Chapter 4.2. Only the EU, under the Directives commonly known as “MiFID II”, extend periodic reporting in a manner that includes fees and costs of underlying investments (noting that these only apply in limited circumstances). Disclosure that only includes amounts deducted from a holder’s account (as was the case in Australia before 2005) only tells a part of the story and is inconsistent with the way that fee and cost impacts are described in the PDS. Layout consistency between PDSs and periodic statements should assist consumers in understanding the data set out in periodic statements and should assist them in broadly reconciling fees and costs actually incurred with what is disclosed in the PDS.

Industry representatives have expressed concerns however that the resultant periodic statement is complex and this complexity does not aid member understanding. Particular concern was expressed regarding: the additional lines of disclosure related to underlying investments chosen in Platforms, the manner in which gross vs net transaction costs are disclosed (for MIS) and how taxation impacts are shown (for superannuation). It has been suggested that the data about

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<sup>118</sup> See [Question number 6, ASIC Questions and answers - fees and costs disclosure – superannuation and managed investment products](#).

taxation impacts has raised many questions from holders about whether this affects their own taxation affairs.

As can be seen from the above, the original objective of expanding periodic statement disclosure to show the approximate, apportioned, impact of fees and costs not directly charged to the account, has proven to be rather complex in practice. Based on the Example 3 in the RG 97 Industry Group Guidance,<sup>119</sup> for a periodic statement for a superannuation product, this would amount to 5 lines (15 dollar figures) showing approximated, apportioned, fee and cost impacts (including columns showing tax benefit and net amount). For Platforms, showing the additional impact of chosen accessible investments would require an additional 2 lines plus extra cells showing taxation benefits.

Whilst I have not been able to review a range of actual periodic statements, it seems likely that the volume of data now presented in periodic statements would be overwhelming to consumers and the presentation has completely reversed the traditional focus on transactions and amounts deducted directly from the holder's account (which comprise only one line in the "Fees and costs summary").

Notwithstanding efforts to align disclosure between them, reconciliation between the PDS and periodic statements, particularly for a superannuation product, would also be challenging given that:

1. the sequencing of the fee items in the periodic statement (broadly account level, then fund level fees then Indirect costs) does not reflect the sequencing or layout of the Fee Template – it would take some effort by a consumer to reconcile which items in the Fee Template are reflected in which part of the periodic statement, and
2. the headings used in the periodic statement (for superannuation products "Direct fees" "Other fees of your investment" and "Indirect costs of your investment") reflect a technically justifiable split, but one that would be very difficult for a consumer to understand (requiring an appreciation of the differences between fees and costs and that "direct" (in the periodic statement) and "indirect" (in ICR) are not used as functional opposites).

It is difficult to propose specific recommendations to address the observations noted above given that any changes to fee and cost disclosure in periodic statements will be dependent on any fee and cost disclosure changes in the PDS. The recommendations set out in other parts of this Report would, if implemented, change the fee and cost disclosure in PDSs in a manner that would have flow on impacts for periodic statements that may naturally simplify its presentation. By way of example:

1. if Recommendation 11 to collapse Indirect costs and Investment fees into a single item (for superannuation) is implemented, items (2) and (3) above could be merged into a single line;
2. if the Fee Template (for superannuation) is adjusted to show "Administration fees and costs", "Investment fees and costs" and "Transaction costs (net)" (as illustrated in Diagram 6-1), then the title of the relevant line in the periodic statement would include both fees and costs and the title should be changed to reflect this;

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<sup>119</sup> RG 97 Industry Working Group, November 2017, "Fee and Cost Disclosure Guidance".

3. if, as proposed, borrowing costs are removed from PDS disclosure (as a component of operational costs), item (7) could be removed from superannuation periodic statements;
4. if, as proposed, transaction costs are included in the headline fee item for MIS, item (7) could be removed from MIS periodic statements; and
5. if, as proposed, Fee Template disclosure for MIS is aligned with superannuation products, periodic statements for the two products can also be aligned to a greater extent (although it is acknowledged that this is not a pressing objective given that the periodic statement is not a comparative document).

Subject to how and whether other recommendations are taken forward, periodic statements for both superannuation and MIS might comprise only three lines in the “Fees and costs summary” that could be styled as follows:

1. “Fees deducted directly from your account”;
2. “Fees and costs deducted from your investments”; and
3. “Total fees and costs you paid”.

It is recognised that there remain some quite technical issues for ASIC and industry to work through regarding the disclosure of the impact of taxation on fees and cost items in periodic statements. This will affect the layout of periodic statements and the number of data points required.

**[Recommendation 16]** I recommend that, subsequent to considering other recommendations in this Report, ASIC consider consequential changes to the disclosure of fees and costs in periodic statements. These should be approached having regard to the following objectives:

1. reducing the relative over emphasis on amounts deducted from investments;
2. reducing the number of data points; and
3. making the item headings easier for consumers to understand.

Although less important, improving alignment between PDS and periodic statements and improving alignment of periodic statements as between MIS and superannuation products should also be kept in view.

## 6.10 Platforms

The final section of this Chapter discusses issues related to how the fee disclosure regime applies to custodial arrangements known as wraps, superannuation platforms or Investor Directed Portfolio Services, also known as IDPS. These products are collectively referred to as “Platforms” in this Report.

### Background

Platforms provide investors with various services, including access to a range of financial products. Typically, the accessible financial products will include a wide range of MIS (over 500 in some cases). The accessible MIS are not part of the Platform product and PDS disclosure for the accessible MIS is the responsibility of the responsible entity of each of the MIS.

Both because of their dual layer structure and in recognition of the sheer volume of accessible products, disclosure arrangements for Platforms have historically been different from those

applying to superannuation products and MIS. Disclosure, including fee disclosure, for the accessible MIS is primarily delivered by the Platform Provider giving potential investors the PDS for the accessible MIS.

In contrast, the primary fee disclosure obligations for the Platform relate only to fees and costs associated with the Platform, including for instance, the administration costs for participation in the Platform (usually tiered), various account administration fees and costs associated with making investment selections. Often, this involves no Investment fees or ICR, as no investment costs are incurred in accessing the Platform.

During the industry engagement process, many comments were made about the way that fees and costs are disclosed for Platforms.

#### Current fee disclosure requirements and practices

In recognition of the importance of Platform investors understanding that they need to take into account the combined costs of accessing the Platform and investing into the accessible MIS or other products, RG 97 includes various supplementary suggestions to ensure that the Platform PDSs will not mislead investors. These are (at RG 97.72 – RG 97.74):

1. prominent statements following the Fee Example that the fees and costs of the Platform relate to access to the investments on the list, not the costs within those investments, and that additional costs will be charged by the issuers of the products that the investor decides to invest in;
2. inclusion of an example illustrating the combined effect of fees and costs of the Platform and of an actual or hypothetical entity that may be regarded as typical for a major proportion of the investments selected by investors in the relevant Platform; and
3. for each investment on the Platform investment list, similar examples of the cumulative effect of the fees and costs of the investment, taking into account the fees of the Platform and the fees and costs for the investment that may be selected.

RG 97.75 and ASIC Q&A number 23 also includes a warning to persons undertaking marketing activities or giving advice that they should ensure that there is no inappropriate comparison between Platforms and other kinds of investment options.

A review of Platform PDSs and investment guides indicates that the prominent statement suggested in (1) above is presented quite differently, and with varying degrees of prominence PDS to PDS. The suggestion in (3) above has not been widely adopted. However, in addition to the above, some Providers show key fee and cost information, such as the Management costs and also Transactional and operational costs of the accessible MIS (as disclosed in the PDS of the MIS), usually in tabular form, within investment menu documents that set out a list of accessible investments. These documents are variously described as “Investment list” or “Options”. This additional information varies significantly however, from Platform to Platform, both as to format and content.

Finally, whilst there is no statutory obligation that a periodic statement for a Platform member should set out costs attributable to accessible investments, ASIC, in ASIC Q&A number 6, suggests that periodic statements for Platforms should provide additional lines of information that include, and sum up, the costs of accessible investments in combination with the fees and

costs of the Platform. This recommendation is reflected in Part 10.9 of the RG 97 Industry Group Guidance. Pending relevant system developments, transitional disclosure suggestions are also set out in the ASIC Q&A.

#### The impact of advisors

In addition to the above, it has been suggested to me that disclosure differences or limitations relating to Platforms may be of limited practical significance because of the role of advisors. Advisors generally play a role both in entry to the Platform and the exercise of investment choices of participants. Even if the task of gathering and considering disclosures of investment selections were too complicated for consumers to handle, then this might not be too much of a concern if all decisions are supported by professional advice. Practically, most Platforms appear to be administered in a way that works most efficiently through the intervention of, or assistance by, advisors.

Whilst it is true that the vast majority of Platform investors are advised, there are at least two categories who are not; those who have left their advisor after joining the Platform and those who can join without the assistance of an advisor. In recognition that Platforms can be complex products and/or the operational advantages of working through professional advisors, most Providers do put in place arrangements or restrictions that prevent or discourage investors who are not advised. Some will only accept new members through an advisor, some have administrative arrangements to find new advisors for members who have left their pre-existing advice relationship, some have additional fees for non-advised members, some limit transactional activity for non-advised members and some impose additional administrative steps for non-advised transactions. There are however some Platforms that do allow non-advised individuals to join directly and there is little that can be done to prevent members from becoming non-advised after joining.

Data provided to me from FSC members suggests that although there are variations from Platform to Platform, broadly it appears that well under 10% of Platform members would be non-advised. This group are reported to be less active than advised members. One Provider said that under 20% of that group had made investment selections. Another said that less than 1% of this group had made investment selections in the previous 12 months. This data can be interpreted as suggesting that less than well under 2% of Platform members make self-guided investment decisions. Whilst the needs of this group should not be dismissed, it should be recognised that the vast majority, perhaps over 98%, of investor decisions regarding Platforms are subject to professional advice.

The degree of comfort that can be taken from the role of advisors is however not a simple issue. Ultimately, advisors need to rely on substantially the same fee disclosures as consumers. In terms of finding and comparing fee data, advisors are often supported by systems that make the task much easier. This can, in effect, reduce concerns about the complications of double layer fee disclosure. However, during consultation, advisors expressed concerns that even they were not sure about which elements of current fee disclosure were relevant when giving a Statement of Advice comparing different products.

#### Concerns expressed

Based on consultation outcomes, the totality of the fee disclosure arrangements as set out above appear to satisfy almost no one.

Platform Providers have raised numerous concerns including:

1. the suggestion that the Platform Providers should provide examples of the cumulative effect of the fees and costs of the Platform plus investment for each investment on the Platform investment list is unreasonable given that the Fee Example is only provided for a single investment option in superannuation and MIS products;
2. the above is, in any event, impractical for hundreds of accessible products;
3. the ability to voluntarily show fees and costs of accessible MIS in investment documents is severely inhibited for superannuation Platforms because of the differences in disclosure requirements between MIS and superannuation funds;
4. even where the data of accessible MIS can be adjusted to superannuation like requirements, this inevitably creates confusion as the MIS PDSs will disclose different information to that provided by the Platform; and
5. the additional lines of fee disclosure in periodic statements (set out in ASIC Q&A number 6) are unduly complex.

Some non-Platform Providers have strenuously raised concerns that, despite the safeguards set out above, consumers could, and are, being enticed to join Platforms without a proper understanding of the cost implications. They say that the double layer fee disclosure for Platforms creates complexity that results in consumers not being able to properly compare fees and costs of Platforms and non-Platform products (particularly for superannuation products). They also raise concerns whether advisors can adequately and fairly make fee comparisons between Platform and non-Platform products.

Advisors raise concerns that the way that fee information is disclosed (some in Fee Templates and the Fee Example, some in AEFC and some elsewhere) makes it difficult for them to know which elements are relevant when comparing the costs of products. This concern is not limited to Platforms but is particularly relevant in that context.

#### Observations & recommendations

Clearly, because of their more complex structure, disclosure for Platforms is always going to be more complex than for non-Platform products. Fee comparison between accessible investments within a given Platform works adequately (largely because the only differences could relate to one layer of fees and costs). Provider level comparison between Platforms and non-Platforms or between investment selections within a Platform and the same or a similar investment option outside of that Platform is rather more complex. Consumers, or in most cases, their advisors, need to appreciate the double layer of fee impact and disclosure and how to aggregate, or disaggregate, this disclosure depending on the comparison being made.

The various warning and safeguards referred to above should assist in ensuring that consumers are aware of the need to aggregate the two levels of disclosure. Advisors would most likely be aware of this in any event.

As detailed above, some Platform Providers assist the “aggregation” process by showing Management costs and other costs of accessible MIS within the investment menu documents. This substitutes in many respects for Fee Template like disclosure. PDSs for Platforms also

provide Fee Examples that aggregate the two levels of fees. Most provide several such examples but, few, if any, provide an example for each accessible MIS.

Notwithstanding these efforts, it is undeniable that the fee and cost “story” for Platforms is harder for consumers to understand than is the case for a superannuation master trust where investment options are a part of the trust. Some have suggested that to bring disclosure for platforms on the same footing as a superannuation master trust Fee Templates should incorporate all fees and charges of accessible investments within one of the fee items in the template. Not only does this present practical problems in terms of layout, but it creates problems in principle regarding the actual “source of truth” for disclosure of accessible products. Such an approach would also create some confusion between the different layers of fees and costs at the different product levels. For Platforms, consumers need to understand and appreciate the costs of the Platform separately from the costs of accessible investments.

This is not easy to overcome, and no simple solutions present. However, when considered together, recommendations in this Report would, if implemented, assist in achieving fee and cost disclosure for Platforms that is functionally, substantially similar to that for MIS and superannuation products. Given the support by advisors in the vast majority of cases, most concerns about making comparisons between products should be addressed.

If adopted, recommendations concerning greater alignment between superannuation product and MIS fee disclosure (see Recommendation 5 and Recommendation 24 as it applies to Transactional and operational costs) will also assist bridge the gap. It is recognised that, absent greater alignment of fee and cost disclosure between superannuation products and MIS, the recommendations below might not be achievable.

Fee Template differences would be moderated by showing key fees and costs of accessible MIS within the Platform’s investment menu documents in tabular format, as is already done in some cases. Greater standardisation of how and where this is done would assist. Exactly which components should be shown will need to be further considered in light of other recommendations affecting the Fee Templates. Standardised introductory text (explaining for instance that the data is extracted from the PDS of the relevant MIS (or provided by an information vendor) and warning potential investors to check the latest PDS of a MIS before selecting it for investment) would assist in managing investor expectations and timing/updating concerns for Providers. Standardisation work could be done in conjunction with Recommendations 3 and 4.

Recommendation 13 (extension of abbreviated Fee Examples (the “Cost of Product” calculation) to all choice products) could also be made applicable to Platforms in a functionally similar manner although various textual changes (including changing the title to (“Cost of Product and accessible investments”)) would be required. In practice this might require the addition of a single column to the table in investment menus referred to in the previous paragraph. Availability of these abbreviated Fee Examples would be important as this is the most relevant comparison point for consumers and their advisors.

For periodic statements, Recommendation 19 would result in functional alignment of fee and cost disclosure as between Platforms and other products.

In addition, I had considered recommending that, to reinforce the need to, and impact of, aggregating two layers of fee disclosure, the Fee Template for Platforms should also include an

additional line showing, as a range, the “Fees and costs that will be incurred when investing through accessible products”. Consultation outcomes were however generally negative on this proposal given the limited value and potential confusion associated with disclosure of a range. Nevertheless, consumer comparison, at least between Platforms would be assisted if there was greater consistency of approach in the way that the prominent statement (that the fees and costs of the Platform in the PDS relate to access to the investments on the list, not the costs within those investments) were presented in a standardised position and with standardised text. Examples where this is included as a point in the Fee Template under Investment Fees (for superannuation products) or Management costs (for MIS) appear to give this due prominence at a relevant point. This practice is one that should be considered. Cross references to the fee and cost information in the investment menus (referred to in the previous two paragraphs) should be included.

I recommend four additional enhancements to disclosure requirements for Platforms:

**[Recommendation 17]** The existing practice of showing fees and costs of the accessible MIS available through a Platform within the Platform’s investment menu documents should be made a specific obligation in Schedule 10. Standardised introductory text should be developed.

**[Recommendation 18]** The investment menu documents for Platforms should also include abbreviated “Cost of Product” figures for accessible MIS, calculated in a manner that is, to the extent possible, consistent with the calculated figure referred to in Recommendation 13 (including both Platform level and MIS level fees and costs).

**[Recommendation 19]** Periodic statement disclosure obligations in Schedule 10 should explicitly include the costs impacts of accessible investments in Platforms. The manner of achieving this, so that it can be comprehensible to consumers, should be further considered in light of proposed and consequential improvements to periodic statements generally (Chapter 6.9). It may be the case that this recommendation can only be achieved by an extra line or two of data points.

**[Recommendation 20]** The text and positioning in the PDS Fee Template of Platforms, of the prominent statement that the fees and costs of the Platform relate to access to the investments on the list, not the costs within those investments, should be standardised and made a requirement. Positioning of the statement within the ‘Investment fees’ or ‘Management costs’ line should be considered. The statement should also provide a cross reference to the location of the “Cost of Product” figure recommended in 18 above.

Exact details of the way forward would have to be considered in light of developments in other recommendations affecting Fee Templates, transactional and operational costs and alignment of disclosure between MIS and superannuation products. Given the contingencies around other recommendations and observations in this Report and their possible impact on the disclosure of fees and costs for Platforms, it would be appropriate to ASIC for undertake a stocktake, and review the resultant disclosure requirements for Platforms once the recommendations set out in this Report, or as subsequently modified, are implemented or sufficiently developed.

**[Recommendation 21]** I recommend that, after implementation of any resultant changes, ASIC further review the practice and policy of disclosure of fees and charges for Platform products. Such review should focus on whether disclosure of fees and charges for Platform-based products is adequately meeting the objective of providing consumers with information that they can use in making more confident and informed value-for-money decisions when choosing investment options within Platforms and when making product level choices between Platforms, MIS and superannuation products.

## 7. Fee disclosure data- discussion and recommendations

### 7.1 The data issue

Notwithstanding the discussion in the previous Chapter about the challenges of the disclosure regime, the issues that were the primary focus of stakeholder comments were not the legislated disclosure tools but more technical questions and concerns about what data elements should go into the specific fee elements that make up the fee and cost items set out in the Fee Template, Fee Example and the AEFC. It is those issues that have dominated discussions with stakeholders. Items that go into the Fee Template feed into the Fee Example and ultimately into periodic statements.

What goes into these fee and cost items raises many quite technical legal issues that are driven by Schedule 10, CO 14/1252 (as amended by the various instruments), RG 97 and the ASIC Q&A. The most debated areas relate to the meaning of defined terms such as Administration fees, Investment fees, Management costs and Indirect costs. Other problematic elements and definitions feed into those definitions including Transactional and operational costs, Interposed vehicle, borrowing costs, property operating costs and Performance fees.

These definitions, as they currently apply, are an outcome of the original legislative drafting which has been modified extensively by CO 14/1252. RG 97 sets out explanations of the modified legal position and, in some areas, also provides interpretational guidance. This is supplemented by the ASIC Q&A and expanded upon in many face-to-face meetings between ASIC and industry.

### Complexity

A preliminary observation is that the regulatory arrangements put in place by Schedule 10, CO 14/1252 and RG 97 are technically complex and difficult to understand. This is largely a consequence of the complexity of the legislative regime, the range of fund types and the variety of charging practices that need to be accommodated in the regulatory arrangements but is exacerbated by the sequential modifications to CO 14/1252 and the manner in which this modifies Schedule 10. It is also recognised that the CO 14/1252 and RG 97 are not consumer-facing documents as they are primarily directed at the affected industry and their advisors. ASIC staff have also expended significant effort in responding to industry questions to explain how the law and policy apply both face-to-face, through correspondence and through the publication of the ASIC Q&As.

Nevertheless, the requirements are very difficult to understand, and I encountered numerous instances during the Review where industry participants had concerns that arose out of a misunderstanding about the requirements and some frankly admitted an inability to understand what was required of them. Many, particularly those who have been less involved in face-to-face meetings, struggle to grasp many of the details. Some who had sought professional advice and/or discussed issues with other industry participants expressed frustration at the conflicting advice and views they received. Some expressed concerns about even finding the law they had to

comply with, given that no authorised, consolidated version of Schedule 10, as modified by the various ASIC instruments, is generally available.<sup>120</sup>

Some have suggested that the regulatory requirements could be simplified by adopting a more principles-based regulatory approach, however others have explicitly asked for a more prescriptive approach to ensure greater consistency. I would accept that in an area driven by the need for consistency to facilitate comparability, more rather than less detail is required.

There is no simple solution in such a technically challenging area. ASIC should however have regard to resultant complexity when administering and modifying such requirements. At a minimum, where complicated sequential modifications are made, such as in this case, ASIC should publicly make available a consolidated version of the relevant provisions, or if it is technically possible, adopt a drafting style that incorporates successive modifications making it easier for users to identify the ultimate modified requirements. A copy of consolidated Schedule 10 is attached as Appendix 3 of this Report however that might not be an obvious place for stakeholders to find it.

**[Recommendation 22]** I recommend that ASIC make publicly available on its website a version of Schedule 10 that consolidates the amendments made by the various ASIC instruments.

**[Recommendation 23]** I also recommend that, if the drafting of RG 97 is to be revisited, an attempt should be made to set out more explanation of the objectives and the context of fees and costs disclosure so that the meaning is more accessible to users. Some of the discussion and observations below might assist in this task.

## 7.2 Issues raised

During the engagement phase of the Review, many specific points of concern and questions about fee elements were raised by industry. Many strong views were expressed about why the current requirements were inappropriate, although in some areas different industry players had different views as to the preferred treatment of individual items.

The following is a listing of the major areas of concern raised, with more commonly raised issues listed higher in the list:

1. property operating costs - where and whether to disclose and calculation methodology;
2. borrowing costs - where and whether to disclose, separation of strategic from operational borrowings;
3. Transactional costs generally - where and whether to disclose;
4. implicit transactional costs - where and whether to disclose, clarity of requirements and calculation methodology;
5. Interposed vehicle definition - in particular the appropriateness of the PDS test and the relative treatment of different investments;
6. performance fees - where and whether to disclose and calculation methodology;
7. performance-related fees - where and whether to disclose and calculation methodology;

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<sup>120</sup> A version of ASIC CO 14/1252 that incorporates amendments made in subsequent instruments is however available through the [Federal Register of Legislation](#).

8. OTC derivatives - treatment as part of Management costs; and
9. tax impacts - where and whether to disclose elements gross or net of tax.

### 7.3 Methodology for dealing with data issues

As indicated above, many technical points have been raised for consideration. There are differing aspects to the points raised but many of the concerns and suggestions relate to the treatment of transactional and operational costs. Concerns and suggestions fall within two broad categories:

1. suggestions that certain items should not be treated as a cost impact that requires any disclosure in the PDS or periodic statements; and
2. suggestions that while certain items should be disclosed, questions are raised about whether they should appear in the Fee Template (with consequential impacts for the Fee Example, periodic statements and potentially any comparative facility as recommended in Chapter 6.4), or only in the AEFC or in some other place such as the product Provider's website.

Notwithstanding the degree of observed dissatisfaction with the current requirements, it should be acknowledged that ASIC has undertaken a rigorous and well considered development process. The outcome, complex as it may be, is driven by legislated definitions, some areas of concessional treatment (e.g. borrowing costs) and some areas of exceptional treatment (e.g. OTC derivatives, calculation of performance fees) that ASIC has built into the regulatory arrangements. Even though ASIC's modifications to the Schedule 10 requirements have been extensive, as noted in Chapter 3.6 above, this has been done within the framework of implementing what ASIC considers to be the legislative and policy intention of the relevant provisions.

As noted in Chapter 3.6, observations and recommendations in this Chapter are primarily directed at achieving outcomes consistent with the primary policy objective identified in Chapter 3.4 above of providing consumers with information that they can use in making more confident and informed value-for-money decisions. Relevance, reliability, consistency with consumer expectations and simplicity are adopted as key drivers in that framework.

The following decision-making framework for considering these more technical, data related issues, has been developed having regard to Australian and overseas disclosure regimes, reactions and concerns of stakeholders both during the Review and during the RG 97 development process and a view that, at the margins, there should be scope for flexibility given there are no absolute, inherently correct positions (this being reflected in the different approaches taken in different jurisdictions to some of these issues). Given that various concessions are already built into Schedule 10 through ASIC modification, it is recognised that ASIC has already implicitly applied a similar decision-making framework.

Broadly, the suggested approach is based on the pre-existing layering of disclosure requirements and focusses primarily on how the disclosure supports consumers in making product comparison decisions. There are some cost impacts affecting investor outcomes that are exempted from disclosure within the current fee disclosure framework (examples being the cost of timing and asset allocation decisions and the operational costs within entities or structures that are considered to be an asset). A second category are other cost impacts that could be disclosed, but are of such tenuous or limited interest or impact that they could stay outside the PDS and

periodic statement framework. Most cost impacts are important enough to be within the PDS and periodic statement framework; for those the question becomes whether they should be contained within the primary comparative tools (the Fee Template and Fee Example with consequential impacts for periodic statements) or set out in the AEFC where they can be disclosed, perhaps in more detail, but not in a way that feeds into the primary comparison tools (current examples being: all Transactional and operational costs for MIS, borrowing costs for superannuation products, implicit transaction costs and property operating costs transitionally).

The suggested categorisation is expanded on below:

**General points:**

1. categorisation should, where possible, minimise cross-over across different tools (for example, where possible, items or data set out in the Fee Template should not be repeated in the AEFC);
2. consequential use of Fee Template information in the Fee Example and periodic statements should be as clean and unadjusted as possible (to minimise consumer confusion about calculation);
3. the categorisation and treatment of items should be done in a manner that limits the need to update the PDS if those items are not material to consumers; and
4. although not a major point, where possible, items should be treated consistently with broader international approaches both to minimise administrative complexity for cross border operators and also to minimise dissatisfaction that can arise from imperfect/uninformed international comparison or benchmarking.

**Category 1** – items that should be disclosed in the headline tools (the Fee Template and Fee Example) would have more of the following characteristics:

1. in accordance with the original statutory design the Fee Template should only include significant fees that can be gleaned at-a-glance;
2. they are to the extent possible, forward looking, creating reliability as a comparative indicator (there is little value in telling consumers they should compare costs, if the information they get only tells them about the past and does not tell them anything reliable about what is likely to happen);
3. they are objectively certain to the extent possible (approximations, estimations and discretionary treatment reduce the reliability of the figures as a forward-looking tool);
4. they are consistent with the public narrative regarding the use of comparative fee/cost information and are consistent with the types of items that consumers would expect to take into account when comparing product cost impacts;
5. they do not distort the narrative (for example some individual items could be so large that when aggregated into a single comparative figure, they overwhelm other potentially more relevant items);
6. they do not require constant updating (which would create administrative challenges and indicate a lack of forward reliability in the data);

7. inclusion in this category does not distort investment behaviour of those making investment decisions for funds or exclusion would create a gameable opportunity (it would be a relevant consideration if inclusion in, or removal from, the comparative figures affected behaviour such that Providers changed structures or investment practices merely to achieve that end); and
8. the item does not require extensive textual explanation (meaning it would fit comfortably within the Fee Template).

**Category 2** items would be those that should be in the PDS/periodic statement framework but do not satisfy the Category 1 criteria, in particular, items that do not readily feed into comparative assessment across the relevant product universe or require some detailed explanation. These items should be disclosed in the AEFC rather than in the Fee Template or Fee Example. If possible, it is best that Category 1 items are not further expanded upon or further explained in the AEFC with other items. Further explanations or further explanatory data may create confusion and double counting.

**Category 3** items would include cost impacts that do not belong in the PDS regime because of limited interest or relevance to consumers, even if the information is relevant or of interest to investment professionals, superannuation trustees, responsible entities and financial or policy analysts. This category could also include items that, because of their volume or constant updating, are unsuited to inclusion in a PDS regime. These types of items could be left to other explanatory documents, Provider websites or statistical returns.

**Category 4** items would cover those cost impacts that are disproportionately burdensome to identify, produce and/or maintain having regard to the relevance to the common understanding of the fee/cost narrative.

#### 7.4 The fee disclosure narrative

As suggested above, one of the points that would be relevant to categorisation, is whether the proposed treatment is consistent with:

1. the public narrative regarding the use of comparative fee/cost information; and
2. consumers' expectations including what they would expect to be included in the fee and costs section of a PDS and what they would expect to take into account when comparing product cost.

Whilst the public narrative and consumer expectations are not necessarily the same, the public narrative is, to some extent, controllable and this should, over time, influence consumer expectations.

During consultation, some claimed that the policy reasoning behind the disclosure requirements are not well explained or understood. At the highest level, I doubt that there is substance to this as most seem to understand that the fee disclosure regime is driven by the need for clarity and comparability that supports member decision-making. The overall policy framework is expanded upon in Chapter 3.

Beyond this high level however, there is some substance to concerns that the objectives behind much of the detail are not well articulated. This is important because it feeds into how various data points should be treated and the narrative to consumers about what the disclosure tells them.

The narrative was much simpler before the Stronger Super Reforms in 2013, although even that is difficult to describe simply to a consumer. Up to that point, the fee disclosure regime focussed on traditional intermediation impacts, or explained another way, the extra costs incurred in investing through the product versus the cost of investing directly. Consumers could probably understand this as it picked up fees incurred either in their own account or in the fund, when moving money into or out of the products, traditional fees by the trustees, investment managers, custodians, distribution costs and expenses incurred in running the fund. The key disclosure tools did not include transaction costs relating to underlying investments because these would be incurred by an investor in any case, but these were disclosed separately in another part of the PDS (the AEFC). Exempting transaction costs on this basis is a little difficult to explain given that there may be little relationship between the costs that would be incurred by a fund and an individual investor. Other complications to the story, that consumers likely did not appreciate,<sup>121</sup> is that fee disclosure also included:

1. the same types of fees and costs of using underlying investment structures (even where the investor would incur these if using the same investment structure); and
2. some amounts that neither the investor nor fund pays (e.g. some costs paid by other parties including costs paid by tenants in a property, fees paid by the borrower in a mortgage or peer-to-peer lending scheme).

Technically, these two complicating inclusions arise as they are costs that affect the consumers return and they also have some anti-avoidance aspects.

In broad terms, this pre Stronger Super Reforms regime is the disclosure regime that continues to apply for MIS.

The Stronger Super Reforms modified many of the relevant fee definitions and inserted new ones for superannuation products (largely because of the MySuper changes) that, most relevantly, did not specifically include the carve out for costs that an investor would incur if they invested directly (including Transactional and operational costs). The view, implicit in RG 97, that ASIC has taken is that the Stronger Super Reforms put in place a new regime for superannuation that looks to all costs affecting consumer returns. In principle this could extend to anything that potentially reduces revenue or income received through the investment chain down to the operational costs of listed companies. Part of ASIC's task in developing RG 97 has been to moderate and clarify the extent of such impacts by, for instance, reinforcing that cost disclosure does not extend beyond what is identified as an asset.

This outcome is perhaps harder to describe to consumers in simple terms: disclosure now extends beyond the costs that a direct investor would incur if they invested directly and extends to all costs incurred by any party down to the asset level but not including the cost of the asset

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<sup>121</sup> Based on ASIC Report 398, it appears that some product Providers were not aware of, or chose not to apply these inclusions either.

and a few specific exceptions. Understanding this statement requires understanding about what is a cost and what is an asset.

The Stronger Super extension described above also complicates the narrative as between fee and cost disclosure and investment returns. Consumers would understand that money is spent, and costs are incurred, in generating investment returns. The returns on any investment, business or enterprise are affected substantially by the business costs of the activities that produces revenues, income, gains, and ultimately, net returns. These costs are reflected in the net return outcomes. The line at which these cost impacts (disclosed as part of net investment returns) should be differentiated from those that are disclosed as fees and costs, lies at the heart of many of the points under discussion.

The objective at this point is not to seek to re-cast the consumer message (this is discussed further in Chapter 8.3) but to identify if there are elements that help in assessing the preferred treatment of fee items.

### 7.5 Application of the suggested methodology

**[Recommendation 24]** I recommended that ASIC apply the characterisation methodology set out in Chapter 7.3 in reconsidering the commonly raised issues listed above and in considering other points that will inevitably arise over time.

It is not appropriate or practically possible for this Report to make specific, considered, recommendations on individual issues given that ASIC would be in a much more informed position to make assessment of issues such as the likely impacts on investment behaviour and the ability of some treatments to be gamed. Issues around consistency with public messaging are also somewhat within ASIC's control as it can influence the messaging and supporting educational material in a way that can not be done by this Review.

Notwithstanding the above, observations are set out below about how the above methodology might be applied to some of the key individual issues raised during consultation.

### 7.6 Transactional and operational costs

A number of issues raised relate to how Transactional and operational costs are disclosed. No doubt, this is the most difficult and contentious area considered in the Review. It is challenging to balance conflicting considerations such as relevance, consumer usability, complexity of treatment, international trends and the practical challenges of collecting various components of transactional costs. Whilst some observations and suggestions are set out below, it is acknowledged that there is scope for different views as to the appropriate outcomes in this area.

Transactional and operational costs are defined in clause 103 of Schedule 10. The definition, both in its original and modified form, does not provide any descriptive explanation of the term but merely sets out a list of included items. Originally, the inclusive part of this definition only included more obvious costs associated with acquiring or disposing of an asset (i.e. brokerage, buy-sell spreads, settlement costs, clearing costs and stamp duty), but the definition has been extended/clarified, by modification, to include others such as property operating costs and certain types of implicit transactional costs.

The inclusive part of the original definition only includes items that could be considered as traditional transaction costs. In the absence of any definitional assistance the scope and meaning

of “operational costs” remains particularly unclear. It is also not clear why the one defined term aggregates quite different concepts of “transactional” and “operational” costs. Operational costs, considered at their widest, could include operational costs associated with assets (e.g. property operating costs and borrowing costs) as well as costs associated with operating the scheme or fund. This aggregated treatment is not evident in any of the other jurisdictions reviewed in Chapter 4.

Currently, Transactional and operational costs are not disclosed as an item in the Fee Template. However, for superannuation products, most transactional costs incurred by the fund or Interposed vehicles are also included in either Investment fees or in Indirect costs and are therefore disclosed within a larger composite figure within the Fee Template (and consequentially the Fee Example).<sup>122</sup> Implicit transactional costs are a part of transactional costs however they are not included in Investment fees or Indirect costs on the basis that they are a part of the costs of the asset,<sup>123</sup> although the buy-sell spread of a MIS (clause 103(1)(b)) is an exception to this in some circumstances.

For MIS, some or all Transactional and operational costs might fall within the definition of Management costs, however they are excluded from the definition of that term.<sup>124</sup> Consequently, MIS Fee Template disclosure does not include Transactional and operational costs (except those relating to OTC derivatives).<sup>125</sup> It is this treatment that largely drives the quantum of differences in disclosure between superannuation funds and MIS.

Both superannuation and MIS funds do however need to disclose details about Transactional and operational costs (including implicit costs) and borrowing costs in the AEFC.<sup>126</sup> Those details include the amount, how and when the costs are recovered and for Transactional and operational costs whether any part of the buy-sell spread is paid to the product issuer or an external manager.

As summarised above, the disclosure status of Transactional and operational costs is quite complicated because of the overlap in treatment of different defined terms, the differences between MIS and superannuation funds, the differences between explicit and implicit costs, the special treatment for borrowing costs,<sup>127</sup> the special treatment for costs of OTC derivatives and the transitional treatment of certain items, such as property operating costs. To some extent, this complex outcome is not surprising given that transactional costs would generally be seen to be testing the limits of where cost impacts should be treated as a disclosable fee or cost versus an impact that is part of the investment process and reflected within the net return outcome.

During consultation, many expressed concerns that the disclosure of elements of Transactional and operational costs in both the Fee Template and the AEFC for superannuation is confusing and often misunderstood in practice. Advisors also expressed some confusion about how to deal with this repeated disclosure.

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<sup>122</sup> There is a transitional exception for property operating costs from Fee Template disclosure until 30 September 2019, see clause 103(1A) and clause 209(ma) of Schedule 10.

<sup>123</sup> See ASIC Q&A number 16 and number 18, RG 97.53 and Example 2 at RG 97.167.

<sup>124</sup> Clause 102(2)(b) of Schedule 10.

<sup>125</sup> Noting however that RG 97.45 encourages MIS Providers to include a sample ratio and dollar figure that combines Management costs and Transactional and operational costs.

<sup>126</sup> Clause 209(j) of Schedule 10.

<sup>127</sup> It is noted that technically borrowing costs likely fall within Administration fees or Investment fees as well as Transactional and operational costs although they are discussed here as an item analogous to operational costs.

Looking to the methodology proposed in Chapter 7.3, some Transactional and operational costs (as defined) are currently treated as Category 1 (i.e. included in the Fee template and Fee Example as a component of other fee items for superannuation products) and some are treated as Category 2 (i.e. set out in the explanation in the AEFC) although some only transitionally. Borrowing costs have, by modification, been excluded from the definition of Transactional and operational costs and other fee definitions and have been treated as a separate Category 2 item, on the basis that they might be distorting.

The key challenge in considering the place of transactional and operational costs disclosure is their relevance and reliability as a comparative indicator.

Transactional and operational costs are necessarily calculated on a backward-looking basis (they are currently determined by looking to the last financial year, although it is noted that in some jurisdictions this is done as a multi-year average) and disclosure practices suggest that industry feel uncertainty around the forward reliability of such figures (many PDSs include warnings in the Fee Template that the figures can vary and should not be relied upon as a guide to future costs). As noted under the international review above in Chapter 4, the only systems other than the Australian superannuation fees and costs disclosure requirements that includes transactional costs as part of their main comparative fee disclosure tool is EU PRIIPS and, in a limited way, Dutch pension funds. In both cases, it is unlikely that asset related operational costs (such as property operating costs) would be included. In the US, transactional costs are explicitly excluded from comparative consumer level disclosure. Nevertheless, it could be observed that the international trend is towards more inclusive fee disclosure.

Unlike traditional intermediation fees, transactional costs could on one view be seen as much more intimately connected with the investment decision. Some suggest that the impact and relevance of transaction costs can not be properly considered separate from the investment strategy, its risk and its returns. Some elements of transactional costs are controllable, but some are not: it is possible to reduce transactional costs for a given strategy by negotiating better terms with brokers, custodians and other suppliers; it is not however possible to reduce the transactional costs of a mid-cap Australian equity strategy relative to those of a passive US large cap equity strategy. In its report to the FCA, Novarca International Ltd states<sup>128</sup> that:

‘It would be misleading to report transaction cost data without also reporting risk and return data for the portfolio. A passively managed, AAA bond fund will necessarily have lower transaction costs than an actively managed, emerging markets equity fund. This does not imply that the bond fund offers better value for money than the equity fund.’

This conclusion supports the analysis in Chapter 3 that relevant consumer decision-making is a difficult task: different factors and different types of fees and costs will be relevant depending on the type of decision being made. For a consumer making a choice between an equity option and a bond fund option within the one superannuation fund, the relevance of transactional costs within a compound fee and costs figure raises difficult questions of principle. Unlike some other parts of the compound costs figure, the transaction cost part is largely a natural, and partly unavoidable, attribute of the asset class. On the other hand, for a decision based on comparing two actively managed Australian equity options in two different funds, incorporating

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<sup>128</sup> Novarca International Limited, 2014 at page 26.

transactional costs data into the decision-making process would be more relevant as differences would reflect something other than the attributes of the asset class.

Another factor that makes transactional costs difficult for a consumer to factor into decision-making is the complexity around who pays for these costs. Some parts of total transactional costs will be paid for by members who are investing into or withdrawing from the fund through the buy-sell spread of the fund. Others will, in effect, be shared proportionately by ongoing investors. While clause 209(j)(iii) of Schedule 10 requires that the AEFC contain details about how Transactional and operational costs are recovered, it would be quite challenging for a consumer to understand how these various disclosures interact and how Transactional and operational costs will affect them. This type of complexity would challenge even professional advisors or analysts.

How Transactional and operational costs sit with consumer expectations is difficult to assess. As pointed out above, transaction costs could be seen to be testing the limits of where cost impacts should be treated as a disclosable fee or cost versus an impact that is part of the investment process and properly reflected within the net return outcome. It seems most unlikely that consumers would understand the nature of the various components of implicit transactional costs, nor understand how they are a part of fee and cost disclosure. Operational costs such as property operating costs could also be understood as being more related to the narrative about returns rather than fees and costs (being the activities necessary to generate a return from the property, enterprise or asset).

An incidental, but substantive, impact of removing all Transactional and operational costs from the Fee Template and Fee Example would be that this would bring alignment of superannuation and MIS fee disclosure much closer. It would also remove overlap between the Fee Template and the AEFC (i.e. Transactional and operational costs would no longer be included in both the Fee Template and the AEFC).

A view could therefore be formed, as suggested by many in the industry, that all Transactional and operational costs for superannuation should be treated as Category 2 (disclosed in the AEFC but not in the Fee Template or the Fee Example). There are however several potential disadvantages to this robust approach:

1. such treatment effectively denies most consumers the value of including transactional cost impacts in decisions where it is relevant (few would look beyond the comparative tools for such information);
2. an approach that treats all elements of Transactional and operational costs in the same manner ignores the substantial differences in the nature of the various sub-components;
3. simply moving all Transactional and operational costs to the AEFC does not address any of the practical challenges associated with collecting and calculating such data;
4. such treatment might be seen as a material reversal in the local and international trend of expanding, rather than reversing, the inclusiveness of fee/cost disclosure, including transactional cost impacts;
5. this may also be seen as fundamentally contrary to the policy direction contained within the Stronger Super Reforms; and

6. there may also be concerns about the extent to which this treatment would affect investment behaviour or is gameable – structures could be used to move costs from fee elements to transaction costs.

If the view were taken that it is not appropriate to treat all Transactional and operational costs as Category 2, then it is necessary to consider, at a more granular level, the treatment of individual components of Transactional and operational costs. Whilst there is some overlap, the types of costs that might be considered to be transactional and operational costs could be broken into the following components:

1. explicit transactional costs;
2. implicit transactional costs including:
  - a. market maker spreads;
  - b. market spreads;
  - c. market impact costs; and
  - d. implementation shortfall; and
3. operational costs including:
  - a. costs relating to operating an asset; and
  - b. costs relating to operating a product.

As noted above, the existing approach already applies different treatment to different elements (e.g. borrowing costs, some operational costs and implicit transaction costs).

#### Operational costs

If the view were taken that it is not appropriate to treat all Transactional and operational costs as Category 2, then consideration can be given to treating some or certain types of operational costs as Category 2, 3 or 4.

The intention of including “operational costs” is not explained in the Explanatory Statement to the 2005 Amendment Regulation. At one extreme operational costs might capture all costs associated with operating a product although this interpretation results in almost complete overlap with other defined terms including and Management costs (inserted in the 2005 Amendment Regulation) and Administration fees (inserted subsequently). This would be a nonsensical interpretation given the way that clause 102(2)(b), in its enacted form, excluded operational costs from the definition of Management costs. The intention must have been that operational costs comprised something much narrower.

The construction of the term is not greatly assisted by reference to the included items originally set out in clause 103 (i.e. brokerage, buy-sell spreads, settlement costs, clearing costs and stamp duty) which relate more to “transactional costs”. It could be argued that, as a matter of construction, the list of included items is narrow (relating to costs arising from the act of acquiring or disposing of assets), suggesting an intention to limit the defined term “Transactional and operational costs” to costs associated with the operational process of acquiring or disposing of assets. Even if this is extended to the costs associated with the ongoing process of holding assets (e.g. custody arrangement costs), this could be distinguished from the costs associated with (a) the operation of a business or asset itself and (b) the costs of operating a product.

The Explanatory Statement to the 2005 Amendment Regulation does note<sup>129</sup> that property operating costs and the costs incurred within listed companies of which a fund holds shares would not be Management costs, only because of the effect of the exclusion in clause 102(2)(h). This is illuminating in that it suggests an intention in the original drafting, that neither satisfied the definition of Transactional or operational costs which were already subject of a separate exclusion (clause 102(2)(b)).

It is therefore difficult to come to any clear view as to what, if any fee or cost elements were intended to be captured by “operational costs” in clause 103 of Schedule 10. This issue was not however one that was raised during industry engagement suggesting that practically, most have focussed on the part of the term relating to “transactional” costs, excepting, as discussed below, property operating costs.

ASIC has clarified the scope of the term somewhat by adding “(ec) property operating costs” into the definition of “Transactional and operational costs” through ASIC Instrument 2017/664. Not being a transactional cost, property operating costs must be considered to be a type of operational cost.

The inclusion of property operating costs within “Transactional and operational costs” and within the scope of the broader term Investment fees (for superannuation products) has been repeatedly raised as a major issue of concern by industry. The effect of those inclusions is that property operating costs are disclosed by MIS and superannuation products within the AEFC<sup>130</sup> and also within Investment fees for superannuation products (subject to transitional exceptions).<sup>131</sup>

Consideration is therefore given to whether “operational costs” or the subset of “property operating costs” should be disclosed in a manner different from the current requirements. Initially, I had thought it preferable to review the treatment of all “operational costs” as a class, but given the uncertainty around the scope of the term and the focus of industry concerns on the subset of “property operating costs” and not other types of “operational costs”, discussion below is limited to “property operating costs”. Those considerations might however extend, by analogy, to borrowing costs as well.

Looking to the methodology set out in Chapter 7.3 property operating costs are, like most transactional costs, backward looking. I have no basis to come to a view as to whether they are more or less reliable as a forward indicator than most transactional costs.

In terms of whether property operating costs are objectively certain, it is noted that many questions have been raised during the review, and in previous correspondence between industry and ASIC about what should or should not be counted as a property operating cost. Very fine distinctions have arisen, for example, in relation to whether a particular expense is incurred by or on behalf of a tenant or on behalf of the product. No doubt these issues can be substantially resolved and clarified over time, however, until that occurs it is difficult to be confident that different providers are applying the same methodology.

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<sup>129</sup> Explanatory Statement Select Legislative Instrument 2005 No 1 at pages 7-8.

<sup>130</sup> Clause 209(j) of Schedule 10.

<sup>131</sup> See the definition of Investment fees in clause 209A of Schedule 10 as modified by CO 14/1252.

The materiality of, and potential distortion caused by, including property operating costs in composite fee figures appears to vary substantially between funds and between investment options. For MIS<sup>132</sup> data provided by Morningstar states that the average net property operating cost disclosed for MIS is 0.03% and the highest amount disclosed is 3.33%. Summary figures for superannuation products are more difficult to obtain.<sup>133</sup> Based on my own sampling of the PDS of five of the largest FMP superannuation funds, the average property operating costs across the 59 investment options offered (46% of which were non-zero) is 0.09%. For the property investment option within those 5 products the average was much higher at 0.175% with a wide range from 0.08% to 1.70%.

Comparing these figures to amounts relating to borrowing costs (which are treated exceptionally due to the possible distortion effect) is somewhat inconclusive – for MIS the Morningstar analysis states that average borrowing costs are 0.06% (as against 0.03% for property operating costs). My own sampling of the five large FMP superannuation funds shows that borrowing costs are on average lower than property operating costs: 0.04% across investment options as against 0.09% for property operating costs. Maximum amounts disclosed, based on the same data sets is for MIS 1.99% (property operating costs) against 4.17% (borrowing costs) and for the 5 superannuation funds 1.70% (property operating costs) against 0.45% (borrowing costs).

It is perhaps not surprising that borrowing costs in superannuation funds are relatively lower than MIS given borrowing restrictions. Relativities between borrowing costs and property operating costs might also be different across a broader data set including retail funds, however it is apparent that there is much variation fund-to-fund which makes it difficult to assess whether, in general, property operating costs are more or less material (and potentially distorting) than borrowing costs. It is clear however that they are more material for some funds.

Industry representatives have provided me with analysis based on real investment examples that, in their view, shows that the inclusion of property operating costs, distorts disclosure by making property investments look more expensive than other investment approaches and could mislead consumers where similar property assets are accessed through different structures. The latter point is addressed, in part, by the way that Interposed vehicle is defined<sup>134</sup> such that vehicles having the same investment objective should disclose the impact of property operating costs in the same manner. Industry representative would assert however that this amplifies the distortion impact on property investments vis-à-vis other asset classes – funds that have high exposure to property as an asset will look more expensive relative to funds investing in other asset classes. As a matter of principle, this should not matter if cost impacts are treated as a subsidiary factor when making asset allocation decisions,<sup>135</sup> however it has to be acknowledged that consumers might not act in a such a logical manner.

Providers also raised concerns about the cost and effort involved in collecting property operating costs given that such costs are not captured through existing custodial and administrative arrangements and the diverse nature of such costs, although I do note that most should have

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<sup>132</sup> This is not required to be disclosed the Fee Template or Fee Examples for MIS.

<sup>133</sup> Morningstar data is based on a limited sample the average being 0.01% but the noted maximum is only 0.26%.

<sup>134</sup> Clause 101B(4) of Schedule 10.

<sup>135</sup> See the discussion under Choice 6 in Chapter 3.2.

some system in place given that the data collection obligation has now been in place for some time.

Internationally, it appears that in most jurisdictions reviewed, costs such as property operating costs were not included in consumer-level fee disclosure regulations or other requirements.<sup>136</sup> The only jurisdiction identified as having a direct reference to property operating type costs at consumer level is the Netherlands pension system (Case study 5 in Chapter 4.2) where such costs are specifically excluded from being treated as a transaction costs. It seems unlikely that any other disclosure system reviewed would include such costs within consumer level fee and cost disclosure.

Looking to treatment of analogous items, operational costs relating to most other assets (such as the operational costs of most listed companies<sup>137</sup> or some infrastructure assets<sup>138</sup>) are already excluded (treated as Category 4) as a consequence of the Interposed vehicle test and as a consequence of an interpretation that the operational costs associated with a share in a company does not include the operational costs of the businesses of that company. The exceptional treatment of borrowing costs on the basis that they might distort disclosure is, as noted above, arguably just as relevant to property operating costs.

Perhaps most relevantly, on one view, costs such as property operating costs are more closely related to the narrative about net returns rather than fees. These types of cost are, arguably, more closely associated with investment outcomes (the costs of generating returns) than the cost of making or even maintaining an investment. It seems unlikely that this type of cost would be within consumer expectation of a fee and cost disclosure regime, although consumer messaging could be adjusted accordingly.

Leaving property operating costs out of the key comparative tools would not necessarily deny interested consumers or other users access to such information but could disclose it in a more appropriate manner for likely use.

In summary, I am of the view that there is a case for removing property operating costs from comparative disclosure tools (for superannuation) and to separate them from disclosure of other Transactional and operational costs in the AEFC (for MIS and superannuation products). The most incremental approach to this would be to leave property operating costs for the previous year within the AEFC. In effect this would preserve the transitional treatment for property operating costs for superannuation products. I can however see a case for moving property operating costs and borrowing costs and some implicit transactional costs, outside of the PDS. This is discussed further below.

#### Implicit transactional costs

Transactional costs can be considered in two parts. The traditionally understood part (referred to as explicit transactional costs) includes observable costs for transactional services, such as brokerage, settlement costs, clearing costs and stamp duty. Other transaction cost impacts that are generally not objectively observable are described as implicit transactional costs. These can

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<sup>136</sup> Note however that these costs are emerging in institutional level costs disclosures in the UK. See the Local Government Pension Advisory Board, Investment Code of Transparency February 2018.

<sup>137</sup> Not including, for instance, listed investment companies which might satisfy the Interposed vehicle definition.

<sup>138</sup> On the basis that economic exposure to infrastructure assets would commonly be obtained by acquisition of an asset that operates the infrastructure business.

be rather more difficult to characterise but include costs that are usually embedded in the price paid for an asset and include several (not necessarily mutually exclusive) components:

1. the bid-ask spread imposed by a counterparty/market-maker;
2. the bid-ask spread that applies in quote driven markets;
3. the market price impact caused by the transaction;
4. OTC mark-ups; and
5. implementation shortfall (the difference in price between the decision to trade and the execution of the trade).

Schedule 10 and RG 97 do not reflect the components above but refer broadly to the difference between the acquisition price of the asset and the price at which the asset could be disposed of.<sup>139</sup>

Explicit transaction costs are generally included as part of Investment fees or Indirect costs for superannuation products. Implicit transactional costs (except for certain OTC derivatives costs) are not included in Investment fees or Indirect costs on the basis that they are a part of the cost of the asset. As such they do not get included in the Fee Template or Fee Example.<sup>140</sup> They are however required to be collected, uplifted and disclosed as part of Transactional and operational costs within the AEFC for both superannuation products and MIS.

Many points of concern were raised by stakeholders regarding the need to calculate, uplift and disclose implicit transaction costs, even though they are not included in key comparative tools (the Fee Template and the Fee Example). Numerous comments were received about the different methodologies that could be applied in calculating or estimating implicit transaction costs. Some urged that ASIC should prescribe a single methodology, others argued that this should not be done as different methodologies were more or less relevant depending on the asset type and investment strategy being adopted.

It is noted that there can be many points of difference in calculation methodologies used globally, including:

1. the extent to which spreads are relied on as a measure of market impact;
2. whether to use full or half spreads;
3. whether to use acquisition price or arrival price;
4. the timing for calculating arrival price (if acquisition price is not used);
5. the timing for calculating execution price;
6. how to deal with multiple, sequential and broken orders;
7. how to deal with orders that are not executed within a single day; and
8. how or whether to adjust for market movements.

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<sup>139</sup> Refer to clause 103(1)(ea) and (eb) and RG 97.53, 104 and 118.

<sup>140</sup> Although query whether they would be included in the ratio and dollar example that RG 97.49 encourages MIS Providers to include.

As set out in Chapter 4.2, the EU PRIIPS Regulation does require disclosure of all transaction costs on a basis that includes implicit costs. The methodology is prescribed within the PRIIPS Regulation and in particular points 12 to 18 of Annex IV to the EU Commission Delegated Regulation 2017/653.

In summary, the relevant Annex provides that “transaction costs” (for any type of “transferable security”) are calculated by subtracting the “net realized execution price” from the price of the instrument at the time the purchase order is transmitted to another person for execution (the “arrival price”) and multiplied by the number of units purchased (vice versa for each sale). The “net realized execution price” is the price at which the transaction was executed, including all commissions and taxes. The arrival price is the mid-market price of the investment at the time when the order to transact is transmitted to another person. For private equity, the calculation could include the use of best estimates adopting, as proxies, either a comparable PRIIP or a peer group. For new PRIIPs that have been operating for less than 3 years, transaction costs are calculated either based on an estimate of the portfolio turnover in each asset class (using a methodology based on reference indices) or an average of the actual costs incurred during the period of operation’

As a relatively new requirement, there have been numerous challenges and concerns with implementation. The major consumer level concern is that the prescribed methodology does not adjust for market movements between the arrival price and the execution price. Whilst this might not matter at a systemic level (the short-term impacts tend to cancel themselves out across the whole market), this can, and has, produced negative transactions costs for individual products. In some cases the quantum of negative transaction costs has been so great that total fees have also been negative. Many have expressed the view that the PRIIPS approach to disclosing implicit transaction costs is distorting and confusing for consumers<sup>141</sup> (in the case of negative costs implying for example that the provider will actually pay the consumer to invest in the product).

How or whether EU authorities will respond to these concerns is not fully known at this time. For the purposes of this Review, the EU experience simply illustrates that implicit transaction costs can be quite material and can distort consumer level disclosure outcomes depending on the calculation methodology. A common, accepted, methodology for calculating implicit transaction costs is yet to emerge. Some comments were provided during industry meetings that a common methodology is in any event unhelpful as different methodologies would be relevant to different analysis depending on the asset type and investment strategy being adopted. Whatever methodology is adopted, there will also be concerns about forward reliability given that reliance will have to be placed on previous periods and/or assumptions and approximations. In some cases, assumptions based on typical market averages are used. The use of averages is not at all helpful as a comparative tool (there is no point in comparing products if they use the same assumed figures) but might be informative for analysis purposes.

In terms of the characterisation methodology suggested in Chapter 7.3, implicit transactional costs including market impact costs are quite unreliable as a forward-looking indicator. Like other transaction costs they are necessarily based on past data and they are transaction specific (and therefore are dependent on trading strategies). Unlike explicit transaction costs, they are to

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<sup>141</sup> See for example Investment Week, 12 June 2018 “FCA’s Bailey promises action on PRIIPs and MiFID II failings”, Investment Week 25 January 2018 “Senior IA adviser calls for ‘heads to roll’ at FCA as he labels PRIIPs worst piece of financial regulation ever” and Ignites Europe, 13 June 2018 “UK industry preps evidence of ‘confusing’ MiFID II cost data”.

some extent subject to different approaches by different operators and are subject to approximations and estimations (particularly for market impact costs). Market impact costs also become more difficult to measure, and therefore more unreliable, for less liquid assets and where assets are not traded on or through regulated markets. Commonly used assets such as real estate and even simple bank products, such as deposits, raise difficult questions of principle, when considering market impact cost calculation and may, as a consequence, involve no calculated market impact costs. Whilst this is a justifiable, practical outcome, it necessarily raises concerns about the relativity of the quantum of fee disclosure across different asset classes and consequentially the manner in which this affects consumer decision-making.

As noted above, it seems most unlikely, given their technical nature, that consumers would understand the various components of implicit transactional costs, nor expect that they are a part of fee and cost disclosure, nor appreciate how they might apply differently for different asset classes.

This supports the current treatment that implicit transaction costs are not included in the key comparative tools, being the Fee Template and the Fee Example. It could also be considered whether some or all implicit transaction costs should not be included with the PDS disclosure requirements, at least until a common, accepted methodology emerges. Where and how this could be disclosed is discussed further below.

#### Counterparty spreads

A qualification to the above discussion about implicit transactional costs is that consideration could be given to treating counterparty spreads (but not other implicit transaction costs) on the same basis as explicit transactional costs. For many products traded on regulated markets, bid-ask or buy-sell spreads charged by counter-parties are readily, and relatively objectively, ascertainable.

The spreads imposed by counterparties are in some respects within the control of the investing party, at least where there is more than one possible counterparty. These types of spreads are also quite analogous to explicit costs like brokerage: dealing with a broker as an agent incurs brokerage or commission costs, whereas dealing with the same broker as a principal incurs a spread cost. In each case the cost covers the broker's actual costs in effecting the transaction and some amount for their service.

This is to be contrasted with the spreads implicit in transactions on quote driven markets. These spreads are not representative of costs or services: they are not paid to any party. These are generally not controllable, although they might be affected by trading strategies such as drip feeding large orders. This type of effect could be seen in the same light as other timing decisions affecting trading and investment outcomes. In this sense, market spreads are in the same category as other timing decisions such as asset allocation decisions and implementation shortfall costs. It should also be observed that market spreads will always be zero at the point of the transaction which can raise fine questions about whether market spreads should be treated as a transaction cost. The distinction between market spreads and counterparty spreads, whilst not a current feature of the approach in Australia, is reflective of the disclosure approach adopted for Dutch pension funds (see Case study 5 in Chapter 4.2).

Treatment of counterparty spreads on the same basis as explicit transaction costs would also overcome concerns that exclusion may incentivise managers to, perhaps inappropriately, adjust

trading practices in a way that will minimise explicit transaction costs, either in terms of the types of assets they acquire, or the method of dealing. Such an approach could also be seen as being more consistent with the original drafting in Amendment Regulation of the definition in clause 103(1) to Schedule 10, which includes the similar concept of “buy-sell spread” (effectively the spread charged by the counterparty operating an underlying MIS).

I accept that the benefits of including counterparty spreads on the same basis as explicit transaction costs would need to be balanced against the costs and effort involved in obtaining and extracting such data, the resultant complexity of yet finer distinctions, and the ongoing challenges in achieving calculation consistency across different types of assets traded on different types of markets. I do, however, consider that if such costs are not incorporated into comparative fee disclosure, then the arguments for excluding other elements of implicit transaction costs from the AEFC disclosure become much weaker.

#### Transactional and operational costs - consequential impacts

On the basis of the discussion above, ASIC should consider separating disclosure of explicit transactional costs and counterparty spreads (referred to as **Disclosed T&O costs** below) from other Transactional and operational costs (including property operating costs) and borrowing costs (referred to as **Excluded T&O costs** below).

Disclosed T&O costs meet many of the criteria set out in Category 1 disclosure above. If calculated based on the previous financial period, they are backward looking, however, absent a major change in investment strategy within an investment option, they should, on a percentage basis, be reasonably reliable as a forward indicator year-on-year. Disclosed T&O costs, being more tangible, should be more consistent with consumer expectations of cost impacts that could be relevant to cross product comparison.

There are therefore strong arguments for including Disclosed T&O costs in the comparative tools (the Fee Template and Fee Example). As identified above however,<sup>142</sup> transaction costs can be meaningful as a comparative indicator in different circumstances from Administration fees and Investment fees. Transactional costs might be most relevant in a choice between similar investment strategies across funds (the relative level of transaction costs would give an insight into trading efficiency and trading frequency) but comparing transaction costs at the fund level or for different types of investment strategies, becomes less relevant because it could be reflective of any number of variables not relevant to the decision being made.

Including transactional costs within an aggregated figure (e.g. within Investment fees and costs for superannuation or Management costs for MIS) brings with it the disadvantage that consideration can not be separated in circumstances where it is relevant to do so. As always, the advantages of separating disclosure elements need to be balanced against the disadvantages of increasing complexity for consumers who may struggle to add multiple lines of data. On balance, I see advantages in this case of showing transaction costs (Disclosed T&O costs) as a separate line in the Fee Template. To ensure appropriate segregation, Disclosed T&O costs would need to be excluded from other fee type definitions (such as Investment fee or Indirect costs). For consumer facing purposes these costs could be described in an abbreviated manner,

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<sup>142</sup> See “Different costs – different relevance” in Chapter 3.2.

such as “Transaction costs (net)”. A proposal as to possible layout is contained with Diagrams 6-1 and 6-2 in Chapter 6.6 above.

The consequential question is whether the transactional costs so disclosed should be included in the Fee Example calculation: is the nature of transaction costs so different that including them in the single illustrative “Cost of Product” figure is of no net benefit to consumers? There are clear advantages in terms of simplicity and avoiding gaming in keeping the Fee Template and Fee Example as closely aligned as possible. On the other hand, transaction costs can be of doubtful relevance, depending on the decision being made. A solution that involves calculation of two different “Cost of Product” calculations, one including transaction costs and one excluding them, is probably not workable within a PDS, given the need to also explain when one or the other figure is relevant. Without a better understanding of how consumers are likely to use the “Cost of Product” calculation, it is difficult to form a view either way. On balance, perhaps the preferred direction is that unless, or until, it can be shown through consumer testing that transaction costs are not relevant to the decision being made in most cases, and there are no material concerns about possible gaming, then transaction costs as disclosed in the Fee Template should also be included in the Fee Example and the abbreviated “Cost of Product” figure proposed in Recommendation 13 (Chapter 6.7).

For Excluded T&O costs, the most incremental approach would be to include figures for the previous year within the AEFC but not in the Fee Template and the Fee Example (i.e. the current requirements for implicit transactional costs and the transitional requirements for property operating costs in superannuation products). The alternate position to consider is whether disclosure of these items should be left outside of the consumer level point-of-sale disclosure regime completely.

The discussion above is not suggesting that implicit transactional costs or operational costs are unimportant in a broader context. Both tell important pieces of information that should be of interest, at a minimum, to analysts, professional investors and fiduciaries in making the types of decisions that they make. In the UK, significant effort is being made in developing common standards so that implicit transaction costs can be better disclosed to fiduciaries<sup>143</sup> (such as independent governance committees of group personal pension plans and trustees of occupational pension plans). Implicit transactional costs can also be material: one study suggests that the mean market impact costs for a round trip trade for active Australian equity managers is 0.27% of the trade cost<sup>144</sup> although figures would likely be much lower for a typical balanced investment option as a percentage of fund size. As fiduciaries, trustees of Australian superannuation funds should, for example, understand and consider the transactional efficiency of managers and funds that they invest members contributions into. Property operating costs may also be of interest to the same group. These items might not however be of general interest to consumers. There is an argument that this type of data should be available to those consumers and other stakeholders such as analysts who are interested, however this needs to be balanced against the effort and cost involved in collecting and presenting this data in a meaningful and consistent manner. Most Providers should already have systems in place for collection of such data but there would be ongoing and developmental costs incurred that will ultimately flow back to all members of relevant funds whether or not they are interested in, or use, the data.

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<sup>143</sup> Financial Conduct Authority, September 2017; Novarca, December 2014.

<sup>144</sup> Gallagher & Looi, An Examination of the Market Impact Costs of Active Australian Equity Managers.

Another point of relevance regarding AEFC disclosure is that, based on current requirements, items appearing within the AEFC need to include the same items uplifted from Interposed vehicles. This incurs even more effort and cost. There is a benefit in having consistency in uplifting requirements for all items that appear in the PDS. The purposes for which implicit transaction costs and operational costs would be reviewed by interested users would not necessarily need to adopt the same approach however. As an example, for a trustee of a superannuation fund investing into a sectoral equities fund, the implicit costs of effecting transactions should be an issue of interest, but whether the trustee is interested in information on a fund stand-alone basis, or on an uplifted basis, would be a matter for the trustee. Provided that the basis and methodology of calculation is made apparent, perhaps it is not necessary that Excluded T&O costs always be presented on an uplifted basis to show the costs incurred by Interposed vehicles.

It should also be noted that inclusion of transaction and/or operational costs in both the Fee Template and the AEFC, will, as now, raise questions and confusion about their relevance to decision-making.<sup>145</sup> Where it is possible to do so, including the same or similar information in both parts should be avoided, although it is recognised that other requirements in clause 209(j) of Schedule 10 require some information about transactional and operational costs in the AEFC in any event. It may be preferable that the clause 209(j) requirements only expand on data set out in the Fee Template rather than import other data content.

This is a finely balanced issue for which there are generally three options:

1. include the Excluded T&O costs in the AEFC;
2. conditionally exempt disclosure of Excluded T&O costs from the PDS where:
  - a. such information is provided annually through some other method that is accessible by consumers and other interested stakeholders; and
  - b. the methodology and limitations, including whether it includes amounts incurred through Interposed vehicles, is also explained in the same document or place; or
3. not mandate disclosure of Excluded T&O costs at all.

This is an issue which ASIC might wish to consult more widely on in light of other recommendations and the way forward in relation to those other recommendations. Given the level of concerns raised about collection calculation and disclosure of Excluded T&O costs, the conclusions that I have drawn about the relevance of these items to fees and costs and the preference for a clean and simple outcome for consumers, I would suggest that the starting point for consultation should be option 3 (i.e. not to mandate disclosure of Excluded T&O costs). Such an approach could be reviewed after a set period of say 5 years as data collection and methodology consistency improve having regard to international practices particularly for market impact costs. This can also facilitate an immediate focus on improving the more important disclosure of fee elements in the comparative tools, as opposed to expending efforts immediately on collecting, calculating and uplifted other less relevant data within the PDS.

The above approach would have consequential impacts for disclosure within periodic statements and the alignment of disclosure between superannuation and MIS.

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<sup>145</sup> See the more detailed discussion in Chapter 6.6 under “Presentational issues”.

The suggested approach may leave operational costs that are not related to assets outside of either Disclosed T&O costs or Excluded T&O costs. Presuming that this remaining category comprises only operational costs relating to operating the fund or scheme, these should be treated as included with proposed Administration fees and costs (superannuation) or Management fees and costs (MIS).

**Periodic statements:** If Excluded T&O costs are taken out of the PDS disclosure, as suggested above, then it would also be appropriate that these amounts not be included within the additional fee impact calculations in periodic statements.<sup>146</sup> This will assist the simplification of the Periodic statement as referred to in Chapter 6.9 and Recommendation 16.

**Alignment between superannuation and MIS:** The proposals and discussion above are intended to have application both to transactional and operational costs and related fee items for superannuation products. There would be some definitional work involved in separating Disclosed T&O costs from Excluded T&O costs, so that they are similarly treated within the definitions of Investment fees and Indirect costs (or merged as proposed in Recommendation 11).

As a drafting matter, the issue applies differently for MIS, as transaction costs are not currently disclosed as a part of Management costs but are disclosed in the AEFC. As a matter of principle however, I am of the view that the different approaches to different types of Transactional and operational costs discussed above, based as it is on the utility of the information to consumers, should apply equally to MIS and superannuation products. Changing where some elements are disclosed would not require any more data collection and calculation than MIS do at the moment. Providers of MIS should be able to adjust where items are disclosed without too much additional effort. Whilst this changes the basis and narrative of MIS fee disclosure to some extent, this is a reasonable extension of their disclosure obligations which brings with it the substantive advantage of closely aligning disclosure as between superannuation products and MIS. The current approach of fully excluding transactional costs impacts from comparative fee disclosure for MIS reflects a position that is somewhat out of date and difficult to justify in principle. This has both practical advantages (in terms of how superannuation funds uplift fee and cost information from MIS) and simplifies the narrative to consumers about fee and cost impacts for functionally similar products.

#### Transactional costs – gross or net or amounts recovered from buy/sell spread

An issue related to the discussions above about Transactional and operational costs is how and whether to disclose the impact of cost recoveries made through a fund's Buy-sell spread which is charged to an investor on entry to or exit from the fund. Transactional costs incurred by a fund may to some extent be offset by the buy and/or sell spreads charged to fund members on issues and withdrawals. For superannuation funds, explicit transactional costs are currently reflected in either Investment fees or Indirect costs. Where this is done it is shown on a net basis (i.e. reduced by the amount of any spread recoveries).

As discussed above, transactional costs are particularly difficult for a consumer to factor into decision-making, partly because of the added complexity associated with understanding who pays for these costs. Some parts of total transactional costs will be paid for by members who are

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<sup>146</sup> Affecting for instance clause 303(1)(d) of Schedule 10 and transitionally clauses 301(1B), 301(1)(C), 301(1)(D), 303(1)(c) and 303(1)(d) of Schedule 10.

investing into or withdrawing from the fund through the buy-sell spread. Others will, in effect, be shared proportionately by ongoing investors.

If as suggested above, Disclosed T&O costs are included in the Fee Template under a heading of “Ongoing Annual Fees and Costs” as a separate line, then this should be shown on a net basis. The gross figure of Disclosed T&O costs should be set out in the AEFC in accordance with clause 209(j)(iii) for information and analysis purposes.

#### Transactional and operational costs - summary

In summary, based on the methodology set out in Chapter 7.3, ASIC could, subject to the further considerations identified, consider modifying RG 97 and CO 14/1252 to achieve the following outcomes for both MIS and superannuation funds in relation to Transactional and operational costs:

1. explicit transaction costs and counterparty spreads (referred to as Disclosed T&O costs) be included, for both superannuation products and MIS as a separate line item in the Fee Template;<sup>147</sup>
2. to avoid double disclosure, Disclosed T&O costs be excluded from other fee definitions including Investment fees;
3. Disclosed T&O costs be included in the Fee Example calculation;
4. property operating costs, borrowing costs and implicit transactional costs (other than counterparty spreads) (referred to as Excluded T&O costs) not be disclosed in the PDS and be excluded from relevant definitions;
5. Disclosed T&O costs set out in the Fee Template be shown on a basis net of cost recoveries made via the buy/sell spread;
6. operational costs that are neither Disclosed T&O costs nor Excluded T&O costs (to the extent that any exist) be treated as a part of Administration fee (for superannuation products)<sup>148</sup> or Management costs (for MIS);
7. the gross figure of Disclosed T&O costs be set out in the AEFC as a part of the details required under clause 209(j)(iii); and
8. periodic statements not show the impact of Excluded T&O costs.

Diagram 7-1 Summary of changes to treatment of Transaction and operational costs

Fee/cost item	Where currently disclosed – MIS	Suggested disclosure point (MIS & Superannuation)	Where currently disclosed – Superannuation
<b>Explicit transaction costs</b>	AEFC	Fee Template & Fee Example (Transaction cost)	Fee Template & Fee Example (Investment Fees or ICR) + AEFC
<b>Buy-sell spread of underlying MIS</b>	AEFC	Fee Template & Fee Example (Transaction cost)	Fee Template & Fee Example (Investment Fees or ICR) + AEFC

<sup>147</sup> See Diagram 6-1 and 6-2 in Chapter 6.6 for possible presentation.

<sup>148</sup> Or “Administration fees and costs” if the earlier recommendation is adopted.

Fee/cost item	Where currently disclosed – MIS	Suggested disclosure point (MIS & Superannuation)	Where currently disclosed – Superannuation
Counterparty spread	AEFC	Fee Template & Fee Example (Transaction cost)	AEFC
Market spreads	AEFC	Nil	AEFC
Other implicit costs	AEFC	Nil	AEFC
Property operating costs	AEFC	Nil	Fee Template & Fee Example (Investment Fees or ICR) after transitional period + AEFC
Borrowing costs	AEFC	Nil	AEFC
Other operating costs	AEFC	Fee Template & Fee Example (Administration fees and costs or Management cost)	Fee Template & Fee Example (Administration fee) + AEFC
OTC derivative costs	Nil or AEFC	Alignment between MIS and superannuation products to be further considered in light of directions agreed on other recommendations	Investment fees or ICR generally

As a concluding observation relating to Transactional and operational costs, given the relationship that Transactional and operational costs have to the narrative about returns, further consideration might be given in the longer-term to whether, and how, those costs could be explained within the context of information about returns. Information about elements such as market impact costs and operational costs might be better understood by consumers within information and analysis about returns and return attribution (i.e. what part of gross returns goes to the consumer, the Provider and related parties and what part is consumed by other types of cost impacts). Within that framework, the comparison reference point for consumers moves, at least in part, from the fees and costs of other products, to the return expectations within the product. Greater reliance could therefore be placed on benchmark or market average calculations which would reduce the effort involved in data collection and calculation. To some extent, the same observation can be made about all fee and cost disclosure (see the discussion under Chapter 8.5 “Observations - the future”). I understand that ASIC has a work stream directed at considering presentation of return information and this might be an appropriate framework within which to consider this issue.

**[Recommendation 25]** I recommend that, over the longer term, ASIC give consideration to whether, and how, Transactional and operational costs could be better explained to consumers within the context of information about returns.

## 7.7 Performance fees and performance-related fees

Performance fees are generally treated as a Category 1 type fee (as described in Chapter 7.3), although some explanatory elements are also set out in the AEFC under current requirements. Their disclosure is rather complex reflecting relevant definitions and regulatory concerns about disclosure of such fees. Calculation and disclosure methodology differs depending on whether the performance fee relates to the whole or only part of a fund, whether it is treated as a cost (in superannuation) and whether the fund has a history or not. As a consequence, in some

circumstances the disclosure in the Fee Template is done on a prospective basis (involving estimation) but in most cases it is done retrospectively by looking to the previous financial period. Without unnecessarily reciting all of the related provisions, some of the resultant differences are set out below:

1. for superannuation fund PDSs, a performance fee deducted from the fund payable to the trustee (though rarely if ever actually done in practice) must be included in Investment fees in the Fee Template (RG 97.125) on a prospective basis;
2. for superannuation fund PDSs, a performance fee deducted in an Interposed vehicle may instead be treated as Indirect costs if the trustee elects in writing (RG 97.125). Whether this election is made or not, the disclosure in the PDS is (as for other costs) retrospective, based on actual performance fees charged during the previous financial year;
3. for MIS, a performance fee payable to the responsible entity forms part of Management costs and the formula must be disclosed in the Fee Template. If a quantification of the cost is provided it must be based on the actual performance fees charged during the previous financial year, (clause 104A of Schedule 10);
4. for both superannuation and MIS, performance-related fees<sup>149</sup> that are charged by an investment manager or in an Interposed vehicle, form part of costs (not fees), and as a consequence disclosure would generally be based on the actual performance fees charged during the previous financial year (RG 97.184);
5. where costs are not known (e.g. for new products or early in the financial year) performance fees and performance-related fees can not be based on previous figures so reasonable estimates are used; and
6. for both superannuation fund PDSs and MIS PDSs, the AEFC must include an estimate (“typical ongoing amount”) of the performance fee that will apply on an annual basis for current and future years along with other descriptive information (RG 97.129).

Concerns have been raised during consultation about the complexity of treatment, the methodology for making estimates, consistency of approach, the reliability of the resultant disclosures made, why refunds or clawbacks are not allowed in the Fee Template and Fee Example and the challenges of assessing whether PDS updates are required. In some cases Providers expressed the view that estimates of zero were often being applied because there was no basis to come up with another figure.

First, it appears from my review of current PDSs, that many Providers have misapplied the requirements, particularly those circumstances affected by clause 104A of Schedule 10 which require the use of the previous year figure rather than an estimate.

Whilst the current requirements are complicated to work through (hence the misapplication referred to above) there is policy and technical consistency in the current treatment, for example the impact when a performance fee is treated as a cost rather than a fee. The concerns expressed during consultation and the resultant disclosure outcomes, do however raise questions about

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<sup>149</sup> Technically a performance fee that does not relate to the whole of a fund is not defined as a performance fee hence the different terminology.

whether the disclosure is actually best designed to assist consumers. Three aspects, in particular, warrant further consideration:

1. whether the distinction between performance fees and performance-related fees serves any purpose for consumers use;
2. whether the reliance of the previous year figure increases the likelihood of unreliable disclosure; and
3. whether disclosure requirements can be simplified.

Performance fees and performance-related fees can be quite volatile year-to-year and as a consequence, the use of a single year historic figure or even estimates based on averages might not give a consumer a reliable indication of what will happen year-to-year. Review of data from a sample of 160 investment options provided from industry sources<sup>150</sup> shows variations year to year within funds and also fund to fund. Large diversified funds which may incur performance related fees only in relation to a particular sub-investment show low amounts of performance fees and low volatility, however individual funds with performance fees relating to the whole fund, showed significant variation and volatility. Some highlights from that analysis:

Diagram 7-2 Analysis of performance fee volatility

<i>Item</i>	<i>Result</i>
Number of funds/options sampled	139 (excluding those with less than 3 year history) 84 super/pension investment options 55 MIS
Average performance fee p.a. over past 5 years	0.36% (0.49% for MIS only)
Standard deviation of yearly performance fee over past 5 years	0.52% (notable that average volatility is higher than average performance fee)
Average difference across sample between highest performance fee and average fee of each fund	0.79% (1.15% - 0.36%)
Average difference between last two yearly figures for each fund/option	0.51%
Highest observed difference between one year performance fee and average for that fund	6.0% (7.5% vs 1.5%)
Highest observed difference between one year performance fee and previous year	7.39% (7.39% vs 0%)
Frequency of difference between one year performance fee and average of > 1.0%	26.4% - (30.9% for MIS only)

In considering the criteria in the methodology discussed in Chapter 7.3, arguments can be made as to why performance fees should not be used as a reliable comparative indicator bundled in with more reliable data in the Fee Template and the Fee Example. Performance fees have high volatility year to year which make them an unreliable indicator of future fee impacts whether

<sup>150</sup> Some provided through the assistance of the FSC and some provided at meetings.

their disclosure is based on an average over a period, and even more unreliable when based on a single previous year as is the current requirement. In over a quarter of the cases sampled, the actual result in any given year was more than 1.0% above a long-term average. Performance fees can also be substantial, even on an average basis, meaning that figures that bundle performance fees can be materially distorted by their inclusions. Performance fees also require significant extra explanation and illustration outside of the Fee Template.

Disclosure of performance fees is however important for some of the same reasons that relate to their unreliability – they can be very material and can vary considerably year to year.

Looking to international practice, it is noted that performance fees are excluded from summary figure fee disclosure in UK pensions, are also excluded from the ongoing charges figure in UCITS KIID and the “total annual expenses” figure for US 401(k) plan disclosure. US mutual fund disclosure includes performance fees however they are not uplifted from underlying investment funds. Of the international jurisdiction case studies considered in Chapter 4, only the EU PRIIPS regime includes performance fees in summary fee disclosure.

The above discussion suggests several options for dealing with disclosure of performance fees:

1. firstly, to broaden the calculation basis to a period that is longer than just the previous financial period;
2. to remove the distinction between performance fees and performance-related fees; and
3. reconsider how and where they are disclosed by either:
  - a. treating them as Category 2 and move disclosure to the AEFC;
  - b. leaving them as Category 1 in the Fee Template but separate them from other fee elements as a separate line (as for UCITS); and
  - c. leaving them as Category 1 in the Fee Template as a sub element of other fee lines and use standardised footnotes to explain the calculation and potential impact.

#### Broadening the calculation basis

To reduce the likelihood of large differences between the disclosed amounts and the actual outcome, it is preferable that the quantum of performance fees included within other items (whether Management costs, Investment fees, Indirect costs or a new measure such as a consolidated Investment Fees and Costs as proposed in Chapter 6.6) be calculated/estimated by reference to a longer-term average. Some have questioned whether this is inconsistent with other cost disclosure (e.g. transaction costs) being calculated by reference to a single previous year. The difference in principle is the year-to-year volatility of performance fees.

A longer period is better, although too long a period will create data carry issues and mean fewer, newer funds will be able to fully comply. A period of 5 years appears reasonable, based on the average adopted under EU PRIIPS. The average calculation should also be able to accommodate any negative (clawback) figures for individual years, although the calculated average figure itself should not be negative. Funds without a 5-year performance history should use whatever shorter number of years is available. Funds that did not have a performance fee charging mechanism in place for the full 5 years should only average across those years when a mechanism was in place. Whilst this has the consequence that a cohort of funds will be

providing data in relation to a different time period, this appears preferable to alternatives such as using models or estimations.

Noting practices related to accrual of performance fees over multiple year periods, it would be appropriate to use accrued performance fees in calculating and disclosing the 5-year average where the accrual is reflected in investment returns (e.g. unit price or account valuation).<sup>151</sup>

During consultation, suggestions were made that Providers should have an over-riding discretion to use some other figure where there is a reasonable basis to do so. The advantage to such an approach is that it overcomes the disclosure challenge when a Provider genuinely believes, on a reasonable basis that the 5-year average figure does not represent the likely outcome. The obvious disadvantage is that including discretions for Providers creates uncertainty and greater scope for diverse or inappropriate practices. It also potentially increases the compliance burden for the whole industry as it may create an obligation in all cases to consider whether the 5-year average figure is reasonable or appropriate. This then starts to revert to a test of using reasonable estimates, the uncertainty of which is the reason why the “previous year rule” was adopted in the first place.

Whilst in principle, it may appear odd to prevent adjustment where the Provider believes that the 5-year figure would be inappropriate, in terms of consistency and reliability, it is best that all Providers adopt the same 5-year average rule. In principle, an exception should apply if there is legal certainty that some other figure will apply for the coming period, however it is difficult to see how this could be the case if, as suggested, calculations are based on accruals rather than actual payments in a period. In contrast, absent legal certainty, if there are circumstances where the Provider genuinely believes that the 5-year figure could be misleading for the coming period, this should be explained in the AEFC.

Consistent with, and to support this approach, the AEFC should set out the performance fees for each year of the period used in the calculation. Some have suggested that this should be accompanied by investment performance information for context. Whilst this should not be required, this could be an option open to Providers.

#### Performance fees and performance-related fees

Whilst there are good technical reasons for the current distinction, from the consumer perspective, it should not matter whether a performance fee is incurred at the product level or in an underlying investment vehicle. Relevant definitions in Schedule 10 could be modified to remove the distinction. Merging Investment fees and Indirect costs (for superannuation products) as recommended above helps simplify this approach.

It is recognised that there could be calculation complexities, at least for a transitional period, associated with incorporating performance-related fees into a 5-year average performance fee. Transitional concessions may be necessary in this respect. The methodology for calculating averages that incorporate and pro rate performance fees related to Interposed vehicles will require some detailed consideration.

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<sup>151</sup> This is consistent with Question 10 in the ASIC Q&A.

### Layout options

Option (iii)(a) (treating performance fees as Category 2 and moving them to the AEFC) has the advantage of moving the relatively unreliable and, necessarily, backward looking performance fees outside of the key comparative tools. This could be supported by the inclusion of a note in the Fee Template that the figures do not include performance fees which can vary substantially year to year which are explained in the AEFC. This approach also has the advantage of encouraging greater focus on the volatility and possible impact of performance fees.

The disadvantages to such an approach are that it removes a significant fee element from the fee comparative tools and may provide incentives to Providers to inappropriately extend the use of performance fees. Examples have been observed in the PDS where the totality of the fee (comprising the excess returns above a stated return) is treated as a performance fee.

Option (iii)(b) (leaving them as Category 1 in the Fee Template but separating them from other elements as a separate line) would maintain performance fees disclosure within the Fee Template but separate their disclosure from the more forward-looking fees in the Fee Template as a separate line item. An example of separating the disclosure of performance fees is the KIID for UCITS in the EU as displayed in Diagram 4-3. This overcomes some of the potential disadvantages of option (a) but complicates the layout of the Fee Template somewhat and departs from the manner in which the Fee Template reflects the defined fees (a performance fee is merely a component of a defined fee type).

Option (iii)(c) (leaving them as Category 1 in the Fee Template as a sub element of other fee lines and using standardised footnotes to explain the calculation and potential impact) is closer to some existing practices. Rather than include a separate line for performance fees, the Fee Template could contain an additional footnote that the relevant fee item (Management costs, Investment fees, Indirect costs or a new measure such as a consolidated Investment Fees and Costs as proposed) which could state as following:

‘Investment fees and costs includes an amount of x.xx% for performance fees. The calculation basis for this amount is set out under “Additional Explanation of Fees and Costs”.

This option is illustrated in Diagrams 6-1 and 6-2 above in Chapter 6.

On balance, for the reasons discussed above, it is suggested that option (iii)(c) be adopted.

### Performance fees – summary

Based on the discussion above and the methodology set out in Chapter 7.3, ASIC should consider modifying RG 97 and Schedule 10 to achieve the following outcomes in relation to performance fees and performance-related fees:

1. relevant definitions be amended such that the distinction between performance fees and those amounts described as performance related fees be removed (i.e. performance fee should include amounts calculated by reference to performance of a product, part of a product, an Interposed vehicle or part of an Interposed vehicle);
2. the amount of performance fees included in the Fee Template (as a component of Management costs, Investment fees, Indirect costs or a new measure such as a consolidated Investment Fees and Costs) be calculated by reference to the average of the performance fees that accrued in the fund and Interposed vehicles in each of the previous 5 years;

3. where a fund was not in operation for the previous 5 years or did not have a performance fee charging mechanism in place for the full 5 years, then the average should be calculated by reference to the number of years in which the fund operated or had a performance fee charging mechanism in place;
4. transitional arrangements may need to accommodate data availability, particularly for Interposed vehicles, in the first 5 years of calculation;
5. the Fee Template contain an additional footnote referring to the AEFC (as illustrated in Diagrams 6-1 and 6-2);
6. the requirements for AEFC set out in clause 209(b)(i) and (ii) be maintained;
7. the requirements for AEFC set out in clause 209(b)(iii) be replaced by a requirement that the AEFC should set out the performance fees that accrued for each year used in the calculated average;
8. the AEFC may also set out related performance information where the Provider chooses to do so; and
9. the AEFC may also set out further explanation in circumstances where the Provider believes that the 5-year figure is not representative for the coming period.

## 7.8 The Interposed vehicle test

The way that the definition of Interposed vehicle in clause 101B of Schedule 10 operates was a common issue of concern raised in the industry consultation undertaken as part of the Review.

In essence, this definition is the key to determining how far down into layers of investment structures it is necessary to look in order to uplift fees and costs into PDS disclosure for the product.

This issue can not be considered strictly within the framework described in Chapter 7.3 because the Interposed vehicle test does not relate to the treatment of a single item of fees or costs. It is an overarching requirement that extends treatment of all items of fees and costs into underlying investment structures. Nevertheless, some of the same principles (e.g. whether the treatment supports comparison and whether it is consistent with the fee narrative and consumer expectations) have application.

Clearly, some requirement to uplift the fees and costs of underlying structures is necessary. Absent some regulatory extension, disclosure outcomes could be easily distorted if fees and/or impacts in underlying trusts and other structures are not uplifted; structures could easily be developed that would disclose no fees or costs at all. At the other extreme, on one view, the Stronger Super Reforms could require uplifting of all costs down to the operating costs of companies whose shares are held as an investment.<sup>152</sup> Between these two extremes, a line needs to be drawn that includes the fees and costs of some entities but excludes fees and costs of others.

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<sup>152</sup> The extension is suggested in the Explanatory Statement for the 2005 Amendment Regulation, which specifically pointed out that these costs would be Management costs were it not for the exemption relating to costs that an investor would incur if he or she invested directly in the asset: Explanatory Statement, Select Legislative Instrument 2005 No. 31 at page 8.

RG 97 and Schedule 10 as amended by CO 14/1252, as set out in Figure 1 under RG 97.55, use three tests: the platform test, the assets test and the PDS test. The Platform test recognises the different legal structure of those products. Disclosure of those products is discussed under Chapter 6.10 above. In combination, the assets test and the PDS test apparently seek to include those vehicles that are investment structures, i.e. a way of investing in assets as opposed to the asset itself. Neither test has regard to the legal form of the entity. Whether the entity is a trust, a MIS, a partnership or a particular type of company is not conclusive. The fees and costs associated with the Interposed vehicle are uplifted as if they were the fees or costs of the superannuation fund or MIS.<sup>153</sup>

The assets test is an objective test that treats entities as an Interposed vehicle according to its nature if not its legal form; if the entity invests more than 70% of its assets in securities or financial products, it is an Interposed vehicle. An entity that is not an Interposed vehicle under the assets test would still be an Interposed vehicle however if it meets the partly subjective PDS test. Under that test, an entity is an Interposed vehicle if, based on information issued by the issuer of the investing fund, the vehicle could reasonably be regarded as the means by which the benefit of the investment is obtained by the investment fund, rather than the end investment itself.

On the whole, very few comments were received about the assets test. A great many views were expressed that the PDS test leads to inappropriate outcomes. Comments were mainly directed at:

1. the consequence that some entities would be an Interposed vehicle for some investing funds but not for others;
2. the resultant treatment of investment in REITs; and
3. the apparent special carve out for infrastructure entities.

#### International references

The IOSCO *Good practice for fees and expenses of collective investment schemes*, does suggest that:

‘It is good practice to disclose a double fee structure by publishing a ‘synthetic TER’ where possible and where the exposure to underlying funds is material enough to affect the total cost to the investor.’<sup>154</sup>

That report however only contemplates underlying “funds” being “collective investment schemes” although the issue is not discussed extensively. IOPS WP20<sup>155</sup> identifies that only 5 of the 20 jurisdictions surveyed uplifted costs of underlying funds.

On the whole, other jurisdictions that do uplift underlying vehicle costs tend to use a simpler, but less refined, test that focuses only on the legal form or nature of the entity. Under EU PRIIPS<sup>156</sup> costs of underlying PRIIPS (which is defined broadly in the Regulation)<sup>157</sup> but not other types of

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<sup>153</sup> See clauses 101A(1)(d) and clause 103(1)(f) of Schedule 10.

<sup>154</sup> IOSCO (2016) at para 95.

<sup>155</sup> IOPS (2014).

<sup>156</sup> See Case study 4 in Chapter 4.2.

<sup>157</sup> Defined in Regulation 4 as “investment, including instruments issued by special purpose vehicles...where, regardless of the legal form of the investment, the amount repayable to the retail investor is subject to

entities, are uplifted regardless of the percentage of assets invested in a particular manner. As a consequence, no test like the PDS test is used. In the US, for both 401(k) pension plans and mutual funds, some fees of underlying funds (but not other entity types) are uplifted. In Hong Kong, both the Fee Table disclosure and the expense ratio only uplift the costs of entities that are defined as “collective investment schemes”. In New Zealand<sup>158</sup> the RG 97 tests have been broadly adopted however in this respect they may be slightly narrower as they only focus on uplifting the costs of “fund like” vehicles.

#### Could a simpler test be adopted

International practice suggests that a simpler test for an Interposed vehicle, such as reference to a financial product or MIS, could be considered. This could, for example treat all financial products or MIS, as defined, as an Interposed vehicle. This would have the advantage of being easier to apply and would overcome the apparent inconsistency that the same entity is an Interposed vehicle for some fund investors but not for others.

The disadvantages of such a simple test is that it would only have regard to legal form and not substance. Adoption of such a broad-brush rule may have unintended consequences. Practically, such a rule would mean that all financial products (all REITs, all MIS, all insurance policies etc), would be treated as an Interposed vehicle regardless of whether they are factually an investment vehicle. All companies (including listed investment companies) would be excluded. Specific inclusions and exemptions could be included, and this would need careful consideration particularly as to how it would apply to entities from other jurisdictions (US mutual funds for instance generally adopt a company structure). The fees and costs of REITs and other listed MIS would have to be uplifted even where they are held as a part of an equities portfolio or index tracking exchange traded fund (**ETF**). Some submissions received suggest that this may present compliance challenges for funds including ETFs that have diverse and/or international, holdings.

Another option that has been suggested is to limit the uplift requirement to the first non-associated entity level or to remove Indirect costs from the fee disclosure regime completely but disclose fees and costs of “associates” separately. This approach would simply accept that Indirect cost impacts affect investment outcomes which, to a lesser or greater extent, should be considered separately from known cost impacts. This would represent a major change, and in some respects a reversal in policy direction that could not be achieved quickly. Consideration would also need to be given to the likely behavioural responses by industry. Such an approach would appear to incentivise and favour the development of structures that rely on outsourcing and multi-layer products, so that explicit fee and costs disclosures are minimised.

It is difficult to consider this issue from the perspective of consumer expectation, fee narrative and whether one approach facilitates comparison better than the others. Under any scenario, the uplifted costs are not readily apparent to consumers as they are already incorporated into more compound figures (either as part of Management costs/Investment fee/Indirect costs or as a part of net investment returns). It is likely however that consumers could better understand a simpler test if trying to understand circumstances in which fees and costs are uplifted.

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fluctuations because of exposure to reference values or to the performance of one or more assets which are not directly purchased by the retail investor”.

<sup>158</sup> See case study 8 in Chapter 4.2.

For the time being, I would not recommend a change to the current approach. Without being dismissive of the concerns raised, no simpler alternative presents that is not without its own challenges and some of the concerns expressed in relation to the current tests may be moderated, over time, by other recommendations in this Chapter. Perhaps the issue could be revisited in due course once some of the other recommendations and options set out in this Chapter have been further considered and developed. Suggestions in relation to Transactional and operational costs for instance would mean that the uplifting task is greatly simplified.

### 7.9 Third party payments and offsets

During meetings with industry, and through correspondence, concerns were raised about the extent to which fee disclosure requirements include amounts that are paid by someone other than the investor or out of the fund or Interposed vehicles. The issue manifests itself in various ways across different types of products such as payments made by borrowers in mortgage schemes or peer-to-peer lending schemes and property operating costs paid by tenants in property funds by way of example.

In essence, the concern raised is that such payments should not be disclosed as a component of fees and costs because they are not paid by the investor nor out of the fund as they are paid by the third party. Even where such items are treated as a fee or cost some complications also arise in relation to the circumstances where the amount should be treated as a Transactional and operational cost as opposed to Administration/Investment fees or Management costs.

ASIC's view is that the law has always required that such amounts be included within an appropriate fee element and clause 101A of Schedule 10 has been modified to clarify the application of the principle to Indirect costs.

The principles behind including such items within fee and cost disclosure is that where an amount is applied to benefit the product by paying for a fee or cost that would otherwise be borne by the product, it should be treated as a fee or cost. The fact that it is paid for by a third party should not affect its characterisation as a fee, cost or other payment. By way of example, payments for the services of a MIS Provider could be derived from various sources including the investor, contributions, the fund or from third parties, but all should be treated equally as a Management cost for disclosure purposes. Similarly, other scheme costs, not related to Provider services such as transaction costs could also be funded from a range of sources. The characterisation of the payment as a transaction cost would not be affected by the source of the payment. Exclusion of one source or another would distort disclosure outcomes, compromise comparability and may create incentives to structure payments in a way that avoids disclosure.

An analogous issue is the treatment of amounts or revenues that offset an amount that is paid out of a product. As a matter of principle, the amount paid as a fee or cost should not be reduced by, or netted off against, offsetting income or other payment. Examples would include income sharing with custodians in securities lending arrangements in equities funds (any income generated by the arrangement does not reduce the cost of the arrangement) or the treatment of tax credits or refunds (the fact that a cost is funded by a tax credit does not affect its characterisation as a cost). Offsetting arrangements are covered explicitly in RG 97.97 to RG 97.99. The disclosure treatment for tax is explained in RG 97.171 to RG 97.172.

As indicated, I support the manner in which third party and offset payments are required to be disclosed although it is recognised that the principles and impact would not be immediately

obvious from reading RG 97 or Schedule 10. The treatment of offsetting income and payments is covered rather more explicitly. The treatment of third party payments is an area where any re-draft of RG 97 (see Recommendation 23) might be able to provide clarification of the principles and explanation of resulting requirements.

<p><b>[Recommendation 26]</b> I recommend that ASIC clarify in RG 97 the principles relating to and required treatment of payments of fees, cost and other amounts paid by third parties or offset against other amounts.</p>
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## 8. Recommendations and observations

This Chapter summarises the recommendations and observations made in this Report. Most of the substantive recommendations and observations are set out in Chapters 6 and 7. These are extracted below in summary form in Chapter 8.1 and Chapter 8.2 with associated Chapter references. Relevant Chapters should be referred to for details, background and qualifications to the recommendations and observations set out in summary form below.

Recommendations of a more generalised nature are set out under Chapter 8.3 and a few drafting points are identified in Chapter 8.4. Broader observations about the future direction of the disclosure of fees and charges are set out in Chapter 8.5.

It is recognised that ASIC will have its own processes to consider the recommendations set out in this Report. This may result in modification to, or departure from, the recommendations as stated. For this reason, no attempt is made to track through all of the consequential impacts that will have to be pursued. Depending on which, if any, of the recommendations and observations are implemented, this will have consequential impacts across a spectrum of areas. At the most obvious level, RG 97 and CO 14/1252 will need to be amended accordingly. Periodic statement disclosure will be affected by a number of recommendations and overall simplification of periodic statements will have to be further considered once these impacts work through. Alignment of disclosure between superannuation products and MIS and the way forward in enhancing comparison between Platform and non-Platform products is dependent on many of the recommendations in Chapter 7. Further consideration will need to be given to those issues once a firm direction on broader issues raised in this Report are set. Depending on the direction adopted regarding Transactional and operational costs (Chapter 7.6), there will be consequential impacts for Fee Templates, how figures are carried into the Fee Example and how items are set out in the AEFC. Treatment of some specific items, such as the exception treatment for OTC derivatives will need to be further considered in light of other agreed directions. Any changes to Fee Templates in Schedule 10 of the Regulation would have consequential impacts on Schedules 10D and 10E.

### 8.1 Recommendations - disclosure regime

**Recommendation 1** (Chapter 6.4) ASIC undertake a feasibility study into whether it, or another government agency could provide, or sponsor, the development of:

1. a publicly accessible, consumer facing facility providing fee and cost information extracted from PDSs that can be searched and compared on a range of criteria; and/or
2. data about average “Cost of Product” figures for specific investment option types that can be included as a reference figure in Fee Examples.

**Recommendation 2** (Chapter 6.4) The feasibility study referred to in Recommendation 1 also consider whether aggregated product or Provider level cost data can be provided, outside of PDSs to support consumers who make Provider or product level choices.

**Recommendation 3** (Chapter 6.6) ASIC work with industry to improve consistency in the way that fee information is set out in Fee Templates.

**Recommendation 4** (Chapter 6.6) ASIC work with industry to improve consistency in the way that fee information is incorporated by reference particularly as regards cross referencing in the Fee Template, location and format of presentation.

**Recommendation 5** (Chapter 6.6) When making future changes to layout of the disclosure tools or the underlying data, including how and whether to implement other recommendations set out in this Report, ASIC should keep in view a subsidiary objective of reducing or eliminating the differences between fee and cost disclosure appearing in PDSs of MIS and superannuation products.

**Recommendation 6** (Chapter 6.6) The superannuation Fee Template in clause 201 of Schedule 10 be modified to group together those fee and cost items that are ongoing separately from those that are dependent on member-initiated transactions or activities.

**Recommendation 7** (Chapter 6.6) If the line “Indirect cost ratio” is retained as a separate line item in the superannuation Fee Template, that the description of the line in clause 201 of Schedule 10 be modified to “Indirect costs”.

**Recommendation 8** (Chapter 6.6) The line item for “Advice fees” in the Fee Template for superannuation products should be removed. Where the amount is not nil, the amount can be incorporated into the line “Administration fee”.

**Recommendation 9** (Chapter 6.6) That the MIS Fee Templates in clauses 202 and 202A of Schedule 10 be modified to place “Management costs” at the top of the template.

**Recommendation 10** (Chapter 6.6) That the MIS Fee Templates in clauses 202 and 202A of Schedule 10 be modified to include a line for “Buy-sell spread”.

**Recommendation 11** (Chapter 6.6) For superannuation products, the distinction between Investment fees and Indirect costs be removed from the Fee Template by merging the two items into a single line item in the Fee Template titled “Investment Fees and Costs”.

**Recommendation 12** (Chapter 6.6) If other elements of Fee Template presentation are to be consumer tested, consumer response to merging Administration fees with Investment fees (or “Investment Fees and Costs” as proposed in Recommendation 11) also be tested as an input into further consideration of whether the two line items should be merged.

**Diagrams 6-1 and 6-2** set out modified versions of the superannuation and MIS Fee Templates (based, to the extent possible, on the existing Fee Templates) that incorporate recommendations 5, 6, 8, 9, 10 and 11 as well as other minor textual changes. These Diagrams could be used as a basis for consultation or consumer testing if undertaken.

**Recommendation 13** (Chapter 6.7) The Fee Example be extended to all investment options by the calculation and disclosure of an abbreviated “Cost of Product” figure. Some flexibility could be provided as to where the “Cost of Product” figure is to be disclosed (either in the PDS, incorporated by reference or in some other manner).

**Recommendation 14** (Chapter 6.7) The Fee Example and the abbreviated “Cost of Product” calculation referred to in the preceding recommendation for superannuation products incorporate a contribution of \$5,000 on the last day of the period.

**Recommendation 15** (Chapter 6.8) If other potential changes to Fee Templates are to be consumer tested, possible change of the name of the AEFC to “Fees and Costs Details” and change of the name of the Fee Template to “Fees and Costs Summary” be tested at the same time.

**Recommendation 16** (Chapter 6.9) Subsequent to considering other recommendations in this Report, ASIC consider consequential changes to the disclosure of fees and costs in periodic statements. These should be approached having regard to the following objectives:

1. reducing the relative over-emphasis on amounts deducted from investments;
2. reducing the number of data point; and
3. making the item headings easier for consumers to understand.

**Recommendation 17** (Chapter 6.10) The existing practice of showing fees and costs of the accessible MIS available through a Platform within the Platform’s investment menu documents be made a specific obligation in Schedule 10. Standardised introductory text should be developed.

**Recommendation 18** (Chapter 6.10) The investment menu documents for Platforms also include abbreviated “Cost of Product” figures for accessible MIS, calculated in a manner that is, to the extent possible, consistent with the calculated figure referred to in Recommendation 13 (including both Platform level and MIS level fees and costs).

**Recommendation 19** (Chapter 6.10) Periodic statement disclosure obligations in Schedule 10 should explicitly include the costs impacts of accessible investments in Platforms. The manner of achieving this, so that it can be comprehensible to consumers, should be further considered in light of proposed and consequential improvements to periodic statements generally (Chapter 6.9).

**Recommendation 20** (Chapter 6.10) ASIC work with industry to further improve consistency in the location and expression, in the PDS Fee Template of Platforms, of the prominent statement that the fees and costs of the Platform relate to access to the investments on the list, not the costs within those investments. Positioning of the statement within the “Investment fees” or “Management costs” line should be considered. The statement should also provide a cross reference to the location of the “Cost of Product” figure referred to in Recommendation 18 above.

**Recommendation 21** (Chapter 6.10) After implementation of other relevant changes set out in this Report, ASIC further review the disclosure of fees and charges for Platform products. Such review should focus on whether disclosure of fees and charges for Platform-based products is adequately meeting the objective of providing consumers with information that they can use in making more confident and informed value-for-money decisions when choosing investment options within Platforms and when making product level choices between Platforms, MIS and superannuation products.

## 8.2 Recommendations and observations – fee data

**Recommendation 22** (Chapter 7.1) ASIC make publicly available on its website a version of Schedule 10 that consolidates the amendments made by the various ASIC instruments.

**Recommendation 23** (Chapter 7.1) If the drafting of RG 97 is to be revisited, an attempt should be made to set out more explanation of the objectives and context of the fees and costs disclosure regime so that the meaning is more accessible to users.

**Recommendation 24** (Chapter 7.5) ASIC apply the methodology set out in Chapter 7.3 in reconsidering the commonly raised data issues listed in the Report and in considering other points that will inevitably arise over time.

**Observations – Transactional and operational costs:** Based on the methodology set out in Chapter 7.3, ASIC could consider modifying RG 97 and Schedule 10 to achieve the following outcomes in relation to transactional and operational costs:

1. explicit transaction costs and counterparty spreads (referred to as Disclosed T&O costs) be included, for both superannuation products and MIS as a separate line item in the Fee Template;
2. Disclosed T&O costs be excluded from other fee definitions including Investment fees;
3. Disclosed T&O costs be included in the Fee Example calculation;
4. property operating costs, borrowing costs and implicit transactional costs (other than counterparty spreads) (referred to as Excluded T&O costs) not be disclosed in the PDS and could be excluded from relevant definitions;
5. Disclosed T&O costs set out in the Fee Template be shown on a basis net of cost recoveries made via the buy/sell spread;
6. operational costs that are neither Disclosed T&O costs nor Excluded T&O costs (to the extent that any exist) be treated as a part of Administration fees (for superannuation products) or Management costs (for MIS);
7. the gross figure of Disclosed T&O costs be set out in the AEFC as a part of the details required under clause 209(j)(iii); and
8. periodic statements need not show the impact of Excluded T&O costs.

**Recommendation 25** Over the longer term, ASIC give consideration to whether, and how, Transactional and operational costs could be better explained to consumers within the context of information about returns.

**Observations – performance fees:** Based on the methodology set out in Chapter 7.3, ASIC could consider modifying RG 97 and related instruments to achieve the following outcomes in relation to performance fees and performance-related fees:

1. relevant definitions be amended such that the distinction between performance fees and those amounts described as performance-related fees be removed (i.e. performance fee should include amounts calculated by reference to performance of a product, part of a product, an Interposed vehicle or part of an Interposed vehicle);
2. the amount of performance fees included in the Fee Template (as a component of Management costs, Investment fees, Indirect costs or a new measure such as a consolidated “Investment Fees and Costs”) be calculated by reference to the average of the performance fees that accrued in the fund and Interposed vehicles in each of the previous 5 years;

3. where a fund was not in operation for the previous 5 years or did not have a performance fee charging mechanism in place for the full 5 years, then the average should be calculated by reference to the number of years in which the fund operated or had a performance fee charging mechanism in place;
4. transitional arrangements may need to accommodate data availability, particularly for Interposed vehicles, in the first 5 years of calculation;
5. the Fee Template contain an additional footnote referring to the AEFC (as illustrated in Diagrams 6-1 and 6-2);
6. the requirements for AEFC set out in clause 209(b)(i) and (ii) be maintained;
7. the requirements for AEFC set out in clause 209(b)(iii) be replaced by a requirement that the AEFC should set out the performance fees that accrued for each year used in the calculated average;
8. the AEFC may also set out related performance information where the Provider chooses to do so; and
9. the AEFC may also set out further explanation in circumstances where the Provider believes that the 5-year figure is not representative for the coming period.

**Recommendation 26** ASIC clarify in RG 97 the principles relating to, and disclosure required for, payments of fees, cost and other amounts by third parties.

### 8.3 Recommendations – other

#### Supervision and enforcement

A number of those who provided comments during the Review were less concerned about the requirements than they were about ensuring that all market participants disclose fees and costs in the same way. Many expressed concerns that their competitors were not doing so. Looking at a PDS will not necessarily evidence whether a Provider is complying, but many expressed a view that figures disclosed (by others) are not credible and create serious suspicion of non-compliance. Non-compliance would provide a competitive advantage which can in some respects be quite material. An example highlighted in one meeting related to the treatment of borrower costs in a mortgage or peer-to-peer lending scheme. Exclusion of such costs could create a difference of up to 4% in disclosed Management costs. Many concerns were expressed about how performance fees were being calculated and disclosed.

Inconsistency of approach can arise from a failure to understand the relevant requirements or a failure to comply with known requirements.

Part of the solution relates to improving clarity of the requirements so that it is clearer to all Providers what they are required to do. Relevant recommendations are already set out above.

No doubt surveillance of PDS disclosure is already within ASIC's plans, however, the recommendation is included for the record.

**Recommendation 27** is that ASIC develop and implement a surveillance strategy on compliance with Schedule 10 disclosure requirements.

The focus of this surveillance would be a matter for ASIC however many of the items discussed in this Report might suggest areas for particular attention.

## Educational material

As discussed in Chapter 7, it is important that fee disclosure is consistent with the public narrative regarding the use of comparative fee/cost information and is consistent with the types of items that consumers would expect to take into account when comparing product cost impacts. This is important so that consumers are not under any misapprehension as to what is being disclosed to them and also so that they are best able to understand and use the information provided.

Information and educational material for consumers needs to go further than just emphasising that fees are important. The simple message that fees are important must create anxiety for consumers in terms of what they are expected to do in response. A simple response to find the least expensive option could lead to inappropriate decisions if not placed in the context of what other factors are important and how they should be considered together. It will be best if the relevance of fees, costs and other factors can be explained in the context of different decisions. The discussion set out under Chapter 3.2 might be of some assistance in this regard.

Information and educational material should also seek to explain the nature and composition of fees and costs as disclosed. Consumer understanding of costs will generally be based on life experiences where the cost of a product is usually represented by a single up-front payment of a sum of money to the seller of the product. Consumers need to understand that the cost of a superannuation fund or MIS is a much more nuanced concept: they will never see a bill or invoice they have to pay for fund based products: they do not get an invoice that needs to be paid separately, some amounts are taken out of their contribution money before it is invested, some amounts may be taken out of their account (even this is somewhat difficult to explain given that accounts are on the whole only a notional concept), most is taken out of the pool of money and assets their contributions are invested into, some is paid for by other parties (e.g. borrower costs and tax benefits) and some is taken out on entry and/or exit as part of the buy/sell spread. Whilst these concepts are challenging and difficult to explain, consumers would need to have some basic understanding of this if they are to make any sense of the way that fees are disclosed in the Fee Template given that that disclosure is based on these concepts.

Information and educational material should also touch on how to use the disclosure tools (particularly the Fee Template and Fee Example) and how they can support decision-making. The relevance and use of transaction cost information in particular should be highlighted subject to the final direction adopted. The distinction and relationship between “Transaction costs (net)” and “Buy-sell spread” in the Fee Template as proposed would require some explanation.

Consumers should also be able to appreciate the relationship between the forward-looking disclosure of fees and costs in PDS and actual outcomes. Some elements (most fees) represent a contractual promise whereas some elements (mostly costs) are based on previous periods and there will inevitably be some difference between what is disclosed and actual outcomes. How, and the extent to which periodic statements can be used to reconcile this, should be explained to consumers.

It is recognised that construction of an effective consumer narrative is not a simple task. Amongst other constraints, a balance needs to be struck between providing more detailed information and keeping messages simple and digestible for consumers.

**Recommendation 28** is that ASIC continue to refine the narrative about the importance and relevance of fees when making decisions about superannuation funds and MIS. ASIC should continue to work with industry and other stakeholders to help disseminate consistent messages.

#### Information for advisors

As noted at several points in the Report, advisors have expressed concerns about how to factor fee disclosure information into their advice to clients. A particular point of concern related to how and whether disclosure of Transactional and operational costs should be incorporated into advice when comparing different products.

**Recommendation 29** is that ASIC work with the industry bodies representing advisors to clarify how they should use fee disclosure when giving advice about choice of products.

Some of the same points would be relevant to advisors and consumers under the point above. Refining the narrative to consumers should be considered in parallel with providing clarification for advisors. Messages about the relevance of transactional costs would be particularly relevant for advisors who often make investment option to investment option comparison. This issue could be significantly resolved if suggestions relating to the disclosure of Transactional and operational costs are adopted.

#### 8.4 Recommendations – drafting

In addition to the policy recommendations set out above, a number of drafting issues relating to Schedule 10, as modified, have been identified throughout the course of the Review. These are set out below for consideration by ASIC. Some of these are relatively minor and some would be overtaken by other recommendations depending on how those recommendations are taken forward.

1. **Recommendation 30** The definition of Administration fees in clause 209A of Schedule 10 has been the subject of discussion with some FMP Providers in relation to how it applies to fees deducted from members accounts, costs paid out of reserves and tax deductions related to those costs. The current drafting of the definition works adequately for retail funds but does not fit well with the structure of FMP funds that use reserves and should be reviewed to clarify how it applies for those funds. It is recognised that clarifying its operation may raise policy and not just drafting issues. My understanding of the overall policy is that the disclosure regime applies to both fees and costs regardless of their source, payment method or characterisation (see the related discussion under Chapter 7.9).
2. **Recommendation 31** The drafting of those parts of Schedule 10 and RG 97 relating to the calculation and disclosure of performance fees should be revisited to clarify the intention. My understanding is that the intention is that generally performance fees and performance-related fees for MIS are calculated by reference to the previous financial period. The drafting of clause 104A should be reviewed to ensure that it is expressed more clearly and is consistent with the intention. The intention as explained in RG 97.128 may need supplementation;
3. **Recommendation 32** RG 97.227 to RG 97.233 set out special requirements relating to members of a “pure defined benefit superannuation fund” which is a term defined in RG 97. Some funds have both defined benefit and defined contribution members. It seems appropriate that the special requirements should apply to the periodic statements of all

defined benefit members regardless of whether the fund of which they are a member also has defined contribution members;

4. **Recommendation 33** The opening words of clause 301(2) of Schedule 10 “The amount inserted must include...” have become separated from the clause they relate to (i.e. clause 301(1)) after the insertion of clauses 1A to 1E. Presumably the words relate to “Indirect costs of your investment” in clause 301(1) and drafting should be adjusted accordingly; and
5. **Recommendation 34** To better reflect the intention, clause 303(2)(d) of Schedule 10 should be amended such that sub clauses (i) and (ii) are in the alternate rather than conjunctive. The word “both” could be deleted from the end of subclause (d) and “or” inserted between (i) and (ii).

## 8.5 Observations – the future

As a concluding point, I make a few short observations about the approach to disclosure of fees and charges in the longer-term. As identified at the very beginning of this Report, in Chapter 2.1, considerations in this Report do not, on the whole, extend into broader framework questions such as the extent to which disclosure, and in particular PDS-based disclosure, can actually play an effective role in consumer decision-making and whether there are better approaches than segregated fee disclosure based primarily on point-of-sale documentation.

Noting the complexities faced by consumers in factoring cost impacts into decision-making, the complexity of information they have available to them and the limitations of supporting tools, it is difficult to be confident that the current regime is an optimal approach. It does however have to be acknowledged that the current regime, based on the toolset of a standardised fee table supported by a worked example set out in a point-of-sale document, is consistent with international approaches. No other major jurisdiction has found a better solution at this stage.

Given the structure and diversity of products, it is difficult to postulate how decision-making could be simplified beyond a continued focus on refining and improving default arrangements (not just limited to investment options). Fee and cost information and disclosure could however be approached in a way that better supports decision-making. Some of the challenges that present at the moment are the way that fee and cost information is largely provided in a point-of-sale context, it is generally product or investment option specific, it is largely static, it is separated from other information relevant to decision-making and it tells a very complex story.

Addressing those challenges in the longer-term would require careful consideration. Some of the directions that could be considered might include:

1. more layering of information that can address different levels of interest or need – instead of diving straight into the inevitable complexities of Fee Templates, some users might only need to understand that fees and costs are incurred and broadly what types of fees and costs affect them, others might need to be signposted to specific pieces of detail;
2. more modular and tailored presentation – it would help consumers if information can be gathered and presented in a manner that can better support specific types of decisions. As an example, a consumer considering whether to switch between investment options within a superannuation fund (Choice 6 in Chapter 3.2) should primarily be interested in information about relative risks and returns of the options under consideration. Information about switching costs would also be relevant as would any ongoing costs differences. These pieces of information are a tiny subset of all of the information in a PDS and it would be difficult, or at least time consuming, for a consumer to extract these pieces. Technology should be

able to support the extraction and presentation of information specific to a decision being considered. “Robo-advice” has comfortably entered the financial services lexicon; the same technological advances should be able to support “Robo-info”;

3. less segregated presentation – perhaps most importantly, information and the “story” about fees and their impacts could be presented as an integrated part of a broader narrative. Currently fee and cost disclosure is somewhat divorced from information about other decision-making factors: whilst information about returns, for example, is included in PDS and MySuper Product Dashboards, no attempt is made to integrate the related pieces of information. Approaches such as explaining fees and returns as part of a more graduated story could be considered (e.g. showing how total returns are allocated between the investor, the Provider, other parties, different types of transaction costs etc). Under such an approach, consideration could be given to whether summary cost information (e.g. the Cost of Product calculation in the Fee Example) should be presented as a percentage<sup>159</sup> rather than as a dollar figure. It would be difficult for consumers to see the relationship between a dollar based Cost of Product figure and return figures expressed as a percentage;
4. adjusting the point of comparison – much of the comparison challenge is driven by the need to compare across products which will always generate challenges because it requires high levels of consistency of approach across industry. Related to the point above, if at least some of the comparison points can be internalised within a product (such as how fee and cost impacts relate to return expectations within the product as discussed under Recommendation 25) some of these challenges can be reduced; and
5. more accessible – the current document (or multi document) based approach has many limitations that are still reflected in electronic delivery of the same documents – technological developments should be able to support more functional and cost effective delivery of information that may be better able to support the directions set out above.

These directions are not something that can be addressed in the short term and would not be limited to disclosures relating to fees and costs. They are raised only with an eye to how the framework might develop into the future. The rather more technical recommendations set out in this Report are not dependent on, or directed at, these possible future directions. As noted in Chapter 2.1 at the start of this Report, the existing PDS-based fee disclosure regime and the current disclosure tool-set are accepted as the starting parameters on which comments recommendations and observations are based.

## 8.6 Conclusions

The recommendations and observations set out above are quite broad in scope. They include a number of quite technical points about fee items and their definition, a number of suggested improvements to the disclosure tools, some suggestions for better support mechanisms for consumers and some observations about how fee disclosure might evolve going forward. Given that most comments received from stakeholders were focussed only on more technical details, some might not have expected recommendations to extend beyond the fee items and definitions, which are largely contained in Chapter 7. All of the observations and recommendations are directed at addressing the stated aim of the Review and the policy objective of achieving disclosure outcomes that can better support consumers in making more confident and informed

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<sup>159</sup> For example see the use of ‘Reduction in yield’ figures in the EU and UK in Chapter 4.

value-for-money decisions. In addressing the more technical points it became apparent that the policy objective could not be met by merely adjusting those technical issues and broader issues also warranted consideration.

Consequently, the recommendations and observations should be seen as a package rather than as a series of unconnected points. In some areas, such as how to disclose certain fee elements, application of that policy objective can, in my view, justify relaxation of current technical requirements in a manner that directly addresses some of the key stakeholder concerns. Conversely, in some other areas, principally in relation to the presentation of the main comparative tools, the same policy objective suggests the need for enhancements that can better support consumer decision-making that will involve extra effort by product Providers.

Some in the industry will not agree with the overall approach. Many will disagree with individual proposals based on their own circumstances. As the recommendations are structured as a package that provides some relaxation of requirements whilst delivering better overall outcomes for consumers, I would encourage ASIC not to allow cherry picking of individual recommendations, particularly those relating to the fee disclosure data. As just one example, proposals such as the relaxed disclosure of market impact costs are deliberately offset by giving consumers more usable disclosure of other transaction costs within the improved Fee Template and expanded Fee Examples.

Whilst the observations and recommendations should be considered as a package, the timing and/or development of individual elements may be affected by other developments. There are many concurrent initiatives affecting regulation of the sector, particularly superannuation, under consideration at the moment. These include:

1. the Treasury Laws Amendment (Improving Accountability and Member Outcomes in Superannuation Measures No. 2) Bill 2017;
2. the deferred MySuper Product Dashboard requirements;
3. the Insurance in Super Working Group deliberations;
4. the government's "Protecting Your Super" Package that was announced in the 2018-19 Budget;
5. ongoing review of APRA's data reporting requirements;
6. the Productivity Commission Draft Report (issued on 29 May 2018); and
7. possible recommendations arising out of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry.

It is impossible to forecast with any certainty, the extent to which these concurrent developments, the scope of which are much wider than the issues considered in this Report, might impact on the directions or timing of recommendations suggested. It is recognised that, at a minimum, these might affect sequencing or the timing of development of individual recommendations.

Hopefully, considered collectively and objectively, the proposed directions will be seen as an opportunity for different parts of the industry to work collaboratively amongst themselves, and with ASIC, in moving forward on an issue that has consumed excessive time and energy in recent years. For ASIC, the recommended directions, particularly in relation to fee data elements, would involve the robust use of ASIC discretionary powers in a manner that might, in some respects, depart from the more established use of those powers. I would accept that ASIC

may be particularly uncomfortable in moving in the proposed directions in the face of substantial industry disagreement or cherry picking. In those circumstances, maintaining the substance of the current approach, which does represent a valid implementation of what ASIC considers to be the policy intent of the legislature, would be a justifiable, if less than ideal, fall-back position.

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# 10. Defined terms and abbreviations

Terms are generally used as defined in the Corporations Law and Regulations except where indicated. To assist readability, some definitions are repeated in the Report.

Unless otherwise indicated or the context otherwise requires, references to sections are to sections of the Corporations Act and references to regulations are references to the Corporations Regulations.

**AEFC:** The additional explanation of fees and costs required to be included in a PDS under Division 4 of Part 2 of Schedule 10.

**AMC:** annual management charge.

**Amendment Regulation:** Corporations Amendment Regulation 2005 (No.1) (Cth) contained in Select Legislative Instrument 2005 No. 31.

**APRA:** The Australian Prudential Regulation Authority.

**ASFA:** The Association of Superannuation Funds of Australia.

**ASIC:** Australian Securities and Investments Commission.

**ASIC Report 23:** ASIC Report 23: *A model for fee disclosure in product disclosure statements for investment products*. Refer to the References section of this Report for further information.

**ASIC Report 398:** ASIC Report 398: *Fee and cost disclosure: Superannuation and managed investment products*. Refer to the References section of this Report for further information.

**ASIC Q&A:** The questions and answers on fees and costs disclosure published on ASIC's website. Refer to the References section of this Report for further information.

**CESR:** Committee of European Securities Regulators.

**CIS:** collective investment schemes.

**COBS:** the FCA Conduct of Business Sourcebook.

**CO 12/749:** ASIC Class Order [CO 12/749].

**CO 14/1252:** ASIC Class Order [CO 14/1252].

**Consumer Advisory Warning:** the consumer advisory warning required to be included in PDSs under Division 7 of Part 2 of Schedule 10.

**Corporations Act:** Corporations Act 2001 (Cth).

**Corporations Regulations:** Corporations Regulations 2001 (Cth).

**DOL:** US Department of Labour.

**EBSA:** Employee Benefits Security Administration.

**ERISA:** Employee Retirement Income Security Act of 1974 (US).

**ETF:** Exchange traded fund.

**EU:** European Union.

**FCA:** the UK Financial Conduct Authority.

**Fee Example:** the example of annual fees and costs based on an amount of \$50,000 required to be included in PDSs under Division 6 of Part 2 of Schedule 10.

**FER:** Fund expense ratio.

**Fee Template:** the fee and cost templates required to be included in PDSs under Division 1 and 2 of Part 2 of Schedule 10.

**FMC Act:** *Financial Markets Conduct Act 2013* (New Zealand).

**FMC Regulations:** Financial Markets Conduct Regulations 2014 (New Zealand).

**FMP Fund:** For member profit funds. These are Australian superannuation funds not run on the basis of providing a profit for the operator or Provider. These includes funds commonly known as industry funds, government funds and corporate funds.

**Funds or funds:** This term is used as a generic description of both superannuation funds and managed investment schemes.

**FSC:** Financial Services Council.

**FSRA:** *Financial Services Reform Act 2001* (Cth).

**GP:** good practice/s.

**ICR:** indirect cost ratio.

**IDPS:** investor directed portfolio service.

**IFSA:** Investment and Financial Services Association.

**IOPS:** the International Organisation of Pension Supervisors.

**IOSCO:** the International Organisation of Securities Commissions.

**IOSCO Report:** the report on “*Good practice for fees and expenses of collective investment schemes (CIS)*” prepared by IOSCO. Refer to the References section of this Report for further information.

**KIID:** key investor information document.

**KiwiSaver Act:** *KiwiSaver Act 2006* (New Zealand).

**MER:** management expense ratio.

**MIS:** managed investment scheme/s or managed investment product/s.

**MPF:** Mandatory provident fund.

**MPFA:** Mandatory Provident Fund Schemes Authority.

**MPFSO:** Mandatory Provident Fund Schemes Ordinance.

**MPFSR:** Mandatory Provident Fund Schemes (General) Regulation.

**MySuper Product Dashboard:** the product dashboard requirements set out in section 1017BA of the Corporations Act.

**NAV:** net asset value.

**OCF:** ongoing charge factor.

**OCI:** ongoing cost illustration.

**OMC:** ongoing management charge.

**OTC:** over the counter.

**PDS:** product disclosure statement.

**Platforms:** Custodial arrangements known as wraps, superannuation platforms or Investor Directed Portfolio Services (also known as IDPS).

**Provider:** this term is used as a collective definition for responsible entities of managed investment schemes and RSE Licensees.

**PRIIPS:** Packaged Retail Investment and Insurance Based Products (EU).

**PRIIPS Regulation:** EU Regulation on Key Information Documents for Packaged Retail and Insurance-based Investment Products (EU1286/2014).

**Ramsay Report:** *Disclosure of Fees and Charges in Managed Investments: Review of Current Australian Requirements and Options for Reform* (identified for ASIC purposes as ASIC Report 16). Refer to the References section of this Report for further information.

**REIT:** real estate investment trust.

**Report:** this document which sets out the findings and recommendations of the Review.

**Review:** the external expert review in relation to RG 97 discussed in this Report.

**RG 97:** ASIC Regulatory Guide 97: *Disclosing fees and costs in PDSs and periodic statements*.

**RIY:** reduction in yield.

**RSA:** a retirement savings account as defined in sections 761A and 764A(1)(h) of the Corporations Act.

**RSA Act:** the *Retirement Savings Account Act 1997* (Cth) and the Retirement Savings Account Regulations (Cth).

**RSE Licensee:** a constitutional corporation, body corporate, or group of individual trustees, that hold an RSE Licence granted by APRA under section 29D of the SIS Act.

**Schedule 10:** Schedule 10 to the Corporations Regulations.

**SEC:** Securities and Exchange Commission.

**SIS Act:** *Superannuation Industry (Supervision) Act 1993* (Cth).

**Stronger Super Reforms:** The legislative changes enacting recommendations in the Super System Review Final Report including the *Superannuation Legislation Amendment (Further MySuper and Transparency Measures) Act 2012* (Cth) and the Superannuation Legislation Amendment (MySuper Measures) Regulation 2013 (Cth).

**Super System Review:** Review of the Governance, Efficiency, Structure and Operation of Australia's Superannuation System chaired by Jeremy Cooper.

**TER:** total expenses ratio.

**UCITS:** Undertakings for Collective Investment in Transferable Securities (EU).

**UCITS Directive:** European Commission Directive 2009/65/EC, Undertakings for the collective investment in transferable securities (UCITS).

**UK:** United Kingdom.

**US:** United States.

**WP 15:** IOPS Working Paper 15: "*Comparative Information Provided by Pensions Supervisory Authorities*". Refer to the References section of this Report for further information.

**WP 20:** IOPS Working Paper 20: "*Update of OPS Work on Fees and Charges*". Refer to the References section of this Report for further information.

**WPPS:** Workplace personal pensions schemes.

# Appendix 1 – List of stakeholders consulted

Diagram Appendix 1-1 List of stakeholders consulted

No.	Name of stakeholder
1.	AMP
2.	ANZ Wealth Australia
3.	Australian Alternative Investment Management Association
4.	Australian Buy Side FIX Working Group together with the following members:
5.	Colonial First State
6.	Dimensional Fund Advisors
7.	FIX Trading Community
8.	Investment Technology Group
9.	T. Rowe Price
10.	University of Melbourne/University of New South Wales
11.	Australian Custodial Services Association
12.	Ausmaq Limited
13.	Australian Ethical Investment Limited
14.	Australian Institute of Superannuation Trustees (AIST) together with the following members:
15.	AustralianSuper
16.	CareSuper
17.	CBus
18.	EquipSuper
19.	First State Super
20.	HESTA
21.	Hostplus
22.	MediaSuper
23.	TelstraSuper
24.	UniSuper
25.	Vision Super
26.	Australian Private Equity and Venture Capital Association. together with the following members:
27.	Commonwealth Superannuation Corporation
28.	HESTA
29.	MLC
30.	Private Equity Partners
31.	Sunsuper
32.	Minter Ellison Lawyers
33.	Australian Prudential Regulation Authority
34.	Austsafe Super
35.	Australian Secure Capital Fund Limited
36.	Australian Unity Limited
37.	AustralianSuper
38.	BlackRock Australia
39.	BUSSQ (Building Unions Super Scheme)
40.	Cbus
41.	Chant West
42.	Club Plus Super

**No. Name of stakeholder**

43. Colonial First State
44. Corporate Superannuation Association
45. Crescent Wealth
46. Cromwell Funds Management Limited
47. Department of Treasury and Finance, Northern Territory
48. EnergySuper
49. Equity Trustees Limited, together with the following managers who engage Equity Trustees as a responsible entity:
  50. Aberdeen Standard
  51. Alexander Funds Management
  52. Alpha Fund Managers
  53. Ambassador Funds Management
  54. BNY Mellon Investment Management
  55. Cooper Investors
  56. Insight Investment
  57. Ironbark Asset Management
  58. L1 Capital
  59. MFS Investment Management
  60. Mirae Asset Global Investments
  61. Neuberger Berman
  62. Orbis Investment Management Limited
  63. Paradice Investment Management
  64. Prodigy Investment Partners
  65. Sanlam Private Wealth
  66. Spire Capital
  67. T Rowe Price
  68. Tribeca Investment Partners
69. Ernst & Young
70. Financial Markets Authority New Zealand
71. Financial Planning Association of Australia Limited, together with the following members:
  72. BT Financial Group
  73. Commonwealth Bank of Australia
  74. Fortnum Private Wealth
  75. Madison Financial Group
76. Financial Services Council, together with the following members:
  77. AMP
  78. AMP Capital Investors
  79. ANZ
  80. BlackRock
  81. BT Financial Group
  82. Colonial First State
  83. Johnson, Winter and Slattery Lawyers
  84. Macquarie Group Limited
  85. National Australia Bank
  86. Norton Rose Fulbright Lawyers
  87. Perpetual
  88. Vanguard
89. HESTA

**No. Name of stakeholder**

90. Hub24
91. Garda Capital Limited/Garda Funds Management Limited
92. HostPlus
93. IOOF Holdings Limited
94. Industry Super Australia
95. Ingwersen & Lansdown Securities Limited
96. Institute of Actuaries
97. InTrustSuper
98. Law Council of Australia (Superannuation Committee)
99. Link Group
100. Macquarie Group
101. McMahon Clarke Lawyers
102. Mercy Super
103. Morningstar
104. MTAA Super
105. National Australia Bank (including MLC)
106. Netwealth
107. OneVue Group
108. Perpetual
109. Property Council of Australia, together with the following members:
  110. AMP Capital
  111. Charter Hall
  112. GPT
  113. Lendlease
  114. QIC
  115. Scentre Group
  116. SunSuper
117. Property Funds Association
118. PwC
119. QIEC Super
120. QSuper
121. RG 97 Industry Working Group
122. Rice Warner
123. Sentinel Countrywide Retail Limited
124. SunSuper
125. Superannuation Compliance Services
126. Super Ratings
127. The Association of Superannuation Funds of Australia (ASFA), together with the following members:
  128. AMP
  129. ANZ
  130. Australia Post Super
  131. AustralianSuper
  132. Catholic Super
  133. CBus
  134. Emergency Services & State (ESS) Super
  135. HostPlus
  136. Kinetic Super
  137. LegalSuper

**No.      Name of stakeholder**

- 138.    MaritimeSuper
- 139.    Meat Industry Employees Superannuation Fund
- 140.    Mercer
- 141.    National Australia Bank
- 142.    Perpetual
- 143.    QIC
- 144.    REI Super (Real Estate Institute Super)
- 145.    Sandhurst Trustees (Bendigo Bank)
- 146.    UniSuper
- 147.    King & Wood Mallesons
- 148.    The Treasury
- 149.    Trilogy Funds Management Limited
- 150.    Vanguard Investments Australia Limited
- 151.    Westpac Group (including BT Financial Group)

# Appendix 2 – Summary of comments received from stakeholders

## General feedback

1. RG 97 is complex and difficult to understand.
2. RG 97 does not sufficiently set out the goals and policy rationale of the fees and costs disclosure regime.
3. The requirements in RG 97 and CO 14/1252 are costly to implement.
4. The fees and costs regime should be more principles-based.
5. The fees and costs regime should be more prescriptive.
6. The fees and costs regime does not meet consumer needs. Comparison has been made more difficult.
7. The fees costs regime makes it difficult for trustees/responsible entities to meet the requirement that disclosure in PDSs must be clear, concise and effective.
8. RG 97 and CO 14/1252 are more burdensome and require much more detailed disclosure of fees and costs than the regimes in other jurisdictions.
9. RG 97 and CO 14/1252 lead to too much focus on fees and costs and not enough on returns and investment risks.
10. Some Providers are concerned that others are not making disclosures in accordance with RG 97.

## Specific feedback

### 1. Inconsistency within the fees costs regime

There is inconsistency between the fees and costs disclosure requirements for superannuation products and MIS products. This makes it hard for consumers to compare products. It also creates practical burdens for industry.

There is inconsistency between the fee and cost disclosure requirements for Platform and non-Platform superannuation products. This makes it harder for consumers to compare products.

There is inconsistency in the treatment of listed and unlisted investments. For example, a fund that invests in a listed REIT may not need to disclose underlying costs relating to the property held by the REIT where a fund that invests in property directly or via an unlisted vehicle may be required to disclose underlying costs.

### 2. Interposed vehicles

The Interposed vehicle test is causing certain costs to be disclosed to consumers which should not be uplifted.

Relying on the wording in a PDS to determine whether or not an entity is an Interposed vehicle (the "PDS test") is not appropriate and can be gamed.

The Interposed vehicle test which requires funds to gather data from underlying investments is burdensome for industry. It is time consuming and difficult for both funds collecting and funds providing information.

### 3. Property operating costs

Property operating costs should not be included in fee and cost disclosure.

It is difficult to determine what types of costs should be included in "property operating costs" and whether a property operating cost is incurred "for the benefit of the tenant".

A property cost that is recoverable from the tenant should not be disclosed as part of "property operating costs" given the net effect on the fund is the same.

### 4. Where fees are disclosed

The fees and costs regime leads to "double disclose" of certain fees. Some fees and costs are included in both the fee template in a PDS also in the "Additional Explanation of fees and costs" section in a PDS.

The flexibility in CO 14/1252 which allows super funds to choose to disclose an amount in either the Investment fees or in Indirect costs makes it harder for consumers to compare funds.

Layout and content of the fee template can be improved to assist consumer understanding.

### 5. Performance fees

Disclosure of performance fees or performance related fees based on a single previous year is likely to mislead consumers given the volatility of such fees.

It is unclear on what basis performance fees and performance-related fees should be calculated and disclosed. The differing requirements may create inconsistent and potentially misleading disclosure.

The current position on disclosing performance fee claw backs does not promote accurate fee disclosure.

### 6. Implicit costs

It is difficult to calculate implicit costs (such as bid/asks spread and market impact costs).

Disclosing implicit costs may not be of benefit to consumers as this information is very technical, difficult to understand and not actionable.

The fees and costs regime should provide a set calculation methodology for calculating implicit costs to aid consistency.

No specific methodology should be prescribed as different methodologies would be relevant depending on the asset, strategy and markets involved.

### 7. OTC derivatives

Treating OTC derivative costs as part of Management costs (for MIS) and as part of Investment fees/Indirect costs (for superannuation products) is inappropriate. This could be better dealt with by including a general anti-avoidance provision so that funds do not structure their investments specifically to avoid having to disclose fees.

The provisions of CO 14/1252 which deal with OTC derivatives are very complex and hard to understand.

#### 8. Borrowing costs

Disclosing of borrowing costs may not be helpful to consumers. It can also be confusing as members sometimes think they are personally incurring a Borrowing cost rather than the fund.

If borrowing costs are to be disclosed, more guidance is needed on how to do this.

Borrowing costs should be split into different categories depending on the purpose of the borrowing and disclosed differently depending on whether the borrowing is pursuing an investment strategy or because of operational requirements.

#### 9. Borrower fees

Mortgage funds should not have to disclose fees paid by borrowers as a fee or cost of the fund.

ASIC needs to provide further guidance on how mortgage funds should disclose fees paid by borrowers.

#### 10. Securities lending

It is unclear whether trustees/responsible entities have to disclose fees received for securities lending where the fee received is split between the trustee/responsible entity and a custodian.

#### 11. Periodic statements

Disclosing fees both as gross and net of tax in periodic statements may be confusing to consumers.

Including member specific level information regarding transaction and operational costs on periodic statements may not be meaningful disclosure for consumers and may be confusing.

#### 12. Updating PDSs

Do funds have to update their PDS by 1 July each year, given that fees and costs information is to be based on information for the previous financial year? This causes difficulties as it takes time for historical fees and costs information to become available.

#### 13. Financial advisers

Financial advisers find RG 97 hard to work with. It is not clear what fees and costs should be included in a statement of advice.

# Appendix 3 – Consolidated version of Schedule 10 to the Corporations Regulations

# Corporations Regulations Schedule 10 — Disclosure of fees and other costs

*As amended by CO 14/1252 (and as that CO has itself been amended by ASIC instruments 2015/876, 2016/1224, 2017/65, 2017/664 and 2017/1138)*

(regulations 7.9.16K, 7.9.16M and 7.9.16N)

## Part 1—Interpretation

### 101 Definitions

In this Schedule:

**activity fee**, for a superannuation product, has the meaning given by subsection 29V(7) of the SIS Act.

**administration fee** has the meaning given by clause 209A.

**advice fee**:

- (a) for a superannuation product—has the meaning given by subsection 29V(8) of the SIS Act; and
- (b) for a managed investment product—means an amount that is:
  - (i) paid or payable to a financial adviser for financial product advice to a retail client or product holder about an investment; and
  - (ii) not included in a contribution fee, withdrawal fee, exit fee, establishment fee or management cost.

**balanced investment option** means an investment option in which the ratio of investment in growth assets, such as shares or property, to investment in defensive assets, such as cash or bonds, is as close as practicable to 70:30.

**borrowing costs** means costs, including costs in an interposed vehicle, relating to a credit facility within the meaning of regulation 7.1.06 relating to the provision of credit within the meaning of subregulation 7.1.06(3) to:

- (a) a trustee of a superannuation entity; or
- (b) an interposed vehicle, or a trustee of an interposed vehicle, in or through which the property of a superannuation fund is invested.

**brokerage** means an amount paid or payable to a broker for undertaking a transaction for the acquisition or disposal of a financial product.

**buy-sell spread**:

- (a) for a superannuation product—has the meaning given by subsection 29V(4) of the SIS Act; or
- (b) for a managed investment product—means an amount, deducted from the value of a financial product of a product holder, that represents an apportionment, among product holders, of the actual or estimated transaction costs incurred by the managed investment scheme.

**contribution fee** means an amount paid or payable against the initial, and any subsequent, contributions made into a product by or for a retail client for the product.

Note: A contribution may be made by an employer on behalf of the product holder or retail client.

**distribution costs** means the costs or amounts paid or payable for the marketing, offer or sale of a product.

Note: This includes any related adviser remuneration component other than an advice fee.

**establishment fee** means an amount paid or payable for the establishment of a client's interest in a product.

Note: This does not include contribution fees paid or payable against the initial contribution into the product.

**exit fee:**

- (a) for a superannuation product—has the meaning given by subsection 29V(6) of the SIS Act; and
- (b) for a managed investment product—means an amount paid or payable on the disposal of all interests held in the product.

**financial year means:**

- (a) in relation to a managed investment product—a financial year of the registered scheme to which the managed investment product relates; and
- (b) in relation to a superannuation product—a period of 12 months ending at the end of a fund reporting period determined under regulation 7.9.32 for holders of the superannuation product.

**incidental fees** means costs or amounts, other than costs or fees defined in this clause, that are:

- (a) paid or payable in relation to the product; and
- (b) not material to a retail client's decision to acquire, hold or dispose of his or her interest in the product.

Example: Cheque dishonour fees.

**indirect cost** has the meaning given by clause 101A.

**insurance fee**, for a superannuation product, has the meaning given by subsection 29V(9) of the SIS Act.

**interposed vehicle** has the meaning given by clause 101B.

**investment fee** has the meaning given by clause 209A.

**lifecycle MySuper product** has the meaning given by regulation 7.9.07N.

**lifecycle stage** has the meaning given by regulation 7.9.07N.

**performance**, of a managed investment product, a superannuation product, a MySuper product or an investment option, includes:

- (a) income in relation to the assets of, or attributed to, the managed investment product, the superannuation product, the MySuper product or the investment option; and
- (b) capital appreciation (realised or unrealised) to the value of the managed investment product, the superannuation product, the MySuper product or the investment option.

**performance fee** means an amount paid or payable, calculated by reference to the performance of a managed investment product, a superannuation product, a MySuper product or an investment option.

**property operating costs** means amounts that are paid or payable in relation to the holding of real property or an interest in real property, but do not include any of the following:

- (a) borrowing costs;
- (b) amounts that are paid or payable relating to the acquisition or disposal of real property or an interest in real property;
- (c) an amount that is otherwise charged as any of the following:
  - (i) an administration fee;
  - (ii) a buy-sell spread;
  - (iii) a switching fee;
  - (iv) an exit fee;
  - (v) an activity fee;
  - (vi) an advice fee;
  - (vii) an insurance fee.

**service fees** means advice fees, special request fees and switching fees.

**special request fees** includes fees paid or deducted from a product holder's managed investment product for a request made to the managed investment scheme.

Example: This applies to a fee for a request for additional information from a managed investment scheme.

**switching fee** :

- (a) for a MySuper product—has the meaning given by subsection 29V(5) of the SIS Act; or
- (b) for a superannuation product other than a MySuper product—means a fee to recover the costs of switching all or part of a member's interest in the superannuation entity from one investment option or product in the entity to another; or
- (c) for a managed investment product—means an amount paid or payable when a product holder transfers all or part of the product holder's interest in the managed investment product from one investment option to another.

**withdrawal fee** means an amount, other than an exit fee, paid or payable in respect of:

- (a) a withdrawal; or
- (b) the disposal of an interest in a product.

## **101A Indirect costs**

- (1) Despite subsection 1013C(2) of the Act, the indirect cost of a MySuper product, an investment option offered within a superannuation product other than a MySuper product, managed

investment product or investment option offered by a managed investment scheme means any amount that:

- (a) either:
    - (i) a responsible person knows, or reasonably ought to know or, where this is not the case, may reasonably estimate has reduced or will reduce (as applicable) whether directly or indirectly the return on the product or option that is paid from or reduces the amount or value of:
      - (A) the income of or the property attributable to the product or option; or
      - (B) the income of or the property attributable to an interposed vehicle in or through which the property attributable to the product or option is invested; or
    - (ii) satisfies both the following:
      - (A) the amount is paid or payable by or on behalf of a person who may make payments that form part of the return on, or the value of, the product or option whether directly or through an interposed vehicle;
      - (B) payment of the amount is a benefit that increases the returns or value of the product or option or provides a benefit to the issuer in relation to the product or option that is retained by the issuer; and
  - (b) for a MySuper product or an investment option offered within a superannuation product other than a MySuper product, is not charged to a member as a fee; and
  - (c) is not a fee as defined in clause 209A or an insurance fee; and
  - (d) subject to subsection (3), would, if the amount had been paid as a cost out of a superannuation entity, be an investment fee or administration fee for the superannuation product or, if the amount had been paid out of the scheme property of the registered scheme, be a management cost of the managed investment product.
- (2) For the purposes of subclause (1):
- (a) property is invested in or through an interposed vehicle even if:
    - (i) the property is in turn invested in or through one or more other interposed vehicles; or
    - (ii) the property was invested in the first mentioned interposed vehicle through or by another interposed vehicle; and
  - (b) property is not invested in or through an interposed vehicle if the property is invested in the vehicle by a body, trust or partnership that:
    - (i) is not an interposed vehicle; and
    - (ii) is not the trustee or responsible entity.

- (3) Without limiting subclause (1), the indirect costs of a product or investment option referred to in subclause (1) include:
- (a) the following amounts where the responsible person knows, or reasonably ought to know or, where this is not the case, may reasonably estimate those amounts:
    - (i) in relation to a derivative financial product that is not an option to acquire or dispose of a financial product—the amount that is the difference between the underlying return and the actual return for the derivative financial product, where the actual return on the product or option is less than the underlying return on the derivative financial product over the relevant financial year; or
    - (ii) in relation to a derivative financial product that is an option to acquire or dispose of a financial product—any amount by which the cost incurred to acquire the derivative financial product exceeds the amount that would be obtained on its disposal at that time; or
  - (b) where the responsible person does not know, does not believe they reasonably ought to know, and is not able to reasonably estimate without taking steps that the responsible person considers unreasonable, the amount in paragraph (a) (as applicable) in relation to a derivative financial product—the following amounts in relation to the derivative financial product:
    - (i) in relation to a derivative financial product that is not an option to acquire or dispose of a financial product—the greater of:
      - (A) the amount calculated using the following formula:
 
$$\text{relevant percentage} \times \text{value} \times (n/365)$$

where:

***n*** means the number of days that the derivative financial product was held by the responsible person or interposed vehicle during the relevant financial year.

***relevant percentage*** means 0.1%.

***value***, in relation to a derivative financial product, means the value of the ultimate reference assets, in each case taking into account any leverage, offsets or similar adjustments applied to or between the ultimate reference assets under the terms of the derivative financial product; and
      - (B) the minimum amount that the responsible person believes or has reasonable grounds to believe would apply under paragraph (a);
    - (ii) in relation to a derivative financial product that is an option to acquire or dispose of a financial product—the lesser of:
      - (A) the amount that would apply under subparagraph (i) if the exclusion from that subparagraph (i) of options did not apply; and
      - (B) the premium paid by the responsible person or interposed vehicle for the option,

where the amount referred to in paragraph (a) or (b) is attributable to:

- (c) the product or investment option; or
- (d) an interposed vehicle through which the property attributable to the product or investment option is invested.

(3A) In subclause (3):

**actual return** means the return that has been or would be received (as applicable), or loss that would be payable, by the responsible entity, trustee or interposed vehicle in relation to the derivative financial product over the relevant financial year if the derivative financial product was:

- (a) acquired at the time the derivative financial product was acquired, or, if the derivative financial product was not acquired during the relevant financial year, acquired at the commencement of the relevant financial year for the same price at which it would have been disposed at the end of the preceding financial year; and
- (b) disposed of at the time the derivative financial product was disposed of, or, if the derivative financial product was not disposed of during the relevant financial year, disposed of at the end of the relevant financial year for the price at which it would have been disposed of at that time.

**derivative financial product** means a financial product that:

- (a) is:
  - (i) a derivative; or
  - (ii) either:
    - (A) a security other than a share in a body or a debenture of a body; or
    - (B) a managed investment product or financial product referred to in paragraph 764A(1)(ba) of the Act other than an interest in a managed investment scheme,

under which:

- (C) financial products (**delivery products**) will be delivered or an amount paid at a specified time (**maturity**) in the future; and
- (D) the value of the delivery products to be delivered at maturity or the amount to be paid is ultimately determined, derived from or varies by reference to the value or amount of one or more of the following (each, a **reference asset**):
  - (I) financial products other than the delivery products;
  - (II) an asset other than a financial product;
  - (III) a rate (including an interest rate or exchange rate);
  - (IV) an index;

provided that the reference asset is not related to the value of:

- (V) a share in a body or debenture of a body to which the delivery products relate; or
  - (VI) the assets of the managed investment scheme to which the delivery products relate; or
  - (VII) the assets attributable to a class of interests in the managed investment scheme to which the delivery products relate; and
- (b) is not able to be traded on a financial market at the time it is acquired.

***reference asset:***

- (a) in relation to a derivative financial product that is a derivative—means the something else that the amount of the consideration, or the value of the arrangement, is ultimately determined, derived from, or varies by reference to and, if the something else is a rate of interest or inflation, the amount on which that rate is applied under the derivative financial product in determining the amount to be paid or received;
- (b) in relation to a derivative financial product that is a security, managed investment product or financial product referred to in paragraph 764A(1)(ba) of the Act other than an interest in a managed investment scheme—has the meaning given by clause 101A(3A)(a)(ii)(D).

***relevant financial year*** means the financial year for which responsible person is calculating indirect costs.

***ultimate reference asset***, in relation to a derivative financial product and each reference asset for the derivative financial product, means:

- (a) to the extent that the reference asset is:
  - (i) a derivative financial product; or
  - (ii) rights in an entity that would be an interposed vehicle if it were held by the superannuation entity or scheme; or
  - (iii) an index that includes a derivative financial product referred to in sub-paragraph (i) or rights in an entity referred to in sub-paragraph (ii),

the asset or assets from which the returns from the derivative financial product or rights in the entity are determined, or any asset or assets that are held in or through any other derivative financial products or entities that would be an interposed vehicle if they were held as part of the superannuation entity or scheme;

- (b) to the extent that the reference asset is not covered by any of the subparagraphs in paragraph (a)—the reference asset.

***underlying return***, in relation to a derivative financial product, means the return that has been or would be received (as applicable), or loss that would be payable, because of the change in the value of the ultimate reference assets taking into account any leverage, offsets or similar adjustments applied to or between the ultimate reference assets under the terms of each relevant derivative financial product or interest in an interposed vehicle over the relevant financial year for which the derivative financial product was held.

- (4) Despite subclause (1) and (3), indirect costs of a managed investment product or an investment option of a managed investment scheme do not include amounts referred to in subclause (3):
  - (a) where the derivative financial product referred to in subclause (3) is acquired or disposed of for the primary purpose of avoiding or limiting the financial consequences of fluctuations in, or in the value of, receipts or costs of the managed investment scheme whether or not the receipts or costs arise in or through an interposed vehicle; and
  - (b) where the indirect costs were calculated under paragraph (3)(a), to the extent that the difference would result from the incurring of transactional or operational costs in relation to the ultimate reference assets.

Note: Costs excluded under subparagraph (4) are likely to be transaction costs under clause 102. Indirect costs for superannuation products generally include transaction costs.

### 101B Interposed vehicle

- (1) A body, partnership or trust (each an *entity*) is an *interposed vehicle* in relation to a product or investment option if both of the following are satisfied:
  - (a) property attributable to the product or investment option to which the Product Disclosure Statement relates is invested in or through the entity;
  - (b) the responsible person for the Product Disclosure Statement believes or has reasonable grounds to believe that the entity has more than 70% of its assets by value invested in securities or other financial products.
- (2) For the purposes of subclause (1) and subject to subclause (3), in determining whether an entity (the *first entity*) has more than 70% of its assets by value invested in securities or other financial products, disregard for the numerator, securities or other financial products that:
  - (a) are reasonably regarded as a means by which the first entity makes an investment in real property or an infrastructure entity; or
  - (b) confer on the first entity control of another entity (the *second entity*), unless the responsible person for the Product Disclosure Statement has reasonable grounds to believe that the second entity has more than 70% of its assets by value invested in securities or other financial products.
- (3) For the purposes of paragraph (2)(b), in determining whether the second entity has more than 70% of its assets by value invested in securities or other financial products, apply subclause (2) to the second entity as if the second entity was the first entity referred to in that subclause.
- (4) An entity is also an *interposed vehicle* in relation to a product or investment option if, having regard to the Product Disclosure Statement for the product or investment option and any other information issued by the responsible person, a security or interest in the entity could be reasonably regarded, by retail clients who may be expected to be given the Product Disclosure Statement or other information, as the means by which the benefit of investments by or through the entity is obtained, rather than the investment of the superannuation entity or registered scheme to which the product or investment option relates.
- (4A) Subject to subclause (4B), an entity is also an *interposed vehicle* in relation to a product or investment option if:

- (a) the Product Disclosure Statement for the product or investment option or any other information issued by the responsible person relating to the product or investment option issued by the responsible person that has been given or may be reasonably be expected to be given to retail clients refers to “property”, “real estate” or “land” or similar terms in the description of the product or investment option or as one of the assets (**relevant asset**) in which investment may be made under the product or investment option; and
  - (b) real property or an interest in land to which the reference relates is directly or indirectly held by or through the entity.
- (4B) An entity is not an **interposed vehicle** because of subclause (4A) if both the following are satisfied:
- (a) the reference in the Product Disclosure Statement or other information is merely part of a reference to an entity (whether specified or not) that directly or indirectly invests in real property or interests in land or to physical infrastructure referred to in paragraphs (a) to (j) of the definition of **infrastructure entity** in subclause (6);
  - (b) a retail client who has read the Statement or other information could not reasonably believe that the product or investment option or the relevant asset may be intended for persons predominantly intending to benefit from increases in the value of, or returns from holding, real property or an interest in land other than physical infrastructure referred to in paragraphs (a) to (j) of the definition of **infrastructure entity** in subclause (6).
- (4C) Subject to subclause (4D), an entity is also an **interposed vehicle** in relation to a product or investment option if:
- (a) the Product Disclosure Statement for the product or investment option or any other information issued by the responsible person relating to the product or investment option that has been given or may be reasonably expected to be given to retail clients refers to the product or option as being directly or indirectly invested in or through an entity (whether specified or not) other than an infrastructure entity which the responsible person believes has a majority of its assets invested in physical infrastructure referred to in paragraphs (a) to (j) of the definition of **infrastructure entity** in subclause (6); and
  - (b) the reference relates to the entity.
- (4D) An entity is not an **interposed vehicle** because of subclause (4C) if:
- (a) either of the following is satisfied:
    - (i) the entity is admitted to the official list of a prescribed financial market or a financial market operated outside of this jurisdiction that is regulated by a foreign government or an agency of a foreign government;
    - (ii) the issuer of the securities or financial products of the entity has applied, or stated in a regulated disclosure that they will apply, for such admission; and
  - (b) the securities or financial products of the entity are, or are to be, held under an investment strategy for the product or investment option that:
    - (i) relates to, or is publicly measured by the responsible person by reference to, a widely used index (**reference index**) of securities or financial products of entities that satisfy subparagraph (a)(i); and

- (ii) is a strategy of holding directly or indirectly securities or financial products:
  - (A) of entities that satisfy paragraph (a); and
  - (B) that represent at least 80% by value of the net assets attributable to the investment strategy; and
- (c) the value of all the securities or financial products of the entity that are in the same class as the securities or financial products held under the investment strategy does not exceed 30% of the value of the reference index.

Note: If paragraphs (a) to (c) are satisfied in relation to an entity, the entity may still be an *interposed vehicle* because of provisions of clause 101B other than subclause (4C).

- (5) Despite anything in subclauses (1) to (4D), an entity will not be an *interposed vehicle* in relation to a product or investment option if all of the following apply:
  - (a) the Product Disclosure Statement for the product or an investment option states that a holder of the product may give instructions, directions or requests for financial products to be acquired;
  - (b) the responsible person for the Product Disclosure Statement has published a list of financial products in relation to which the instructions, directions or requests may be given that includes a security or interest in the entity;
  - (c) the arrangement under which the instructions would be acted on is a custodial arrangement as defined in subsection 1012IA(1) of the Act.

- (6) In this clause:

***infrastructure entity*** means an entity that provides a return to its shareholders or members mainly from owning or operating any of the following:

- (a) airports;
- (b) electricity generation, transmission or distribution facilities;
- (c) gas transmission or distribution facilities;
- (d) hospitals;
- (e) ports;
- (f) railways;
- (g) roads;
- (h) sewerage facilities;
- (i) telecommunication facilities;
- (j) water supply facilities; or
- (k) other physical infrastructure.

## 102 Management costs

- (1) **Management costs**, for a managed investment product, means any of the following:
  - (a) an amount payable for administering the managed investment scheme;
  - (b) for a custodial arrangement—the cost involved, or amount paid or payable, for gaining access to, or participating in, the arrangement;
  - (c) distribution costs;
  - (d) other expenses and reimbursements in relation to the managed investment scheme;
  - (e) amounts paid or payable for investing in the assets of the managed investment scheme;
  - (f) amounts deducted from a common fund by way of fees, costs, charges or expenses, including:
    - (i) amounts retrieved by an external fund manager or a product issuer; and
    - (ii) amounts deducted from returns before allocation to the fund;
  - (g) estimated performance fees;
  - (h) any other investment-related expenses and reimbursements, including any associated with custodial arrangements;
  - (i) indirect costs.
- (2) The following fees and costs are not management costs for a managed investment product:
  - (a) a contribution fee;
  - (b) transactional costs and operational costs other than those costs under subclause 101A(3);
  - (c) an additional service fee;
  - (d) an establishment fee;
  - (e) a switching fee;
  - (f) an exit fee;
  - (g) a withdrawal fee;
  - (h) costs (related to a specific asset (other than a security or interest in an interposed vehicle or derivative financial product within the meaning of subclause 101A(3A)) or activity to produce income) that an investor would incur if he or she invested directly in the asset;
  - (i) incidental fees.

## 103 Transactional and operational costs

- (1) **Transactional and operational costs** include the following:
  - (a) brokerage;

- (b) buy-sell spread;
- (c) settlement costs (including custody costs);
- (d) clearing costs;
- (e) stamp duty on an investment transaction;
- (ea) where an asset is acquired other than through a financial market, any part of the acquisition price of the asset that exceeds the price at which the asset could have been disposed of;
- (eb) where an asset is acquired through a financial market, any part of the acquisition price of the asset that exceeds the bid price in the financial market that would apply without the acquisition having occurred either:
  - (i) immediately following the acquisition; or
  - (ii) if the acquisition was a part of multiple acquisitions reflecting a single and non-recurring instruction to acquire, after the last acquisition made in accordance with the instruction;
- (ec) property operating costs;
- (f) costs incurred in or by an interposed vehicle that would be transactional and operational costs if they had been incurred by the superannuation entity to which the superannuation product or investment option relates or for the registered scheme to which the managed investment products relate;

and for a superannuation product does not include borrowing costs or costs that are indirect costs because of subclause 101A(3).

- (1A) Before 30 September 2019, transactional and operational costs do not include property operating costs for a MySuper product or investment option if details of the property operating costs are disclosed in accordance with paragraph 209(ma).

## 104 Indirect cost ratio

- (1) The ***indirect cost ratio (ICR)***, for a MySuper product or an investment option offered by a superannuation entity, is the ratio of the total of the indirect costs for the MySuper product or investment option, to the total average net assets of the superannuation entity attributed to the MySuper product or investment option.

Note: A fee deducted from a member's account or paid out of the superannuation entity is not an indirect cost.

- (1A) The ***indirect cost ratio (ICR)***, for an investment option offered by a managed investment scheme, is the ratio of the management costs for the option that are not deducted directly from a product holder's account, to the total average net assets of the managed investment scheme that relates to the investment option.

Note: A fee deducted directly from a product holder's account is not included in the indirect cost ratio.

- (2) Despite clause 214, the ICR for a Product Disclosure Statement that is available during a particular financial year is to be determined for the previous financial year except that if the product or investment option was not offered from at least 11 months before the end of the previous financial year, the ICR for the Statement is to be determined based on the

responsible person's reasonable estimate at the time the Statement is prepared of the ICR that will apply for the current financial year and if the product or investment option was first offered in the current financial year, since the time the product or investment option was first offered, adjusted to reflect a 12 month period.

- (2A) Despite clause 214, the part of a fee for a MySuper product or an investment option offered by a superannuation entity disclosed in a Product Disclosure Statement that is available during a particular financial year that relates to the costs incurred by the trustee of the superannuation entity or in an interposed vehicle or derivative financial product, is to be determined for the previous financial year except that if the product or investment option was not offered from at least 11 months before the end of the previous financial year, the costs are to be determined based on the responsible person's reasonable estimate at the time the Statement is prepared of those costs that will apply for the current financial year and if the product or investment option was first offered in the current financial year, since the time the product or investment option was first offered, adjusted to reflect a 12 month period.
- (3) The ICR for a periodic statement is to be determined over the latest reporting period.

#### **104A Costs in management costs**

Despite clause 214, the part of the management costs for an investment option offered by a managed investment scheme disclosed in a Product Disclosure Statement that is available during a particular financial year that is not a fee payable to the responsible entity, other than a performance fee, is to be determined for the previous financial year except that if the investment option was not offered from at least 11 months before the end of the previous financial year, that part of the management costs is to be determined based on the responsible person's reasonable estimate at the time the Statement is prepared of those costs that will apply for the current financial year and if the product or investment option was first offered in the current financial year, since the time the product or investment option was first offered, adjusted to reflect a 12 month period.

## Part 2—Fees and Costs Template, example of annual fees and costs and Consumer Advisory Warning for Product Disclosure Statements

### Division 1—The fees and costs template for superannuation products

#### 201 Template for superannuation products

##### Fees and other costs

This document shows fees and other costs that you may be charged. These fees and other costs may be deducted from your money, from the returns on your investment or from the assets of the superannuation entity as a whole.

Other fees, such as activity fees, advice fees for personal advice and insurance fees, may also be charged, but these will depend on the nature of the activity, advice or insurance chosen by you.

Taxes, insurance fees and other costs relating to insurance are set out in another part of this document.

You should read all the information about fees and other costs because it is important to understand their impact on your investment.

*[If relevant]* The fees and other costs for each MySuper product offered by the superannuation entity, and each investment option offered by the entity, are set out on page *[insert page number]*.

<i>[Name of superannuation product]</i>		
<i>Type of fee</i>	<i>Amount</i>	<i>How and when paid</i>
<i>Investment fee</i>		
<i>Administration fee</i>		
<i>Buy-sell spread</i>		
<i>Switching fee</i>		
<i>Exit fee</i>		
<i>Advice fees</i> relating to all members investing in a particular MySuper product or investment option		
<i>Other fees and costs<sup>1</sup></i>		
<i>Indirect cost ratio</i>		

1. *[If there are other fees and costs, such as activity fees, advice fees for personal advice or insurance fees, include a cross-reference to the “Additional Explanation of Fees and Costs”.]*

## Division 2—The fees and costs template for managed investment products

### 202 Template for a multiple fee structure—managed investment products

#### Fees and other costs

This document shows fees and other costs that you may be charged. These fees and costs may be deducted from your money, from the returns on your investment or from the assets of the managed investment scheme as a whole.

Taxes are set out in another part of this document.

You have 2 different fee payment options:

- (a) to pay contribution fees upfront, at the time when you make each investment into the managed investment scheme; or
- (b) to pay contribution fees later (for example, on the termination of your investment or by way of other increased fees).

Note: You may pay more in total fees if you choose to pay contribution fees later.

You should read all the information about fees and costs because it is important to understand their impact on your investment.

*[If relevant]* Fees and costs for particular investment options are set out on page *[insert page number]*.

<i>[Name of managed investment product]</i>			
Type of fee or cost	Amount		How and when paid
	Option to pay contribution fees upfront	Option to pay contribution fees later	
<b>Fees when your money moves in or out of the managed investment product</b>			
<i>Establishment fee</i> The fee to open your investment			
<i>Contribution fee<sup>1</sup></i> The fee on each amount contributed to your investment			
<i>Withdrawal fee<sup>1</sup></i> The fee on each amount you take out of your investment			
<i>Exit fee<sup>1</sup></i> The fee to close your investment			
<b>Management costs</b>			
<i>The fees and costs for managing your investment<sup>1</sup></i> The amount you pay for specific investment options			

<i>[Name of managed investment product]</i>		
Type of fee or cost	Amount	How and when paid
is shown at page <i>[insert page number]</i>		
<b>Service fees<sup>2</sup></b>		
<i>Switching fee</i> The fee for changing investment options		

1. This fee includes an amount payable to an adviser. (See Division 4, “Adviser remuneration” under the heading “Additional Explanation of Fees and Costs”.)
2. *[If there are other service fees, such as advice fees or special request fees, include a cross-reference to the “Additional Explanation of Fees and Costs”.]*

## 202A Template for single fee structure—managed investment products

### Fees and other costs

This document shows fees and other costs that you may be charged. These fees and costs may be deducted from your money, from the returns on your investment or from the assets of the managed investment scheme as a whole.

Taxes are set out in another part of this document.

You should read all the information about fees and costs because it is important to understand their impact on your investment.

*[If relevant]* Fees and costs for particular investment options are set out on page *[insert page number]*.

<i>[Name of managed investment product]</i>		
Type of fee or cost	Amount	How and when paid
<b>Fees when your money moves in or out of the managed investment product</b>		
<i>Establishment fee</i> The fee to open your investment		
<i>Contribution fee<sup>1</sup></i> The fee on each amount contributed to your investment		
<i>Withdrawal fee<sup>1</sup></i> The fee on each amount you take out of your investment		
<i>Exit fee<sup>1</sup></i> The fee to close your investment		
<b>Management costs</b>		
<i>The fees and costs for managing your investment<sup>1</sup></i>		

<i>[Name of managed investment product]</i>		
<b>Type of fee or cost</b>	<b>Amount</b>	<b>How and when paid</b>
The amount you pay for specific investment options is shown at page <i>[insert page number]</i>		
<b>Service fees<sup>2</sup></b>		
<i>Switching fee</i> The fee for changing investment options		

1. This fee includes an amount payable to an adviser. (See Division 4, “Adviser remuneration” under the heading “Additional Explanation of Fees and Costs”.)
2. *[If there are other service fees, such as advice fees or special request fees, include a cross-reference to the “Additional Explanation of Fees and Costs”.]*

## **Division 3—How to fill in the template**

### **203 The preamble**

The material in the preamble to the template should only include matters that are relevant to the product.

Example: Insurance costs will generally not be relevant to a managed investment product.

### **204 Column 2—presentation of amounts**

- (1) This clause, clause 205 and clause 206 are subject to regulations 7.9.15A, 7.9.15B and 7.9.15C.
- (2) If a particular fee or cost is not charged, 'nil', 'zero', '0' or 'not applicable' (if it would not be misleading) must be written in column 2 opposite the type of fee or cost.
- (3) If it is not possible to determine a single amount or percentage of a fee or cost, it may be written as a range of fees or costs.
- (4) If the exact amount of a fee or cost paid or payable is not known, an amount that is a reasonable estimate of the amount attributable to the retail client must be shown.
- (5) An amount set out in accordance with subclause (4) must be clearly designated as an estimate.
- (6) If an amount or cost has a number of components, the amount of each component must be listed separately.  
Example: Management costs: 1.8% of product holder's balance + \$70 per year.
- (7) A cost or amount paid or payable must include, if applicable:
  - (a) GST less any reduced inputs tax credits; and
  - (b) stamp duty.

### **205 Column 2—include information for each MySuper product or investment option**

- (1) The fee information must be set out:
  - (a) for superannuation products—for each MySuper product and each investment option offered by the relevant superannuation entity; and
  - (b) for managed investment products—for each investment option offered by the relevant managed investment scheme.
- (2) It may be:
  - (a) set out in the table; or
  - (b) cross-referenced in the table to another section of the Product Disclosure Statement that contains the relevant fee information.

### **206 Presentation of multiple fee payment options**

If a superannuation entity or managed investment scheme has more than 2 options for the payment of fees:

- (a) the number of fee payment options must be set out in the preamble; and
- (b) details of all fee payment options must be set out in the template.

### **207 Column 3—how and when fees and costs are payable**

Column 3 of the template must set out:

- (a) how the fee is or will be recovered, for example by deduction from:
  - (i) the member's investment balance; or
  - (ii) the assets of the superannuation entity or managed investment scheme;
  - (iii) contributions; or
  - (iv) withdrawals; and
- (b) the recurrence of the recovery of the fee; and
- (c) the timing of the recovery of the fee.

### **208 Other material to be included in the template**

- (1) The template must clearly indicate which fees and costs are negotiable (for example, by stating in column 3 'The amount of this fee can be negotiated.').
- (2) An indication that a fee or cost is negotiable must be cross-referenced to an explanation outside the template in the 'Additional Explanation of Fees and Costs' part of the fees section.

## **Division 4—Additional explanation of fees and costs**

### **209 Matters to be included as additional explanation of fees and costs**

The following information, if relevant to the particular superannuation product or managed investment product, must be included under the heading ‘Additional Explanation of Fees and Costs’:

- (a) the explanation of the fees mentioned in footnote 1 for superannuation products and footnote 2 for managed investment products;
- (b) information on performance fees including:
  - (i) a statement about how performance fees affect administration fees and investment fees for a superannuation product, or management costs for a managed investment product; and
  - (ii) the method for calculating the fees; and
  - (iii) the amount of the fees, or an estimate of the amount if the amount is not known;
- (c) for tax—a cross reference to the “Tax” part of the Product Disclosure Statement;
- (ca) for insurance fees and other costs relating to insurance (if relevant)—a cross reference to the “Insurance” part of the Product Disclosure Statement;
- (d) if the product is subject to tax—whether the benefit of any tax deduction is passed on to the investor in the form of a reduced fee or cost;
- (e) an explanation of adviser remuneration that forms part of any fee or cost in the table, including (if known to the product issuer):
  - (i) the method of calculation; and
  - (ii) the amounts of commission or the range of amounts; and
  - (iii) whether the amounts are negotiable or rebatable; and
  - (iv) the way in which amounts may be negotiated or rebated;
- (f) an explanation of advice fees;
- (g) for a negotiated fee or cost—contact details of the person or body with whom the fee or cost can be negotiated and the manner of negotiation;
- (h) worked examples (if appropriate);
- (i) additional details of incidental fees (if appropriate);
- (j) details of transactional and operational costs such as brokerage and buy-sell spread, including:
  - (i) a description of the cost; and
  - (ii) the amount, or an estimate if the amount is not known; and
  - (iii) how and when the costs are recovered; and
  - (iv) a statement that the cost is an additional cost to the investor; and

- (v) whether any part of the buy-sell spread is paid to the product issuer or an external manager;
- (k) the following information about fee changes:
  - (i) if applicable, a statement about the issuer's right to change the amount of fees without the investor's consent;
  - (ii) any indexation arrangements that apply;
  - (iii) the period of advance notice required for fee changes;
  - (iv) any change in fee structure that is dependent on a person's employment;
- (l) if the issuer has instituted a flexible charging structure, for each applicable fee, if known:
  - (i) any maximum, and when it would apply; and
  - (ii) any waiver, and when it would not apply;
- (m) for a superannuation product—details of borrowing costs including:
  - (i) a description of the cost; and
  - (ii) the amount, or an estimate if the amount is not known; and
  - (iii) how and when the costs are recovered; and
  - (iv) a statement that the cost is an additional cost to the investor;
- (ma) before 30 September 2019, details of property operating costs to the extent those costs are not included in the investment fee or indirect costs for the relevant MySuper product or investment option offered by a superannuation entity, including:
  - (i) a description of the cost; and
  - (ii) the amount, or an estimate if the amount is not known; and
  - (iii) how and when the costs are recovered; and
  - (iv) a statement that the cost is an additional cost to the investor.

## **209AA Calculating transactional and operational costs**

For paragraphs 209(j) and (m), information about transactional and operational costs and, for a superannuation product or investment option in a superannuation product, borrowing costs and property operating costs for a product or investment option disclosed in a Product Disclosure Statement that is available during a particular financial year is to be determined for the previous financial year except that if product or investment option was not offered from at least 11 months before the end of the previous financial year, the transactional and operational costs and, for a superannuation product or investment option in a superannuation product, borrowing costs and property operating costs are to be determined based on the responsible person's reasonable estimate at the time the Statement is prepared of those costs that will apply for the current financial year, and if the product or investment option was first offered in the current financial year, since the time the product or investment option was first offered, adjusted to reflect a 12 month period.

## Division 4A—Defined fees for superannuation products

### 209A Defined fees for superannuation products

The following definitions must be included for a superannuation product under the heading “Defined fees”, or incorporated by reference:

#### *Activity fees*

A fee is an **activity fee** if:

- (a) the fee relates to costs incurred by the trustee *[OR the trustees]* of the superannuation entity that are directly related to an activity of the trustee *[OR the trustees]*:
  - (i) that is engaged in at the request, or with the consent, of a member; or
  - (ii) that relates to a member and is required by law; and
- (b) those costs are not otherwise charged as an administration fee, an investment fee, a buy-sell spread, a switching fee, an exit fee, an advice fee or an insurance fee.

#### *Administration fees*

An **administration fee** is a fee that relates to the administration or operation of the superannuation entity and includes costs that relate to that administration or operation, other than:

- (a) borrowing costs; and
- (b) indirect costs that are not paid out of the superannuation entity that the trustee has elected in writing will be treated as indirect costs and not fees, incurred by the trustee *[OR the trustees]* of the entity or in an interposed vehicle or derivative financial product; and
- (c) costs that are otherwise charged as an investment fee, a buy-sell spread, a switching fee, an exit fee, an activity fee, an advice fee or an insurance fee.

#### *Advice fees*

A fee is an **advice fee** if:

- (a) the fee relates directly to costs incurred by the trustee *[OR the trustees]* of the superannuation entity because of the provision of financial product advice to a member by:
  - (i) a trustee of the entity; or
  - (ii) another person acting as an employee of, or under an arrangement with, the trustee *[OR the trustees]* of the entity; and
- (b) those costs are not otherwise charged as an administration fee, an investment fee, a switching fee, an exit fee, an activity fee or an insurance fee.

#### *Buy-sell spreads*

A **buy-sell spread** is a fee to recover transaction costs incurred by the trustee *[OR the trustees]* of the superannuation entity in relation to the sale and purchase of assets of the entity.

### *Exit fees*

An **exit fee** is a fee to recover the costs of disposing of all or part of members' interests in the superannuation entity.

### *Indirect cost ratio*

The **indirect cost ratio (ICR)**, for a MySuper product or an investment option offered by a superannuation entity, is the ratio of the total of the indirect costs for the MySuper product or investment option, to the total average net assets of the superannuation entity attributed to the MySuper product or investment option.

Note: A fee deducted from a member's account or paid out of the superannuation entity is not an indirect cost.

### *Investment fees*

An **investment fee** is a fee that relates to the investment of the assets of a superannuation entity and includes:

- (a) fees in payment for the exercise of care and expertise in the investment of those assets (including performance fees); and
- (b) costs that relate to the investment of assets of the entity, other than:
  - (i) borrowing costs; and
  - (ii) indirect costs that are not paid out of the superannuation entity that the trustee has elected in writing will be treated as indirect costs and not fees, incurred by the trustee *[OR the trustees]* of the entity or in an interposed vehicle or derivative financial product; and
  - (iii) costs that are otherwise charged as an administration fee, a buy-sell spread, a switching fee, an exit fee, an activity fee, an advice fee or an insurance fee.

Note: The costs referred to in paragraph (b) do not include transactional and operational costs referred to in paragraphs (b), (ea) and (eb) of the definition of **transactional and operational costs**.

### *Switching fees*

#### *[In the case of a MySuper product:]*

A **switching fee** for a MySuper product is a fee to recover the costs of switching all or part of a member's interest in a superannuation entity from one class of beneficial interest in the entity to another.

#### *[In the case of a superannuation product that is not a MySuper product:]*

A **switching fee** for a superannuation products other than a MySuper product, is a fee to recover the costs of switching all or part of a member's interest in the superannuation entity from one investment option or product in the entity to another.

Note: If a Product Disclosure Statement covers both a MySuper product and another superannuation product, both definitions of **switching fee** must be included.

## Division 5—Example of annual fees and costs

### 210 Example of annual fees and costs

The example of annual fees and costs:

- (a) must contain fees and costs in accordance with the table in clause 211 or 212; and
- (b) must be set out using the headings and the form in clause 211 or 212; and
- (c) must be included in the 'Fees' section of a Product Disclosure Statement, following the fees and costs template.

### 211 Superannuation products—Example of annual fees and costs

This table gives an example of how the fees and costs for the *[insert name of generic MySuper product or other investment option as required by subclause 220(1)]* for this superannuation product can affect your superannuation investment over a 1 year period. You should use this table to compare this superannuation product with other superannuation products.

<b>EXAMPLE</b> — <i>[insert name of generic MySuper product or other investment option as required by subclause 220(1)]</i>		<b>BALANCE OF \$50 000</b>
Investment fees	1.6%	For every \$50 000 you have in the superannuation product you will be charged \$800 each year
<b>PLUS</b> Administration fees	\$52 (\$1 per week)	<b>And</b> , you will be charged \$52 in administration fees regardless of your balance
<b>PLUS</b> Indirect costs for the superannuation product	1.2%	<b>And</b> , indirect costs of \$600 each year will be deducted from your investment
<b>EQUALS</b> Cost of product		If your balance was \$50 000, then for that year you will be charged fees of <b>\$1 452</b> for the superannuation product.

Note: \* Additional fees may apply. **And**, if you leave the superannuation entity, you may be charged an **exit fee** of **\$x** and a **buy/sell spread** which also applies whenever you make a contribution, exit, rollover or investment switch. The **buy/sell spread** for exiting is **y%** (this will equal to **\$z** for every \$50,000 you withdraw).

Note: Substitute the relevant exit fee, buy/sell spread and total amount payable you charge for \$x, y% and \$z.

### 212 Managed investment products—Example of annual fees and costs for a balanced investment option or other investment option

#### Example of annual fees and costs for a balanced investment option or other investment option

This table gives an example of how the fees and costs in the balanced investment option for this managed investment product can affect your investment over a 1 year period. You should use this table to compare this product with other managed investment products.

<b>EXAMPLE</b> — <i>[insert name of balanced investment option or other investment option required by subclause 220(2)]</i>		<b>BALANCE OF \$50 000 WITH A CONTRIBUTION OF \$5 000 DURING YEAR</b>
Contribution Fees	0-4%	For every additional \$5 000 you put in, you will be charged between \$0 and \$200.

<b>EXAMPLE</b> — <i>[insert name of balanced investment option or other investment option required by subclause 220(2)]</i>		<b>BALANCE OF \$50 000 WITH A CONTRIBUTION OF \$5 000 DURING YEAR</b>
<b>PLUS</b> Management Costs	1.3%	<b>And</b> , for every \$50 000 you have in the <i>[insert name of balanced investment option or other investment option required by subclause 220(2)]</i> you will be charged \$650 each year.
<b>EQUALS</b> Cost of <i>[insert name of balanced investment option or other investment option required by subclause 220(2)]</i>		<p>If you had an investment of \$50 000 at the beginning of the year and you put in an additional \$5 000 during that year, you would be charged fees of from:</p> <p style="text-align: center;"><b>\$650 to \$850*</b></p> <p><b>What it costs you will depend on the investment option you choose and the fees you negotiate.</b></p>

\* Additional fees may apply:

**Establishment fee**—\$50

**And**, if you leave the managed investment scheme early, you may also be charged **exit fees** of between 0 and 5% of your total account balance (between \$0 and \$2 500 for every \$50 000 you withdraw)

## 213 Defined benefit funds

An example of fees and costs is not required in a Product Disclosure Statement for a defined benefit fund.

Note: **Defined benefit fund** is defined in subregulation 1.03(1) of the SIS Regulations.

## **Division 6—How to fill in the example of annual fees and costs**

### **214 Fees and costs must be ongoing amounts**

The fees and costs stated in the example must be typical ongoing fees that apply to the MySuper product or investment option.

Note: The example should not be based on “honeymoon rates”. It must be consistent with the statement for an existing member or product holder having the stated balance and level of contributions each year.

### **214A Example of annual fees and costs for a MySuper product—lifecycle MySuper product**

If the example of fees and costs for a MySuper product uses a lifecycle MySuper product, the investment fee quoted in the example must be the highest investment fee for a lifecycle stage of the lifecycle MySuper product.

### **215 Minimum entry balance rule**

If the minimum balance required to enter a superannuation entity or a managed investment scheme is greater than \$50 000, the example of annual fees and costs must be based on an amount that is the lowest multiple of \$50 000 that exceeds the minimum entry balance.

Example: If a superannuation entity or a managed investment scheme has a minimum entry balance of \$65 000, the relevant amount for the example of annual fees and costs is \$100 000.

### **216 Exit fees**

If an exit fee may be charged, it must be described in footnote to the table, based on:

- (a) a balance of \$50 000; or
- (b) if clause 215 applies—an amount that is a multiple of \$50 000.

### **217 Contribution fees**

- (1) The amounts of contribution fees to be inserted in the example of annual fees and costs for a managed investment product, are applied against a \$5 000 investment.
- (2) If a Product Disclosure Statement relates to a product:
  - (a) that is paid for by a single lump sum amount; and
  - (b) for which no additional contributions can be made;

the example of annual fees and costs should be modified by removing references to contributions or contribution fees.

- (3) The example must be based on a balance:
  - (a) of \$50 000; or
  - (b) worked out in accordance with clause 215.

Note: If there is a fee paid for the initial contribution, it should be described as the establishment fee.

## **218 Administration fees and investment fees for a superannuation product**

### *Administration fees*

- (1) The example of administration fees for a MySuper product or an investment option offered by a superannuation entity is applied to an amount of \$50 000 or an amount that is a multiple of \$50 000 if clause 215 applies.

Note: In calculating the amount, do not include contributions that may be made during the year.

- (2) If there is a range in the amount of administration fees that may be charged for a MySuper product or an investment option offered by a superannuation entity, the example must use the highest administration fees in the range.

### *Investment fees*

- (3) The example of investment fees for a MySuper product or an investment option offered by a superannuation entity is applied to an amount of \$50 000 or an amount that is a multiple of \$50 000 if clause 215 applies.

Note: In calculating the amount, do not include contributions that may be made during the year.

- (4) If there is a range in the amount of investment fees that may be charged for a MySuper product or an investment option offered by a superannuation entity, the example must use the highest investment fees in the range.

### *Indirect costs for a MySuper product or investment option*

- (5) The example of indirect costs for a MySuper product or an investment option offered by a superannuation entity must be worked out by applying the indirect cost ratio for the MySuper product or the investment option to an amount of \$50,000 or an amount that is a multiple of \$50,000 if clause 215 applies.

## **218A Management costs for a managed investment product**

- (1) The example of management costs for an investment option offered by a managed investment scheme is applied to an amount of \$50 000 or an amount that is a multiple of \$50 000 if clause 215 applies.

Note: In calculating the amount, do not include contributions that may be made during the year.

- (2) If there is a range in the amount of management costs that may be charged for an investment option offered by a managed investment scheme, the example must use the highest management costs in the range.
- (3) Management costs that are not deducted directly from a product holder's account must be calculated using the indirect cost ratio for the relevant investment option offered by the managed investment scheme.
- (4) Any percentage based management costs that are deducted directly from a product holder's account should be added to the percentage amount calculated under subclause (3).
- (5) Any dollar based management costs that are deducted directly from a product holder's account must be shown separately in the management costs cell.

Example 1: Management costs: 2 % deducted directly from your account + 1.6% deducted indirectly.

Example 2: Management costs: \$52 per year (\$1 per week) deducted directly from your account + 1.6% deducted indirectly.

Example 3: Management costs: \$52 per year (\$1 per week) + 1% deducted directly from your account + 1.6% deducted indirectly.

## **219 Withdrawal fees and exit fees**

- (1) The example of a withdrawal fee or an exit fee for a superannuation product or a managed investment product is applied against an amount of \$50 000 or an amount that is a multiple of \$50 000 if clause 215 applies.
- (2) In calculating the amount, do not include contributions that may be made during the year.

## **220 If there is no generic MySuper product or balanced investment option**

### *Superannuation entities*

- (1) If a superannuation entity does not offer a generic MySuper product, the example should be based on:
  - (a) where the superannuation entity offers a balanced investment option—the balanced investment option under which most assets of the superannuation entity are invested; and
  - (b) where the superannuation entity does not offer a balanced investment option—the investment option under which most assets of the superannuation entity are invested.

### *Managed investment schemes*

- (2) If a managed investment scheme does not offer a balanced investment option, the example should be based on:
  - (a) where the scheme offers a default investment option—that option; and
  - (b) where the scheme does not offer a default investment option—the investment option under which most assets of the scheme are invested.

## Division 7—Consumer Advisory Warning

### 221 Consumer advisory warning

#### (1) *Superannuation products*

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##### **DID YOU KNOW?**

**Small differences in both investment performance and fees and costs can have a substantial impact on your long term returns.**

**For example, total annual fees and costs of 2% of your account balance rather than 1% could reduce your final return by up to 20% over a 30 year period (for example reduce it from \$100 000 to \$80 000).**

**You should consider whether features such as superior investment performance or the provision of better member services justify higher fees and costs.**

**You or your employer, as applicable, may be able to negotiate to pay lower fees. Ask the fund or your financial adviser.**

##### **TO FIND OUT MORE**

If you would like to find out more, or see the impact of the fees based on your own circumstances, the **Australian Securities and Investments Commission (ASIC)** website ([www.moneySMART.gov.au](http://www.moneySMART.gov.au)) has a superannuation calculator to help you check out different fee options.

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#### (2) *Managed investment products*

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##### **DID YOU KNOW?**

**Small differences in both investment performance and fees and costs can have a substantial impact on your long term returns.**

**For example, total annual fees and costs of 2% of your account balance rather than 1% could reduce your final return by up to 20% over a 30 year period (for example reduce it from \$100 000 to \$80 000).**

**You should consider whether features such as superior investment performance or the provision of better member services justify higher fees and costs.**

**You may be able to negotiate to pay lower contribution fees and management costs where applicable. Ask the fund or your financial adviser.**

##### **TO FIND OUT MORE**

If you would like to find out more, or see the impact of the fees based on your own circumstances, the **Australian Securities and Investments Commission (ASIC)** website ([www.moneySMART.gov.au](http://www.moneySMART.gov.au)) has a managed funds fee calculator to help you check out different fee options.

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#### (3) In the Consumer Advisory Warning in subclause (2) ‘account’ may be replaced with ‘investment’.

## **222 Where to place the Consumer Advisory Warning**

The Consumer Advisory Warning referred to in subclause 221(1) must be located at the beginning of the fees section of the Product Disclosure Statement for superannuation products and the Consumer Advisory Warning referred to in subclause 221(2) must be located at the beginning of the fees section of the Product Disclosure Statement for managed investment products where fees or costs may be deducted from amounts to be held for members of the managed investment scheme.

## **Part 3—Fees and costs in periodic statements**

### **Division 1—Other Management Costs**

#### **301 Indirect costs related to investment and administration of accounts**

- (1) For a MySuper product or an investment option offered by a superannuation entity, the following text and the appropriate amounts, in dollars, must be inserted after the part of the periodic statement that itemises transactions during the period.

##### **Indirect costs of your investment**

This approximate amount has been deducted from your investment and covers amounts that have reduced the return on your investment but are not charged as a fee.

##### **Other fees of your investment**

This approximate amount or amounts have been deducted from your investment and covers fees that are not reflected as transactions on this statement.

Note: Other fees may be reported by the type of fees charged.

- (1A) For an offer of a managed investment product, the following text and the appropriate amount, in dollars, must be inserted after the part of the periodic statement that itemises transactions during the period.

##### **Indirect costs of your investment**

This approximate amount has been deducted from your investment and covers amounts that have reduced the return on your investment but are not charged to you directly as a fee.

- (1B) For a periodic statement for a MySuper product or an investment option offered by a superannuation entity, for a period ending on or before 29 June 2019, the amount disclosed for other fees under subclause (1) may be calculated excluding the buy-sell spread if it is stated in accordance with subclause (1E) that, “The total fees you paid do not include the buy-sell spread fee, because it is not reasonably practicable for us to include the buy-sell spread fee that you incurred during the period.”.
- (1C) For a periodic statement for a MySuper product or an investment option offered by a superannuation entity, for a period ending on or before 29 June 2019, the amount disclosed for other fees under subclause (1) may be calculated excluding property operating costs if it is stated in accordance with subclause (1E) that, “The total fees you paid do not include the property operating costs that you incurred during the period.”.
- (1D) For a periodic statement for a MySuper product or an investment option offered by a superannuation entity, for a period ending after 29 June 2019, and on or before 29 September 2019, the amount disclosed for other fees under subclause (1) may be calculated excluding property operating costs if it is stated in accordance with subclause (1E) that, “The total fees you paid do not include the property operating costs that you incurred during the period. An estimate of the amount of property operating costs incurred by the holder during the period is provided in the periodic statement.”.
- (1E) For the purposes of subclauses (1B) to (1D), a statement is stated in accordance with this subclause if the statement and each other statement made for the purposes of subclauses (1B) to (1D) is included:

- (a) immediately under the amount of total fees you paid in the periodic statement; or
  - (b) if it is not reasonably practicable to include the statements in that position in the periodic statement—a separate document that accompanies the periodic statement and that includes those statements as consecutive statements.
- (2) The amount inserted must include:
- (a) for a MySuper product or an investment option offered by a superannuation entity—the indirect costs for the MySuper product or investment option; and
  - (b) for an investment option offered by a managed investment scheme—all management costs not deducted directly from a product holder’s account during the reporting period.
- (3) The amount must be shown as a single total amount in dollars.
- (4) The amount for a managed investment product must be calculated by multiplying the indirect cost ratio for the relevant investment option by the product holder’s average account balance for the option over the reporting period.
- (5) For a superannuation product that is subject to tax, for any reporting period ending after 29 June 2019, if a reduced fee or cost is disclosed in the statement because of the benefit of any income tax deduction, the indirect costs, or other fees as appropriate, for the product must include the part of the cost that reduced the disclosed fee or costs.
- (6) For a managed investment product that is subject to tax, for any reporting period ending after 29 June 2019, if a reduced fee or cost is disclosed in the statement because of the benefit of any income tax deduction, the indirect costs for the product must include the part of the cost that reduced the disclosed fee or cost.

## **Division 2—Total fees**

### **302 Total of fees in the periodic statement**

- (1) The following text and the appropriate amount, in dollars, must be displayed:
- (a) at the end of the part of the periodic statement that itemises transactions during the period; or
  - (b) in a summary part of the periodic statement.

#### **TOTAL FEES YOU PAID**

This approximate amount includes all the fees and costs which affected your investment during the period.

- (2) The total fees you paid are the total of all fees and costs disclosed in the periodic statement.

## Division 3—Additional Explanation of Fees and Costs

### 303 Matters to be included as additional explanation of fees and costs

#### *Superannuation products*

- (1) The following information must be included in the periodic statement for a superannuation product under the heading “Additional Explanation of Fees and Costs”, if it has not been included in another part of the periodic statement:
  - (a) details of any activity fees, advice fees and insurance fees that were incurred by the member during the period;
  - (b) for a superannuation product that is subject to tax—whether the benefit of any tax deduction has been passed on to the investor in the form of a reduced fee or cost; and
  - (c) for any reporting period ending on or before 29 June 2019:
    - (i) the approximate total amount of borrowing costs that affected the investment of the member during the period or that amount combined with the amount required to be disclosed in accordance with subclause 302(1); or
    - (ii) details, including the relevant website address, about how to obtain information about borrowing costs for each MySuper product and investment option on the fund’s website; and
  - (d) for any reporting period ending after 29 June 2019, the approximate total amount of borrowing costs that affected the investment of the member during the period or that amount combined with the amount required to be disclosed in accordance with subclause 302(1).

#### *Managed investment products*

- (2) The following information must be included in the periodic statement under the heading “Additional Explanation of Fees and Costs”, if it has not been included in another part of the periodic statement:
  - (a) details of incidental fees, such as cheque dishonour fees, that were incurred by the product holder during the period;
  - (b) details of any service fees that may have been incurred by the product holder;
  - (c) for a managed investment product that is subject to tax—whether the benefit of any tax deduction has been passed on to the investor in the form of a reduced fee or cost; and
  - (d) for any reporting period ending after 29 June 2019, the approximate total amount of transactional and operational costs for the managed investment product that affected the investment of the holder during the period or that amount combined with the amount required to be disclosed in accordance with paragraph 302(1)(b) excluding costs that are both:
    - (i) referred to in paragraph (b), (ea) or (eb) of the definition of **transactional or operational costs** and that are a necessary part of the acquisition price of an asset;
    - (ii) recovered by a buy-sell spread for the managed investment product where the estimated amount of the buy-sell spread that the holder has paid in the period in dollars is disclosed in the periodic statement.

# Appendix 4 – Schedule 10 to the Corporations Regulations without CO 14/1252 amendments

# Schedule 10—Disclosure of fees and other costs

(regulations 7.9.16K, 7.9.16M and 7.9.16N)

## Part 1—Interpretation

### 101 Definitions

In this Schedule:

**activity fee**, for a superannuation product, has the meaning given by subsection 29V(7) of the SIS Act.

**administration fee**, for a superannuation product, has the meaning given by subsection 29V(2) of the SIS Act.

**advice fee**:

- (a) for a superannuation product—has the meaning given by subsection 29V(8) of the SIS Act; and
- (b) for a managed investment product—means an amount that is:
  - (i) paid or payable to a financial adviser for financial product advice to a retail client or product holder about an investment; and
  - (ii) not included in a contribution fee, withdrawal fee, exit fee, establishment fee or management cost.

**balanced investment option** means an investment option in which the ratio of investment in growth assets, such as shares or property, to investment in defensive assets, such as cash or bonds, is as close as practicable to 70:30.

**brokerage** means an amount paid or payable to a broker for undertaking a transaction for the acquisition or disposal of a financial product.

**buy-sell spread**:

- (a) for a superannuation product—has the meaning given by subsection 29V(4) of the SIS Act; or
- (b) for a managed investment product—means an amount, deducted from the value of a financial product of a product holder, that represents an apportionment, among product holders, of the actual or estimated transaction costs incurred by the managed investment scheme.

**contribution fee** means an amount paid or payable against the initial, and any subsequent, contributions made into a product by or for a retail client for the product.

Note: A contribution may be made by an employer on behalf of the product holder or retail client.

**distribution costs** means the costs or amounts paid or payable for the marketing, offer or sale of a product.

Note: This includes any related adviser remuneration component other than an advice fee.

**establishment fee** means an amount paid or payable for the establishment of a client's interest in a product.

Note: This does not include contribution fees paid or payable against the initial contribution into the product.

***exit fee:***

- (a) for a superannuation product—has the meaning given by subsection 29V(6) of the SIS Act; and
- (b) for a managed investment product—means an amount paid or payable on the disposal of all interests held in the product.

***incidental fees*** means costs or amounts, other than costs or fees defined in this clause, that are:

- (a) paid or payable in relation to the product; and
- (b) not material to a retail client's decision to acquire, hold or dispose of his or her interest in the product.

Example: Cheque dishonour fees.

***indirect cost*** of a MySuper product or an investment option offered by a superannuation entity means any amount that:

- (a) a trustee of the entity knows, or reasonably ought to know, will directly or indirectly reduce the return on the investment of a member of the entity in the MySuper product or investment option; and
- (b) is not charged to the member as a fee.

***insurance fee***, for a superannuation product, has the meaning given by subsection 29V(9) of the SIS Act.

***investment fee***, for a superannuation product, has the meaning given by subsection 29V(3) of the SIS Act.

***lifecycle MySuper product*** has the meaning given by regulation 7.9.07N.

***lifecycle stage*** has the meaning given by regulation 7.9.07N.

***performance***, of a managed investment product, a superannuation product, a MySuper product or an investment option, includes:

- (a) income in relation to the assets of, or attributed to, the managed investment product, the superannuation product, the MySuper product or the investment option; and
- (b) capital appreciation (realised or unrealised) to the value of the managed investment product, the superannuation product, the MySuper product or the investment option.

***performance fee*** means an amount paid or payable, calculated by reference to the performance of a managed investment product, a superannuation product, a MySuper product or an investment option.

***service fees*** means advice fees, special request fees and switching fees.

***special request fees*** includes fees paid or deducted from a product holder's managed investment product for a request made to the managed investment scheme.

Example: This applies to a fee for a request for additional information from a managed investment scheme.

***switching fee:***

- (a) for a superannuation product—has the meaning given by subsection 29V(5) of the SIS Act; or
- (b) for a managed investment product—means an amount paid or payable when a product holder transfers all or part of the product holder's interest in the managed investment product from one investment option to another.

***withdrawal fee*** means an amount, other than an exit fee, paid or payable in respect of:

- (a) a withdrawal; or
- (b) the disposal of an interest in a product.

## **102 Management costs**

- (1) ***Management costs***, for a managed investment product, means any of the following:
  - (a) an amount payable for administering the managed investment scheme;
  - (b) for a custodial arrangement—the cost involved, or amount paid or payable, for gaining access to, or participating in, the arrangement;
  - (c) distribution costs;
  - (d) other expenses and reimbursements in relation to the managed investment scheme;
  - (e) amounts paid or payable for investing in the assets of the managed investment scheme;
  - (f) amounts deducted from a common fund by way of fees, costs, charges or expenses, including:
    - (i) amounts retrieved by an external fund manager or a product issuer; and
    - (ii) amounts deducted from returns before allocation to the fund;
  - (g) estimated performance fees;
  - (h) any other investment-related expenses and reimbursements, including any associated with custodial arrangements.
- (2) The following fees and costs are not management costs for a managed investment product:
  - (a) a contribution fee;
  - (b) transactional and operational costs;
  - (c) an additional service fee;
  - (d) an establishment fee;
  - (e) a switching fee;
  - (f) an exit fee;
  - (g) a withdrawal fee;
  - (h) costs (related to a specific asset or activity to produce income) that an investor would incur if he or she invested directly in the asset;
  - (i) incidental fees.

### 103 Transactional and operational costs

*Transactional and operational costs* include the following:

- (a) brokerage;
- (b) buy-sell spread;
- (c) settlement costs (including custody costs);
- (d) clearing costs;
- (e) stamp duty on an investment transaction.

### 104 Indirect cost ratio

- (1) The *indirect cost ratio (ICR)*, for a MySuper product or an investment option offered by a superannuation entity, is the ratio of the total of the indirect costs for the MySuper product or investment option, to the total average net assets of the superannuation entity attributed to the MySuper product or investment option.

Note: A fee deducted directly from a member's account is not included in the indirect cost ratio.

- (1A) The *indirect cost ratio (ICR)*, for an investment option offered by a managed investment scheme, is the ratio of the management costs for the option that are not deducted directly from a product holder's account, to the total average net assets of the managed investment scheme that relates to the investment option.

Note: A fee deducted directly from a product holder's account is not included in the indirect cost ratio.

- (2) The ICR for a Product Disclosure Statement is to be determined for the financial year before the Product Disclosure Statement is issued.
- (3) The ICR for a periodic statement is to be determined over the latest reporting period.

## Part 2—Fees and Costs Template, example of annual fees and costs and Consumer Advisory Warning for Product Disclosure Statements

### Division 1—The fees and costs template for superannuation products

#### 201 Template for superannuation products

##### Fees and other costs

This document shows fees and other costs that you may be charged. These fees and other costs may be deducted from your money, from the returns on your investment or from the assets of the superannuation entity as a whole.

Other fees, such as activity fees, advice fees for personal advice and insurance fees, may also be charged, but these will depend on the nature of the activity, advice or insurance chosen by you.

Taxes, insurance fees and other costs relating to insurance are set out in another part of this document.

You should read all the information about fees and other costs because it is important to understand their impact on your investment.

*[If relevant]* The fees and other costs for each MySuper product offered by the superannuation entity, and each investment option offered by the entity, are set out on page *[insert page number]*.

<i>[Name of superannuation product]</i>		
<i>Type of fee</i>	<i>Amount</i>	<i>How and when paid</i>
<i>Investment fee</i>		
<i>Administration fee</i>		
<i>Buy-sell spread</i>		
<i>Switching fee</i>		
<i>Exit fee</i>		
<i>Advice fees</i>		
relating to all members		
investing in a particular		
MySuper product or investment		
option		
<i>Other fees and costs<sup>1</sup></i>		
<i>Indirect cost ratio</i>		

1. *[If there are other fees and costs, such as activity fees, advice fees for personal advice or insurance fees, include a cross-reference to the “Additional Explanation of Fees and Costs”.]*

## Division 2—The fees and costs template for managed investment products

### 202 Template for a multiple fee structure—managed investment products

#### Fees and other costs

This document shows fees and other costs that you may be charged. These fees and costs may be deducted from your money, from the returns on your investment or from the assets of the managed investment scheme as a whole.

Taxes and insurance costs are set out in another part of this document.

You have 2 different fee payment options:

- (a) to pay contribution fees upfront, at the time when you make each investment into the managed investment scheme; or
- (b) to pay contribution fees later (for example, on the termination of your investment or by way of other increased fees).

Note: You may pay more in total fees if you choose to pay contribution fees later.

You should read all the information about fees and costs because it is important to understand their impact on your investment.

*[If relevant]* Fees and costs for particular investment options are set out on page *[insert page number]*.

<i>[Name of managed investment product]</i>			
Type of fee or cost	Amount		How and when paid
	Option to pay contribution fees upfront	Option to pay contribution fees later	
<b>Fees when your money moves in or out of the managed investment product</b>			
<i>Establishment fee</i> The fee to open your investment			
<i>Contribution fee<sup>1</sup></i> The fee on each amount contributed to your investment			
<i>Withdrawal fee<sup>1</sup></i> The fee on each amount you take out of your investment			
<i>Exit fee<sup>1</sup></i> The fee to close your investment			

<i>[Name of managed investment product]</i>		
Type of fee or cost	Amount	How and when paid
<b>Management costs</b>		
<i>The fees and costs for managing your investment<sup>1</sup></i> The amount you pay for specific investment options is shown at page <i>[insert page number]</i>		
<b>Service fees<sup>2</sup></b>		
<i>Switching fee</i> The fee for changing investment options		

1. This fee includes an amount payable to an adviser. (See Division 4, “Adviser remuneration” under the heading “Additional Explanation of Fees and Costs”.)
2. *[If there are other service fees, such as advice fees or special request fees, include a cross-reference to the “Additional Explanation of Fees and Costs”.]*

## 202A Template for single fee structure—managed investment products

### Fees and other costs

This document shows fees and other costs that you may be charged. These fees and costs may be deducted from your money, from the returns on your investment or from the assets of the managed investment scheme as a whole.

Taxes and insurance costs are set out in another part of this document.

You should read all the information about fees and costs because it is important to understand their impact on your investment.

*[If relevant]* Fees and costs for particular investment options are set out on page *[insert page number]*.

<i>[Name of managed investment product]</i>		
Type of fee or cost	Amount	How and when paid
<b>Fees when your money moves in or out of the managed investment product</b>		
<i>Establishment fee</i> The fee to open your investment		
<i>Contribution fee<sup>1</sup></i> The fee on each amount contributed to your investment		

<i>[Name of managed investment product]</i>		
<b>Type of fee or cost</b>	<b>Amount</b>	<b>How and when paid</b>
<i>Withdrawal fee<sup>1</sup></i> The fee on each amount you take out of your investment		
<i>Exit fee<sup>1</sup></i> The fee to close your investment		
<b>Management costs</b>		
<i>The fees and costs for managing your investment<sup>1</sup></i> The amount you pay for specific investment options is shown at page <i>[insert page number]</i>		
<b>Service fees<sup>2</sup></b>		
<i>Switching fee</i> The fee for changing investment options		

1. This fee includes an amount payable to an adviser. (See Division 4, “Adviser remuneration” under the heading “Additional Explanation of Fees and Costs”.)
2. *[If there are other service fees, such as advice fees or special request fees, include a cross-reference to the “Additional Explanation of Fees and Costs”.]*

## **Division 3—How to fill in the template**

### **203 The preamble**

The material in the preamble to the template should only include matters that are relevant to the product.

Example: Insurance costs will generally not be relevant to a managed investment product.

### **204 Column 2—presentation of amounts**

- (1) This clause, clause 205 and clause 206 are subject to regulations 7.9.15A, 7.9.15B and 7.9.15C.
- (2) If a particular fee or cost is not charged, 'nil', 'zero', '0' or 'not applicable' (if it would not be misleading) must be written in column 2 opposite the type of fee or cost.
- (3) If it is not possible to determine a single amount or percentage of a fee or cost, it may be written as a range of fees or costs.
- (4) If the exact amount of a fee or cost paid or payable is not known, an amount that is a reasonable estimate of the amount attributable to the retail client must be shown.
- (5) An amount set out in accordance with subclause (4) must be clearly designated as an estimate.
- (6) If an amount or cost has a number of components, the amount of each component must be listed separately.  
  
Example: Management costs: 1.8% of product holder's balance + \$70 per year.
- (7) A cost or amount paid or payable must include, if applicable:
  - (a) GST less any reduced inputs tax credits; and
  - (b) stamp duty.

### **205 Column 2—include information for each MySuper product or investment option**

- (1) The fee information must be set out:
  - (a) for superannuation products—for each MySuper product and each investment option offered by the relevant superannuation entity; and
  - (b) for managed investment products—for each investment option offered by the relevant managed investment scheme.
- (2) It may be:
  - (a) set out in the table; or
  - (b) cross-referenced in the table to another section of the Product Disclosure Statement that contains the relevant fee information.

## **206 Presentation of multiple fee payment options**

If a superannuation entity or managed investment scheme has more than 2 options for the payment of fees:

- (a) the number of fee payment options must be set out in the preamble; and
- (b) details of all fee payment options must be set out in the template.

## **207 Column 3—how and when fees and costs are payable**

Column 3 of the template must set out:

- (a) how the fee is or will be recovered, for example by deduction from:
  - (i) the member's investment balance; or
  - (ii) the assets of the superannuation entity or managed investment scheme;
  - (iii) contributions; or
  - (iv) withdrawals; and
- (b) the recurrence of the recovery of the fee; and
- (c) the timing of the recovery of the fee.

## **208 Other material to be included in the template**

- (1) The template must clearly indicate which fees and costs are negotiable (for example, by stating in column 3 'The amount of this fee can be negotiated.').
- (2) An indication that a fee or cost is negotiable must be cross-referenced to an explanation outside the template in the 'Additional Explanation of Fees and Costs' part of the fees section.

## **Division 4—Additional explanation of fees and costs**

### **209 Matters to be included as additional explanation of fees and costs**

The following information, if relevant to the particular superannuation product or managed investment product, must be included under the heading ‘Additional Explanation of Fees and Costs’:

- (a) the explanation of the fees mentioned in footnote 1 for superannuation products and footnote 2 for managed investment products;
- (b) information on performance fees including:
  - (i) a statement about how performance fees affect administration fees and investment fees for a superannuation product, or management costs for a managed investment product; and
  - (ii) the method for calculating the fees; and
  - (iii) the amount of the fees, or an estimate of the amount if the amount is not known;
- (c) for tax—a cross reference to the “Tax” part of the Product Disclosure Statement;
- (ca) for insurance fees and other costs relating to insurance (if relevant)—a cross reference to the “Insurance” part of the Product Disclosure Statement;
- (d) if the product is subject to tax—whether the benefit of any tax deduction is passed on to the investor in the form of a reduced fee or cost;
- (e) an explanation of adviser remuneration that forms part of any fee or cost in the table, including (if known to the product issuer):
  - (i) the method of calculation; and
  - (ii) the amounts of commission or the range of amounts; and
  - (iii) whether the amounts are negotiable or rebatable; and
  - (iv) the way in which amounts may be negotiated or rebated;
- (f) an explanation of advice fees;
- (g) for a negotiated fee or cost—contact details of the person or body with whom the fee or cost can be negotiated and the manner of negotiation;
- (h) worked examples (if appropriate);
- (i) additional details of incidental fees (if appropriate);
- (j) details of transactional and operational costs such as brokerage and buy-sell spread, including:
  - (i) a description of the cost; and
  - (ii) the amount, or an estimate if the amount is not known; and
  - (iii) how and when the costs are recovered; and
  - (iv) a statement that the cost is an additional cost to the investor; and
  - (v) whether any part of the buy-sell spread is paid to the product issuer or an external manager;
- (k) the following information about fee changes:
  - (i) if applicable, a statement about the issuer’s right to change the amount of fees without the investor’s consent;
  - (ii) any indexation arrangements that apply;
  - (iii) the period of advance notice required for fee changes;

- (iv) any change in fee structure that is dependent on a person's employment;
- (l) if the issuer has instituted a flexible charging structure, for each applicable fee, if known:
  - (i) any maximum, and when it would apply; and
  - (ii) any waiver, and when it would not apply;
- (m) for a superannuation product—details regarding the protection of small accounts (member protection rules) unless already included in the Product Disclosure Statement.

## Division 4A—Defined fees for superannuation products

### 209A Defined fees for superannuation products

The following definitions must be included for a superannuation product under the heading “Defined fees”:

#### *Activity fees*

A fee is an **activity fee** if:

- (a) the fee relates to costs incurred by the trustee [*OR the trustees*] of the superannuation entity that are directly related to an activity of the trustee [*OR the trustees*]:
  - (i) that is engaged in at the request, or with the consent, of a member; or
  - (ii) that relates to a member and is required by law; and
- (b) those costs are not otherwise charged as an administration fee, an investment fee, a buy-sell spread, a switching fee, an exit fee, an advice fee or an insurance fee.

#### *Administration fees*

An **administration fee** is a fee that relates to the administration or operation of the superannuation entity and includes costs incurred by the trustee [*OR the trustees*] of the entity that:

- (a) relate to the administration or operation of the entity; and
- (b) are not otherwise charged as an investment fee, a buy-sell spread, a switching fee, an exit fee, an activity fee, an advice fee or an insurance fee.

#### *Advice fees*

A fee is an **advice fee** if:

- (a) the fee relates directly to costs incurred by the trustee [*OR the trustees*] of the superannuation entity because of the provision of financial product advice to a member by:
  - (i) a trustee of the entity; or
  - (ii) another person acting as an employee of, or under an arrangement with, the trustee [*OR the trustees*] of the entity; and
- (b) those costs are not otherwise charged as an administration fee, an investment fee, a switching fee, an exit fee, an activity fee or an insurance fee.

#### *Buy-sell spreads*

A **buy-sell spread** is a fee to recover transaction costs incurred by the trustee [*OR the trustees*] of the superannuation entity in relation to the sale and purchase of assets of the entity.

#### *Exit fees*

An **exit fee** is a fee to recover the costs of disposing of all or part of members’ interests in the superannuation entity.

### *Indirect cost ratio*

The **indirect cost ratio (ICR)**, for a MySuper product or an investment option offered by a superannuation entity, is the ratio of the total of the indirect costs for the MySuper product or investment option, to the total average net assets of the superannuation entity attributed to the MySuper product or investment option.

Note: A dollar-based fee deducted directly from a member's account is not included in the indirect cost ratio.

### *Investment fees*

An **investment fee** is a fee that relates to the investment of the assets of a superannuation entity and includes:

- (a) fees in payment for the exercise of care and expertise in the investment of those assets (including performance fees); and
- (b) costs incurred by the trustee [*OR the trustees*] of the entity that:
  - (i) relate to the investment of assets of the entity; and
  - (ii) are not otherwise charged as an administration fee, a buy-sell spread, a switching fee, an exit fee, an activity fee, an advice fee or an insurance fee.

### *Switching fees*

A **switching fee** is a fee to recover the costs of switching all or part of a member's interest in the superannuation entity from one class of beneficial interest in the entity to another.

## Division 5—Example of annual fees and costs

### 210 Example of annual fees and costs

The example of annual fees and costs:

- (a) must contain fees and costs in accordance with the table in clause 211 or 212; and
- (b) must be set out using the headings and the form in clause 211 or 212; and
- (c) must be included in the 'Fees' section of a Product Disclosure Statement, following the fees and costs template.

### 211 Superannuation products—Example of annual fees and costs for a MySuper product

This table gives an example of how the fees and costs for the generic MySuper product for this superannuation product can affect your superannuation investment over a 1 year period. You should use this table to compare this superannuation product with other superannuation products.

<b>EXAMPLE—MySuper product</b>		<b>BALANCE OF \$50 000</b>
Investment fees	1.6%	For every \$50 000 you have in the MySuper product you will be charged \$800 each year
<b>PLUS</b> Administration fees	\$52 (\$1 per week)	<b>And</b> , you will be charged \$52 in administration fees regardless of your balance
<b>PLUS</b> Indirect costs for the MySuper product	1.2%	<b>And</b> , indirect costs of \$600 each year will be deducted from your investment
<b>EQUALS</b> Cost of product		If your balance was \$50 000, then for that year you will be charged fees of <b>\$1 452</b> for the MySuper product.

Note: \* Additional fees may apply. **And**, if you leave the superannuation entity early, you may also be charged **exit fees** of between 0% and 5% of your total account balance (between \$0 and \$2 500 for every \$50 000 you withdraw).

### 212 Managed investment products—Example of annual fees and costs for a balanced investment option

#### Example of annual fees and costs for a balanced investment option

This table gives an example of how the fees and costs in the balanced investment option for this managed investment product can affect your investment over a 1 year period. You should use this table to compare this product with other managed investment products.

<b>EXAMPLE—the Balanced Investment Option</b>		<b>BALANCE OF \$50 000 WITH A CONTRIBUTION OF \$5 000 DURING YEAR</b>
Contribution Fees	0-4%	For every additional \$5 000 you put in, you will be charged between \$0 and \$200.

<b>PLUS</b> Management Costs	1.3%	<b>And</b> , for every \$50 000 you have in the balanced investment option you will be charged \$650 each year.
<b>EQUALS</b> Cost of balanced investment option		<p>If you had an investment of \$50 000 at the beginning of the year and you put in an additional \$5 000 during that year, you would be charged fees of from:</p> <p style="text-align: center;"><b>\$650 to \$850*</b></p> <p><b>What it costs you will depend on the investment option you choose and the fees you negotiate.</b></p>

\* Additional fees may apply:

**Establishment fee**—\$50

**And**, if you leave the managed investment scheme early, you may also be charged **exit fees** of between 0 and 5% of your total account balance (between \$0 and \$2 500 for every \$50 000 you withdraw)

## 213 Defined benefit funds

An example of fees and costs is not required in a Product Disclosure Statement for a defined benefit fund.

Note: *Defined benefit fund* is defined in subregulation 1.03(1) of the SIS Regulations.

## **Division 6—How to fill in the example of annual fees and costs**

### **214 Fees and costs must be ongoing amounts**

The fees and costs stated in the example must be typical ongoing fees that apply to the MySuper product or investment option.

Note: The example should not be based on “honeymoon rates”. It must be consistent with the statement for an existing member or product holder having the stated balance and level of contributions each year.

### **214A Example of annual fees and costs for a MySuper product—lifecycle MySuper product**

If the example of fees and costs for a MySuper product uses a lifecycle MySuper product, the investment fee quoted in the example must be the highest investment fee for a lifecycle stage of the lifecycle MySuper product.

### **215 Minimum entry balance rule**

If the minimum balance required to enter a superannuation entity or a managed investment scheme is greater than \$50 000, the example of annual fees and costs must be based on an amount that is the lowest multiple of \$50 000 that exceeds the minimum entry balance.

Example: If a superannuation entity or a managed investment scheme has a minimum entry balance of \$65 000, the relevant amount for the example of annual fees and costs is \$100 000.

### **216 Exit fees**

If an exit fee may be charged, it must be described in footnote to the table, based on:

- (a) a balance of \$50 000; or
- (b) if clause 215 applies—an amount that is a multiple of \$50 000.

### **217 Contribution fees**

- (1) The amounts of contribution fees to be inserted in the example of annual fees and costs for a managed investment product, are applied against a \$5 000 investment.
- (2) If a Product Disclosure Statement relates to a product:
  - (a) that is paid for by a single lump sum amount; and
  - (b) for which no additional contributions can be made;the example of annual fees and costs should be modified by removing references to contributions or contribution fees.
- (3) The example must be based on a balance:
  - (a) of \$50 000; or
  - (b) worked out in accordance with clause 215.

Note: If there is a fee paid for the initial contribution, it should be described as the establishment fee.

## **218 Administration fees and investment fees for a superannuation product**

### *Administration fees*

- (1) The example of administration fees for a MySuper product or an investment option offered by a superannuation entity is applied to an amount of \$50 000 or an amount that is a multiple of \$50 000 if clause 215 applies.

Note: In calculating the amount, do not include contributions that may be made during the year.

- (2) If there is a range in the amount of administration fees that may be charged for a MySuper product or an investment option offered by a superannuation entity, the example must use the highest administration fees in the range.

### *Investment fees*

- (3) The example of investment fees for a MySuper product or an investment option offered by a superannuation entity is applied to an amount of \$50 000 or an amount that is a multiple of \$50 000 if clause 215 applies.

Note: In calculating the amount, do not include contributions that may be made during the year.

- (4) If there is a range in the amount of investment fees that may be charged for a MySuper product or an investment option offered by a superannuation entity, the example must use the highest investment fees in the range.

### *Indirect costs for a MySuper product or investment option*

- (5) The example of indirect costs for a MySuper product or an investment option offered by a superannuation entity must be worked out by applying the indirect cost ratio for the MySuper product or the investment option to an amount of \$50,000 or an amount that is a multiple of \$50,000 if clause 215 applies.

## **218A Management costs for a managed investment product**

- (1) The example of management costs for an investment option offered by a managed investment scheme is applied to an amount of \$50 000 or an amount that is a multiple of \$50 000 if clause 215 applies.

Note: In calculating the amount, do not include contributions that may be made during the year.

- (2) If there is a range in the amount of management costs that may be charged for an investment option offered by a managed investment scheme, the example must use the highest management costs in the range.
- (3) Management costs that are not deducted directly from a product holder's account must be calculated using the indirect cost ratio for the relevant investment option offered by the managed investment scheme.
- (4) Any percentage based management costs that are deducted directly from a product holder's account should be added to the percentage amount calculated under subclause (3).

- (5) Any dollar based management costs that are deducted directly from a product holder's account must be shown separately in the management costs cell.

Example 1: Management costs: 2 % deducted directly from your account + 1.6% deducted indirectly.

Example 2: Management costs: \$52 per year (\$1 per week) deducted directly from your account + 1.6% deducted indirectly.

Example 3: Management costs: \$52 per year (\$1 per week) + 1% deducted directly from your account + 1.6% deducted indirectly.

## **219 Withdrawal fees and exit fees**

- (1) The example of a withdrawal fee or an exit fee for a superannuation product or a managed investment product is applied against an amount of \$50 000 or an amount that is a multiple of \$50 000 if clause 215 applies.
- (2) In calculating the amount, do not include contributions that may be made during the year.

## **220 If there is no generic MySuper product or balanced investment option**

### *Superannuation entities*

- (1) If a superannuation entity does not offer a generic MySuper product, the example should be based on:
  - (a) where the superannuation entity offers a balanced investment option—the balanced investment option under which most assets of the superannuation entity are invested; and
  - (b) where the superannuation entity does not offer a balanced investment option—the investment option under which most assets of the superannuation entity are invested.

### *Managed investment schemes*

- (2) If a managed investment scheme does not offer a balanced investment option, the example should be based on:
  - (a) where the scheme offers a default investment option—that option; and
  - (b) where the scheme does not offer a default investment option—the investment option under which most assets of the scheme are invested.

## **Division 7—Consumer Advisory Warning**

### **221 Consumer advisory warning**

#### **DID YOU KNOW?**

**Small differences in both investment performance and fees and costs can have a substantial impact on your long term returns.**

**For example, total annual fees and costs of 2% of your account balance rather than 1% could reduce your final return by up to 20% over a 30 year period (for example, reduce it from \$100 000 to \$80 000).**

**You should consider whether features such as superior investment performance or the provision of better member services justify higher fees and costs.**

**Your employer may be able to negotiate to pay lower administration fees. Ask the fund or your financial adviser.**

#### **TO FIND OUT MORE**

If you would like to find out more, or see the impact of the fees based on your own circumstances, the **Australian Securities and Investments Commission (ASIC)** website ([www.moneysmart.gov.au](http://www.moneysmart.gov.au)) has a [*superannuation or managed investment fee*] calculator to help you check out different fee options.

### **222 Where to place the Consumer Advisory Warning**

The Consumer Advisory Warning must be located at the beginning of the fees section of the Product Disclosure Statement.

## **Part 3—Fees and costs in periodic statements**

### **Division 1—Other Management Costs**

#### **301 Indirect costs related to investment and administration of accounts**

- (1) The following text and the appropriate amount, in dollars, must be inserted after the part of the periodic statement that itemises transactions during the period.

#### **Indirect costs of your investment**

This approximate amount has been deducted from your investment and includes amounts that have reduced the return on your investment but are not charged directly to you as a fee.

- (2) The amount inserted must include:
  - (a) for a MySuper product or an investment option offered by a superannuation entity—the indirect costs for the MySuper product or investment option;  
and
  - (b) for an investment option offered by a managed investment scheme—all management costs not deducted directly from a product holder's account during the reporting period.
- (3) The amount must be shown as a single total amount in dollars.
- (4) The amount for a managed investment product must be calculated by multiplying the indirect cost ratio for the relevant investment option by the product holder's average account balance for the option over the reporting period.

## **Division 2—Total fees**

### **302 Total of fees in the periodic statement**

- (1) The following text and the appropriate amount, in dollars, must be displayed:
  - (a) at the end of the part of the periodic statement that itemises transactions during the period; or
  - (b) in a summary part of the periodic statement.

#### **TOTAL FEES YOU PAID**

This approximate amount includes all the fees and costs which affected your investment during the period.

- (2) The total fees you paid are the total of all fees and costs disclosed in the periodic statement.

## **Division 3—Additional Explanation of Fees and Costs**

### **303 Matters to be included as additional explanation of fees and costs**

#### *Superannuation products*

- (1) The following information must be included in the periodic statement for a superannuation product under the heading “Additional Explanation of Fees and Costs”, if it has not been included in another part of the periodic statement:
  - (a) details of any activity fees, advice fees and insurance fees that were incurred by the member during the period;
  - (b) for a superannuation product that is subject to tax—whether the benefit of any tax deduction has been passed on to the investor in the form of a reduced fee or cost.

#### *Managed investment products*

- (2) The following information must be included in the periodic statement under the heading “Additional Explanation of Fees and Costs”, if it has not been included in another part of the periodic statement:
  - (a) details of incidental fees, such as cheque dishonour fees, that were incurred by the product holder during the period;
  - (b) details of any service fees that may have been incurred by the product holder;
  - (c) for a managed investment product that is subject to tax—whether the benefit of any tax deduction has been passed on to the investor in the form of a reduced fee or cost.