

EXPLANATORY STATEMENT for ASIC Corporations (Amendment) Instrument 2017/664

Prepared by the Australian Securities and Investments Commission

Corporations Act 2001

The Australian Securities and Investments Commission (*ASIC*) makes *ASIC Corporations (Amendment) Instrument 2017/664* (the ***Amendment Instrument***) under subsection 1020F(1) of the *Corporations Act 2001* (the *Act*).

Subsection 1020F(1) of the *Act* provides that ASIC may:

- (a) exempt a person or financial product or a class of persons or financial products from all or specified provisions of Part 7.9 of the *Act*; or
- (b) declare that Part 7.9 of the *Act* applies in relation to a person or financial product, or a class of persons or financial products, as if specified provisions were omitted, modified or varied as specified in the declaration.

Under subsection 33(3) of the *Acts Interpretation Act 1901*, where an Act confers a power to make, grant or issue any instrument (including rules, regulations or by-laws), the power shall be construed as including a power exercisable in the like manner and subject to the like conditions (if any) to repeal, rescind, revoke, amend, or vary any such instrument.

The *Amendment Instrument* amends ASIC Class Order [CO 14/1252] (***ICO 14/1252***).

1. Background

Schedule 10 to the Corporations Regulations 2001 (the ***Regulations***) was introduced in 2005 and sets out requirements for the disclosure of fees and costs of superannuation and managed investment products in Product Disclosure Statements and in periodic statements that must be given to product holders.

Stronger Super reforms introduced from 1 July 2013 included a number of amendments to the Regulations. Some of the amendments caused unintended inconsistencies in terminology between Schedule 10 and Schedules 10D and 10E to the Regulations that apply to short form superannuation Product Disclosure

Statements and registered managed investment scheme Product Disclosure Statements, respectively. The Stronger Super reforms also included some minor drafting anomalies that could be interpreted in a way that did not reflect the intention with which they were made.

In 2013/14, ASIC undertook a review of industry fee and cost disclosure practices. A key finding of this review was that some industry participants were adopting various interpretations of Schedule 10 to the Regulations, in particular interpretations of 'indirect costs' for superannuation products and of 'management costs' for managed investment products. For example, some products issuers had formed the view that, contrary to the intention of the Regulations, the Regulations do not require costs associated with investing through interposed vehicles to be included in their products' indirect costs or management costs. In response to the review, after consultation with industry and relevant stakeholders, on 8 December 2014 ASIC made [CO 14/1252] which revised some of the definitions in Schedule 10, including the indirect cost and management cost definitions, and clarified the costs that must be disclosed, in keeping with the intended effect of Schedule 10 to the Regulations. [CO 14/1252] also addressed some provisions that could be interpreted in an anomalous way that were included in the Regulations as part of the Stronger Super reforms.

Following the release of [CO 14/1252], ASIC consulted on revisions to ASIC Regulatory Guide 97 Disclosing fees and costs in PDSs and periodic statements. In response to this consultation we received feedback from industry indicating that amendments to [CO 14/1252] were required. ASIC has since made a number of legislative instruments clarifying:

- (a) the definitions of 'interposed vehicle' and 'indirect cost';
- (b) how derivative fees and costs need to be disclosed as part of indirect costs;
- (c) the requirements for periodic statements.

ASIC has also defined borrowing costs, to assist in cost disclosure.

2. Purpose of the instrument

The purpose of the Amendment Instrument is to amend [CO 14/1252] which modifies the Act and Schedule 10 to the Regulations. The Amendment Instrument amends for a temporary period the disclosure of property operating costs for superannuation products. It also clarifies the definition of interposed vehicles inserted by [CO 14/1252] and modifies the reporting of some fees and costs on periodic statements for a temporary period.

The Amendment Instrument provides responsible entities of managed investment products with the ability to permanently elect a reduced maximum period in which to

give periodic statements for investors exiting the product. The Amendment Instrument also makes a few minor amendments to correct a few small typographical errors in [CO 14/1252].

3. Operation of the instrument

Through Schedule 1 to the Amendment Instrument, the Amending Instrument amends [CO 14/1252], which modifies or varies Part 7.9 of the Act as it applies in relation to managed investment and superannuation products.

Paragraph 1 in Schedule 1 to the Amendment Instrument inserts paragraph 5CB into [CO 14/1252]. This inserted paragraph modifies paragraph 1017D(3) of the Act to provide issuers of managed investment products with the ability to reduce the maximum period in which they must provide periodic statements to investors exiting those products (exit statements). An Issuer will be required to give exit statements to exited investors as soon as practicable after the issuer becomes aware that the investors have ceased to hold the product and in any event the issuer will need to give the exit statements to the exited investors within the current maximum period of six months, or alternatively can elect to provide exit statements to exited investors within a specified maximum period of at least one month and less than six months from the end of the reporting period. Issuers electing to provide exit statements within a maximum specified period of at least one month and less than six months from the end of the reporting period may do so by publishing a notice on their website. This notice cannot be amended or revoked.

This modification enables issuers of managed investment products to bring forward the time at which exit statements must be provided to a time before the disclosure requirements as modified by [CO 14/1252] apply. In turn this allows issuers to defer the reporting period end date for exit statements from which [CO 14/1252] otherwise applies—[CO 14/1252] applies in relation to periodic statements which may be given on or after 1 January 2018. For example, if a managed investment product issuer elects to provide exit statements for the product within a maximum period of one month of the investor ceasing to hold the product, the reporting period end date from which [CO 14/1252] applies to this product's exit statements becomes 1 December 2017. If the elected specified period is two months, the reporting period end date from which [CO 14/1252] applies becomes 1 November 2017.

Paragraph 2 in Schedule 1 to the Amendment Instrument inserts paragraph 5E into [CO 14/1252]. This inserted paragraph omits paragraph 7.9.75(1)(b) of the Regulations for superannuation products and managed investment products. Paragraph 7.9.75(1)(b) requires inclusion of information about the notional proportion of expenses, costs and charges incurred including in common funds into which money

from the financial product is invested. The Amending Instrument replaces the obligations imposed by paragraph 7.9.75(1)(b) with provisions that have more certain operation, and transitional arrangements.

Paragraph 3 in Schedule 1 to the Amendment Instrument modifies sub-subparagraph 6(a)(iaa) in [CO 14/1252] to clarify the definition of borrowing costs. The amendment ensures that costs that relate to lending are not treated as borrowing costs.

Paragraph 4 in Schedule 1 to the Amendment Instrument inserts after sub-subparagraph 6(a)(iaa) in [CO 14/1252] sub-subparagraph 6(a)(iib) that defines 'property operating costs'. This definition is inserted to facilitate providing superannuation trustees by the Amending Instrument the option until 30 September 2018 to disclose 'property operating costs' under 'Additional Information about fees and costs' in the product disclosure statement rather than as part of the Investment fee or Indirect Costs.

Paragraph 5 in Schedule 1 to the Amendment Instrument modifies sub-subparagraph 6(a)(iv) in [CO 14/1252] by omitting “by inserting after the definition of *withdrawal fee*” and substitutes “after the definition of *withdrawal fee*, insert”. The modification also clarifies the application of notional paragraph 101A(1)(a)). This modification is to avoid doubt that amounts that are paid by persons who are paying returns to the relevant product or investment option or to the issuer of the relevant product or option that are retained by the issuer are included as indirect costs, subject to defined exceptions. This includes any payments of expenses by tenants for the benefit of the landlord who is the issuer or an interposed vehicle, and includes any fees and costs paid by borrowers from loan-based funds, such as mortgage funds and marketplace lending funds, retained by the issuer.

This paragraph also clarifies the definition of ‘indirect costs’ in notional paragraph 101A(1)(b). Paragraph 6 in Schedule 1 to the Amendment Instrument modifies Sub-subparagraph 6(a)(v) in [CO 14/1252]. The modifications to this sub-subparagraph insert after notional paragraph 101B(4) paragraphs 101B(4A), 101B(4B), 101B(4C) and 101B(4D) to Schedule 10 the Regulations. These paragraphs modify the definition of interposed vehicle. The amendments make more certain that entities through which exposures to property or similar are obtained are interposed vehicles. Further the amendments make clear that investments in entities that are not infrastructure entities, as defined, are treated as interposed vehicles unless the entities form part of an investment strategy that is directed to securities of listed entities.

Paragraph 7 in Schedule 1 to the Amendment Instrument inserts “;” at the end of sub-subparagraph 6(a)(v).

Paragraph 8 in Schedule 1 to the Amendment Instrument repeals and replaces sub-paragraph 6(baa). The replacement sub-paragraph inserts (baa) in clause 103((definition of *transactional and operational costs*) to Schedule 10 to the Regulations. The amendment makes clear for avoidance of doubt that transactional

costs that are included in the price of an asset being acquired are to be included as transactional and operational costs, even if they are not a buy-sell spread (the buy-sell spread is already required to be disclosed).

Paragraph 9 in Schedule 1 to the Amendment Instrument modifies sub-paragraph 6(e). The modification to sub-paragraph 6(e) inserts, after clause 209(m) in Schedule 10 to the Regulations, clause 209(ma) which provides for disclosure of the amount of property operating costs before 30 September 2018, if the superannuation trustee elects not to include property operating costs in the disclosed investment fee or indirect costs in a PDS until then.

Paragraph 10 in Schedule 1 to the Amendment Instrument modifies Subparagraph 6(ea) (notional clause 209AA) omits from notional clause 209AA “subclause 209(j) and paragraph 209(m)” and substitutes “paragraphs 209(j) and (m)”. This corrects a previously incorrect description. It also inserts by inserting "and property operating costs" after “borrowing costs” (wherever occurring), to allow for reasonable estimates of property operating costs to be included in Product Disclosure Statements in certain situations.

Paragraph 11 in Schedule 1 to the Amendment Instrument modifies sub-sub-paragraph 6(f)(ib). This sub-sub-paragraph inserts two notes at the end of the notional definition of investment fees. The first note clarifies that the costs referred to in paragraph (b) of the definition do not include transactional and operational costs referred to in paragraphs (b), (ea) and (eb) of the definition of transactional and operational costs. The second note explains that transitional provisions apply in relation to the notional definition of investment fee until 30 September 2018. These provisions are outlined in paragraph 11 of the [CO 14/1252].

Paragraph 12 in Schedule 1 to the Amendment Instrument modifies sub sub-paragraph 6(f)(ii) by omitting “by omitting the definition of switching fees, and substituting”, substitute “omit the definition of switching fees, substitute”.

Paragraph 13 in Schedule 1 to the Amendment Instrument amends sub-paragraph 6(i) (notional subclause 301(1A)) by inserting subclauses 301(1B), 301(1C), 301(1D) and 301(1E).

Subclauses 301(1B) and 301(1C) modify 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 2018, the amount disclosed for other fees under subclause 301(1) relating to disclosure of the buy-sell spread fee and property operating costs.

subclause 301(1D) modifies for a periodic statement given for a MySuper product or an investment option offered by a superannuation entity, for a period ending on or before 29 June 2018 and on or before 29 September 2018, the amount disclosed for other fees under subclause 301(1) in relation to property operating costs.

Subclause 301(1E) states where a statement for the purposes of subclauses (1B) to (1D) that 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.

Paragraph 14 in Schedule 1 to the Amendment Instrument inserts At the end of subparagraph 6(i) subparagraph 6(j), 6(k) and 6(l). Under the amendment in subparagraph (j) inserts in clause 301, after subclause 301(4) in Schedule 10 to the Regulations subclause 301(5) and subclause 301(6). Subclause 301(5) provides that for a superannuation product that is subject to tax, for any reporting period ending after 29 June 2018, 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. Subclause 301(6) provides that for a managed investment product that is subject to tax, for any reporting period ending after 29 June 2018, 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. In each case the disclosure required under the heading, “total fees you paid”, must include the amount of the fees and costs without any reduction because of the benefit of a tax deduction.

Sub-paragraph 6(k) inserts in paragraph 303(1)(b) of Schedule 10 to the Regulations paragraphs 303(1)(c) and 303(1)(d). Paragraph 303(1)(c) provides that for any reporting period ending on or before 29 June 2018 for a periodic statement for a superannuation product needs to include 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 paragraph 302(1)(b) or 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. Paragraph 303(1)(d) provides that for any reporting period ending after 29 June 2018 for a periodic statement for a superannuation product, 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 paragraph 302(1).

Sub-paragraph 6(l) inserts, after paragraph 303(2)(c) to Schedule 10 to the Regulations, paragraph 303(2)(d). This paragraph provides that a periodic statement for any reporting period ending after 29 June 2018, must include the approximate total amount of transactional and operational costs for the managed investment product (other than costs referred to at subclause (b), (ea) or (eb) of the definition of transactional or operational costs that are a necessary part of the acquisition price of an asset that are recovered by a buy-sell spread for the managed investment product, where the estimate amount of buy-sell spread that the holder has paid in the period in dollars is disclosed in the periodic statement) 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). This requirement replaces the

requirement that has applied under paragraph 7.9.75(1)(b) of the Corporations Regulations which is to be omitted for superannuation products and managed investment products by paragraph 2 of Schedule 1.

Paragraph 15 in Schedule 1 to the Amendment Instrument inserts after paragraph 9 in [CO 14/1252] paragraphs 10 and 11. Paragraph 10 provides that despite paragraph 9, paragraph 5CB applies from the commencement of ASIC Corporations (Amendment) Instrument 2017/664. Paragraph 11 amends the investment fee definition before 30 September 2018 if a Product Disclosure Statement for a MySuper product or investment option includes separate details of the property operating costs (within the meaning of the notional definition of property operating costs inserted by sub-paragraph 6(a)(iib)) under Additional Explanation of Fees and Costs for the MySuper product or investment option.

4. Consultation

ASIC has engaged extensively with various industry associations, lawyers, superannuation trustees and responsible entities about the amendments and clarifications to [CO 14/1252].

The amendment providing responsible entities of managed investment products with the ability to permanently elect a reduced period in which to produce periodic statements for investors exiting the product was in response to an application supported by industry associations representing most of the superannuation and managed investment industries. The amendments to allow more time to provide buy-sell spread fee disclosure for MySuper product and superannuation fund investment options and for disclosure of borrowing costs was in response to an application supported by industry associations representing most of the superannuation and managed investment industries. The amendments to clarify other aspects of [CO 14/1252] reflect industry concerns about the risk of different interpretations.

ASIC has determined that the Amendment Instrument only makes minor modifications to the operation of [CO 14/1252], and that these modifications have a minor and machinery impact and therefore no Regulation Impact Statement is required.

Statement of Compatibility with Human Rights

Prepared in accordance with Part 3 of the Human Rights (Parliamentary Scrutiny) Act 2011

ASIC Corporations (Amendment) Instrument 2017/664

ASIC Corporations (Amendment) Instrument 2017/664 is compatible with the human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*.

Overview

ASIC Corporations (Amendment) Instrument 2017/664 (the Amendment Instrument) amends ASIC Class Order [CO 14/1252].

[CO 14/1252] relates to Schedule 10 to the Corporations Regulations 2001 (the Regulations). Schedule 10 sets out requirements for the disclosure of fees and costs of superannuation and managed investment products in Product Disclosure Statements and in periodic statements that must be given to members.

The Amendment Instrument amends Class Order [CO 14/1252] to clarify the disclosure obligations of superannuation funds in respect of borrowing costs, buy-sell fees and gross of reported other fees and total fees by any income tax deduction in periodic statements. The Amendment Instrument provides responsible entities of managed investment products with the ability to permanently elect a reduced period in which to produce periodic statements for investors exiting the product. The Amendment Instrument also modifies the definition of interposed vehicles in relation to vehicles used to gain exposure to property.

Human rights implications

This legislative instrument does not engage any of the applicable rights or freedoms.

Conclusion

This legislative instrument is compatible with human rights as it does not raise any human rights issues.

Australian Securities and Investments Commission