

EXPLANATORY STATEMENT

Select Legislative Instrument 2005 No. 31

Issued by the Parliamentary Secretary to the Treasurer

Corporations Act 2001

Corporations Amendment Regulations 2005 (No. 1)

Subsection 1364(1) of the *Corporations Act 2001* (the Act) provides that the Governor-General may make regulations prescribing matters required or permitted by the Act to be prescribed by regulations or necessary or convenient to be prescribed by such regulations for carrying out or giving effect to the Act.

The *Financial Services Reform Act 2001* (FSRA) commenced on 11 March 2002. It amended the Act to introduce a uniform licensing, conduct and disclosure regime for all financial service providers. The FSRA allowed two years for existing industry participants to transition to the new financial services regulatory regime.

The purpose of the Regulations is to support the reforms to the regulation of the financial services industry which were implemented in the FSRA and associated legislation. The Regulations promote regulatory certainty by clarifying, where necessary, the operation of various provisions relating to the regulation of financial services.

The Regulations include amendments that:

- set out measures for the disclosure of transactions and fees and costs to give effect to the fee disclosure package announced on 16 June 2004 by the Australian Government in support of the Superannuation Choice of fund reforms;
- specify certain activities that would not constitute the provision of a financial service under the financial services regulation;
- provide practical relief in relation to some requirements of the financial services regulatory regime; and
- make technical and other amendments to the Act.

Details of the Regulations are set out in the Attachment.

Regulations 1 to 3 and Schedules 1 and 2 commence on the day after they are registered on the Federal Register of Legislative Instruments. Schedule 3 commences on 1 July 2005.

ATTACHMENT

DETAILS OF THE CORPORATIONS AMENDMENT REGULATIONS 2005 (NO. 1)

Regulation 1 provides that the name of the Regulations is the *Corporations Amendment Regulations 2005 (No. 1)*.

Regulation 2 provides that Regulations 1 to 3 and Schedules 1 and 2 commence on the day after they are registered and Schedule 3 commences on 1 July 2005.

Regulation 3 provides that Schedules 1, 2 and 3 of the Regulations amend the *Corporations Regulations 2001* (the Principal Regulations).

SCHEDULE 1: AMENDMENTS RELATING TO DISCLOSURE OF TRANSACTIONS AND FEES AND CHARGES**Overview**

The amendments relating to disclosure of transactions and fees and charges contained in Schedule 1 give effect to the enhanced fee disclosure measures announced on 16 June 2004 by the former Parliamentary Secretary to the Treasurer, Mr Ross Cameron.

Part 7.9 of the *Corporations Act 2001* (the Act) establishes a uniform disclosure regime for financial services providers, including in relation to superannuation and managed investment products. Under Part 7.9, financial service providers must provide retail clients with a Product Disclosure Statement (PDS), before the consumer purchases the financial product. The PDS is designed to inform the consumer about important features of the product, including costs, and can be used to aid the consumer make a decision as to whether to purchase the product or not.

Part 7.9 also contains ongoing disclosure requirements in relation to superannuation and managed investment products, such as through periodic statements.

The regulations modify the Act and amend the Principal Regulations to introduce various requirements for the disclosure of fees and charges in PDSs and periodic statements for superannuation and managed investment products.

Product disclosure statement requirements

The regulations mandate the inclusion of:

- ‘Fees and costs template’

A standardised fee template that simplifies the disclosure of fees and costs and allow for more effective comparison across products.

- ‘Additional explanation of fees and costs section’

A separate section that includes additional important information about fees and costs.

- ‘Example of annual fees and costs table’

Provides an illustrative worked example of fees and charges in a balanced investment option for a specified account balance and level of contributions.

- ‘Consumer advisory warning box’

Alerts consumers to the importance of value for money and the compounding value of fees and costs and their impact over time on end benefits.

These regulations also provide greater certainty and consistency through a set of definitions which define the fees and costs that are to be included in the ‘Fees and Costs template’. Further consistency is to be obtained through requiring these terms to be used when describing fees or costs in periodic statements.

Periodic statement requirements

The regulations mandate the inclusion of:

- ‘Other management costs’

An item that shows the approximate amount of management costs that were not paid directly out of a member’s or product holder’s account stated in dollars.

- ‘Total fees you paid’

An item that shows a single dollar amount that includes the total fees a member or product holder paid during the period. This amount does not include transactional and operational costs that may have been incurred.

The regulations also introduce the concept of an ‘Indirect Cost Ratio’ (ICR) to provide a consistent methodology for the calculation of ‘management costs’ which are not deducted directly from a member’s or product holder’s account. This methodology allows for the consistent calculation and apportionment of such amounts between members or product holders. In addition, management costs calculated using the ICR need to be clearly displayed in dollars in periodic statements under the label ‘Other management costs’.

Finally, for financial products that have an investment component, transactions need to be itemised and described consistent with new regulation 7.9.60B (see below). As a result, consumers will be able to better understand the transactions that have affected their investment. This will provide greater transparency and in doing so enable more accurate comparisons to be made between investments.

Items 1-4, 6, 8, 9, 11 and 12 Consequential changes

The regulations make several consequential changes to the Act. The changes are necessary in order to ensure that the new requirements are integrated into the Act.

Generally, the consequential changes to the Principal Regulations either repeal now superfluous definitions or remove disclosure requirements which are replaced by these regulations.

Item 5 Fee Disclosure for certain financial products

Item 5 inserts a new Division 4C (Fee Disclosure for certain financial products) into Part 7.9 of the Principal Regulations.

Subdivision 4C.1 – New regulations 7.9.16J and 7.9.16K – The exclusion of certain superannuation products

Regulations 7.9.16J and 7.9.16K prescribe the products and disclosure statements to which the new Division 4C applies.

The requirements imposed under Division 4C are not appropriate for all types of superannuation products. As a result, regulation 7.9.16J clarifies which superannuation products are to be affected by Division 4C by excluding the following superannuation products:

- Self-managed superannuation funds;

A member of a self-managed superannuation fund generally has greater control, flexibility and choice in the operation of the fund – thus enhanced disclosure is less relevant in this context. As a result, the cost of imposing these requirements on self-managed superannuation funds outweighs the benefits of improved disclosure to their members.

- Risk-only life insurance policies offered through a superannuation fund;

The regulations do not suit this style of product where the end benefit is an insured amount generally known to the consumer at the time of purchasing the product. These superannuation products have no investment component and as such the impact of fees are not relevant as in the case of an accumulations style superannuation product.

- Annuities (except market linked annuities including both investment linked and investment account annuities);

Whilst these products may be classified as a superannuation product where they are purchased with a superannuation benefit, they are not intended to be captured by the regulations. These products are not accumulation type superannuation products and the investment return a consumer will receive will generally be known before the investment is made.

- Traditional or conventional life insurance policies offered through a superannuation fund.

These products include whole of life, endowment and pure endowment policies sold via a superannuation arrangement. These policies are not intended to be captured by these regulations as they are not investment accumulation type superannuation products.

Subdivision 4C.2 – New regulations 7.9.16L, 7.9.16M and 7.9.16N – Product Disclosure Statements (PDS)

New regulation 7.9.16L provides that a PDS must include details of fees and costs, as set out in item 10 (Part 2 of Schedule 10).

New regulation 7.9.16M modifies paragraph 1015C(5)(b) of the Act in relation to products mentioned in new regulation 7.9.16J, so that the regulations may specify the requirements as to the presentation, structure and format of a PDS.

New regulation 7.9.16N prescribes the presentation, structure and format of fees and costs disclosed in a PDS, for the purpose of paragraph 1015C(5)(b) of the Act. This new regulation provides that

the specific requirements for the disclosure of fees and costs are set out in item 10 (Part 2 of Schedule 10).

Subdivision 4C.3 – New regulation 7.9.16O – Periodic Statements

New regulation 7.9.16O modifies section 1017D of the Act, in relation to products specified in new regulation 7.9.16J, to insert a new subsection (8) that allows regulations to prescribe requirements about the presentation structure and format of a periodic statement.

New regulation 7.9.16O uses subsection 1017D(8) to prescribe the presentation, structure and format of fees and costs disclosed in a periodic statement. The new regulation also provides that the specific requirements for the disclosure of fees and costs in the periodic statement are set out in item 10 (Part 3 of Schedule 10).

Possible relief for certain superannuation and managed investment products

The implementation of regulations such as these may give rise to significant changes and upgrades to information technology systems for product providers. As such, it is important that there is a mechanism that allows for relief to be provided in appropriate cases – particularly in the case of ‘legacy products’ (products that are no longer issued to new members and which are supported by outmoded systems).

The Government’s policy intention is to rely on ASIC using its general exemption and modification powers in section 1020F of the Act, to deal with individual fund circumstances. Superannuation funds and managed investment product providers may apply for relief from the periodic statement requirements in circumstances where the regulations impose an unreasonable burden on a provider in making reports from a fund compliant, possibly resulting in detriment to fund members as well.

Extending coverage of the regulations to investment life insurance policies

In addition, consistent with the intention of ASIC’s preferred model for fee disclosure released on 16 June 2004, the Government will examine how to appropriately extend the coverage of Division 4C to include investment life insurance policies by 1 July 2006.

The Government intends to consult with the life insurance and related industries prior to broadening the scope of Division 4C.

Item 7 Regulation 7.9.60B – Disclosure of Transactions in Periodic Statements

Application

<i>Product</i>	<i>Commencement</i>
Superannuation	<p>Applies to –</p> <ul style="list-style-type: none"> periodic statements (other than exit statements) that relate to a reporting period commencing on or after 1 July 2005; and any exit statement issued on or after 1 July 2006.
Managed investment	Applies to –

	<ul style="list-style-type: none"> • periodic statements (other than exit statements) that relate to a reporting period commencing on or after 1 July 2006; and • any exit statement issued on or after 1 July 2007.
RSA, investment life insurance, deposit	<ul style="list-style-type: none"> • Applies to any periodic statement that relates to a reporting period commencing on or after 1 July 2005.

Summary of requirements

Under the *Financial Services Reform Amendment Act 2003*, paragraph 1017D(5)(c) of the Act was amended to insert a regulation-making power to enable the requirements in relation to the disclosure of information for transactions to be specified.

The previous disclosure requirement that required a summary of all transactions in relation to the product during the reporting period, indicating the nature and purpose of those transactions, was ambiguous in its operation. That is, it was unclear whether a summary of all transactions or a summary of each transaction was required.

Regulation 7.9.60B ensures that members and product holders are provided with information about transactions in a clear, concise and effective manner. The regulation affects financial products that have an investment component, namely those listed under paragraph 1017D(1)(b):

- managed investment products;
- superannuation products;
- RSA products;
- investment life insurance products; and
- deposit products.

Specific requirements

Regulation 7.9.60B requires periodic statements to include a brief description of each transaction in relation to the product during the reporting period. The description should be sufficient to allow consumers to have an understanding of the transaction which has taken place. Moreover, in the case of a contribution paid into a superannuation account, the description must be sufficient to identify the source of the contribution, to the extent such information has been recorded by the fund.

Importantly, the regulation also allows for certain transactions to be grouped where appropriate. Specifically, transactions which are of the same kind can be described together. Such transactions should be grouped on a consistent basis. In most cases it would be appropriate to describe the transaction in the periodic statement at the same rate as the transaction's actual occurrence – unless the frequency of the transaction would unduly add to the length of the statement.

In addition, it would generally not be appropriate for linked transactions to be grouped inconsistently. Therefore, if a contribution was made to an investment every quarter, and hence itemised on a quarterly basis, any applicable contribution fee should also be itemised on a quarterly basis.

Importantly, transactions also include any fees and costs charged or incurred in the relevant period. However, in the case of superannuation and managed investment products, fees and costs that require itemisation are only those included in the 'Fees and Costs template' for the product. This ensures that there is consistent terminology covering fees and costs disclosed in the PDS and the periodic statement.

Further, where a particular fee or cost is not relevant to a fund or financial product because such a fee or cost is not charged/levied by the fund or financial product, it does not need to be itemised.

If additional information to that provided in the description of a transaction must be included in a periodic statement because of a content requirement in the law, the additional information would be included elsewhere in the statement.

Item 10 Substitution of Schedule 10 – Disclosure of fees and other costs

Item 10 substitutes existing Schedule 10 of the Principal Regulations, inserting new Parts 1, 2 and 3 of Schedule 10.

Part 1 Interpretation

Clause 101 Definitions

The regulations are underpinned by a comprehensive set of definitions that would provide greater consistency across superannuation products and managed investment products. The definitions and common terms also provide for greater comparability between PDSs and periodic statements.

Additional guidance on certain definitions follows.

Balanced investment option

Describes the investment option that to be used for the 'Example of annual fees and costs' table in PDSs. This option is considered the most appropriate for comparison purposes across funds. Recognising that not every fund offers a precise 70:30 (growth to defensive) asset mix, the investment option offered which is as close as practicable is also available for use.

Clause 102 Management costs

The definition of 'management costs' has been drafted on a principles basis in order to capture all the relevant costs involved in managing the fund and deriving an investment return for members or product holders.

Importantly, 'management costs' includes amounts deducted from a common fund by way of fees, costs, expenses or charges. Therefore, complying with the Indirect Cost Ratio methodology (see below) amounts to complying with the requirement to disclose common fund amounts pursuant to paragraph 1013D(D)(iii) of the Act and regulation 7.9.75 of the Principal Regulations.

However, due to the broad definition given to 'management costs', it would be necessary to exclude certain discrete fees or costs which are not intended to be captured by the definition. These include 'contribution fees', 'transactional and operational costs', 'service fees', 'establishment fees', 'switching fees', 'termination fees', 'withdrawal fees' and 'incidental fees'.

In addition, fees or costs related to a specific asset or activity to produce income, that an investor would necessarily incur if they invested directly in the asset, are to be excluded from the definition where they could be identified and isolated. Therefore, costs a fund incurs such as operating costs

associated with the maintenance of a property investment or other investment asset such as repairs or refurbishment etc would not be ‘management costs’.

This principle also extends to cases where, for example, an investor invests in a managed investment product such as a share fund. In such a case, the costs incurred within the listed companies in which the share fund holds shares are not management costs as the investor would necessarily incur such costs if they acquired shares directly in the company rather than through the share fund.

Importantly, however, where an investor invests in a superannuation fund or managed investment product which itself has made an investment through a trust or other structure which holds the underlying investment assets, the costs of investing through the interposed entity must be captured as they are not costs which an investor would necessarily incur if they invested directly in the underlying investment assets. This ensures that layers of ‘management costs’ are captured where there are a chain of entities involved.

In defining ‘management costs’ in this way, ‘management costs’ only comprise the *additional* fees or costs that a member or product holder incurs by investing in a superannuation fund or managed investment product rather than investing directly in the underlying assets.

Clause 103 Transactional and operational costs

Clause 103 prescribes costs that are included in any calculation of transaction and operational costs.

Clause 104 Indirect Cost Ratio (ICR)

The ICR provides a ratio of a fund’s ‘management costs’ that are not deducted directly from a member’s or product holder’s account to its total average net assets over a given period.

The ICR enables funds to consistently apportion such ‘management costs’ between members or product holders. The ICR is for use in the ‘Example of annual fees and costs’ table and in periodic statements in order to derive the amount to be included in the ‘Other management costs’ item.

For a PDS, the relevant period for the calculation is the financial year before the PDS is issued. However, where a current or prospective fee level is known, and it is different to that applying over the financial year before the PDS was issued, it is preferable for the most recent fee to be used in the calculation. This ensures consumers are provided with the most up to date information about fees and costs.

For a periodic statement, the relevant period for the calculation is the latest reporting period for which the relevant information is available. However, it is acceptable if the necessary information is sourced from data relating to the fund’s most recent year of income/financial statement.

Further, it is expected that funds will produce an ICR for each investment option offered so that consumers receive the most accurate information possible in their periodic statements. Where a member has switched investment options during a reporting period, the ICR for the respective investments option may be averaged providing an estimate for the reporting period. It is preferable that a weighted average method that accounts for the amount of funds switched and the duration of the reporting period for which the member’s funds were invested in each option be used.

Where an average ICR is used, a note indicating that the ‘Other management costs’ amount stated in the periodic statement is only an approximation due to the mid-period investment option switch should be included.

In the case of a new product, the ICR should be determined based on a reasonable estimate of the expected applicable fees and costs for that product. Again, a note to this effect should be included in a member's periodic statement.

In calculating any ICR, fund's should take care not to double count any fees or costs, either because they are relying on a prospective fee or cost rather than a historical fee or cost, or because of any overlap due to the principle based definition of 'management costs'.

The ICR is equivalent to the previously announced 'Total Expense Ratio' (TER) concept. Importantly, the ICR is consistent with the approach proposed by the International Organization of Securities Commissions in its paper of February 2004 titled 'Elements of International Regulatory Standards on Fees and Expenses of Investment Funds'. However, the label 'ICR' was adopted to avoid confusion about the composition of the ratio and any possible misrepresentation to consumers.

Part 2 Requirements for Product Disclosure Statements

Application

<i>Product</i>	<i>Commencement</i>
Superannuation	• Applies to any PDS from 1 July 2005.
Managed investment	• Applies to any PDS from 1 July 2006.

Any new PDS issued after the relevant commencement date (see regulation 7.9.16K) is required to comply with Subdivision 4C.2. However, where no new PDS is issued after the relevant commencement date, the product provider is required to issue a supplementary PDS that complies with Subdivision 4C.2. This requirement only applies to open products – where there is an active requirement for a PDS to be in circulation/available.

Summary of requirements

Under the regulations, PDSs for superannuation and managed investment products will be required to include:

- 'Fees and costs template'
A standardised fee template that simplifies the disclosure of fees and costs and allows for more effective comparison across products.
- 'Additional explanation of fees and costs section'
A separate section that includes additional important information about fees and costs.
- 'Example of annual fees and Costs table'
Provides an illustrative worked example of fees and costs in a balanced investment option for a specified account balance and level of contributions.
- 'Consumer advisory warning box'

Alerts consumers to the importance of value for money and the compounding value of fees and costs and their impact over time on end benefits.

Specific requirements

Specific requirements

Clauses 201 to 208 Fees and costs template

The ‘fees and costs template’ is designed to show the most significant costs that may be incurred in respect of a superannuation or managed investment product. The simple table format allows for more effective comparisons between like products. The template is preceded by an appropriate preamble highlighting to consumers the purpose of the document and its features.

Information that is required to be included in the ‘Fees and costs template’ includes information about the amount of a fee or cost, how the fee or cost is charged, the frequency of the payment, its timing and whether it is negotiable.

The template also allows for customisation where there is an option to pay contribution fees upfront or later through higher ongoing fees as well as where other options may be offered. In addition, the template permits product providers to disclose multiple investment options in a single ‘Fees and costs template’. This ensures PDSs are not unnecessarily lengthened by a requirement to present the fees and costs for each investment option in separate templates.

However, where the inclusion of multiple investment options in a single template is likely to confuse or mislead consumers because of the volume of information presented, a cross-reference must be provided in the template to a separate part of the PDS where the fees and costs for each investment option are clearly disclosed, consistent with how the fees and costs are presented in the template. The ‘Fees and costs template’ should always include at least the balanced investment option fee structure and the default investment option fee structure (if relevant or applicable).

The regulations also contain detailed instructions on how to fill in the template to ensure consistency. As such, amounts are to be specified in a manner consistent with the dollar disclosure regulations applying to PDSs (see regulations 7.9.15A, 7.9.15B and 7.9.15C). The template also specifically allows for the use of ranges (either in dollars or as a percentage) in disclosing the amount of a fee or cost so that consumers are made aware of the range of fees which may apply to their investment. This is particularly relevant where, for example, a certain fee decreases over time or where a fee is levied depending on a member’s or product holder’s account balance.

It is acknowledged that certain fees and costs, namely those dependent on a member’s or product holder’s account balance, will not be able to be disclosed in dollars. As a result, the template permits amounts to be disclosed as a percentage. Consistent with the dollar disclosure requirements, the ‘Example of annual fees and costs table’ is to be used as the relevant worked example for contribution fees, managements costs, establishment fees, withdrawal fees and termination fees to the extent these fees and costs are applicable in the example template.

In respect of fees and costs that are charged as a percentage and which are not applicable in the example table, a description of the fee or cost including a separate worked dollar example either in the ‘Fees and costs template’ or the ‘Additional explanation of fees and costs section’ must be provided.

Clause 209 Additional explanation of fees and costs section

The 'Fees and costs template' is also linked to an 'Additional explanation of fees and costs' section in the PDS. This section contains other important information about fees and costs which is not contained in the template. This information is kept separate in order to preserve the simplicity of the 'Fees and costs template'.

Importantly, this section allows for examples to be included where appropriate (such as in relation to buy/sell spreads) as well as for information about adviser remuneration, transactional and operational costs, how to negotiate lower fees and details about any fee changes to be disclosed.

The level of detail to be provided in this section should be consistent with the importance of the fee or cost being disclosed. Therefore, a more significant fee or cost should receive a more detailed explanation than a less significant fee or cost. The requirement to include any worked examples should be interpreted in a similar manner. However, it is important that where a very concise approach to disclosure has been taken that the consumer is provided with details on how to contact the fund for more details if necessary.

Clauses 210 to 220 Example of annual fees and costs table

The regulations will mandate the inclusion of a standardised example to be included in all superannuation and managed investment product PDSs. In the absence of a standardised example, it would not be possible for consumers to easily compare the costs of different investments over a 12 month period.

The 'Example of annual fees and costs table' (the example table) is based on a \$50,000 account balance and an annual contribution of \$5,000 – where the financial product is one which accepts additional contributions to be made. Note, if the financial product is not one which allows additional contributions to be made, the example table is to be based on only the initial contribution of \$50,000.

Further, the example table should relate to the fees and costs for the 'balanced investment option' or an option as close as practicable to it. If a fund does not offer an investment option akin to a 'balanced investment option', the example table is to be based on the fund's default investment option. However, if a particular fund offers neither, the example table should include the fees and costs for the investment option with the most funds invested. This approach provides an appropriate balance between consistency to enable effective comparisons and flexibility in cases where a 'balanced investment option' is not offered.

Importantly, the example table is preceded by an appropriate preamble indicating that the purpose of the table is to provide an illustration of how much a consumer may pay in fees and costs over a 12 month period in this product. The model enables consumers to gain an appreciation of the impact of fees on their investment and to make effective comparisons with similar products.

The example table covers the main fees and costs which are generally applicable to superannuation and managed investment products, and refers to others which may apply during the course of the investment. Discretionary fees and costs such as transactional and operational costs and service fees are not included as these often relate to optional services that a fund member or product holder can choose whether or not to receive.

Specific instructions are also provided on how to calculate each of the various fees and costs illustrated in the example table. This will avoid different product issuers making different assumptions about how to calculate the respective fees – adding to the consistency of the model.

In addition, the integrity of the example table is maintained by ensuring ‘honeymoon’ rates are not permitted to be used. ‘Honeymoon’ rates are typically more favourable in the first year or in early years and once the ‘honeymoon’ period expires the fees revert to their typical ongoing level. Therefore, as the example table assumes the person is already a member or product holder, it is appropriate that the example table be based on the typical ongoing level of fees or costs for that fund and investment option.

The example table is also able to be customised appropriately where a product has a minimum entry balance requirement in excess of \$50,000. This ensures that consumers are always presented with a realistic example of the fees and costs which may apply.

Finally, the regulations appropriately exclude PDSs for ‘defined benefit funds’ (defined in subregulation 1.03(1) of the *Superannuation Industry (Supervision) Regulations 1994*) from having to include an example table as it is not suited to this type of superannuation product.

In a true ‘defined benefit fund’, the employer-sponsor of the fund bears the risk of ensuring the benefits to be received by its members are able to be met from the fund. In this regard, the defined benefits that the members of the fund receive are not affected by the level of ongoing fees or costs in the fund or the investment performance of the fund but rather by other variables such as the employees’ income level and years of service.

Clauses 221 and 222 Consumer advisory warning box

The advisory warning for inclusion in PDSs emphasises to consumers the importance of considering ‘value for money’. It also shows how a small difference in a fund’s investment performance or fees and costs can have a significant impact on long term investment returns.

In addition, by providing a link to superannuation and managed investment calculators on the Australian Securities and Investments Commission’s website, consumers can make personalised comparisons (including over the longer term) with the appropriate tools.

Importantly, the advisory warning also encourages consumers to shop around and attempt to negotiate lower fees and costs with their fund or adviser.

An appropriate preamble to the advisory warning box indicating that the warning is required under Australian law and that specific information about fees and costs is available elsewhere in the PDS may be provided. However, any preamble text must not be inconsistent with the messages or themes contained in the ‘consumer advisory warning’ box.

Part 3 Requirements for periodic statements

Application

<i>Product</i>	<i>Commencement</i>
Superannuation	<p>Applies to –</p> <ul style="list-style-type: none"> periodic statements (other than exit statements) that relate to a reporting period commencing on or after 1 July 2005; and any exit statement issued on or after 1 July 2006.
Managed investment	Applies to –

	<ul style="list-style-type: none"> • periodic statements (other than exit statements) that relate to a reporting period commencing on or after 1 July 2006; and • any exit statement issued on or after 1 July 2007.
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Summary of requirements

Under the regulations, periodic statements for superannuation and managed investment products will be required to include:

- ‘Other management costs’
An item showing the approximate amount of management costs that were not paid directly out of a member’s or product holder’s account stated in dollars.
- ‘Total fees you paid’
An item showing a single dollar amount that includes the total fees a member or product holder paid during the period. This amount excludes transactional and operational costs that may have been incurred.
- ‘Additional explanation of fees and costs section’
A separate section that includes additional important information about fees and costs.

Specific requirements

In addition to the requirements imposed by regulation 7.9.60B (discussed above), periodic statements for superannuation and managed investment products are required to include information about ‘management costs’ not deducted directly from a member’s or product holder’s account as well as specifying the total fees paid during the relevant period covered by the periodic statement (usually 12 months).

Clause 301 Other management costs

This item shows consumers the approximate amount of ‘management costs’ that have affected their investment which were not deducted directly from their account. Since all ‘management costs’ which are deducted directly from their account will be itemised (as per regulation 7.9.60B), consumers will be able to calculate the approximate total of ‘management costs’ which they have incurred in the relevant period.

‘Other management costs’ are to be calculated by using the ICR for the applicable fund investment option and multiplying it against the member’s average account balance over the reporting period. The average may be calculated by reference to either the investor’s daily, monthly or opening and closing account balance depending on the capability of the product provider’s information system.

Importantly, as this amount is only an estimate (due to it being determined on the basis of an individual’s average account balance), it is to be included below the itemised section of the periodic statement. This will preserve the integrity of the itemised section of the statement.

See also the related explanation of the Indirect Cost Ratio above which is integral to the disclosure of this item.

Clause 302 Total fees you paid

This item includes all the known fees and costs that affected an individual's investment over the reporting period. Transactional and operational costs will not be included in this amount as they are typically reflected by the fund in either the price paid for an asset or in the investment return received by the consumer. However, to the extent that the current law requires the disclosure of costs such as transaction costs, that information, be it about the level or when they may be incurred, should continue to be provided elsewhere in the periodic statement.

There should only be one 'Total fees you paid' item in a periodic statement and it should be shown at the end of the part of the periodic statement that itemises transactions or in any summary part which provides a summary of the events that affected the member's or product holder's investment during the reporting period.

Clause 303 Additional explanation of fees and costs section

Broadly, this section allows for other fees and costs which a consumer has incurred but which have not been included elsewhere in the periodic statement to be disclosed.

Taxation matters

In general, item 10 also provides certainty for the presentation of fees and costs in both PDSs and periodic statements by indicating how various taxes are to be accounted.

In a PDS, fees or costs must be shown gross of income tax (but including GST and any applicable stamp duty) and net of any applicable reduced input tax credits. Disclosure in this manner is required as the impact of any entity level tax deductions and the extent to which they will be passed on to members or product holders through lower after tax fees or costs is not known at the time of preparing a PDS.

For periodic statements, it is essential that the actual amount charged or incurred by the member or product holder is indicated on the statement. For this reason, transactions, fees and costs must be shown net of income tax and GST and any applicable stamp duty. That is, inclusive of any income tax deduction which may have reduced the actual amount of a fee or cost charged. This ensures that consumers are aware of exactly how much they have paid in fees and costs.

SCHEDULE 2: OTHER FINANCIAL SERVICES AMENDMENTS

Item 1 Amendment of Regulation 1.0.02 – definition of legally incapacitated person

This amendment inserts a definition of *enduring power of attorney*, which is relevant to the amendment contained in item 10 (see below).

Item 2 New regulation 7.1.04G – meaning of issuer of a foreign exchange contract

The meaning of issuer is prescribed under section 761E of the Act. A product issuer may be obliged to meet the disclosure obligations of the Act, where a product is issued to a ‘retail client’.

Because a foreign exchange contract imposes mutual obligations on the contract parties, it is difficult to determine which party is the issuer of the contract for the purposes of subsection 761E(4). Without knowing who the issuer of the product is, there is difficulty in determining which party, if any, is obliged to disclose information required under the financial services regulation.

This scenario is similar to derivatives. The Act solves the problem in relation to derivatives by prescribing both parties as the issuer of the product.

Foreign exchange contracts are essentially a special type of derivative. As such, to clarify who the issuer of a foreign exchange contract is, (and hence who may need to meet the disclosure requirements of the Act) this new regulation specifies that, like derivatives, each party to a foreign exchange contract is deemed the issuer.

Item 3 Amendment of paragraph 7.1.35(1)(b) – conduct that does not constitute dealing in a financial product

Paragraph 7.1.35(1)(b) currently provides that certain conduct does not constitute dealing in a financial product, where that conduct is carried out in relation to the holding of a financial product on trust for, or on behalf of, another person, and the holding of the product does not constitute the provision of a custodial or depository service because of paragraphs 7.1.40(a) to (d).

Regulation 7.1.40 is being altered by items 7, 8 and 9, which amend existing paragraph 7.1.40(g) and insert a new paragraph 7.1.40(i). This item makes a consequential amendment to paragraph 7.1.35(1)(b) to include a reference to paragraphs 7.1.40(g) and (i), such that where the holding of a financial product does not constitute the provision of a custodial or depository service due to paragraphs 7.1.40(g) and (i), conduct carried out in relation to the holding of that product will not constitute dealing in a financial product.

Item 4 Substitution of paragraph 7.1.40(g) – conduct that does not constitute the provision of a custodial or depository service

This item amends paragraph 7.1.40(g), which currently provides that the holding of a financial product under an order of the Court does not constitute the provision of a custodial or depository service under section 766E of the Act. The amendment extends the operation of the paragraph to include the order of any court (the words “court” and “Court” are defined in section 58AA of the Act) as well as the order of a board or tribunal established under State or Territory law, or a direction by the holder of a statutory office established under State or Territory law.

Items 5 and 6 Amendment of subparagraph 7.1.40(h)(iv) and new paragraph 7.1.40(i) – conduct that does not constitute the provision of a custodial or depository service

Item 8 makes a minor amendment to facilitate the insertion of the new paragraph 7.1.40(i), which is affected by item 9. The new paragraph provides that the holding of a financial product by a trustee appointed under State or Territory law to administer compensation monies awarded to a person, or appointed under a trust established for a charitable purpose, will not constitute the provision of a custodial or depository service by that trustee.

A trust established for a charitable purpose is one that does not have specific beneficiaries. It would not, for example, include an investment trust established by a charitable organisation as a means of providing finance which may then be used to promote charitable purposes.

Item 7 New subregulation 7.6.02(5) – external dispute resolution schemes

This item inserts a new subregulation 7.6.02(5), the effect of which is to provide that a financial services licensee does not have to comply with the requirements of paragraph 912A(2)(b) of the Act (which requires licensees who provide financial services to retail clients to be members of one or more external dispute resolution schemes), in respect of financial services provided by the licensee in the capacity of – a trustee appointed under the will or on the intestacy of a person; a trustee appointed under an express trust, of which the settlor is a natural person, where the interest in the trust is not a financial product; or an attorney appointed under an enduring power of attorney – where complaints in respect of the provision of those services may be made to a State or Territory Ombudsman.

The new subregulation therefore provides an exemption for licensees from the requirement to be members of external dispute resolution schemes in respect of the provision of certain defined financial services, if those licensees are subject to oversight by a State or Territory Ombudsman in respect of the provision of those services.

Item 8 Amendment of subregulation 7.6.02AA(2) – deferring commencement of section 912B

Paragraph 926B(1)(c) of the Act provides that the regulations may provide that Part 7.6 applies as if specified provisions were omitted, modified or varied as specified in the regulations. This item amends regulation 7.6.02AA which was inserted under this power to modify section 912B of the Act in Part 7.6.

Section 912B imposes a requirement on financial services licensees who provide financial services to retail clients to have adequate compensation arrangements. The issues surrounding compensation were considered in an Issues Paper released by the Government in September 2002, which was followed by a Position Paper released in December 2003. Submissions received in response to both papers revealed a wide range of views on the scope and nature of appropriate compensation mechanisms.

Regulation 7.6.02AA was inserted to defer the application of the requirement in section 912B from 11 March 2004 until 11 March 2005. In the meantime, however, the regulation continues to apply the requirements which applied prior to the enactment of section 912B, and which have continued to apply during the transition period for the *Financial Services Reform Act 2001*.

There are many complex issues surrounding compensation arrangements, and they require careful and detailed consideration. It is also necessary to provide interested stakeholders with an opportunity to comment on any proposed compensation mechanism(s) and sufficient time to transition to any new arrangements.

It is apparent that there will not be sufficient time for the Government to develop a final position, consult with interested stakeholders and implement the arrangements before 11 March 2005. This item therefore amends regulation 7.6.02AA to further defer the commencement of the application of section 912B until 1 July 2006.

Item 9 New subregulations 7.8.01(11), (12), (13) and (14)

Part 7.8 Division 2 of the Act stipulates requirements for how a financial services licensee is to deal with the money of clients. Generally, the licensee must hold prescribed client monies on trust in a specified account. Section 981B of the Act specifies, amongst other things, that the licensee (or authorised representative) can only place certain monies into a Part 7.8 trust account.

Industry has expressed concern about the practical difficulties it has encountered in only being allowed to place and then hold certain monies in the trust account. Industry believes that this limitation may result in unnecessary costs for clients.

For example, licensees often receive a single payment from a client in relation to services provided. Such a payment may contain both money that must be held on trust and money that cannot be held in the Part 7.8 trust account. If a licensee receives such a payment, under the current law they will technically breach the law regardless of whether they initially place the single payment into the trust account, or another account.

The only way to overcome this problem is to instruct the client to make two or more separate payments to the licensee. It has been argued that this process could more easily be achieved (and at less cost) by the licensee.

Similar problems arise in relation to the receipt of unidentified monies, which may be in total, or in part, money that is required to be held on trust.

The amendments provide practical relief for licensees that receive mixed or unidentified payments from clients. The amendments maintain the integrity of the trust account by ensuring that licensees identify and remove the non-trust money from the trust account, as soon as reasonably practicable or within 1 month.

The amendments take account of the fact that different licensees require different time to remove non-trust monies from the account. As such, it may be reasonably practicable for some licensees to remove money every couple of days. However, it may only be reasonably practicable for other licensees to remove non-trust money once per month.

Item 10 New regulation 7.8.14A – lodgement of annual profit and loss statement and balance sheet

Section 989B requires a financial services licensee to lodge a profit and loss statement, balance sheet and auditor's report with ASIC in respect of each financial year. Section 989D stipulates the time for lodging these documents, which for a licensee that is a non-body corporate, is within 2 months after the end of the financial year and for a body corporate, within 3 months.

Regulation 7.8.14A modifies paragraph 989D(1)(b) to distinguish between those bodies corporate that are disclosing entities or registered schemes and those that are not. In doing so, the new

regulation extends the time for lodgement of the reports for a body corporate that is not a disclosing entity or a registered scheme to four months. The amendment aligns the reporting timing obligations in section 989D of the Act with those in section 319 as well as other audit related disclosures required by the Australian Prudential Regulation Authority.

Items 11 to 13 Amendment of paragraph 7.9.08(1)(b), new paragraph 7.9.08(1)(c) and new regulation 7.9.08D – dealing with money received for a financial product before the product is issued – statutory funds to which the *Life Insurance Act 1995* applies

Part 4 of the *Life Insurance Act 1995* (LIA) sets out the obligations of registered life insurance companies in respect of statutory funds. In particular, section 30 of the LIA requires life insurance companies to credit all amounts received in respect of the business of a statutory fund, including unallocated initial premiums, into a statutory fund.

Despite the requirement in the LIA, section 1017E of the Act requires an issuer to deposit all unallocated application monies (including for life insurance policies) into a separate designated trust account.

The amendments prescribe statutory funds to which the LIA applies under subparagraph 1017E(2)(a)(ii) to enable a statutory fund to satisfy section 1017E of the Act. Further, the provision is to operate as if paragraph 1017E(2)(b) is omitted, to enable statutory funds to continue to operate in their current form.

The amendments therefore rectify the inconsistency between the two Acts and reduce administrative difficulties and additional costs for industry. This is achieved while recognising that situations under the Acts both aim to provide similar levels of protection to consumers' assets from creditors of the product issuer or life insurance office.

Item 14 Amendment to regulation 7.9.72 – modification of section 1017D of the Act: information already given

With the introduction of regulation 7.9.60B (Disclosure of transactions in periodic statements), a consequential amendment to regulation 7.9.72 is required.

Regulation 7.9.72 is intended to rationalise the disclosure obligations applying to superannuation and RSA products by ensuring that where they have complied with Subdivisions 5.2 and 5.3, paragraphs 1017D(5)(a) to (e) do not apply.

Specifically, regulation 7.9.72 is amended to ensure that regulation 7.9.60B, made under paragraph 1017D(5)(c), applies to superannuation and RSA product periodic statements.

If regulation 7.9.60B is introduced and regulation 7.9.72 is not amended, superannuation and RSA products would be excluded from complying with regulation 7.9.60B.

Item 15 New regulation 7.9.97 – Off-market trading by professional investors etc

Division 5A of the Corporations Act was introduced to protect unsophisticated investors from people offering to purchase their financial products, off-market.

In that regard, Division 5A was not intended to interfere with off-market trading between sophisticated investors. For this reason, the 'business relationship' test was introduced into Division 5A.

Industry has expressed concern that there may still be situations where off-market trading could occur and professional investors might be caught by the Division 5A disclosure provisions. As this was not the intention of the legislation, this new regulation introduces a further test under section 1019D, which ensures that Division 5A only applies in relation to offers made to ‘retail’ investors. This new test is modelled, as closely as possible, on the ‘retail client’ test under section 761G of the Act.

Item 16 Substituted subregulations 1017D(8) & (9) – exit reporting disclosure: referencing correction

Part 13 of Schedule 10A (which modifies section 1017D) was inserted to provide an exception to exit reporting disclosure by removing the obligation for superannuation and retirement savings account providers to supply a periodic statement in order to prevent a possible duplication of information. Specifically this relates to an event where the benefits of former product holders are transferred to another entity, and that entity supplies the required information.

Part 13 was inserted on the basis of the requirements which were previously in the *Superannuation Industry (Supervision) Regulations 1994*. Unfortunately the references in subparagraphs 1017D(8)(b)(i) – (iii) and 1017D(9)(b)(i) – (iii) were incorrectly drafted to apply to the wrong subdivisions of Part 7.9 of the Principal Regulations.

The amendments rectify this technical error by ensuring that the relevant paragraphs refer to the appropriate informational requirements set out in the regulations.

SCHEDULE 3: AMENDMENTS COMMENCING ON 1 JULY 2005**Item 1 Repeal of regulation 7.9.72A – modification of section 1013D of the Act: amount payable for financial product**

With the introduction of Schedule 1, it is no longer appropriate for this regulation (dealing with providing information about the basis for the calculation of an amount rather than specifying the amount) to continue to operate.