Law Council
OF AUSTRALIA

18 June 2014

Ms Ashly Hope
Strategic Policy Advisor
Australian Securities & Investments Commission
GPO Box 9827
Melbourne VIC 3001

By email: deregulation@asic.gov.au

Dear Ms Hope

ASIC's deregulatory initiatives

I am pleased to enclose a submission prepared by the Superannuation Committee of the Legal Practice Section of the Law Council of Australia in response to *Report 391 ASIC's Deregulatory Initiatives*.

The Committee would welcome the opportunity to discuss its submission and respond to any queries you may have. In the first instance, please contact:

- Ms Pam McAlister, Chair, Superannuation Committee T: 03 9603 3185
  E: pam.mcalister@hallandwilcox.com.au or
- Mr Luke Barrett, Chair, Legislation and Policy Subcommittee T: 03 9910 6145
  E: luke.barrett@unisuper.com.au.

Yours sincerely

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Report 391 ASIC's Deregulatory Initiatives

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Executive Summary

In *Report 391 ASIC's Deregulatory Initiatives*, ASIC seeks views on:

- any changes that might be made to ASIC forms;
- suggestions for regulatory change that ASIC might discuss further with the Australian Government including Treasury; and
- any changes that might be made to ASIC processes or procedures.

This submission focuses primarily on the second topic. Our suggestions can be grouped under three main themes:

1. Stronger Super gaps and anomalies
2. Disclosure overload
3. Clarity of the law

We also comment briefly on some of ASIC's proposals in Section C of its report.

About the Law Council of Australia's Superannuation Committee

The Law Council of Australia is the peak national representative body of the Australian legal profession; it represents some 60,000 legal practitioners nationwide. Attachment A outlines further details in this regard.

This submission has been prepared by the Law Council of Australia's Superannuation Committee (the Committee), which is a committee of the Legal Practice Section of the Law Council of Australia.

The Committee's objectives are to ensure that the law relating to superannuation in Australia is sound, equitable and demonstrably clear. The Committee makes submissions and provides comments on the legal aspects of virtually all proposed legislation, circulars, policy papers and other regulatory instruments which affect superannuation funds.

Stronger Super gaps and anomalies

The Committee has identified a number of gaps and anomalies in the Stronger Super reforms that ASIC might raise with Treasury. These include:

- the lack of any regulations made under s 29WA(5) of the *Superannuation Industry Supervision Act 1993* (Cth) (SIS Act) in order to prescribe the situation where a member gave an investment direction to a 'predecessor' fund as a 'circumstance in which an investment direction is taken to be given'. This is an important issue so that contributions for a member in a 'successor fund' do not need to be allocated to a 'MySuper' investment option that is different from the investment option that the member may have actively selected in the predecessor fund, thereby undermining the 'equivalent rights' rationale for the transfer.

- the mis-insertion of s 29QB and 29QC at the end of a non-existent Division 6 of Part 2B in the SIS Act.[1]
- equity issues emerging by reason of the fact that MySuper fees and charges must be the same across all MySuper members. This is particularly an issue for:
    - funds with percentage-based fees where members with larger balances are effectively cross-subsidising members with small balances; and
    - funds recovering a percentage fee from returns to build the operational risk reserve, where an influx of a new cohort of members increases the amount of the reserve and therefore the required recovery from pre-existing members.

  With the benefit of this experience, the Committee suggests that some flexibility to the MySuper fee charging rules should be introduced.

The Committee would also like to reiterate its concerns about portfolio holding disclosure (now deferred until 1 July 2015) as a disincentive for overseas funds managers to do business in Australia.

In terms of s 29QC (now also deferred until 1 July 2013) the Committee endorses industry raise concerns about the '50% probability' test for MySuper target returns, and therefore investment objectives, resulting in member expectations being raised without any understanding of the 50% probability.

The Committee is also concerned that s 29QC (as recently interpreted by ASIC and APRA) has the potential to perversely impact the formulation of investment objectives and asset allocations (a case of the disclosure 'cart' driving the investment 'horse'). The Committee hopes that the deferral period will provide an opportunity for the regulators to resolve these concerns.

Disclosure overload

The Committee shares ASIC's view that disclosure has its limitations in terms of driving investor understanding. The Committee is also concerned that disclosure overload may lead to investors ignoring key communications and messages.

Potential alternative model for product disclosure

The Committee has considered the possibility of a two-tiered approach to reducing disclosure overload. The Committee suggests that a Product Disclosure Statement (PDS) should only be required for clients who are not advised by a licensed financial adviser, while for clients who do receive financial advice, the adviser should be given the obligation to ensure that the client understands the product before applying for it.

For unadvised clients, the Committee questioned ASIC's proposal for a PDS to be replaced with a key facts sheet and a compulsory 'understanding' tool. A better solution might be to introduce an open ended disclosure obligation (i.e. what members reasonably need to know to understand the product) rather than the overly prescriptive wording and formats that have crept into the legislation over time. The onus would then be on the product issuer to demonstrate that its disclosure had met the test by reference to its target

[1] See Endnote 7—Misdescribed amendment Superannuation Laws Amendment (Capital Gains Tax Relief and Other Efficiency Measures) Act 2012 (No. 158, 2012)

market.[2] The Committee recognises that the downside of this approach would be to sacrifice comparability, but the Committee questions whether upfront disclosure documents need to be comparable, especially for superannuation products where the new product dashboards potentially serve this purpose.

Removal of barriers to electronic disclosure and advertising

The Committee endorses ASIC's proposal to examine barriers to using electronic disclosure as the preferred means of communication.

As a separate matter, the Committee also suggests that ASIC should consider how disclosure obligations should apply to social media, such as Twitter and Facebook. Many superannuation funds are endeavouring to boost member engagement, especially with younger members who are typically disengaged. Engaging with members through social media is potentially part of the solution and numerous superannuation funds have become active in this space. However, there is considerable uncertainty as to whether (and if so, how) the legislative provisions regarding general advice warnings and the analogous disclosure for advertising apply to social media. For example, messages posted on social media are subject to length constraints, typically a small number of characters. It is simply not possible (nor consistent with the objective of building engagement with young members) to include lengthy warnings in this context.

Aligning sustainability disclosure with recent shorter disclosure reforms

The Committee suggests that ASIC revisit *Regulatory Guide 65: Section 1013DA disclosure guidelines* (RG 65) with a view to withdrawing or significantly streamlining the disclosures contemplated in that document.

Unlike other regulatory guides, there is a legislative obligation under s 1013DA of the *Corporations Act 2001* (Cth) for product issuers to comply with ASIC's disclosure guidelines in circumstances where labour standards, environmental, social or ethical considerations are factored into the investment strategy. As such, RG 65 cannot necessarily be regarded as mere guidelines which are optional in nature.

RG 65 was presumably designed to address particular issues which were perceived at the time it was originally introduced.

However, in the intervening time, the disclosure regime under the Corporations Act has undergone significant changes; first with the introduction of short-form PDSs and more recently with the introduction of shorter PDSs and product dashboards. One may query whether sustainable and ethical products ever became as prevalent as perhaps may have been contemplated when s1013DA and RG 65 were first introduced.

Given these developments, RG 65 leads to a particular category of financial product (i.e. sustainable and ethical products) being subject to disclosure obligations which are disproportionate to other financial products, and perhaps disproportionate to the risk of any real mischief.

This imbalance is most pronounced in the case of investment options within superannuation funds, where the disclosures required for MySuper products are well defined and far more targeted than what is required for a relatively boutique choice product.

[2] In some cases a key facts sheet might suffice but this would be a matter for the issuer.

In light of the above, the Committee suggests that RG 65 be revisited and withdrawn or significantly streamlined.

Clarity of the law

From a 'process' perspective, the Committee is concerned about lack of clarity in the law, particularly in the context of Chapter 7 of the Corporations Act and related regulations. This lack of clarity is due to the overlay of regulations and class orders that amend the provisions of the Act; exacerbated by the fact that the regulations include further 'Schedules' that modify the law. This means that it is necessary to go to several sources in order to ascertain what the law on a particular subject actually is.

The Committee also considers that, at some point, significant ASIC class orders should be legislated. Examples of legislation by significant ASIC class order include the Investor Directed Portfolio Services regime (IDPS regime) and the Managed Discretionary Accounts regime (MDA regime), which have now become entrenched as features of the regulatory landscape, and yet are creatures of ASIC policy.

ASIC's proposals

The Committee wholly supports ASIC's proposals to:

- make its class order instruments clear and user friendly (and to rationalise their content and conditions);
- take a 'no surprises' approach to regulation; and
- improve the usability of its website.

In this latter regard, the Committee would welcome a more sophisticated search tool in order to locate items on the ASIC website.

The Committee would welcome the opportunity to discuss this submission and respond to any queries you may have. In the first instance, please contact:

- Ms Pam McAlister, Chair, Superannuation Committee T: 03 9603 3185
  E: pam.mcalister@hallandwilcox.com.au or
- Mr Luke Barrett, Chair, Legislation and Policy Subcommittee T: 03 9910 6145
  E: luke.barrett@unisuper.com.au.

Attachment A: Profile of the Law Council of Australia

The Law Council of Australia exists to represent the legal profession at the national level, to speak on behalf of its Constituent Bodies on national issues, and to promote the administration of justice, access to justice and general improvement of the law.

The Law Council advises governments, courts and federal agencies on ways in which the law and the justice system can be improved for the benefit of the community. The Law Council also represents the Australian legal profession overseas, and maintains close relationships with legal professional bodies throughout the world.

The Law Council was established in 1933, and represents 16 Australian state and territory law societies and bar associations and the Large Law Firm Group, which are known collectively as the Council's Constituent Bodies. The Law Council's Constituent Bodies are:

- Australian Capital Territory Bar Association
- Australian Capital Territory Law Society
- Bar Association of Queensland Inc
- Law Institute of Victoria
- Law Society of New South Wales
- Law Society of South Australia
- Law Society of Tasmania
- Law Society Northern Territory
- Law Society of Western Australia
- New South Wales Bar Association
- Northern Territory Bar Association
- Queensland Law Society
- South Australian Bar Association
- Tasmanian Independent Bar
- The Large Law Firm Group (LLFG)
- The Victorian Bar Inc
- Western Australian Bar Association

Through this representation, the Law Council effectively acts on behalf of approximately 60,000 lawyers across Australia.

The Law Council is governed by a board of 17 Directors – one from each of the Constituent Bodies and six elected Executives. The Directors meet quarterly to set objectives, policy and priorities for the Law Council. Between the meetings of Directors, policies and governance responsibility for the Law Council is exercised by the elected Executive, led by the President who serves a 12-month term. The Council's six Executive are nominated and elected by the board of Directors. Members of the 2013 Executive are:

- Mr Michael Colbran QC, President
- Mr Duncan McConnel President-Elect
- Ms Leanne Topfer, Treasurer
- Ms Fiona McLeod SC, Executive Member
- Mr Justin Dowd, Executive Member
- Dr Christopher Kendall, Executive Member

The Secretariat serves the Law Council nationally and is based in Canberra.