
**FINANCIAL REGULATOR REFORM (NO. 2) BILL 2019: FEES (FSRC RECS 3.2
& 3.3: ADVICE FEES FOR MYSUPER AND CHOICE PRODUCTS)**

EXPOSURE DRAFT EXPLANATORY MATERIALS

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Glossary

The following abbreviations and acronyms are used throughout this explanatory memorandum.

<i>Abbreviation</i>	<i>Definition</i>
AFS licensee	Australian Financial Services licensee
ASIC	Australian Securities and Investment Commission
APRA	Australian Prudential Regulatory Authority
Bill	Financial Regulator Reform (No. 2) Bill 2019: fees (FSRC Rec 3.2 and 3.3)
Corporations Act	<i>Corporations Act 2001</i>
Financial Services Royal Commission	Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry
Legislation Act	<i>Legislation Act 2003</i>
RSE licensee	Registrable Superannuation Entity licensee
SIS Act	<i>Superannuation Industry (Supervision) Act 1993</i>

Chapter 1

Financial Services Royal Commission Recommendations 3.2 and 3.3: Advice fees for MySuper and choice products

Outline of chapter

1.1 Schedule 1 to the Bill amends the SIS Act to provide greater protection for superannuation members against paying for inappropriate financial advice and fees for no service. Where advice fees are not prohibited, the amendments are aimed at increasing the visibility of advice fees in superannuation, and better allowing members to make an assessment about the value of the advice they are receiving.

1.2 The amendments implement Recommendations 3.2 and 3.3 of the Financial Services Royal Commission.

1.3 Unless otherwise stated, all references in this Chapter are to the SIS Act.

Context of amendments

1.4 The SIS Act sets out the general fee charging rules in Part 11A (general fee rules) that provide direction on charging and deducting fees from a superannuation interest, including:

- prohibiting the charging of entry fees and exit fees;
- applying a fee cap on low balance products; and
- prohibiting the cost of advice provided to employers being borne by members.

1.5 Section 99F prohibits a trustee from passing the costs of particular types of financial product advice incurred by a member on to any other member.

1.6 Although it is not defined, advice fees charged to other members that is *not* prohibited by section 99F is generally referred to as ‘intra-fund advice’. It allows superannuation funds to provide a member with advice that may be collectively charged across the fund’s membership, including simple, non-ongoing personal advice on the member’s interest in the fund.

1.7 Part 2C contains additional rules about the fees that can be charged to a MySuper product (MySuper fee rules), including a list of

allowable fees and how these fees can be charged. These rules apply in conjunction with the general fee rules.

1.8 MySuper products are simple products with basic features and one investment option. These products are designed as ‘default’ options suitable for, but not limited to, disengaged members.

1.9 Under the MySuper fee rules, fees can only be charged to a MySuper product if they fall within one of seven categories and comply with applicable ‘charging rules’ (see sections 29V and 29VA). The seven categories are administration fees, investment fees, buy-sell spreads, switching fees, activity fees, advice fees and insurance fees.

1.10 It is a general expectation that trustees have in place appropriate systems for ensuring compliance with the general fee rules and MySuper fee rules.

Financial Services Royal Commission

1.11 In Recommendations 3.2 and 3.3 of the Financial Services Royal Commission, Commissioner Hayne recommended prohibiting the deduction of advice fees from MySuper products and imposing limitations on the deduction of advice fees from choice products.

1.12 Commissioner Hayne recommended removing the ability for superannuation trustees to deduct advice fees (other than for intra-fund advice) from a MySuper product, consistent with the status of MySuper as a simple product with basic features. If a MySuper member sought financial advice about their superannuation, Commissioner Hayne’s view was that these members should pay for that advice directly.

1.13 Commissioner Hayne was particularly concerned with the ‘invisibility’ of advice fees. This is particularly so where fees are ongoing; members may have previously agreed to pay advice fees but not had adequate opportunity to reassess the value of ongoing advice. Commissioner Hayne emphasised that advice fees should only be paid for the actual provision of a service.

1.14 To address this, Commissioner Hayne recommended prohibiting the deduction of any advice fee (other than for intra-fund advice) from superannuation choice products except where requirements about annual renewal, prior written identification of services and provision of the client’s express written authority have been met. These requirements were set out in Recommendation 2.1 in connection with ongoing fee arrangements (OFAs). See the ‘Context of amendments’ part of the Explanatory Memorandum for Recommendation 2.1 ‘Ongoing Fee Arrangements’ for more information.

1.15 This risk of invisible fees may arise whether fees are ongoing or non-going. The amendments address this risk by imposing requirements on fees that are not ongoing. This is consistent with superannuation trustees' existing best interests and sole purpose test obligations, as well as the expectation that trustees have appropriate oversight of fees that are deducted from member's accounts.

1.16 Commissioner Hayne made clear that intra-fund advice should not be subject to the prohibitions on advice fees that he recommended and noted that during the Financial Services Royal Commission there was no suggestion of misconduct associated with intra-fund advice.

Summary of new law

1.17 Schedule 1 to the Bill amends Part 11A of the SIS Act to ensure that a superannuation trustee can only charge advice fees (other than fees for intra-fund advice) to a member where certain conditions are satisfied. These conditions are that the fee is in accordance with an arrangement that the member has entered in to, the member has consented in writing to being charged the fee, and the trustee has the written consent or a copy of it.

1.18 The requirement that the fee be charged in accordance with the terms of an arrangement ensures that, for OFAs, the various requirements in the Corporations Act are met. For arrangements that are not OFAs, ASIC may determine the content for members' written consent by legislative instrument

1.19 Schedule 1 to the Bill also amends Part 2C of the SIS Act to remove a trustee's ability to charge advice fees in relation to MySuper products. Trustees are still permitted to charge fees in relation to intra-fund advice as administration fees (which must be collectively charged in accordance with the applicable charging rules in section 29VA).

1.20 These amendments implement the Government's response to Recommendations 3.2 and 3.3 of the Financial Services Royal Commission.

Comparison of key features of new law and current law

<i>New law</i>	<i>Current law</i>
<p>The general fee rules prohibit a trustee from charging a member fees for advice provided to that member (other than collectively charged advice, such as intra-fund advice) unless the fee is charged in accordance with an arrangement that the member has entered into, the member has consented to being charged the fee in accordance with the arrangement, and the trustee has the consent or a copy of the consent. Section 99F continues to apply to fees for advice charged to other members.</p>	<p>The general fee rules do not include requirements for trustees charging a member for advice provided to that member. Section 99F applies to fees for advice charged to other members.</p>
<p>A trustee cannot charge an advice fee to a MySuper product. Trustees can continue to collectively charge fees relating to intra-fund advice as administration fees. Section 99F continues to apply to fees for advice charged to other members.</p>	<p>Trustees can charge an advice fee to a MySuper product. Trustees can collectively charge fees relating to intra-fund advice as advice fees or administration fees. Section 99F applies to fees for advice charged to other members.</p>

Detailed explanation of new law

General requirements for charging advice fees

1.21 The amendments implement Recommendation 3.3 by introducing new requirements into Part 11A for charging fees in respect of advice.

1.22 A superannuation trustee cannot charge a member for the cost of financial product advice provided to the member, unless:

- the cost is to be paid in accordance with the terms of an arrangement entered into by the member;
- the member has expressly consented to being charged for the cost of providing the financial advice; and

- the trustee has the consent, or a copy of the consent.

[Schedule 1, item 3, section 99FA]

1.23 These requirements are explained in further detail below.

1.24 The reference to a charge for the ‘cost of providing financial product advice’ means that the new fee rule applies to any fee that is, in substance, charged to a member for advice they received. It does not matter whether a particular fee is actually described as an advice fee. For example, the new fee rule applies to fees paid to financial advisers for the cost of financial advice that may be labelled to the member as contribution, brokerage or portfolio management fees. This approach is consistent with other fee rules such as section 99F (which applies to costs of financial advice that are collectively charged, irrespective of how they are labelled).

1.25 While the new requirements apply to all fees including those charged in relation to MySuper products, the amendments implementing Recommendation 3.2 separately prevent trustees from charging advice fees in relation to MySuper products (other than fees for collectively charged advice, such as intra-fund advice).

1.26 The new requirements apply to the trustee of a superannuation fund irrespective of whether they provided the advice directly to the member, or whether the advice was provided by a third party and the cost is being arranged to be deducted from the member’s superannuation account.

Fees must be charged in accordance with an arrangement

1.27 The term ‘arrangement’ takes on its ordinary meaning and includes both ***ongoing fee arrangements*** (which is a type of arrangement defined in the Corporations Act and the subject of Recommendation 2.1) and non-OFAs. The use of the term ‘arrangement’ ensures that the new requirements in the SIS Act are appropriately linked to the requirements for OFAs in the Corporations Act.

1.28 Trustees can only charge fees covered by the new rule if the fee was authorised under an arrangement entered into by the member.

[Schedule 1, item 3, paragraph 99FA(1)(a)]

1.29 This requirement obliges trustees to consider the basis on which a particular fee is charged and be satisfied that the fee is permitted under an arrangement that the member has agreed to.

1.30 Note that the additional requirements about the member’s consent about being charged a fee apply in conjunction with the requirements about arrangements. Those requirements are explained in further detail below.

Ongoing fee arrangements

1.31 An OFA is defined in section 962A of the Corporations Act as an arrangement under which:

- a financial services licensee or their representative gives personal financial product advice to a person as a retail client;
- that person enters into an arrangement with the financial services licensee or a representative of the financial services licensee; and
- under that arrangement a fee is to be paid during a period of more than 12 months.

1.32 Division 3 of Part 7.7A of the Corporations Act, as amended by the changes implementing Recommendation 2.1, contains requirements that must be satisfied in relation to OFAs. These include the requirement that advisers renew the arrangement annually, and outline to the client both the services that will be provided and the fee that will be charged in the next 12 months.

1.33 A failure to comply with these requirements results in the statutory termination of an OFA, which means that there will no longer be any arrangement in accordance with which fees can be charged (see subsection 962F(1) of the Corporations Act as amended by the amendments implementing Recommendation 2.1). An OFA also terminates if the revised consent requirements introduced as part of the amendments implementing Recommendation 2.1 are not complied with (see proposed section 962FA of the Corporations Act).

1.34 Trustees are expected to implement appropriate processes for determining whether the requirements for an OFA are met. Trustees are also advised to obtain adequate information to be satisfied that an OFA exists and the relevant fee is covered by that arrangement.

Non-ongoing fee arrangements

1.35 Non-OFAs are not defined in the Corporations Act but refer to any arrangement for the provision of financial advice that are not covered by section 962A of that Act. Non-OFAs include any arrangement that relates to a particular service provided to the member on a one-off basis or over a period of up to 12 months.

1.36 While specific statutory rules do not apply in respect of arrangements of this kind, trustees must still determine whether the relevant fee can be charged under the arrangement. This will require trustees to have regard to the terms of the arrangement.

Consent to charge the fee

1.37 In addition to being satisfied that a fee is charged in accordance with an arrangement, a trustee can only charge a fee to a member if the member has provided written consent about the fee being passed on to them. *[Schedule 1 item 3, paragraph 99FA(1)(b)]*

1.38 Such consent must be provided in writing, and the trustee must either have the consent, or a copy of it. *[Schedule 1 item 3, paragraph 99FA(1)(e)]*

1.39 The requirement about consent complements the additional requirements on advisers introduced into Division 3 of Part 7.7A of the Corporations Act through Recommendation 2.1. Those obligations prevent what the Corporations Act labels ‘fee recipients’ (generally financial advisers) from deducting, or requesting the deduction, of fees from a client’s account without the client’s written consent.

1.40 If the fee recipient holds the account from which the fee is to be deducted, proposed section 962R of Corporations Act requires that the client has consented to the fee recipient deducting the fee from their account. If the fee recipient does *not* hold the account (for example because it is held by a third party, such as a superannuation trustee) proposed section 962S of the Corporations Act requires that the client has consented to the fee recipient arranging to have the fee deducted from their account.

1.41 A failure to comply with the applicable requirement to obtain consent will also mean that the arrangement is terminated (see proposed section 962FA of the Corporations Act).

1.42 The new fee rules in the SIS Act require that, for OFAs, the member has provided either of the consents referred to in proposed sections 962R or 962S of the Corporations Act. *[Schedule 1 item 3, subparagraph 99FA(1)(c)(ii)]*

1.43 This requirement is separately imposed on the trustee of a superannuation fund under the SIS Act to ensure that trustees are always satisfied that the applicable consent is in place for OFAs, and that they obtain the written consent of a member (or a copy of that consent) before determining that a fee can be charged. The requirement is particularly relevant for trustees who do not provide the advice, as the requirement to obtain consent under the Corporations Act applies to the fee recipient.

1.44 For fees charged in accordance with OFAs, the consent must also satisfy any requirements specified by ASIC in relation to OFAs under proposed section 962T of the Corporations Act. This ensures symmetry between the consent requirements under the respective regimes in the event that ASIC determines requirements for the giving of consent.

1.45 For arrangements that are not OFAs, the amendments also allow ASIC to specify requirements about the content of the consent through a legislative instrument. [*Schedule 1 item 3, paragraph 99FA(1)(d)*]

1.46 This instrument making power does not extend to the form in which consent must be provided. This ensures that trustees and advisers have the flexibility in developing consent forms in a way that is compatible with their existing systems.

1.47 The requirement that the written consent is provided by the member to the fee recipient ensures that third parties, such as an employer, cannot provide consent on the member's behalf.

1.48 It is expected that superannuation trustees would keep records of written consents they receive in relation to OFAs and non-OFA's in order to be able to demonstrate their compliance with the requirements introduced by these amendments.

1.49 Such legislative instruments are exempt from disallowance under section 42 of the Legislation Act because they relate to superannuation (see item 3 of in section 9 of the *Legislation (Exemptions and Other Matters) Regulation 2015*).

1.50 These legislative instruments are also exempt from sunseting under section 54 of the Legislation Act because they relate to superannuation (see item 6 of section 11 of the *Legislation (Exemptions and Other Matters) Regulation 2015*). However to ensure that they remain current and continue to be appropriate, it is expected that ASIC will continue to review them periodically.

Fees for intra-fund advice

1.51 The new requirements do not change a trustee's existing ability to provide intra-fund advice and charge the costs of intra-fund advice collectively, provided the charge is not prohibited by section 99F. Collectively charged advice fees are fees that are charged to all members or to a group of members of a particular superannuation product and are subject to the restrictions contained in section 99F.

1.52 To achieve this, the new requirements do not apply to a cost that is shared by passing it on to the individual member and other members of the fund. [*Schedule 1 item 3, subsection 99FA(3)*]

1.53 In addition to the prohibition in section 99F, the inappropriate passing of costs from a member to others members is generally prohibited by the duties and covenants contained in the SIS Act, including the best interest duty and requirement to fairly distribute costs between classes of beneficial interests.

General administration of the new fee rule

1.54 Consistent with section 99F, the new fee charging rule is administered by ASIC. This outcome is achieved through separate amendments to section 6 that are being introduced in respect of Recommendations 3.8, 6.3, 6.4, and 6.5.

Prohibition against advice fees for MySuper products

1.55 Recommendation 3.2 is implemented through amendments to the MySuper fee rules in Part 2C of the SIS Act.

1.56 Under these amendments, ‘advice fees’ are removed from the list of fees that trustees can charge in relation to a MySuper product. *[Schedule 1, item 5, paragraph 29V(1)(g) and subsection 29V(8)]*

1.57 The amendments also repeal the related charging rule for advice fees that permitted trustees to charge fees directly related to advice requested by the member. *[Schedule 1, item 14, subsection 29VA(9A)]*

1.58 These changes prevent trustees from charging any fees as advice fees to MySuper products.

1.59 The amendment also modifies the charging rules applicable to activity fees. The changes ensure that the rules that allow activity fees to be directly charged to the member or members that requested a particular action do not apply where the activity fee also satisfies the criteria for being an advice fee. This removes the ability for trustees to re-characterise an advice fee as an activity fee and directly charge it to a member. *[Schedule 1, item 11 to 13, subsections 29VA(5) to (7)]*

1.60 Trustees are permitted to continue to charge fees in respect of intra-fund advice, provided that they do so as an administration fee in accordance with paragraph 29V(2)(a). The charging rules in subsections 29VA(2) to (4) are applicable to administrative fees and mean that any such fees can only be charged on a collective basis. This may be through the same flat fee or as the same percentage of a member’s account balance or a combination of both.

Consequences of contravening the new fee rules

1.61 There are a range of existing enforcement tools available to APRA and ASIC under the SIS Act to enforce compliance with the general fee rules and the MySuper fee rules.

1.62 A standard condition on all RSE licenses that are held by superannuation trustees is compliance with the ‘RSE licensee law’, which includes the general fee rules and MySuper fee rules.

1.63 If a trustee licensee fails to comply with a provision of the SIS Act, including the general fee rules and the MySuper fee rules, APRA can issue directions under section 131D or 131DA requiring the trustee to comply.

1.64 Failure to comply with directions made by APRA is an offence with a maximum penalty of 100 penalty units (see section 131DD). If a body corporate RSE licensee is convicted of an offence, subsection 4B(3) of the *Crimes Act 1914* allows a court to impose a fine of up to 500 penalty units.

1.65 Furthermore, if a trustee becomes aware that it has breached or will breach a licence condition, and is of the view that the breach is or will be significant, the RSE licensee must report that to APRA. Failure to comply with this requirement is an offence with a maximum penalty of 50 penalty units.

1.66 Additionally, a RSE licensee who has authorisation to offer a MySuper product must comply with the general fee rules and the MySuper fee rules. If a RSE licensee does not comply with these rules, or APRA has reason to believe that they cannot continue to comply with these fee rules, APRA may remove their authorisation to offer a MySuper product.

1.67 It is a strict liability offence to offer a MySuper product when not authorised to do so with a maximum penalty of 60 penalty units.

1.68 In addition to consequences that arise under the SIS Act, a failure to comply with the general fee rules and MySuper fee rules can constitute a breach of the ‘financial services law’, compliance with which is a standard obligation on an Australian financial service licensee (see paragraph 912A(1)(c) of the Corporations Act). Amendments introduced in respect of Recommendations 3.8, 6.3, 6.4, and 6.5 expand the scope of activities for which a superannuation trustee must have an Australian financial services licence. As a consequence, the scope of what is included in the financial services law for a superannuation trustee is also expanded.

1.69 ASIC may take action in relation to entities that hold an Australian financial service licence through the enforcement tools available to them under the Corporations Act. These include, imposing additional conditions on a licence, issuing banning orders and suspending or cancelling a licence.

Consequential amendments

1.70 The amendments relocate the existing definition of ‘advice fee’ in subsection 29V(8), with minor amendments to ensure the definition can

apply generally. This allows the definition to continue to be used by other provisions despite the fact that it is no longer a category of fee that is authorised to be charged in respect of MySuper products.

1.71 Consequential amendments to the definition of ‘advice fee’ in item 101 of Schedule 10 to the *Corporations Regulations 2001* (which refers directly to subsection 29VA(8)) will be made through separate regulations to reflect the relocated definition.

Application and transitional provisions

1.72 The amendments apply from 1 July 2020 in relation to any fees payable under an arrangement entered into on or after 1 July 2020. *[Schedule 1, item 17(a)]*

1.73 The amendments apply from 1 January 2021 to any fees in respect of OFAs that were previously grandfathered under the Future of Financial Advice reforms. *[Schedule 1, item 17(b)]*

1.74 These are OFAs that were carved-out from the termination, disclosure and renewal provisions that were applied to OFAs when the Future of Financial Advice reforms were enacted in 2013. This ‘grandfathering’ for pre-existing arrangements is provided for in Subdivision C of Division 3 of Part 7.7A of the Corporations Act and is being removed from 1 January 2021 by the amendments implementing Recommendation 2.1.

1.75 The amendments apply from 1 July 2021 in relation to any other existing arrangements that were entered into before 1 July 2020. *[Schedule 1, item 17(c)]*

1.76 This ensures that any other existing arrangements, including OFAs, have a 12 month transitional period before the amendments begin to apply from 1 July 2021. Arrangements that are not OFAs will have generally ceased to apply by this time.