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THE PARLIAMENT OF THE COMMONWEALTH OF AUSTRALIA

HOUSE OF REPRESENTATIVES

FINANCIAL SECTOR REFORM (HAYNE ROYAL COMMISSION RESPONSE—
PROTECTING CONSUMERS (2020 MEASURES)) BILL 2020

EXPOSURE DRAFT EXPLANATORY MEMORANDUM

(Circulated by authority of the Treasurer, Josh Frydenberg MP)

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Glossary

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

<i>Abbreviation</i>	<i>Definition</i>
ASIC	Australian Securities and Investments Commission
Corporations Act	<i>Corporations Act 2001</i>
Financial Services Royal Commission	Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry

General outline and financial impact

Ongoing fee arrangements

Schedule # amends the Corporations Act to require ongoing fee arrangements to be renewed annually, require fee recipients to disclose in writing the total fees that will be charged and to set out the services that will be provided during the following 12 month period. It also requires written consent before fees under an ongoing fee arrangement can be deducted from a client's account.

Date of effect: The amendments commence on 1 July 2020.

Proposal announced: The Government announced that it would improve the ongoing fee regime for financial advice on 4 February 2019 as part of the Government's response to the Financial Services Royal Commission.

Financial impact: This Schedule has no financial impact.

Human rights implications: This Schedule does not raise any human rights issue. See *Statement of Compatibility with Human Rights*.

Compliance cost impact:

The Financial Services Royal Commission Final Report has been certified as being informed by a process and analysis equivalent to a Regulation Impact Statement for the purposes of the Government decision to implement this reform.

The Financial Services Royal Commission Final Report can be found at the following link:

<https://treasury.gov.au/publication/p2019-fsrc-final-report>

Chapter 1

Ongoing Fee Arrangements

Outline of chapter

1.1 Schedule # amends the Corporations Act to require financial services providers that receive fees (fee recipients) to:

- seek annual renewal from clients for all ongoing fee arrangements;
- require fee recipients to disclose in writing the total fees that will be charged;
- set out the services that will be provided during the following 12 month period; and
- obtain written consent before fees under an ongoing fee arrangement can be deducted from a client's account.

1.2 All legislative references in this Chapter are to the Corporations Act unless otherwise stated.

Context of amendments

Existing Law

1.3 Division 3 of Part 7.7A of the Corporations Act sets out the requirements for ongoing fees.

1.4 Section 962A provides that an ongoing fee arrangement exists if:

- a financial services licensee or their representative gives personal advice to a person who is 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.

1.5 Section 962B provides that an ongoing fee is any fee which is paid under an ongoing fee arrangement.

Disclosure obligation

1.6 Sections 962G, 962H (for ongoing fee arrangements entered into prior to 1 July 2013) and 962S (for all other ongoing fee arrangements)

provide that where there is an ongoing fee arrangement, the fee recipient must provide the client with a fee disclosure statement within 60 days of the disclosure day for the arrangement.

1.7 Section 962H provides that the fee disclosure statement is a backward looking document which details the services provided to the client, any services that the client received and was entitled to receive and fees charged during the previous 12 month period. Under the existing law the fee disclosure statement does not include any information about the services or fees being charged for the following 12 month period.

Renewal notice

1.8 Section 962K provides that a fee recipient must give a renewal notice in relation to the ongoing fee arrangement to the client before the end of a period of 60 days beginning on the renewal notice day for the arrangement.

1.9 To renew the ongoing fee arrangement, the client must elect in writing to renew it within 30 days of being given the renewal notice and fee disclosure statement. If the client does not elect to renew the ongoing fee arrangement, then the agreement will terminate and no further advice will be provided to the client. If the client does not notify the fee recipient whether or not they wish to renew the ongoing fee arrangement then the arrangement terminates 30 days after the end of the renewal period.

1.10 ASIC also has the power to exempt a person, or class of persons, from compliance with the requirement to provide a renewal notice if they are subject to a code of conduct approved by ASIC.

1.11 Section 962E provides that a client may, at any time, terminate the ongoing fee arrangement and cannot be required to pay any amount that is more than the amount referred to in the ongoing fee arrangement and any other costs incurred by the fee recipient as a result of the termination.

1.12 Section 962F provides that the ongoing fee arrangement will terminate if the fee recipient does not comply with the renewal notice obligation in section 962G.

1.13 Ongoing fee arrangements which were entered into prior to the Future of Financial Advice (FOFA) reforms which took effect from 1 July 2013 are not currently required to comply with renewal requirements, but are required to comply with the fee disclosure statement requirements.

Financial Services Royal Commission

1.14 In the Final Report of the Financial Services Royal Commission, Commissioner Hayne found that over the last decade, many people who

sought and obtained advice from a financial adviser were charged ongoing fees for services that were not provided. These fees were charged ‘invisibly’ from clients’ accounts, without clients being able to determine whether the promised services were delivered.

1.15 The Commissioner identified a number of causes of the fee for no service conduct. On that basis, the Commissioner identified that changes in relation to ongoing fee arrangements should address those causes by focusing on the following:

- The information that an adviser must give a client about the services to be provided under such arrangement, in order for the client to assess whether the services provided under the ongoing fee arrangement represent value for money.
- The period for which a contract for future services can be made.
- The mechanism by which advisers should be permitted to charge ongoing fees to clients so that fees can no longer be charged ‘invisibly’.

1.16 In considering potential changes in these areas, Commissioner Hayne recommended that a client should be required to opt-in to the arrangement annually (rather than the current two years). He also recommended that the client should be given a forward looking summary of the services that the client will be entitled to receive and the fees payable for those services (in addition to the existing disclosure of fees and services).

1.17 In addition, Commissioner Hayne also recommended that the client’s express written authority should be obtained prior to the deduction of fees from any account held by the client and that the authority must be renewed annually.

1.18 If ongoing fee arrangements have these characteristics, the Commissioner considered that the arrangements will be unlikely to give rise to the ‘fee for no service’ conduct that was the subject of evidence before the Commission.

Summary of new law

1.19 Schedule # amends the Corporations Act to require ongoing fee arrangements to be renewed annually, require fee recipients to disclose in writing the total fees that will be charged and to set out the services that will be provided during the following 12 month period. It also requires written consent before fees under an ongoing fee arrangement can be deducted from a client’s account.

Comparison of key features of new law and current law

<i>New law</i>	<i>Current law</i>
Fee recipients are required to seek renewal of ongoing fee arrangements by clients annually.	Ongoing fee arrangements are required to be renewed every two years. Ongoing fee arrangements entered into prior to 1 July 2013 are not required to be renewed.
Fee disclosure statements will include information on the fees to be charged and services to be provided in the coming year, as well as information about the previous year.	Fee disclosure statements are retrospective which provide a summary of the fees and services provided during the previous year.
Written consent must be obtained prior to fees being deducted under an ongoing fee arrangement and consent generally cannot be obtained for a period of more than 12 months. Fee recipients must obtain written consent to continue an ongoing fee arrangement annually.	There is no ongoing requirement to obtain consent after the client’s initial consent to ongoing fee arrangements.

Detailed explanation of new law

New and existing ongoing fee arrangements to be renewed annually

1.20 The law will be amended to remove previous exemptions that applied for fee arrangements entered into prior to the Future of Financial Advice (FOFA) reforms. The amendments will provide that these ongoing fee arrangements will be subject to the application of these new provisions. The amendments also provide that a fee recipient must seek a client’s renewal of an ongoing fee arrangement annually, rather than every two years. *[Schedule #, items 2, 18 and 19, sections 962D, 962L and sections 962R to 962X of the Corporations Act]*

1.21 The law will be amended to remove the ability for a person or class of persons to be exempted from the requirement to give a renewal notice. *[Schedule #, item 1, section 962CA of the Corporations Act]*

Enhanced fee disclosure statements

1.22 The amendments will require the fee recipient to provide the client with an annual fee disclosure statement that details the services the

client is entitled to receive and that are paid for by the client, the amount of each ongoing fee, any additional fees payable in relation to the services described in the fee disclosure statement and any other prescribed matters. This is intended to ensure that clients are aware of the services that they are entitled to receive under the ongoing fee arrangements and the fees payable. *[Schedule #, items 12, 13 and 16, sections 962H and 962K of the Corporations Act]*

1.23 The amendments provide that the fee recipient must include the following information with regard to the upcoming year:

- information about the services the client is entitled to receive under the ongoing fee arrangement;
- the amount of each ongoing fee that the client will be required to pay, including any fees payable at the end of the upcoming year; and
- any other prescribed information.

[Schedule #, items 8, 9, 10 and 12, section 962H of the Corporations Act]

1.24 Fee disclosure statements will be required to express the fee amounts in Australian dollars, unless an alternative is provided in the regulations. Where the amount of an ongoing fee cannot be determined, the fee disclosure statement must include a reasonable estimate of the fees and an explanation of the method used to work out the estimate. These amendments will supplement, not replace, the existing fee disclosure statement regime. *[Schedule #, items 11, 13 and 14, section 962H of the Corporations Act]*

1.25 Section 962K of the Corporations Act will also be amended to be a civil penalty provision. *[Schedule #, item 17, section 962K of the Corporations Act]*

Written consent for the deduction of fees under ongoing fee arrangements

1.26 The amendments will require that fee recipients obtain the client's express written consent to deduct, arrange to deduct, or accept an amount for payment of, fees under an ongoing fee arrangement.

1.27 Where the fee recipient controls the account to be debited, the amendments provide that the consent must be obtained prior to making the deduction. Where the account to be debited is controlled by a third party, the fee recipient must obtain express written consent to arrange the deduction and have provided a copy of that consent to the third party prior to, or as part of, arranging the deduction.

1.28 Where an account is held jointly, the fee recipient must satisfy the consent requirements for all account holders, not only the client. The

amendments provide that where a fee recipient does not comply with the consent requirements, the ongoing fee arrangement will terminate.

1.29 The amendments provide that a Court may order that the fee recipient refund amounts deducted without consent.

1.30 Ongoing fee arrangements are not permitted to include conditions that require consent or that do not permit variation or withdrawal of consent. Any conditions to that effect are void. *[Schedule #, item 19, section 962W of the Corporations Act]*

1.31 The amendments provide that where ASIC has determined requirements for giving consent to deductions, that the instrument may require a specific form or form of words must be used for giving consent and may also require that the consent include specified information. *[Schedule #, item 19, section 962T of the Corporation Act]*

1.32 The amendments provide that an account holder may withdraw or vary the consent at any time by providing notice to the fee recipient in writing. If the fee recipient receives notice from the client withdrawing or varying the consent, then the fee recipient is required to:

- give written confirmation to the account holder that the consent was received within five business days; and
- if the consent was provided to an account provider, the fee recipient must also give the account provider a copy of the notice within five business days.

1.33 The amendments provide that contravention of this requirement is subject to civil penalty proceedings. *[Schedule #, item 19, section 962U of the Corporations Act]*

1.34 The amendments repeal section 962G (the previous requirement to provide a fee disclosure statement) and any associated references and section 962J (the definition of disclosure day) as these provisions are redundant following these amendments. Section 962K requires fee recipients to provide a fee disclosure statement with the renewal notice annually. *[Schedule #, items 3, 4, 5, 7 and 15, subsection 962F(1), (2) and (3), section 962G and section 962J of the Corporations Act]*

1.35 The amendments provide that a client's consent will cease to have effect if the ongoing fee arrangement is terminated, or at the end of the period of 30 days after the end of the first renewal period after consent is given for the ongoing fee arrangement.

1.36 Under the existing law, each time a renewal notice and fee disclosure statement is provided to a client, a 60 day period to the expiry of consent will commence. During this renewal period, a fee recipient will be required to again seek the client's written consent for deductions of ongoing fees. The new consent will operate from the date that it was

obtained, and the previous consent will automatically terminate at the end of the 30 day period after the end of the renewal period. *[Schedule #, item 19 section 962V of the Corporations Act]*

Record-keeping requirements

1.37 Fee recipients will be required to keep appropriate records to demonstrate their compliance with Division 3 of Part 7.7A. These records must be kept for five years and a failure to do so will be a criminal offence with a penalty of up to one year imprisonment. Further records may be specified in the regulations. *[Schedule #, item 19, section 962X of the Corporations Act]*

Consequential amendments

1.38 The definition of civil penalty order will be amended to insert a reference to section 1317GB and to include in the definition penalties in relation to the deduction of ongoing fees without consent, arrangement of the deduction of ongoing fees without consent or acceptance of such deductions and the confirmation of receipt of variation of withdrawal of consent for deductions of ongoing fee arrangements. *[Schedule #, items 22 and 23, section 9 of the Corporations Act]*

1.39 The amendments repeal the definition of disclosure day and the table item referring to the amendment civil penalty provision for section 962S. *[Schedule #, items 25 and 27, section 960 and subsection 1317E(3) (table item dealing with subsection 962S(1)) of the Corporations Act]*

1.40 The amendments provide new table items in subsection 1317E(3) for the civil penalty provisions for:

- a fee recipient failing to comply with the requirement to obtain consent to deduct ongoing fees from an account;
- a fee recipient failing to comply with the requirement to obtain consent to arrange for deductions of ongoing fees from an account;
- a fee recipient failing to comply with the requirement not to accept payment of ongoing fees resulting from a deduction from an account without consent; and
- a fee recipient failing to comply with the requirement to confirm receipt of a variation or withdrawal of consent for deductions of ongoing fees.

[Schedule #, items 26 and 27, subsection 1317E(3) of the Corporations Act]

1.41 The amendments provide that where a civil penalty order is made, that the court gives preference to and has regard for any refund

amounts payable to persons who suffer damage as a result of a contravention of the provisions. *[Schedule #, items 28 and 29, subparagraph 1317QF(2)(a)(ii) and paragraph 1317QF(3)(b) of the Corporations Act]*

1.42 The amendments provide relief from liability for a contravention of a civil penalty provision where a person meets the requirements of section 1317S. *[Schedule #, item 27, subsection 1317S(1) of the Corporations Act]*

1.43 The amendments insert a reference to the criminal offence provision into the table in Schedule 3 of the Corporations Act. *[Schedule #, item 31, Schedule 3 of the Corporations Act]*

Application and transitional provisions

Ongoing fee arrangements in force immediately before 1 July 2020 subject to Subdivision C of Division 3 of Part 7.7A

1.44 The transitional provisions apply to:

- Ongoing fee arrangements subject to the former Subdivision C of Division 3 of Part 7.7A of the Corporations Act that were in force immediately before 1 July 2020; and
- Ongoing fee arrangements a in force immediately before 1 July 2020 and not subject to Division 3 of Part 10.45.

[Schedule #, item 19, sections 1672B and 1672F of the Corporations Act]

1.45 For these ongoing fee arrangements, the transitional provisions provide that from 1 July 2020 until 31 December 2020, subsection 962K(1) applies in relation to the ongoing fee arrangement as if it were replaced with subsection 1672C(3). This subsection requires a fee recipient to:

- give the client a renewal notice and fee disclosure statement in relation to the ongoing fee arrangement before the end of the six month transition period; and
- seek the client’s consent to deductions prior to 1 January 2021, after which the new Subdivision C applies to these ongoing fee arrangements.

1.46 If the client provides the fee recipient consent for the purposes of the new Subdivision C prior to 1 January 2021, then sections 962U and 962X apply from the date the consent is given.

1.47 These transitional provisions provide that section 1350 of the Corporations Act does not apply to the operation of Subdivision B of Division 3 of Part 7.7A, in respect of the ongoing fee arrangement. *[Schedule #, item 19, section 1672C of the Corporations Act]*

1.48 The amendments provide that where an obligation exists under sections 962G and 962S before 1 July 2020 that was not discharged before that date, these obligations cease on 1 July 2020, however fee recipients will be required to comply with the fee disclosure statement requirements during the transition period. This means that only one fee disclosure statement will need to be provided during the six month transition period. *[Schedule #, item 21, sections 1672C and 1672G of the Corporations Act]*

Ongoing fee arrangements in force immediately before 1 July 2020 to which the former Subdivision C did not apply

1.49 The amendments provide that from 1 July 2020 until 30 June 2021, that subsection 962K(1) applies in relation to the ongoing fee arrangement as if it were replaced with subsection 1672G(3). This requires the fee recipient to:

- give the client a renewal notice and fee disclosure statement in relation to the ongoing fee arrangement before the end of the 12 month transition period; and
- seek the client's consent to deductions prior to 1 July 2021, after which the new Subdivision C commences for these ongoing fee arrangements.

1.50 If the client provides the fee recipient consent for the purposes of the new Subdivision C prior to 1 January 2021, then sections 962U and 962X apply from the date the consent is given.

1.51 Section 1350 does not apply in relation to the operation of Subdivision B of Division 3 of Part 7.7A, in respect of the ongoing fee arrangement. *[Schedule #, item 19, section 1672G of the Corporations Act]*

1.52 The amendments provide that where an obligation exists under sections 962G, 962K and 962S before 1 July 2020 that was not discharged before that date, these obligations cease on 1 July 2020, however fee recipients will be required to comply with renewal notice and fee disclosure statement requirements during the transition period. This means that only one fee disclosure statement will need to be provided during the 12 month transition period. *[Schedule #, item 19, sections 1672C and 1672G of the Corporations Act]*