

DRAFT EXPLANATORY STATEMENT

Issued by authority of the Minister for Financial Services and Superannuation

Corporations Act 2001
Corporations Regulations 2001

The *Corporations Act 2001* (the Act) provides for the regulation of corporations, financial markets, and products and services, including in relation to licensing, conduct, financial product advice and disclosure.

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

The *Corporations Amendment Regulation 2013 (No. F)* (the Regulation) amends the *Corporations Regulations 2001* (the Principal Regulations). The amendment is in respect of the provisions in Parts 7.7A and 10.18 of the Act, dealing with the ban on conflicted remuneration. Specifically, the Regulation deals with the application of the ban on conflicted remuneration and amends the ‘grandfathering’ arrangements.

Details of the Regulation are set out in Attachment A. A statement of the Regulation’s compatibility with human rights is set out in Attachment B.

The Regulation is a legislative instrument for the purposes of the *Legislative Instruments Act 2003*.

The Act does not specify any conditions that need to be satisfied before the power to make the Regulation may be exercised.

The Regulation commences on the day after it is registered.

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Details of the proposed Corporations Amendment Regulation 2013 (No. F)

Section 1 – Name of Regulation

This section specifies the name of the Regulation as the *Corporations Amendment Regulation 2013 (No. F)*.

Section 2 – Commencement

This section specifies that the Regulation commences the day after registration.

Section 3 – Authority

This section provides that the authority for making the Regulation is the *Corporations Act 2001* (the Act).

Section 4 – Schedule(s)

This section provides that Schedule 1 amends the *Corporations Regulations 2001* (the Principal Regulations).

Schedule 1 – Amendments

Item 1 inserts a new regulation 7.7A.12EA to specify a type of monetary benefit that is not conflicted remuneration for the purposes of paragraph 963B(1)(e) of the Act. It is intended to cover what are commonly referred to in the financial advice industry as ‘buyer of last resort’ arrangements. These arrangements allow a licensee to acquire the business of a representative for a purchase price using a specified formula. This regulation deems that purchase price not to be conflicted remuneration if it is based, in whole or in part, on the number or value of financial products held by the representative’s clients and the weighting attributed to the financial products that are issued by the licensee are the same of the weighting attributed to other financial products. In these situations, buyer of last resort arrangements would not influence the advice provided by a representative because favourable weighting is not provided to the licensee’s products.

Item 2 replaces the current regulation 7.7A.16 ‘Application of ban on conflicted remuneration’ with a new regulation 7.7A.16 ‘Application of ban on conflicted remuneration – platform operator’. The heading of the regulation is changed to better describe regulation 7.7A.16, distinguishing it from the new regulation 7.7A.16A ‘Application of ban on conflicted remuneration – person other than platform operator’ also introduced by Item 2.

Regulation 7.7A.16 prescribes circumstances in which the ban on conflicted remuneration in Division 4 of Part 7.7A of the Act does not apply to a benefit given by a platform operator. That is, regulation 7.7A.16 provides for the ‘grandfathering’ of these payments.

The term ‘platform operator’ is defined in section 1526 of the Act. Broadly, a platform operator is a financial services licensee or ‘RSE licensee’ (as defined in the *Superannuation Industry (Supervision) Act 1993*) that offers to be the provider of a custodial arrangement. A ‘custodial arrangement’ is an arrangement where the client may instruct the platform to acquire certain financial products, and the products are then either held on trust for the client, or the client retains some interest in the product.

A person subject to Division 4 of Part 7.7A of the Act (the ban on conflicted remuneration) will be either a platform operator, or a person other than a platform operator. Benefits given by these two types of persons are grandfathered separately, in regulations 7.7A.16 and 7.7A.16A respectively. However, in both cases, the ban on conflicted remuneration will apply to all new clients after 1 July 2014.

Regulation 7.7A.16 repeals the existing grandfathering provisions for platform operators and introduces new provisions. Under these provisions, a benefit will not be subject to the ban on conflicted remuneration if that benefit is:

- given by a platform operator;
- given under an arrangement that was entered into before the application day; and
- relates to a regulated acquisition under a custodial arrangement provided by the platform operator on the instructions of a person who had given an instruction for a regulated acquisition under the custodial arrangement before 1 July 2014.

The 'application day' is defined in subsection 1528(4) of the Act as the earlier of 1 July 2013 or the day specified in a notice lodged with ASIC indicating that the obligations and prohibitions imposed under Part 7.7A of the Act are to apply to a person. This reflects the transitional arrangements for the Future of Financial Advice reforms, under which compliance becomes mandatory on 1 July 2013, but persons can formally elect to comply with the measures at an earlier date.

The effect of regulation 7.7A.16 is to grandfather benefits given under pre-FOFA arrangements except where they relate to a new client coming onto the platform after 1 July 2014. Arrangements between financial services licensees and platform operators entered into after 1 July 2013 will not be grandfathered and must be negotiated on a FOFA-compliant basis.

It may be that contracts are amended from time to time for various reasons, including allowing parties to restructure for efficiency purposes (which may result in a change to the name of a party to a contract). Subregulation 7.7A.16(3) allows for changes to the parties to the arrangement without this event triggering a new arrangement for the purposes of the grandfathering provisions. However, restructuring simply in order to continue or increase grandfathered payments may attract the operation of the relevant anti-avoidance provision of the Act (section 965). Grandfathering will not be brought to an end where the application of the ban would bring about an acquisition of property otherwise than on just terms (see subsection 1528(3) of the Act).

Regulation 7.7A.16A prescribes circumstances in which Division 4 of Part 7.7A of the Act applies to benefits given by persons other than platform operators (where Division 4 would not otherwise apply by virtue of subsection 1528(1) of the Act). Regulation 7.7A.16A excludes from grandfathering benefits that:

- are given under an arrangement entered into before the application day; and
- are not given by a platform operator; and
- are given in relation to the acquisition of a financial product by a retail client who did not have an interest in the financial product immediately before 1 July 2014.

The effect of regulation 7.7A.16A is to limit the grandfathering to conflicted remuneration paid under pre-FOFA arrangements relating to the existing investments of clients at 1 July 2014. Conflicted remuneration from non-platform operators will be subject to the ban for new investments in different products after 1 July 2014 regardless of whether these investments are made through a platform/custodian or directly by the client.

However, subregulations 7.7A.16A(4) and (5) allows for a client to increase their interest in an existing managed investment scheme or superannuation scheme without being taken to have acquired a new financial product. This means that non-platform operators can continue to pay conflicted remuneration in relation to clients who increases their exposure to a product that the client held before 1 July 2014. In addition, if it is possible for the client to change the nature of their interest without resulting in the acquisition of a different underlying product, this will not cause grandfathering to cease. This may be the case, for example, where a client moving between generic investment risk options (that is, from the 'growth' option to the 'balanced option') in a managed investment scheme or superannuation scheme.

As is the case for regulation 7.7A.16, regulation 7.7A.16A allows for changes to the parties to an arrangement without this event triggering a new arrangement (see subregulation 7.7A.16A(3)).

Together, regulations 7.7A.16 and 7.7A.16A grandfather benefits given by platform operators and persons other than platform operators according to a consistent approach. In both cases, benefits given in relation to new clients are not grandfathered, even if the benefit is given under a pre-existing arrangement.

With regard to platform operators, conflicted remuneration can continue to be paid in relation to new investments on that platform only if the client had an interest held through the platform before 1 July 2014.

Non-platform operators, for example fund managers, are only able to pay conflicted remuneration in relation to new investments if the client is increasing their interest in an existing product (for example, investing more money in a particular superannuation scheme or managed investment scheme). If the client is investing in a completely different product, no conflicted remuneration can be paid. However, limited switching within a product will not cease grandfathering (as outlined above).

The grandfathering for platform operators is crafted on a 'negative' basis in the sense that it indicates circumstances when a benefit from a platform operator will *not* be subject to the ban on conflicted remuneration. This is different from the grandfathering arrangements in this regulation for benefits from non-platform operators which is crafted on a positive basis (that is, it indicates circumstances when a benefit from a non-platform operator will be subject to the ban on conflicted remuneration). This difference in phrasing is necessary because of the different approach to grandfathering between platform and non-platform operators in the Act. In particular, the Act currently provides for no grandfathering of benefits from platform operators. That means the ban on conflicted remuneration applies to all benefits from platform operators to the extent constitutionally possible. Because the ban in the Act applies to all platform operators, it is necessary in this regulation for the grandfathering to specify the circumstances under which a benefit from a platform operator will *not* be subject to the ban. In contrast, the Act already provides grandfathering for benefits from non-platform operators. Given this, this regulation

needs to specify circumstances under which benefits from non-platform operators that are subject to the ban.

Benefits paid under existing arrangements can continue to be paid to the extent that those benefits have been grandfathered by this regulation. For the avoidance of doubt, regulation 7.7A.17 specifies that the validity of those arrangements as they apply to grandfathered benefits is not affected by the commencement of the ban on conflicted remuneration.

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ATTACHMENT B

Statement of Compatibility with Human Rights

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

Corporations Amendment Regulation 2013 (No. F)

This Legislative Instrument is compatible with the human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*.

Overview of the Legislative Instrument

The *Corporations Amendment Regulation 2013 (No. F)* amends the ‘grandfathering’ arrangements for the ban on conflicted remuneration.

Human rights implications

This Legislative Instrument does not engage any of the applicable rights or freedoms.

Conclusion

This Legislative Instrument is compatible with human rights as it does not raise any human rights issues.

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