12 March 2012

Manager
Financial Services Unit
Retail Investor Division
The Treasury
Langton Crescent
PARKES ACT 2600

Email: instalmentwarrantcorpregs@treasury.gov.au

Dear Madam/Sir,

The Self Managed Superannuation Funds Professionals' Association of Australia ("SPAA") welcomes the opportunity to make a submission in relation to the proposed Corporations Amendment Regulations regarding limited recourse borrowing arrangements (LRBAs).

The key points of this submission are:

- **In SPAA's view there is significant ambiguity regarding the meaning of 'issuer' in the regulations.**
- **To address difficulties associated with determining which party is the 'issuer' and when the product is issued, SPAA recommends that the term 'arrangement' be defined in the Corporations Law and Act.**
- **SPAA recommends an entity who is a related party of the fund as defined in section 10(1) of the SIS Act, should be excluded from the definition of issuer in the Regulations.**

SPAA is the peak professional body representing the self managed superannuation fund (SMSF) sector throughout Australia. SPAA represents professionals, irrespective of their personal membership and professional affiliations, who provide advice to individuals aspiring to higher levels of participation in the management of their superannuation savings. Membership of SPAA is principally accountants, auditors, lawyers, financial planners and other professionals such as actuaries.

SPAA is committed to raising the standard of professional advice and conduct in the SMSF sector by working proactively with Government and the industry. In doing so, SPAA has contributed to SMSF advisors providing a higher standard of advice to SMSF trustees. This in turn has enabled trustees to make more informed decisions addressing the adequacy, sustainability and longevity of their own retirement savings. SMSFs offer trustees greater control and flexibility and have become

SMSF Professionals' Association of Australia Ltd
ABN 67 103 739 617

SPAA House
Level 1, 366 King William Street
Adelaide SA 5000
Tel 1300 779 096

PO Box 6540
Halifax Street
Adelaide SA 5000

Fax +61 8 8212 5993
enquiries@spaa.asn.au
www.spaa.asn.au

an integral part of the Australian Superannuation landscape by providing significant and viable options for managers, business owners, executives and retail operators alike.

SPAA supports the Government's move to ensure that superannuation funds are protected by the *Corporations Act 2001* (Corporations Act) financial consumer protection framework when they enter into a LRBA. This will provide SMSFs with an adequate level of consumer protection from unlicensed and unqualified advice and dealings. However, SPAA believes that the proposed amendments create ambiguities and uncertainties for SMSFs and their advisors.

Approach to defining 'issuer'

The current draft of the regulations is ambiguous in regards to the meaning of an 'issuer' of a LRBA. The proposed regulations will make any party to a LRBA held by a superannuation fund an issuer of a product for the purpose of the Corporations Act.

The attachment to the explanatory memorandum accompanying the proposed regulations describes the complex nature of LRBAs and the numerous parties involved. SPAA acknowledges that these complicated transactions make it difficult to determine which parties are 'issuers' and the associated difficulties in determining which party, if any, is obliged to disclose information under the Corporations Act.

However, the approach taken in the draft regulations which makes any party to an arrangement an issuer of the product seems excessively broad. The current approach may inadvertently catch entities that are part of the LRBA issuing process who, if required to meet the requirements to be imposed on issuers, would clearly provide no additional consumer protection benefits for the trustees and members of the fund.

SPAA views that there are three broad groups involved in LRBAs:

- parties to the arrangement;
- financial planners authorised to give financial advice in relations to the LRBA; and
- other professionals that provide advice or are involved in providing services to their clients.

Each of these groups has different obligations in relation to a LRBA, and it is their obligations that should determine what level of disclosure and licensing they should need to comply with – that is, whether they are a LRBA issuer. The proposed regulations' definition of issuer does not seem to have regard for the different obligations that these different groups have in relation to LRBAs.

SPAA believes that clarifying the scope of the term arrangement can resolve this issue. This is discussed further below. If the approach of clarifying the scope of the term arrangement is not adopted, then the way in which the term 'issuer' will be applied to entities who are part of the process of creating a LRBA, still needs to be clarified.

The term 'arrangement'

It is not clear from the exposure draft what is meant by the term 'arrangement'. Proposed regulation 7.1.04J indicates that the "arrangement relating to the acquisition of an acquirable asset under 67A or 67B of the SIS Act is declared to be a financial product". However, it is unclear whether this regulation is referring to the acquirable asset only, the establishment of the holding trust, the loan or all components that ensure the requirements of section 67A are met. Further, subregulation 7.1.06(2) states that the arrangement is not a credit facility; however, it would seem that the loan obtained by the fund constitutes a credit facility. To avoid doubt as to what the regulation is specifying in regards to the arrangement, perhaps the Regulations could specify that the 'arrangement' consists of particular components as set out in section 67A of the SIS Act.

There is also a timing issue with the question of the commencement of the 'arrangement' in view of the number of transactions and components that may be involved. In our view, it should be made clear whether the arrangement commences at the time the first or last document is executed.

A person enters into a legal relationship that sets up the arrangement

Regulation 7.1.04H states that the arrangement is issued when a person enters into a legal relationship that sets up the arrangement. As alluded to above, this would appear to extend beyond the parties to the arrangement and may include other professionals who are involved in setting up the arrangement. It may include lawyers who are involved in drafting the relevant documents, accountants involved in setting up the accounts and financial planners who would be advising on the appropriateness of the arrangement. It is inappropriate for these entities to be included as issuers of LRBA.

While there is uncertainty about the breadth of the term 'arrangement' it is difficult to imagine that the term 'arrangement' should extend to aspects of the process of entering into the relevant transactions. The scope of the term should be narrowed so that entities involved in assisting in transactions to create a LRBA are not deemed to be issuers of a product — for example, lawyers, accountants and financial planners.

Furthermore, there are also difficulties in determining what kind of disclosure should be provided in relation to the various components, who should provide it and, where there is more than one issuer involved, how it should be coordinated. The exposure draft regulations and explanatory memorandum do not provide the industry with any guidance on these issues.

Holding trust trustees

Where SMSFs use a holding trust to hold an asset associated with a LRBA (as required by the *Superannuation Industry (Supervision) Act 1993*) (SIS Act), the holding trust trustee will be a party to the arrangement. This will make the holding trust trustee an issuer for the purposes of the Corporations Act because of the operation of subregulation 7.1.04H(2). Consequently, the holding trust trustee will need to hold an Australian Financial Services Licence (AFSL) in order to comply with the Corporations Act financial consumer protection laws. It is possible that 7.1.04J(2) attempts

to exclude the holding trust arrangement from the arrangement and thus exclude the trustee from being an issuer but it is not clear in the draft regulations whether or not this would be the case.

When an SMSF enters into a LRBA, it is common for one or more of the trustees of the SMSF to also be a trustee or director of a corporate trustee which acts as the trustee of the holding trust. The Corporations Act exempts SMSF trustees from having to hold an AFSL (paragraph 911A(2)(j)) in relation to the fund. However, it is unclear in the draft regulations whether a person/related party when acting in the capacity of a trustee of the holding trust in these circumstances would be exempt from the licensing requirements.

Requiring the holding trust trustee in these circumstances to hold an AFSL will undermine the commercial amenity of LRBAs and undermine the legislative intent of subsection 67A(4) of the SIS Act which legitimises investments by superannuation fund trustees in traditional instalment warrants that include underlying borrowings.

Related party borrowing

It is common for the lender in a LRBA to be a related party of the fund. As defined in the draft regulations, a related party borrower in these circumstances would constitute an issuer of the product and would presumably require the related party to hold an AFSL or be an authorised representative of an entity that holds an AFSL.

Given the intent of the proposed amendments is to provide fund members with increased levels of consumer protection, it is difficult to see how requiring a related party lender to be licensed in these circumstances would provide any additional consumer protection for members.

Furthermore, in most cases the related party borrower will simply lack the necessary experience or credentials to hold an AFSL and they are also unlikely to be able to meet the substantial cost of applying for an AFSL.

The EM seems to indicate when discussing Item 2 that a person who provides credit would not be caught by the new arrangements but Item 2 merely excludes an arrangement from being a credit facility, not a credit facility from being an arrangement.

Recommendations

- To address some of the difficulties associated with determining which party is the 'issuer' and when the product is 'issued', SPAA recommends that:
    - the term 'arrangement' for the purposes of the LRBA be defined in the Corporations Law; and
    - Regulation 7.01.04H should indicate that it is a party to the arrangement for purposes of acquiring an acquirable asset under section 67A or 67B of the SIS Act who is the issuer of the product.

- SPAA recommends that for the purposes of a LRBA, any entity who is a related party of the fund for purposes of subsection 10(1) of the SIS Act should be excluded from the definition of an 'issuer'.

We would be happy to provide further information or to discuss our submission with you in more detail if need be.

Contact Numbers:
Tel: (08) 8205 1900

Mrs. Andrea Slattery
Chief Executive Officer

Mr. Peter Burgess
Technical Director

Yours sincerely

Andrea Slattery
CEO