

29 April 2019

The Treasury
Financial Services Reform Implementation
Taskforce
Langton Crescent
PARKES ACT 2600

By email: FOFAGrandfathering@treasury.gov.au

Dear Sir/Madam

Ending Grandfathered Conflicted Remuneration for Financial Advisers

- 1 We refer to the exposure drafts of the *Treasury Laws Amendment (Ending Grandfathered Conflicted Remuneration) Bill 2019* and the *Treasury Laws Amendment (Ending Grandfathered Conflicted Remuneration) Regulations 2019*.
- 2 We consider there to be a significant loophole in proposed section 963M that undermines the intent of proposed Subdivision CA and the regulations, which is to ensure that where conflicted remuneration ceases to be given as a result of the removal of the current “grandfathering” arrangements, the amount of the conflicted remuneration is rebated to retail clients rather than retained by the giver of the conflicted remuneration.
- 3 Achieving this intent hinges upon proposed section 963M, as it will determine whether a person will be covered by a scheme for rebating conflicted remuneration made by regulations made under section 963N.
- 4 Proposed section 963M provides that it covers a person in relation to conflicted remuneration who “*is legally obliged (disregarding Subdivision C) to give, on or after 1 January 2021, the conflicted remuneration to another person.*”
- 5 Thus, a person who is giving conflicted remuneration to another person up until 1 January 2021 will not be covered by a scheme made under section 963N if the person is not legally obliged (disregarding Subdivision C) to give conflicted remuneration to the other person on or after 1 January 2021.
- 6 Evidence given to the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry demonstrated that in some cases trustees of superannuation funds or parties related to them have been giving conflicted remuneration (by paying commissions) despite not being contractually obligated to do so. In other cases, the evidence cast doubt on whether there was any contractual obligation. In other cases, the evidence demonstrated that the trustee or related party had the power to unilaterally cease paying commissions or to bring any contractual obligation to an end, for example by terminating the contract.¹
- 7 Further, any contractual obligation to pay commissions may hinge on Product Disclosure Statements disclosing that they will be paid. If the Product Disclosure Statement ceases to

¹ See for example: Final Report, Volume 2 at 2.3.5 in relation to Colonial First State Investments Limited; Exhibit 5.2.24, clauses 4.4(a)(vi), 4.5 and 5.1(a) in relation to NULIS Nominees (Australia) Limited.

disclose that commissions will be paid, then the obligation to pay them may come to an end.²

- 8 Where a person is giving conflicted remuneration up to 1 January 2021 not as a result of a contractual obligation, but rather voluntarily, then it will not be covered by proposed section 963M and therefore it will not be required by any scheme made under section 963N to rebate to retail clients the amount of the conflicted remuneration that it ceases to pay from 1 January 2021 in order to comply with Subdivision C.
- 9 Similarly, if a person ceases to be contractually obligated to give conflicted remuneration otherwise than because of Subdivision C, for example by terminating the relevant contract or ceasing to disclose that commissions will be paid in the Product Disclosure Statements, then the person will also not be covered by proposed section 963M.
- 10 Accordingly, persons giving conflicted remuneration may be able to easily avoid the requirements of any scheme made under section 963N, either because they have never been contractually obligated to give the conflicted remuneration, or by bringing that obligation to an end otherwise than by reason of Subdivision C. Those persons will therefore be able to retain the amount of conflicted remuneration they had been giving prior to 1 January 2021 as additional profit, rather than rebate the amounts to retail clients.
- 11 In order for the intent of Subdivision CA to be achieved, proposed section 963M must be broadened to also cover a person in relation to conflicted remuneration that it had been giving at any time between 22 February 2019 and 1 January 2021 or in respect of which there are reasonable grounds to consider that it would, but for Subdivision C, give to a person after 1 January 2021.
- 12 It would not be sufficient to extend proposed section 963M only to cover persons in relation to conflicted remuneration given immediately prior to 1 January 2021, as persons giving conflicted remuneration could easily avoid this by ceasing to give the conflicted remuneration shortly before 1 January 2021.
- 13 There must also be consequential changes to the proposed regulations.
- 14 Where proposed regulations 7.7A.15AL and 7.7A.15AM refer to "*the day by which the covered person is legally obliged (disregarding Subdivision C of Division 4 of Part 7.7A of the Act) to give the conflicted remuneration to another person*", this should be changed to:

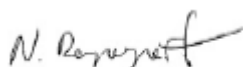
the day by which the covered person is legally obliged (disregarding Subdivision C of Division 4 of Part 7.7A of the Act) to give the conflicted remuneration to another person, or if the person is not legally obliged (disregarding Subdivision C of Division 4 of Part 7.7A of the Act) to give the conflicted remuneration to another person, the day by which there are reasonable grounds to consider that the covered person would have given the conflicted remuneration to another person but for Subdivision C.

- 15 We also suggest that an interpretive provision be inserted as follows:

For the purpose of determining the day by which there are reasonable grounds to consider that the covered person would have given the conflicted remuneration to another person but for Subdivision C, regard is to be had to the practice of the covered person between 22 February 2019 and 31 December 2020.

- 16 If you have any questions in relation to this submission, please do not hesitate to contact us.

Yours faithfully



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² See for example, Exhibit 5.2.24, clause 4.1(a).