MinterEllison.

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Dear Treasurer

Submission on Exposure Draft Bill to implement Quality of Advice Tranche 1 reforms

We appreciate the opportunity to make a submission on the *Treasury Laws Amendment (2024 Measures No. 1) Bill 2024: Quality of Advice Tranche 1* (**Draft Bill**), which seeks to implement Recommendations, 7, 8, 10, 13.1 to 13.5 and 13.7 to 13.9 of the Quality of Advice Review Final Report (**QAR Report**).

MinterEllison is a leading Australian law firm. We advise major financial institutions, including banks, insurance companies and superannuation funds, as well as specialist fund managers, platform operators, financial advice firms, stockbrokers, and other financial intermediaries in Australia and overseas.

The views expressed in our submission are ours alone and do not necessarily reflect the views of our clients.

MinterEllison has previously made submissions to Treasury in relation to the Quality of Advice Review (**QAR**), in which we supported the key proposals of the QAR and made some suggestions for further reforms which we would regard as complementary to those proposed in the QAR.

1. Recommendation 7

1.1 With respect to the proposed changes in Part 1 of Schedule 1 of the Draft Bill which are intended to implement Recommendation 7 from the QAR Report, in our view the proposed changes do not adequately implement the changes recommended or address the specific concerns set out in the QAR Report.

1.2 Recommendation 7 was that 'superannuation trustees should be able to pay a fee from a member's superannuation account to an adviser for personal advice provided to the member about the member's interest in the fund on the direction of the member'.

Issue 1: Amendments do not address the sole purpose test

1.3 As an initial comment, recommendation 7 is based on the premise that fees should only be payable from a member's superannuation account for advice that is:

(a) provided to a member (and not, for example, advice provided to a member and the member's spouse); and

(b) limited to advice that is wholly or partly about the member's interest in the fund.

[redacted]

1.4 The restrictions above are apparently intended to reflect the limitations inherent in the 'sole purpose test' in section 62(1) of the *Superannuation Industry (Supervision) Act 1993* (**SIS Act**). The Draft Bill does not, however, amend the sole purpose test and yet as pointed out in the QAR Report, it is difficult to know the extent to which the payment of advice fees as contemplated in section 99FA is consistent with that test[1].

1.5 This section requires the trustee to maintain a regulated superannuation fund 'solely' for 'the provision of benefits' for or in respect of members at retirement, death, reaching a certain age, termination of employment, or cessation of work due to ill-health. In our view, the current section 62(1) is inconsistent with the general legislative policy that superannuation monies should be available for payment of certain personal advice fees and creates uncertainty, particularly as the payment of advice fees are, at best, only indirectly related to the payment of benefits to members.

1.6 While APRA has the power to approve the provision of other benefits as "ancillary benefits", it has not used this power to provide greater certainty in this area.

1.7 APRA issued regulatory guidance in 2001 in the form of Superannuation Circular No. III.A.4, which contained some commentary about APRA's view of the relationship between the sole purpose test and use of fund assets to pay for advice services. This commentary illustrates the difficulty in drawing a bright line between when (in APRA's view) financial planning services may be paid for from fund assets and when they cannot.

1.8 It is apparent from the Circular that APRA envisaged a situation where a trustee made arrangements to provide financial advice services and did not contemplate payment for services sourced independently by members.

1.9 Unfortunately, APRA recently announced that its guidance on the sole purpose test would be retired, leaving trustees without guidance on this topic. The Draft Bill does not address this void because it does not make any amendments to the sole purpose test to clarify the position. In our view, in order for the law reform to operate as intended, section 62 should be amended to:

(a) clarify that advice fees may be paid from members' accounts;

(b) set appropriate boundaries for these arrangements. Importantly, the boundaries should be clear and simply to administer.

1.10 The limits contemplated by the Draft Bill are problematic because:

(a) while we note that the drafting contemplates that advice may be given that is 'wholly ***or partly***' about the member's interest in the fund, the only amount that can be paid from the member's account will be the amount representing the cost of providing advice **about the member's interest in the fund**;

(b) financial planners typically would not provide advice that is so limited in scope. A financial planner would likely seek to provide more holistic advice, in which case, it may be impractical or artificial to seek to apportion fees based on the extent to which the advice relates to a member's interest in a particular fund;

(c) in our view, it is poor policy to incentivise advisers to provide such limited scope advice to their clients – if a client does not have the funds to pay for such advice outside of super, why should they not also obtain advice on broader topics such as whether this particular fund is suitable for their needs?; and

(d) at a practical level, we consider it places an unduly onerous obligation on trustees if the regulators expect them to check that in every case, the fees the member is seeking to have deducted represent fees payable only for advice which is limited to advice about the

[1] "*Most trustees have formed the view that providing advice about members' interests in the fund is consistent with the sole purpose test. I do not disagree. However, I do note the question has never been considered by a court and so the precise scope of what is a proper use of fund resources … is uncertain*." (page 111 of the QAR Report):

member's interest in the fund. This is in our view an example of the kind of red tape that adds cost, with no corresponding benefit, to our regulatory framework.

1.11 We consider that the limit should instead be expressed far more simply as a dollar amount or percentage of the account balance, significantly reducing the "red tape" burden on superannuation trustees. Limitations of this kind would be far simpler to monitor and should also provide flexibility for one member of a couple to use their superannuation account balance to fund advice given to both members of the couple.

1.12 To address these concerns, a new subsection could be added to section 62 to give trustees greater certainty that the payment of advice fees for personal advice given to members would not contravene the sole purpose test. For instance:

(4) A trustee of a regulated superannuation fund does not contravene subsection (1) if the trustee pays an amount from the fund at the request or direction of a member in respect of the costs of financial product advice that is personal advice obtained by the member (or by the member and the member's spouse) subject to any restrictions specified in Regulations made for this purpose.

1.13 Regulations could be made placing limits of the kind discussed above on the amounts that can be deducted from time to time.

Issue 2: Amendments do not empower trustees – rather, they are framed as a prohibition with exceptions

1.14 In the QAR Report, the rationale for recommendation 7 is that trustees should be given permission to pay such fees and that the SIS Act should authorise a trustee to pay advice fees (including ongoing advice fees) at a member's direction. The QAR Report recommends that the direction work in the same way as the way the SIS Act authorises a trustee to act on an investment direction or binding death benefit nomination given by a member.

1.15 The SIS Act authorises trustees to act on these kinds of directions and nominations through exceptions to the general restrictions in section 58(1) and section 59(1), which generally prohibit the governing rules of a superannuation fund from either permitting a trustee to be subject to direction in the exercise of its powers (section 58(1)) or permitting a discretion under the rules from being exercisable by a person other than a trustee of the fund (section 59(1)).

1.16 The main ways in which the SIS Act authorises a trustee to act on an investment direction or binding death benefit nomination are as follows (we note other provisions are relevant):

(a) section 58(2)(d) allows a trustee to be subject to a direction given by a beneficiary to take up, dispose of or alter the amount invested in an investment option, subject to regulation 4.02A of the *Superannuation Industry (Supervision) Regulations 1994* (Cth) (**SIS Regulations**); and

(b) section 59(1A) allows the governing rules (subject to conditions in the regulations) to permit a member to require the trustee, by notice (in accordance with the regulations), to provide benefits in respect of the member on or after the member's death to a legal personal representative, dependent or dependants of the member specified in the notice.

1.17 Our understanding of recommendation 7 is that a **further exception to the restriction** in section 58(1) should be inserted into section 58(2), so that the governing rules of a superannuation fund could provide that a member may give a direction to the trustee to pay for personal advice provided to the member concerning their interest in the fund. Currently, the SIS Act prohibits the governing rules of a fund from allowing a member to give such a direction to the trustee. The proposed amendments do not address this issue.

1.18 As an example, a new subsection 58(2)(h) of the SIS Act could provide:

58 Trustee not to be subject to direction

(1) Subject to subsection (2), the governing rules of a superannuation entity other than a superannuation fund with no more than 6 members or an excluded approved deposit fund

must not permit a trustee to be subject, in the exercise of any of the trustee's powers under those rules, to direction by any other person.

(2) Subsection (1) does not apply to:

…

(h) a direction given by a member of a regulated superannuation fund that the trustee pay an amount, to be deducted from the member's interest in the fund, in respect of the costs of personal financial product advice obtained by the member (or by the member and the member's spouse) and subject to any restrictions specified in Regulations made for this purpose.

1.19 Section 963B(1)(ba)(ii) in Part 4 of Schedule 1 of in the Draft Bill would then need to be amended accordingly.

1.20 While proposed section 99FA(5)[2] may have been intended to authorise a trustee to pay such a fee, it does not, in our view, achieve this result because it has no application, by its express terms, to the trustee's compliance with the fund's governing rules or other legislation including taxation legislation. Instead, it contains a statutory prohibition against charging fees against a member's interest in the fund, subject to an exception corresponding to the limited circumstances in which fees should be allowed to be paid from a member's superannuation account.

Issue 3: Scope of exemption provided in proposed section 99FA

1.21 In addition to our more fundamental comments above, we have a number of more specific concerns about the provisions of proposed new section 99FA.

1.22 As mentioned above, we consider it impractical for an assessment to have to be made as to the portion of fees charged by a financial planner which represent the cost of providing advice **about the member's interest in the fund**. It is unclear whether the trustee will be permitted to rely on an allocation determined by the adviser or will have to make its own assessment of the cost of providing advice about the member's interest in the fund. Use of the word "cost" implies that the trustee will be required to consider not only what the invoice, on its face, discloses as the fee for that service but rather, what such advice should reasonably cost. If so, this would be an onerous requirement.

1.23 We also query the prescriptive requirements for client consent set out in section 99FA(1)(c). In other circumstances where members may give directions (such as in relation to choosing investment strategies) there is no prescribed form for evidencing the direction. In particular, we question the appropriateness of requiring clients to sign a 'written' consent and the associated record-keeping requirements. The *Electronic Transactions Act 1999* (Cth) does not apply to this part of the SIS Act and therefore would not apply to a consent given for the purposes of section 99F(1)(e). It therefore appears that clients would be required to physically sign the consent and other means of clearly indicating their consent, e.g. by confirming it in an email, would not appear to be available.

1.24 It appears that the proposed section 99FA(5) is only relevant to SIS Regulation 5.02(a) which allows the trustee to determine direct costs of establishing, operating and terminating the fund to be charged against a member's benefits. This characterisation does not seem to be appropriate since these costs are member-specific and should simply be charged to the member directly rather than being subject to a regulated cost allocation process across the entire fund of the kind contemplated in SIS Regulation 5.02.

2. Recommendations 8 and 10

2.1 Subject to the following comments, we support the proposed changes to implement Recommendations 8 and 10 in Parts 2 and 3 of Schedule 1 of the Draft Bill:

[2]This subsection deems the cost of the advice to be a direct cost of operating the fund but only for the purposes of the SIS Act and regulations.

(a) We query the appropriateness of requiring clients to 'sign' the consent to an ongoing fee arrangement (**OFA**) in proposed sections 962E(1)(c) and 962T(d). Section 110A of the Corporations Act relating to technology neutral signing does not apply to Chapter 7 of the Corporations Act and therefore do not apply to OFA consents. It therefore appears that clients would be required to physically sign the consent and other means of clearly indicating their consent, e.g. by confirming it in an email, would not appear to be available.

(b) We note that the Minister will have the power to approve consent forms in proposed section 962Y. The Explanatory Memorandum states that an approved form is not mandatory but could be relied on as evidence of consent (paragraphs 1.82 and 1.83). However, there is nothing to this effect in the proposed provisions themselves. This should be made clear in the legislation.

(c) The Draft Bill provides that the transition period for implementing the new consent requirements will be six months (proposed Part 10.76). In our view, this period is too short. The proposed changes will require licensees to implement system changes and implement appropriate compliance and training arrangements. We believe a 12 month transition period would be more appropriate.

3. Recommendations 13.1 to 13.5

3.1 Subject to the following comments, we support the proposed changes to implement these Recommendations in Part 4 of Schedule 1 of the Draft Bill:

(a) The proposal to move the exemptions in sections 963B(1)(d) and 963C(1)(e) of the Corporations Act into the definition of conflicted remuneration in proposed section 963A is appropriate if the exemptions are fully captured by the change. However, they are not. The exemption for fees relating to the issue or sale of a financial product (i.e. product fees) is not carried over into the proposed changes to section 963A. This could have the effect of preventing product issuers from providing any advice relating to their own products to the extent that any such advice could potentially be influenced by product fees charged by the issuer.

We acknowledge that the QAR Report recommended repealing the exemptions in sections 963B(1)(d)(i) and 963C(1)(e)(i). However, this was on the basis that they would be redundant if the change in Recommendation 13.1 is made. This recommendation was not as limited as the proposed change to 963A and we therefore submit that the exemptions in sections 963B(1)(d)(i) and 963C(1)(e)(i) are still required and should be included in proposed section 963A(1)(b).

(b) While most of the changes in Part 4 of Schedule 1 of the Draft Bill are technical in nature and do not therefore require a transition period, the removal of the exemptions in section 963D for Australian ADIs may have a significant impact. We therefore submit there should be an appropriate period to allow ADIs to adjust to the removal of this exemption. We suggest that this should be at least 12 months.

4. Recommendations 13.7 to 13.9

4.1 Subject to the following comments, we support the proposed changes to implement these Recommendations in Part 5 of Schedule 1 of the Draft Bill:

(a) Proposed section 963BB(3) provides a necessary exemption for business transfers. However, proposed section 963BB(3)(a) only seems to contemplate transfers of businesses to a licensee and does not allow for a transfer of business from one representative to another (whether of the same licensee or not). We submit that proposed sections 963BB(3)(a) and (b) should be amended as follows:

*(a) the original licensee's financial product advice business is sold or transferred to another financial services licensee (the **new licensee**) or another representative of a financial services licensee (also the **new licensee**); and*

(b) *the new recipient is the new ~~that other financial services~~ licensee ~~or a representative of that other financial services licensee~~.*

(b) We note that the transition period for implementing measures to obtain client consent to receipt of commissions is only three months. We do not believe that this is long enough to implement system changes and appropriate compliance and training measures. We submit the transition period should be at least 12 months.

Yours faithfully
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Annexure A: Extracts from APRA Superannuation Circular No. III.A.4

41. It is open to trustees to develop features of their fund which add value to, or differentiate it from, other funds. For example, fund sponsored member awareness, education and financial advice programs, targeted at fund specific issues such as benefit features (including insurance options, the making of binding death benefit nominations etc) or investment choices offered in the fund, may be appropriate. However, fund sponsored programs, including financial planning services, which are targeted at broader, non-superannuation savings and investment opportunities, products or services, such as investment or tax advice and health insurance, are inappropriate. 42. As a guiding principle, there should always be a reasonable, direct and transparent connection between a particular scheme feature or trustee action, and the core or ancillary purposes. The more tenuous the linkage between a service or activity and the retirement savings objective, the greater will be the difficulty in the fund meeting the sole purpose test.

42 ….

Financial planning service

43. Financial planning is now a service which many trustees are considering offering to members. As noted in paragraph 41, if the service is aimed only at a member's interest in the fund, such services would generally fall within the sole purpose test. If, however, broader advice is offered, it would be inappropriate for the cost to be borne by the fund. Trustees wishing to make such broad services available to members may wish to consider other means of funding the service. These means might include, for example, arranging alliances with providers that involve no cost to the fund or, as noted in paragraph 39, the trustee itself (or other service providers) paying for the services without increasing the costs charged to the fund in respect of such extended purposes. This might appropriately be done, for example, from the trustee's discretionary expenditure of moneys received from a trustee fee it charges to the fund.

44. Even where the service relates solely to the options available to members within the fund such as insurance, investment choice, additional voluntary contributions and roll-overs, the trustee would be expected to negotiate arrangements where members are not required to pay fees regardless of their wish to use such services. Where the costs are charged to the members’ balances in the fund, trustees must ensure that the services relate exclusively to fund matters.