financial services law bulletin

september 2007

Ebsworth & Ebsworth LAWYERS

PRUDENTIAL REGULATION

DOFI regulation affects foreign and domestic insurers

On 13 September the Financial Sector Legislation Amendment (Discretionary Mutual Funds and Direct Offshore Foreign Insurers) Bill 2007 was passed by Parliament. The Act implements the reforms to the regulation of discretionary mutual funds and DOFIs announced on 3 May 2007. The reforms will commence on 1 July 2008.

Proposed reforms and timing

The Australian Prudential Regulation Authority (APRA) intends to release Prudential Standards revised to cater for DOFIs in early 2008 so DOFIs that need to become authorised can apply in advance of the 1 July 2008 start date. On 31 July 2007, APRA released a discussion paper on 'Refinements to the General Insurance Prudential Framework' outlining the proposed amendments. Exemptions to the requirement to be authorised have not yet been developed. Treasury is preparing a consultation paper on how it proposes to determine these exemptions. This paper is scheduled to be released in September.

Responses to the APRA discussion paper are due by 28 September 2007. The 11 September date has been extended to provide an overlap in the discussion periods for the two papers.

Overview of proposed reforms

The key changes to be introduced by the Act in relation to DOFIs are:

- the existing definition of 'insurance business' in the *Insurance Act 1973* (Cth) will be expanded and clarified with the result that more DOFIs will be caught and required to be authorised if they are to continue providing insurance in Australia;
- certain exemptions to the definition and therefore the requirement for authorisation will be promulgated;
- offshore reinsurers will not be required to be authorised but may choose to be as an indirect result of prudential requirements with which domestic insurers must comply.

Expanded definition of 'insurance business'

The activities targeted by the reforms are those leading up to and including undertaking liability under an insurance contract. The current definition of 'insurance business' will be expanded so that the following conduct will be caught:

- inducing others to enter into insurance contracts;
- publishing or distributing a statement relating to a person's willingness to enter into an insurance contract; and
- procuring the publication or distribution of such a statement.

continued on page 2 >

in this issue

introduction

Kathryn Rigney
Partner

Welcome to the latest issue of our *Financial Services Law Bulletin*. As we go to press, the DOFI legislation (see main article) has just been passed. The impact of the legislation and other regulatory developments are covered in this issue.

Partner Ann Newbrun will also review the new legislation at the International Bar Association Annual Conference in Singapore in October, in her discussion on 'Effective regulation in an increasingly globalised marketplace: Continuing reform of regulation of the Australian insurance market'.

DOFI regulation affects foreign & domestic insurers > from page 1

Any conduct listed above that is done outside Australia will be taken to occur in Australia to the extent that it has, or is likely to have, its effect in Australia. Insurers acting through an agent, broker or other intermediary will be caught where their conduct amounts to carrying on insurance business.

Exemptions

The exemptions will likely include:

- insureds who fulfil the 'big end of town' criteria; and
- risks that cannot be placed with an authorised insurer.

The challenge will be in developing the scope and application of these exemptions.

Authorisation of DOFIs

In order to become authorised, DOFIs must meet the regulatory requirements contained in the Prudential Standards, such as maintaining minimum capital, maintaining the required assets in Australia and appointing a local agent. They will be subject to ongoing compliance and reporting requirements and payment of levies. APRA's application fee for authorisation is currently $68,200. The Act contains some transitional provisions. DOFIs that are caught will also need to consider whether to become registered with ASIC under the Corporations Act.

Prohibition on brokers, agents and other intermediaries

Agents and brokers will be prohibited from placing insurance with unauthorised DOFIs (if an exemption does not apply) as there will be a prohibition on financial services licensees, and their authorised representatives, dealing with unauthorised DOFIs. Companies will be able to be appointed as local agents; they will need to fulfil the criteria required by the Insurance Act and Prudential Standards.

DMFs

The Act introduces a regime for the collection of information on DMFs, which will be complemented by enhanced disclosure requirements under the Corporations Regulations.

Implications for reinsurance

Reinsurance business will be excluded and reinsurers will not be subject to regulation under the Insurance Act unless they choose to be authorised.

However, APRA is proposing to apply higher investment risk charges to reinsurance recoverables from foreign reinsurers than those from APRA-authorised reinsurers. This will mean that Australian domestic insurers may have to reconsider their use of foreign reinsurers. APRA is also recognising reinsurance recoverables as part of an insurer's capital base where the recoverables have been outstanding for less than 12 months. However, where they have been outstanding for more than 12 months, they will only be recognised if they are due from an APRA-authorised reinsurer or are otherwise supported by assets in Australia.

Finally, APRA will emphasise that the total amount of premium an insurer may cede to reinsurers is not expected to exceed 60% of gross written premium.

Modified Prudential Standards

As part of the reforms, APRA will modify the Prudential Standards to take account of the risk profiles of different categories of authorised insurers. The proposals in APRA's discussion paper apply to insurers currently authorised by APRA, as well as to those that will be authorised in the future when the changes to the Insurance Act become effective.

APRA proposes to introduce five categories of insurer. By introducing these categories, APRA will provide a greater degree of certainty to regulated entities regarding the regulatory burden they will face, which it is hoped will make ongoing compliance more efficient, and also encourage foreign insurers who may have previously been reluctant to enter the Australian market to apply for authorisation.

Categories and some proposals are:

- Category A: Locally incorporated insurer – the main changes proposed are those in relation to reinsurance cessions (which also apply to other categories);
- Category B: Wholly owned subsidiary of a local or foreign insurance group – strategic plans prepared on a group basis will be accepted and Australian subsidiaries of foreign insurance groups will be allowed to use a group actuary who is not an Australian resident;
- Category C: Foreign insurer operating as a foreign branch – the 'assets in Australia' requirements will be more flexible regarding the use of a trust structure to hold these assets, and fit and proper requirements will apply to corporate agents;
- Category D: Association captive – the total amount of premium ceded to reinsurers is not expected to exceed 90% of gross written premium; and
- Category E: Sole parent captive – in addition to the 90% rule, APRA will lower the floor for the calculated risk-based minimum capital requirement from $5 million to $2 million. The expected buffer will increase from 20% to 50% when the insurer's minimum capital requirement is less than $5 million.

APRA's enforcement powers

To ensure that the regime can be effectively enforced, the Act includes additional enforcement powers to enable APRA to investigate persons it believes are carrying on insurance business without being authorised and those persons aiding, abetting, counselling or procuring such activity. These investigative powers include powers to access the premises of a person and to gather information from persons APRA is investigating.

continued on page 3 >

DOFI regulation affects foreign & domestic insurers > from page 2

Implications for the Australian general insurance market

The regulation has many implications for all parts of the Australian general insurance market. The main uncertainty is the extent of the exemptions. Insureds, Australian authorised insurers, DOFIs and intermediaries will all be interested in the proposed exemptions. Accordingly, not all implications can be determined, but some likely implications are:

DOFIs will need to consider whether their conduct falls within the new definition of insurance business and, if so, whether:

- they can vary their business practices so they are not caught; or
- an exemption will apply.

When Treasury releases the exemption consultation paper, DOFIs and their intermediaries should consider whether their business falls within the scope of any exemption. DOFIs should consider making a submission in response to the paper if:

- the exemptions do not apply to their business and they believe it should; or
- they are unsure if an exemption applies to their business.

DOFIs that are captured by the reforms will have to consider carefully the initial cost of applying for authorisation and ongoing cost of complying with the Prudential Standards and whether they should make a submission to APRA in respect of the proposed Prudential Standards.

Preparing for and applying for authorisation is a lengthy process, so must be planned well in advance of the start date of the reforms. The costs involved mean that there should be some consideration about whether to continue providing insurance in Australia.

Intermediaries will need to update their systems to identify authorised or exempt insurers to ensure they do not breach the prohibition by dealing with an insurer that does not fulfil these criteria. If they intend to act as a corporate agent, they will need to ensure they meet the applicable requirements.

Insureds who insure with a DOFI and wish to continue this arrangement will need to consider whether they fall within an exemption or whether the DOFI will become authorised.

Authorised insurers will need to examine their reinsurance arrangements and, when the exemptions consultation paper is released, evaluate those exemptions.

Reinsurers will need to analyse the implications for their business of the proposed changes to investment risk charges on reinsurance recoverables and capital recognition of reinsurance recoverables older than 12 months.

Ann Newbrun Partner
e: anewbrun@ebsworth.com.au

Isla Chisholm Lawyer
e: ichisholm@ebsworth.com.au

☐ CORPORATE GOVERNANCE

ASX revised corporate governance rules

The Australian Securities Exchange (ASX) Corporate Governance Council released the Revised Corporate Governance Principles and Recommendations on 2 August 2007. The revised principles were released following a public consultation process between November 2006 and February 2007.

Background

Eric Mayne, Chairman of the Council and Chief Supervision Officer for ASX, noted this is the first revision of the Council's corporate governance principles since they were released in March 2003. Mr Mayne said that 'this is testimony to the durability of Australia's flexible, principles-based approach to corporate governance'.

The Council received more than 100 public submissions, which overall showed strong support for the principles and the 'if not, why not' approach to corporate governance disclosure, and agreement that there should be no exemption from the principles for small and medium-sized entities.

In relation to sustainability and corporate social responsibility (CSR), many submissions to the Council indicated that any new regulation in this area should avoid constraining the ability of companies to adopt approaches that best suit their circumstances and the needs and interests of their investors and stakeholders, and should not restrict their ability to comment on other aspects and objectives of their sustainability or CSR activities. The Council is of the view that sustainability or CSR issues are best reflected in the 'mainstream' of corporate governance activities, that is, through strengthened risk management processes and reporting.

Key changes

- The term 'best practice' has been removed from the document in order to eliminate any perception that the

continued on page 4 >

ASX revised corporate governance rules > from page 3

principles are prescriptive, and so as not to discourage companies from adopting alternative practices and 'if not, why not' reporting where appropriate.

- The number of principles has been reduced and the principles have been amalgamated to make them more user friendly.

- Principle 2 now sets out a list of relationships affecting independent status rather than a definition of independence and a company should take these into consideration when determining the independence of a director. If a company considers a director to be independent notwithstanding the existence of such a relationship, the company should disclose the reasons why they regard the director as independent.

- The Council recommends that companies' trading policies should prohibit hedging unvested options, and that any hedging or vested options should be disclosed under Principle 3 (Promote ethical and responsible decision-making).

- Principle 7 (Recognise and manage risk) has been amended to clarify that material business risks involve both financial and non-financial risks. Companies are encouraged to adopt appropriate risk oversight, management policies and internal control systems rather than disclosing specific material business risks.

- Recommendation 9.4, which recommended that companies ensure that payment of equity-based executive remuneration is made in accordance with thresholds, has been deleted, and instead commentary has been added to Recommendation 8.2 suggesting companies may wish to consult shareholders about equity-based incentive plans involving the issue of new shares to executives, other than directors, prior to implementing them.

Implementation

The Revised Principles will become effective for a listed entity on their first financial year commencing on or after 1 January 2008. The disclosure dates will vary according to the financial year of the entity.

Commentary

At the launch of the Revised Principles, the Hon Chris Pearce, Parliamentary Secretary to the Treasurer, stated that 'the Government's approach to improving corporate governance in Australian companies is to steer well away from imposing arbitrary "black letter rules" that prescribe detailed governance practices that companies must adopt. We believe that a better – and far more workable – approach to corporate governance is to facilitate private and voluntary transactions between market participants'.

Mr Pearce also said that these Revised Principles complement the Government's efforts to reduce the regulatory burden on business and improve the quality of disclosure. He pointed out that the ASX's most recent compliance report demonstrated that 90% of listed companies met their reporting requirements, and that the ASX has worked hard to improve this compliance result and continues to engage with, and provide guidance to, those entities where a need is identified.

The Revised Principles have been welcomed by the peak professional body for governance professionals, Chartered Secretaries Australia, which noted that the update has strengthened and supported sensible outcomes for both business and investors.

The Principles have also been well received by the Australian Institute of Company Directors, which said they are a distinct improvement for company directors and now provide Australia with a governance framework that is well suited to the current business environment, shifting the focus from a 'tick-the-box' to one of effective governance.

Implications

Corporate governance continues to be important for both the public and private sectors, making the Revised Principles of interest to unlisted entities, even though they apply only to listed entities.

Their release provides an opportunity for every entity to review its own governance process and ensure that it best serves the requirements of the entity and the board.

Kathryn Rigney Partner
e: krigney@ebsworth.com.au

Isla Chisholm Lawyer
e: ichisholm@ebsworth.com.au

If you need help reviewing your business governance process, please contact a member of our Financial Services Team.

☐ PROFESSIONAL INDEMNITY

Compensation and insurance arrangements for AFS licensees

Section 912B of the *Corporations Act 2001* requires AFS licensees that provide financial services to retail clients to have compensation arrangements in place. These arrangements must be approved by the Australian Securities & Investments Commission (ASIC) or satisfy the requirements set out in the Regulations. In 2002, ASIC 'turned off' the requirement to comply with section 912B as a result of various factors, although there were some transitional compensation arrangements. This is now changing.

A new Corporations Regulation (7.6.02AAA) modifying the requirements of section 912B commenced on 1 July 2007. In late July, ASIC released a consultation paper setting out how ASIC proposes to administer the new compensation requirements and seeking feedback from interested parties.

The new requirements

The Regulation requires most AFS licensees to have 'adequate' professional indemnity (PI) insurance. The Regulation makes the licensee responsible for assessing what is adequate PI insurance, but provides that regard must be given to:

- the licensee's membership of an external dispute resolution scheme; and
- relevant considerations in relation to the financial services business carried on by the licensee, including the volume of business, the number and kind of clients, the kind of business and the number of representatives of the licensee.

Licensees with an AFS licence commencing before 1 January 2008 must have insurance in place by 1 July 2008. New licensees (commencing on or after 1 January 2008) must meet the compensation requirements from the date their licence commences.

Exemptions

The Regulation provides that certain licensees are exempt from the compensation requirements. This applies to general insurance companies, life insurance companies and authorised deposit-taking institutions regulated by the Australian Prudential Regulation Authority (APRA). Licensees related to these APRA-regulated entities are also exempt where they have a guarantee from the APRA-regulated entity that has been approved by ASIC. ASIC proposes to approve guarantees only where they provide no less protection than adequate PI insurance cover.

Basic policy principles

ASIC states that its Policy Objective is to maximise the potential of the compensation requirements to reduce the risk that a retail client's losses cannot be compensated by the licensee due to a lack of financial resources. The following principles will guide ASIC's administration of the compensation requirements:

- the primary way for licensees to comply with the compensation requirements will be to have adequate PI insurance;
- the PI insurance must substantially deliver the Policy Objective;
- the standard of 'adequate PI insurance cover' will be the benchmark for ASIC approval of any alternative arrangements to PI insurance; and
- it is the basic responsibility of each licensee to determine what arrangements are 'adequate' in their circumstances.

What is adequate PI insurance?

Whether a PI insurance policy is adequate depends on three factors: the amount of the cover, the scope of the cover and whether the terms, conditions and exclusions of the cover undermine the overall effect.

ASIC proposes that a licensee's PI insurance policy should have a per claim limit at least as high as the maximum limit that applies to their external dispute resolution (EDR) scheme(s), and that minimum aggregate cover should be assessed on a sliding scale, starting at a minimum of $2 million cover where revenue from retail services is up to $1 million. For insurance brokers, ASIC proposes that maintaining the aggregate amount of cover required under the superseded *Insurance (Agents and Brokers) Act 1984* will be adequate.

ASIC proposes that the Policy Objective and the legislation require the following

continued on page 7 >

☐ PRUDENTIAL REGULATION

APRA's disqualification powers

The recent increase in the number of disqualifications of directors and senior managers by the Australian Prudential Regulation Authority (APRA) serves as a reminder of one of APRA's key enforcement powers.

Consistent with their mission to establish and enforce prudential standards, APRA has the power to disqualify an individual from holding prudentially significant roles within the Australian authorised deposit-taking, general insurance, life insurance (only in relation to approved auditors and appointed actuaries) and superannuation industries.

APRA's power in relation to each industry relies on a different piece of legislation. Whilst this article focuses on **general insurance**, the process and grounds for disqualification are similar in the authorised deposit-taking and superannuation industries, with APRA looking at the fitness and propriety of individuals. APRA's powers in the life insurance industry are limited to declaring an individual not eligible for appointment as a life company's actuary if the person has failed to adequately perform functions and duties under the *Life Insurance Act 1995*, or not approving a person as an auditor of life companies if satisfied that the person does not have sufficient experience.

The *Insurance Act 1973* makes it an offence for a disqualified person to be, or act as, a director or senior manager of a general insurer or authorised non-operating holding company (NOHC), or as a senior manager or agent of a foreign general insurer.

Under section 25 of the Act, an individual automatically becomes a disqualified person if they are convicted of certain offences (including dishonest conduct or conduct relating to a financial sector company), or if they become bankrupt.

When a director or senior manager of a general insurer comes to APRA's attention for lack of fitness or propriety, section 25(1)(f) of the Act provides that an individual may be disqualified by APRA pursuant to section 25A. Section 25A(1) provides that APRA may disqualify a person if it is satisfied that the person is not a fit and proper person.

Process

If concerns are raised about the fitness and propriety of a director or senior manager, APRA will undertake a preliminary internal assessment of the individual's alleged conduct. If APRA is satisfied that a sound preliminary case has been made for disqualification, it invites the individual to 'show cause' as to why they should not be disqualified. The individual will be provided with the material on which APRA based its preliminary assessment. In most instances, the individual's response to the show cause letter will be by written submission.

After the individual's submissions have been considered, and if disqualification is still considered appropriate, a recommendation is made to the APRA delegated decision-maker. Disqualifications are administrative decisions made on a 'balance of probabilities' basis by APRA delegates (and not by APRA staff). If the APRA delegate's decision is to disqualify, APRA advises the individual of the reasons.

Normally, a notice of the disqualification will be published, a record of the disqualification will be entered on the register and, where appropriate, APRA will inform other regulators and professional associations. The register only records individuals disqualified by APRA pursuant to section 25A, and not those that are automatically disqualified.

Appeals

The appeal processes available to disqualified individuals are:

- Within 21 days of the APRA delegate's decision, the disqualified individual may request that a second APRA delegate reconsider the decision. The disqualified individual may make further submissions and the second delegate has 21 days to decide.
- The disqualified individual may apply to the Administrative Appeals Tribunal (AAT) for a review of the decision within 28 days of confirmation (or variation) of the original decision by the second delegate.
- The disqualified individual can apply to the Federal Court at any time under the *Administrative Decision (Judicial Review) Act 1977*.

Of the 109 individuals on the disqualification register, eight have AAT reviews pending and a further two have had an AAT stay granted on the disqualification (pending a full hearing).

Insurance Act examples

From 27 September 2004 to 29 August 2007, 32 disqualifications pursuant to section 25A were recorded on the disqualification register. Of note is that 2007 has seen an increase in the number of disqualifications, with two more being registered to the end of August than for all of 2006.

As an example of the determinative factors APRA looks at when making a decision to disqualify a director or senior manager, APRA recently concluded that an individual was not fit and proper in circumstances where the individual:

- was aware of the purpose and effect of a transaction that resulted in the company's profits being overstated, with the effect that the company appeared to meet the regulatory solvency requirement when it did not;
- knowingly facilitated the transaction; and
- misled the Board and auditors regarding the effect of the transaction.

Major investigations

APRA has disqualified six former Zurich Australia Insurance Limited (ZAIL)

continued on page 7 >

APRA's disqualification powers > from page 6

executives following investigations into improper financial reinsurance transactions undertaken in 2000. APRA reported that its investigation into ZAIL has concluded.

As at June 2007, APRA had disqualified 26 individuals in connection with HIH (five of whom are currently subject to AAT appeal). APRA's investigation into HIH has not concluded however, and a further three individuals are still subject to assessment.

In 2007 APRA concluded its investigation into a set of improper financial reinsurance transactions entered into by General Reinsurance Australia Limited between 1997 and 2001. In total, APRA disqualified six individuals based on their positions with the General Reinsurance group of reinsurers.

Legislative amendments

As we go to press, a Bill amending the process outlined above is before the House of Representatives. If passed, the changes will introduce a court-based process for disqualifying individuals. APRA will no longer have a 'direct' disqualification power and will instead have to make an application to the Federal Court. This will place a higher burden of proof on APRA.

The Bill addresses concerns about inconsistencies between APRA-determined disqualification and the court-based disqualification regime under the *Corporations Act 2001*.

Conclusion

The majority of recent APRA disqualifications pursuant to section 25A of the Act have come out of historical activities related to financial reinsurance transactions or the HIH collapse. Although these particular investigations are either finished or coming to an end, APRA will continue to exercise its powers to disqualify directors and senior managers of regulated entities when it determines that they are not fit and proper. We will update this article if the proposed amendments are enacted.

Mark Kimberley Senior Associate
e: mkimberley@ebsworth.com.au

Mark Fairlie Graduate at Law
e: mfairlie@ebsworth.com.au

compensation and insurance arrangements for AFS licensees > from page 5

as key features of an adequate PI insurance policy:

- it must cover loss or damage suffered by retail clients because of breaches of Chapter 7 of the Corporations Act;
- it must cover breaches by both the licensee and its representatives;
- it must be available to cover compensation awards made by the EDR to which the licensee belongs; and
- as far as possible it must continue to provide cover for a period of time after the licensee ceases business (e.g. run-off cover).

Inadequate PI insurance

Where a licensee is considering a 'partially adequate' policy, ASIC proposes that they should identify and estimate their exposure to uninsured claims and ensure that their cash flow is sufficient to cover this exposure.

Issues

The ability of PI insurance to put licensees in funds to meet claims will be limited by what the insurance market is prepared to provide. Currently there are no policies explicitly based on the obligation for AFS licensees to hold PI insurance.

ASIC recognises that PI insurance policies covering all consumer losses falling within the scope of the obligations might not be available to all licensees. As an example, many current PI insurance policies do not cover losses caused by advice provided by a licensee's representatives about products that are not on the licensee's approved product list.

Conclusion

Comments on the Consultation Paper were due by 14 September 2007. ASIC will issue a formal Regulatory Guide in November 2007.

Kathryn Rigney Partner
e: krigney@ebsworth.com.au

Mark Fairlie Graduate at Law
e: mfairlie@ebsworth.com.au

☐ FINANCIAL PLANNING REGULATION

Recent regulatory developments impacting financial planning networks

A number of changes are on the horizon that dealer groups should be aware of. The Australian Securities & Investments Commission (ASIC) has made proposals to amend Regulatory Guide 146 (former Policy Statement 146), which sets out ASIC's policy on training standards for financial product advisers. The purpose of the amendment is to facilitate flexible and cost-effective training for financial product advisers while maintaining suitable training standards.

The review of Regulatory Guide 146 (RG 146) is occurring in line with the federal government's Corporate and Financial Services Regulation Review, and as part of ASIC's practice of regularly reviewing its guidance material. The proposals focus on possible changes to RG 146 to address:

- the issues raised in the Corporate and Financial Services Regulation Review that training may, at times, not be appropriate for services provided, and RG 146 may not adequately recognise prior study and training; and
- concerns about the standard of courses, as raised by industry groups in discussions with ASIC.

Importantly, ASIC has indicated that it does not propose to fundamentally rethink the policy framework in RG 146 as part of the current review. The proposals are contained in ASIC Consultation Paper 88. Submissions can be made until 25 September 2007, and a revised RG 146 is expected to be released in December 2007.

A review which may ultimately result in more substantial change is the report by the Parliamentary Joint Committee on Corporations & Financial Services, tabled in August 2007, recommending that Treasury undertake a comprehensive review of the laws and regulations governing superannuation to identify how they may be rationalised and simplified. A number of issues were reviewed by the Committee including remuneration models for financial advice.

On the topic of commissions and shelf fees, the Committee commented that:

> *...it would be premature to recommend the prohibition of commissions as recommended by industry funds. The financial planning industry appears to be shifting towards a fee-for-service model and superannuation funds themselves are moving to facilitate the use of member accounts to pay for up front advice. These are welcome trends...*
>
> *...the Committee has concerns about shelf fees. As the industry is progressively moving from commission-based to fee-based advice fees, so it should move from shelf fees to a more competitive means of meeting the cost of product listings. The ultimate ideal for the industry would be movement towards fees for advice, payment for funds management and payment for administrative services...*
>
> *In the meantime the Committee is of the view that the key issue is transparency and disclosure.*

Among others, the following Committee recommendations were made on this topic:

- that ASIC work with industry to provide investors with more effective and detailed disclosure of shelf fees;
- that the Government investigate the most effective way to develop with industry appropriate nomenclature where the product recommendation advice available to consumers is limited by sales imperatives; and
- that ASIC release a policy statement mandating that financial advisers disclose the ownership structure of their licensee when making a superannuation product recommendation.

In this issue of our Bulletin (page 5) we also report on ASIC's proposals for administering the new compensation and professional indemnity insurance requirements which apply to licensees who provide financial services to retail clients (commencing 1 July 2008 for existing licensees).

Brian Thomas Partner
e: bthomas@ebsworth.com.au

Emily Kuo Senior Associate
e: ekuo@ebsworth.com.au

Our Financial Services Team will continue to monitor and report on how the regulatory environment develops in relation to financial planning networks.

☐ CORPORATIONS REGULATIONS

Shorter SOAs and PDSs now a possibility

Recent amendments to the Corporations Regulations 2001 refine the disclosure requirements for Statements of Advice and Product Disclosure Statements to allow certain information to be incorporated by reference.

The issue

When dealing with retail clients, licensees, authorised representatives and product issuers are required to provide various disclosure documents.

The *Corporations Act 2001* prescribes content requirements for these disclosure documents and regulated entities must ensure that each document they produce satisfies those requirements.

Complying with the content requirements can lead to information being repeated, and a client may receive the same information more than once. For example, a financial planner may produce numerous Statements of Advice (SOAs) for a client over the course of their relationship. Until recently, the content requirements of the Act caused repetition of some information across multiple SOAs.

Another example is where a client has received information about the product from a source other than a Product Disclosure Statement (PDS). In this case, the Act also required the entity to provide the information in a disclosure document, despite the client already having the information in another form. To address this problem of repetitive disclosure, the Government has implemented incorporation by reference.

Changes to SOAs

Regulation 7.7.09B allows a providing entity to incorporate information ordinarily in the SOA by reference to a statement or information that has previously been provided to the client. The SOA must:

- refer to the statement or information;
- provide sufficient details about the statement or information to enable the client to identify and locate it and decide whether they should read or obtain it; and
- state that the financial adviser must provide the statement or information on request and free of charge.

Not all information can be incorporated by reference. Clients must still be warned if advice is based on incomplete or inaccurate information. In circumstances where a financial adviser recommends the replacement of one product with another, the Act requires that information regarding charges and benefits be provided to the client.

Changes to PDSs

Regulation 7.9.15DA allows a responsible person to decide not to include certain information in a PDS if the information is publicly available in writing elsewhere, such as on the internet. The PDS must:

- refer to the other statement or information;
- state that a copy of the statement or information may be obtained at no charge from the responsible person on request; and
- give sufficient details about the statement or information to enable a person to identify and locate the statement or information and decide whether or not to read or obtain a copy of the statement or information.

However, certain core information must still be included in the PDS. This includes:

- a summary description of the purpose, key features and key risks of the product;
- the name and contact details of the issuer of the financial product;
- the fees and costs template and the Consumer Advisory Warning for investment products;
- information about the dispute resolution system that covers complaints by holders of the product; and
- information about any cooling-off regime for acquisitions of the product.

Implications

The Government's objective in addressing this issue was to reduce repetitive disclosure in SOAs and PDSs in order to reduce costs to business and provide clearer disclosure to consumers.

Kathryn Rigney Partner
e: krigney@ebsworth.com.au

Mark Fairlie Graduate at Law
e: mfairlie@ebsworth.com.au

Corporations legislation amendment

Certain provisions of the *Corporations Legislation Amendment (Simpler Regulatory System) Act 2007* have been proclaimed to come into effect on 1 September 2007.

The provisions that are to come into effect include those in the 'small business guide' of the Corporations Act relating to notifications to ASIC regarding officeholders of proprietary companies limited by shares and advertising restrictions for certain fundraising.

For all of the amendments see the Federal Register of Legislative Instruments (F2007L02629) and the Corporations Legislation.

NEWS IN BRIEF

Second tranche of AML/CTF reforms

The Attorney-General's Department has released the draft second tranche of Anti-Money Laundering and Counter-Terrorism Financing reforms. The second tranche of reforms amend the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* by adding new 'designated services' in section 6 of that Act. These new 'designated services' extend the application of the AML/CTF Act's regulatory obligations to particular transactions undertaken by real estate agents, precious stones and precious metal dealers, and particular legal, accounting, trust and company services. The Attorney-General's Department called for public submissions by 7 September 2007 (for further details see the Attorney-General's website).

In related news, AUSTRAC has released two sets of draft rules under the AML/CTF Act. These are revised rules regarding details required to be reported for threshold transactions to AUSTRAC, and requirements of ongoing customer due diligence. The draft rules can be accessed on the AUSTRAC website.

(Sources: Attorney-General's Department; AUSTRAC)

Super report

The Parliamentary Joint Committee on Corporations and Financial Services has released its inquiry into the structure and operation of the *Superannuation Industry (Supervision) Act 1993* and the superannuation industry. It made 31 recommendations in order to deal with the complexities and inefficiencies in the current laws and regulations.

The report covered a wide variety of issues including those related to the overall regulatory framework, promotional advertising and third party transactions, the safeguarding of superannuation savings, member investment choice and self-managed superannuation funds. The recommendations included:

- that APRA should release its legal advice on the role of the trustee in a member investment situation and to further consult with industry to clarify the role of a trustee in this situation;
- that the Government create a mandatory unit pricing methodology for all public offer superannuation funds and that APRA implement improved operational risk parameters in relation to this;
- that ASIC should give guidance to superannuation funds regarding communication with fund members which does not require a statement of advice; and
- that the Australian Tax Office raise the maximum number of trustees for any one self-managed superannuation fund from four to 10.

(Source: Parliamentary Joint Committee on Corporations and Financial Services, The Structure and Operation of the Superannuation Industry)

Consolidated group reporting for general insurers

APRA has released a Discussion Paper on 'Consolidated Group Reporting for General Insurers' (dated 31 August 2007) for public consultation with submissions due by 12 October 2007. The paper proposes that APRA will provide consolidated supervision to level 2 insurance groups, that is, the ultimate APRA-regulated parent insurance entity and its insurance subsidiaries including any controlled entities that are integral to the general insurance business in Australia.

Level 2 insurance group consolidated supervision aims to ensure that the relevant insurance group complies with its capital adequacy requirements and is financially sound, whilst reducing the compliance burden on the group. The paper proposes less detailed financial reporting than that required for individual APRA-authorised insurers (level 1 insurers) including submission of fewer forms.

Later this year APRA intends to release a paper on draft prudential and reporting standards for general insurance groups covering capital adequacy, risk management, outsourcing, business continuity and reinsurance management.

Veena Srianandarajah Lawyer
e: vsrianandarajah@ebsworth.com.au

Angela George Paralegal
e: ageorge@ebsworth.com.au

For more information, please contact us:

Philip Battye Partner	e: **pbattye@ebsworth.com.au**	t: **61 3 8602 1009**
Peter Daley Partner	e: **pdaley@ebsworth.com.au**	t: **61 7 3303 8812**
Ian Enright Partner	e: **ienright@ebsworth.com.au**	t: **61 2 9234 2302**
Peter MacKenzie Partner	e: **pmackenzie@ebsworth.com.au**	t: **61 2 9234 2591**
Ann Newbrun Partner	e: **anewbrun@ebsworth.com.au**	t: **61 2 9234 2533**
Kathryn Rigney Partner	e: **krigney@ebsworth.com.au**	t: **61 2 9234 2279**
Brian Thomas Partner	e: **bthomas@ebsworth.com.au**	t: **61 2 9234 2592**

sydney melbourne brisbane