Investment & Financial Services Association Ltd
ACN 080 744 163

4 July 2008

Financial Services and Credit Reform Green Paper
Corporations and Financial Services Division
Treasury
Langton Crescent
PARKES ACT 2600

Via email: financialservicesgreenpaper@treasury.gov.au

Dear Sir/Madam,

FINANCIAL SERVICES AND CREDIT REFORM GREEN PAPER

IFSA welcomes the opportunity to make submissions in response to the Governments Green Paper on Financial Services and Credit Reform which is aimed at improving, simplifying and standardising financial services and credit regulation.

IFSA is a national not-for-profit organisation which represents the retail and wholesale funds management, superannuation and life insurance industries. IFSA has over 140 members who are responsible for investing over $1 trillion on behalf of more than ten million Australians. Members' compliance with IFSA Standards and Guidance Notes ensures the promotion of industry best practice.

IFSA's comments in response to the Green Paper are limited to the proposals on:

1. Mortgages, Mortgage Broking and Non-Deposit Taking Institutions;
2. Trustee Corporations;
3. Margin Lending; and
4. Debentures.

1. Mortgages, Mortgage Broking and Non-Deposit Taking Institutions

Those IFSA members with a direct or indirect involvement or exposure to mortgage broking have indicated support for the establishment of a single licensing regime for mortgage broking practitioners and mortgage broking activity being brought within Chapter 7 of the Corporations Act 2001. For any proposed change to the regulation for mortgage brokers and mortgage broking activity regard should be had to streamlining the transition process and ensuring that it is as seamless and cost efficient as possible.

Regulation through a suitable Commonwealth Government body operating in unison with existing industry bodies would serve to improve the consumer protection, enhance the integrity and efficiency of the mortgage broking market through greater disclosure and monitoring of industry practice, and remove current inconsistencies across jurisdictional boundaries.

2. Trustee Corporations

IFSA welcomes the agreement reached at the recent Commonwealth Heads of Government (**COAG**) meeting which paves the way for the Commonwealth to assume responsibility for the

regulation of trustees.

IFSA agrees that the existing regulatory framework places an unnecessary burden on trustee corporations given the inconsistencies in the current fragmented regulatory framework. A single licensing regime for trustee corporations should, in our view, promote a more competitive market place removing barriers that prevent trustees from operating nationally.

In relation to the two options proposed in the Green Paper, IFSA endorses Option 1. A regulatory framework focussed on investor/consumer protection and supervised by ASIC would prove, in our opinion, be more appropriate for the following reasons:

- ASIC's regulatory focus is on investor/consumer protection and business efficiency;
- ASIC's regulation of managed investment scheme responsible entities (trustees) is quasi prudential in so far as a responsible entity is required to:
    - satisfy certain capital requirements for capacity and operational purposes;
    - adopt particular compliance and governance structures; and
    - is clearly focussed on the best interests of fund (trust) members;
- a number of synergies could be realised if trustee licensing was based on the existing financial services licensing framework; and
- ASIC oversees disclosure documentation.

IFSA members are currently subject to regulatory oversight from both ASIC and APRA and consider that prudential regulation, whilst effective in ensuring stability within the economy at an industry and entity level, is not ideally suited to consumer protection. Trustee corporations that offer superannuation products will continue to be regulated by APRA in respect of their superannuation business.

Other improvements which could be made to the regulation of trustee corporations include:

- allowing trustee corporations standing to be appointed solely as administrators;
- deregulating fees charged by trustee corporations and removing any statutory caps;
- distinguishing fees from expenses definitionally would be of benefit;
- defining the operation of Common Funds and their relationship with managed investment schemes; and
- allowing trustee corporations to invest in their own investment products or related party products provided appropriate disclosure is made and sufficient controls are in place to safeguard the best interests of investors/consumers.

3. Margin Lending

Margin lending is a long established practice available to investors. Where used as part of an investment strategy margin loans can provide various advantages and consequent benefits to investors. However, utilising a margin loan facility is, like any investment, not without its risks.

IFSA is, subject to a proper cost benefit analysis, broadly supportive of measures that enhance transparency and disclosure of activities involved in the provision of financial services. The second option outlined in the Green Paper involving the inclusion of margin loans as financial products for the purposes of Chapter 7 of the Corporations Act 2001 requires, in our view, a much more detailed analysis of the costs and benefits as well as margin loan facility structures. Certainly, from a whole of industry perspective, we would discourage a knee jerk reaction to the Opes-Prime and Lift Capital failures. Neither is representative of the mainstream providers.

Over regulation in this area will simply increase costs with minimal benefit to investors. Light touch regulation and a focus on consumer eduction is we believe a viable option. We note the concerns raised in the Green Paper in relation to retail clients' understanding of how their margin loan facility operates. A range of publications and information is available to retail clients including IFSA's margin lending fact sheet, entitled '*The nuts and bolts of gearing*',

developed in 2007 (**Attachment A**). That publication is publicly available at:

http://www.ifsa.com.au/documents/Fact%20Sheet_Managed%20Funds_nuts%20and%20bolts.pdf

Recent issues and margin lending: Director and Executive trading

Where directors have substantial shareholdings or trade in a company's securities, the market expects that they will disclose such activity as currently required under the Corporations Act 2001, both upon their initial appointment and on an ongoing basis. We note that the ASX has recently referred a significant number of possible breaches relating to insider trading, continuous disclosure rules and market manipulation to ASIC for investigation. We also note that ASIC has released Regulatory Guide 193: *Notification of directors' interests in securities – listed companies*, clarifying how directors of listed companies should comply with the disclosure requirements mentioned above. This appears to be primarily an enforcement issue.

We reaffirm the joint IFSA and Australian Council of Superannuation Investors statement (28 March 2008) that companies should have defined policies on directors and senior executives trading and exposures in their company's securities (**Attachment B**). The company policy should set out:

1. the rules applying to directors or senior executives entering into margin loans over the company's stock;
2. the requirements for such loans to be made known to the company; and
3. the policy of the company towards the disclosure of such loans to the market where the holdings and/or exposures are material.

The company policy should be disclosed to shareholders.

4. Debentures

The decision of the Court of Appeal of the Western Australian Supreme Court in a ruling that promissory notes issued by Westpoint's Emu Brewery were not debentures under the control of the Corporations Act 2001, has highlighted the need for legislative action and clarification of the law where public capital raising activities to retail investors are conducted.

Paragraph (d) of the definition of debenture in the section 9 of the Corporations Act does not include "an undertaking to pay money under a promissory note that has a face value of at least $50,000". Clearly, this definition needs to be amended and the threshold brought into line with the current scheme of regulation under the Corporations Act for capital raising activities directed at retail investors.

As is indicated in the 2004 decision of the West Australian Supreme Court, the legislative intention of paragraphs (a) to (f) of the definition of debenture in section 9 of the Corporations Act is "to exclude banking and other commercial transactions involving dealings in debt of a sort for which the protective provisions in Chapter 6D (requiring disclosure documents) and Chapter 2L (requiring a trust deed and a trustee) are not required : see Ford et al, Ford's Principles of Corporations Law, Butterworths, Sydney, 1995. While Government has made huge advances in ensuring that Australian laws both facilitate business activity and ensures that retail investors are appropriately protected, the exclusion at paragraph (d) from the definition of debenture in section 9 of the Corporations Act appears to be one of those pockets missed in the modernising of our laws.

We would be pleased to further discuss any aspect of this submission and provide additional clarification if necessary.

Yours sincerely

David O'Reilly,
Policy Director - Regulation

Level 24, 44 Market Street, Sydney NSW 2000 Ph: 61 2 9299 3022
Email: ifsa@ifsa.com.au Fax: 61 2 9299 3198