

Newsletter

December 2010

Short form PDS

In June 2010, new Product Disclosure Statement (PDS) requirements came into effect (Corporations Amendment (No. 5) Regulations 2010)¹. The regulations require shorter and simpler PDS's for:

- superannuation products
- simple managed investment schemes, and
- standard margin lending facilities.

The key features of the regulations include²:

1. a maximum page length of 8 pages (for superannuation and managed investment scheme PDSs) and 4 pages (for margin loan PDSs), together with a prescribed minimum font size
2. prescribed section headings to make it easier for consumers to find important information in the PDS and compare across products
3. key content requirements to ensure that consumers are provided with the key information they need to make an investment decision
4. provision for other material to be located outside the PDS document itself, but form part of the PDS through incorporation by reference, and
5. provision for inclusion of additional information within the PDS, provided the prescribed length is not exceeded.

If you are subject to the new regulations then you need to consider the insurance implications - specifically item 4 (underlined) needs consideration.

In some cases, policy coverage hinges off the documents disclosed at renewal and/or specifically listed in the policy. If this is the case for your insurance, then you need to ensure that any additional information (located outside of the PDS) is included as part of your disclosure to Insurers. In some cases it may even be necessary to amend the policy document to accommodate information/material located outside the PDS document, but forming part of the PDS through incorporation by reference.

This is not a big issue at all and is easily checked/fixed. However, like many things, it's often the simplest little matter which causes a problem down the track if left unattended.

¹ Effective for Margin Lenders by 1 Jan 2011; new PDS/Supps by 22 June 2011; all products by 22 June 2012.

² ASIC Information Sheet 133

Consultation Paper 140 – Responsible Entities: Financial Requirements.

Prepared by Terry Dalziel

ASIC has now closed submissions for the above consultation paper. The aspects considered within the paper were:

- restricting guarantees and indemnities granted by Responsible Entities;
- requiring Responsible Entities to create rolling 12-month cash flow projections;
- increasing the net tangible asset capital (NTA) requirements for Responsible Entities; and
- specifying cash composition in the NTA/liquidity requirements for Responsible Entities.

Currently the financial conditions relating to Responsible Entities(RE) are contained in RG 166 Licensing: Financial Requirements.

The proposals are aimed at providing a structured approach to dealing with both expected and unexpected risks across a 12-month forecast period. The proposals in the Consultation Paper would replace the cash needs requirement in RG166.22(c). The other base level financial requirements in RG166.22(a), (b) and (d) would remain unchanged

What is proposed?

Guarantees and Indemnities

Restrict guarantees and indemnities to related parties to maximise the likelihood that a responsible entity will survive the insolvency of a parent or related entity.

Cash flow projections

That responsible entities be required to prepare, and make available to ASIC upon request, rolling cash flow forecasts with anticipated revenue and expenses over at least 12 months in a “business as usual” situation, to be approved by the directors of the responsible entity. Whilst acknowledging that forecasts such as these are only as sound as the assumptions on which they are based and the rigour with which they are prepared. For this reason, we think it is important for directors of a responsible entity to review them.

Currently a RE prepares the cash flow projection, based on the projection of cash flows and on an individual or in certain cases group basis, that it will have access to enough financial resources to meet its liabilities over the projected term of at least the next 3 months, including any additional liabilities that may be incurred during this time.

The requirement applicable for cash flow projections is a negative assurance on the reasonableness of assumptions used and positive assurance on their calculation. It is ASIC's intention to maintain this approach to the audit requirements with the proposed change.

Net Tangible Asset Requirement

ASIC is proposing two alternatives to the NTA calculation (see comment below as to the form to be held in).

1. the greater of: \$150,000; 0.5% of the average value of scheme property (capped at \$5 million); and 10% of its average gross revenue (with no maximum); or
2. 10% of its average gross revenue with a minimum of \$500,000 and no maximum;

If the average gross revenue of a responsible entity is below a minimum percentage of the average value of scheme property, that a minimum percentage, set at between 1 and 2%, be used to calculate the required NTA. Eligible undertakings that may be included in the NTA calculation be limited to those provided by an ADI or which are otherwise approved by ASIC.

Current requirements outlined in RG166.63 are for a RE to hold a minimum NTA of 0.5% of the value of the assets plus any other scheme property not counted in calculating the value of the assets of the registered schemes it operates, with a minimum requirement of \$50,000 and a maximum requirement of \$5 million.

ASIC provides the following table as to possible impact on NTA as to what is required:

	Funds under Management (\$'000)	Revenue (\$'000)	NTA Requirement (\$'000)		
			Current RG 166.25	Proposal 1	Proposal 2
Example A	50,000	500	250	250	500
Example B	500,000	5,000	2,500	2,500	500
Example C	1,000,000	60,000	5,000	6,000	6,000
Example D	5,000,000	50,000	5,000	5,000	5,000

The amount of funds under management and NTA held by a RE is to be submitted to ASIC annually.

A responsible entity that does not use an external custodian will continue to be required to hold \$5 million NTA, subject to existing exemptions for tier \$500,000 assets and special custody assets.

Components of NTA

It is proposed that 50% of the required NTA is to be held in cash or cash equivalents with a minimum of \$150,000

Period of implementation

For existing REs either

1. 12 months until 1 July 2012; or
2. 24 months until 1 July 2013

Commentary

There is likely to be a change in the current financial conditions that RE's will need to meet. There will be a transitional period for this to occur. It is possible that some aspects proposed will have a shorter transitional period than others; e.g. cash flow projection obligations v NTA. You will need to consider the matters in the consultation paper and how the alternatives impact on the financial resources. ASIC could be expected to finalise its position in the new year.

The above has been prepared by Terry Dalziel who you can contact on 03 9381 4516 if you wish to discuss its contents. Terry provides compliance advice to persons operating in the financial services markets and personal risk minimisation strategies (as an Authorised Representative) to protect a business, individuals and their families should unplanned events occur - providing you with greater control; less risk.