



"CORPORATE CITIZENSHIP"

A NEWSLETTER OF
THE AUSTRALIAN COUNCIL OF SUPERANNUATION INVESTORS

TREASURY RELEASES DRAFT REGULATIONS ON SRI

On 22 December 2001, the Department of Treasury released draft regulations relating to the Financial Services Reform Act ("FSRA"). While Funds should ensure that they are properly apprised of all issues referred to in the draft regulations, this newsletter briefly outlines recent developments arising out of the socially responsible investment ("SRI") provisions in the FSRA. Treasury has also requested that any feedback on these proposed regulations be submitted to them by 31 January 2002.

The FSRA provisions set out what needs to be contained in a product disclosure statement *"if the product has an investment component – the extent to which environmental, social, ethical considerations or labour standards are taken into account in the selection, retention or realisation of an investment"*.

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The FSRA also states that the *"Australian Securities and Investment Commission ("ASIC") may develop guidelines that must be complied with where a Product Disclosure Statement makes any claim that environmental, social, ethical considerations or labour standards are taken into account in the selection, retention or realisation of an investment"*.

DRAFT TREASURY REGULATIONS

Outlined below is a brief commentary on the exposure draft of the *second* stage FSR regulations.

The proposed Treasury regulation 7.9.14A outlines the obligation for issuers of products with an investment component, to disclose the extent to which labour standards or environmental, social or ethical considerations are taken into account in the selection, retention or realisation of an investment.

Onus On Product Issuers To Select Considerations Taken Into Account

The proposed regulation seeks to clarify that it is for the particular product issuer to select the considerations that it wishes to take into account in investment decision-making, and to then disclose against those considerations.

Product issuers will need to consider which, if any, of those considerations they regard as 'environmental, social or ethical considerations'.

They will also need to consider whether they will be regarding any standards taken into account in the selection, retention or realisation of an investment as 'labour standards'.

This approach emphasises that it is for each product issuer to determine those considerations, if any, that they will be regarding as 'environmental, social or ethical considerations'; and to then determine which of those matters will be factored into their investment decision-making processes.

It will ensure that product issuers have the flexibility to consider the **widest range of matters** that could be considered to be labour standards or environmental, social and ethical considerations; and to then determine which of those matters will be factored into their investment decision-making processes.

Where Socially Responsible Considerations Are Not Taken Into Account

Proposed regulation 7.9.14A clarifies that the obligation to disclose 'the extent to which' socially responsible considerations are taken into account, includes an obligation to disclose if these

matters are not taken into account at all.

Treasury has sought feedback from product issuers on whether this requirement is needed to ensure that product issuers disclose if they taken these matters into account 'to no extent', or whether the test in paragraph 1013D(1)(1) is sufficient for this purpose.

Where Socially Responsible Considerations Are Taken Into Account

Where a product issuer does claim to incorporate socially responsible considerations into their investment decision-making processes, two further disclosure obligations will apply.

First, a product issuer will need to outline in their Product Disclosure Statement (PDS) those matters that they will be considering as labour standards or environmental, social or ethical considerations when it comes to making decisions about the investment.

Second, a product issuer will need to provide an explanation of the extent to which those matters are taken into account in the selection, retention or realisation of an investment. This is intended to provide retail clients with an outline of the extent to which the considerations selected by a product issuer fed into an impact on the process of making decisions about the investment.

The disclosure of information under these two requirements is governed by the test in subsection 1013D(1) relating to the main requirements of the Product Disclosure Statement content. Under these provisions product issuers are obliged to disclose information only to the extent that a person would reasonably require for the purpose of making a decision, as a retail client, whether to acquire the financial product.

In the context of the SRI issues, Treasury does not consider it necessary to further elaborate upon the level of disclosure of methodologies underpinning the SRI considerations. Treasury takes the view that competitive and marketing pressures across product issuers will further drive the disclosure of SRI on these matters.

ASIC Guidelines

As mentioned earlier, addition to the regulation-making powers, the Australian Securities and Investments Commission (ASIC) may develop compulsory guidelines where a PDS claims that labour standards or environmental, social or ethical considerations are taken into account in the selection, retention or realisation of the investment (section 1013DA).

Treasury is seeking feedback on whether the regulations should require product issuers to include a statement in their PDSs that ASIC has developed guidelines in this area, if any guidelines are developed. The purpose of this disclosure would be to bring the existence of the guidelines to the attention of retail clients.

A further issue would be whether the regulations should then require product issuers to include a positive statement that the information disclosed in their PDS about socially responsible investment considerations has been disclosed in compliance with ASIC's guidelines.

Product issuers, who did not comply with ASIC's guidelines, would potentially be liable for including a misleading or deceptive statement in a PDS under Division 7 of Part 7.9 of the Corporations Act. However, Treasury acknowledges that compliance could be difficult to determine, for example, if any guidance took the form of industry best practice and was intended to be voluntary. A regulation in this area would also potentially require product issuers to update or

supplement their PDSs after any guidelines were developed or changed by ASIC.

In summarising Treasury is seeking comment on:

- (a) Whether it is necessary to clarify that the requirement to disclose "the extent to which" socially responsible considerations are taken into account includes a requirement to disclose if these considerations are not taken into account to any extent; and
- (b) Whether the regulations should require product issuers to disclose the existence of any guidelines developed by ASIC and that they have complied with those guidelines.

Because the legislation has been proclaimed to commence on 11 March 2002, Treasury has requested that any submissions be sent by 31 January 2002. Any submission should be sent by email to fsr@treasury.gov.au or by mail to:

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WILL ASIC BE PRODUCING GUIDELINES ABOUT DISCLOSURE OF ETHICAL INVESTING CONSIDERATIONS IN PRODUCT DISCLOSURE STATEMENTS?

According to ASIC, it is presently considering whether they should be issuing Guidelines for the purposes of 1013DA at this point in time and, if so, what they should contain. To gain a better understanding of the issues involved, and the views of interested stakeholders, they have been participating in consultation processes managed by Environment

Australia about the new financial reporting requirements. These processes have involved industry, government, academics and a wide range of peak national associations.

There doesn't appear to be any indication that ASIC has conferred with any industrial relations bodies such as the ACTU, trade unions and employer associations etc, in relation to dealing with labour standards.

According to ASIC the consultations to date have revealed consensus on two issues:

- (a) first, that there is little support for Government selecting the standards which should be reported against when a product issuer complies with its PDS content requirement in s 1013D(1)(I); and
- (b) secondly, that most organisations would like some additional guidance on the requirements. A number of vehicles for providing this additional guidance have been considered including regulations, ASIC Guidelines, industry self-regulatory initiatives or a combination of these.

ASIC will be considering the contents of the draft Treasury regulations and the results of Treasury's and our own consultations to determine whether or not they should issue Guidelines in the immediate near future or whether they should maintain a close watching brief on how the new requirement is complied with and review the need for Guidelines in the future. Should they decide that

This newsletter is correct to the best of our knowledge and belief at the time of going to press. It is, however, written as a general guide so it is recommended that specific professional advice is sought before any action is taken

there is a need for ASIC Guidelines now, then a more formal consultation process will be established by ASIC.

Any party with particular views on the role ASIC should play in providing guidance on the new ethical disclosure requirements, and the form any such guidance should take, are encouraged to email their comments to ACSI at FSRProjectOffice@asic.gov.au.

At this stage of ASIC's examination of the issue, they appear to agree with the feedback received, that no part of Government should be selecting the standards which labour, environmental, social and ethical considerations should be measured against when making disclosure in a PDS in compliance with s1013D(1)(I).

When the results of Treasury's consultations on its draft regulations have been completed, and the final form of the regulations on disclosure of labour standards or environmental, social and ethical considerations is known, ASIC will

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provide an update of its intentions.