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Provided by email: mfund@asx.com.au
Attention: Andrew Campion

Dear Andy,

FSC Submission to ASX Consultation on the future of the ASX Managed Fund Settlement Service (Consultation)

1. About the Financial Services Council (FSC)

The FSC is a peak body which sets mandatory Standards and develops policy for more than 100 member companies in one of Australia's largest industry sectors, financial services. Our Full Members represent Australia's retail and wholesale funds management businesses, superannuation funds, investment platforms and financial advice licensees. Our Supporting Members represent the professional services firms such as ICT, consulting, accounting, legal, recruitment, actuarial and research houses. The financial services industry is responsible for investing more than $3 trillion on behalf of over 15.6 million Australians. The pool of funds under management is larger than Australia's GDP and the capitalisation of the Australian Securities Exchange (ASX) and is one of the largest pools of managed funds in the world.

2. Introduction

The FSC welcomes the opportunity to provide feedback to the Consultation which seeks industry and stakeholder feedback to assist the ASX with its determination of whether or not mFund should be wound down and closed.

The following outlines key positions and recommendations in the FSC's submission;

- Our preference is that mFund is not closed, given once mFund closes this infrastructure providing greater investor access to unlisted funds will cease, however it is also acknowledged that in its current form mFund is unlikely to play a significant role in fund manager's distribution, product design or manufacturing. A number of system frictions would need to be addressed to facilitate ease of use and enhance the investor experience. This also requires greater broker system integration and wider broker adoption of mFund.
- If the ASX however makes a decision to close mFund, ASX support, including forward planning with stakeholders, is required to facilitate an orderly transition and to help industry to best manage the significant administrative, financial and resource imposition that arises from mFund closure. Member feedback recommends that there be at least a two year transition process from announcement that mFund will close, to enable transition.
- Failure to provide an orderly transition, will result in a poor investor experience which can range from blocked accounts, forced redemptions and lack of investor understanding as to why new application forms and identification material must be provided to issuers for existing investments.

Investors should have adequate advance notice of mFund closure and understanding of what it means for them (most will need to complete a new application form and provide identification documentation to the product issuer to enable the issuer to meet Know Your Client (KYC) and Anti-Money Laundering (AML) obligations). It will also require broker, adviser, issuer and registry co-ordination in relation to any current investor information being shared and all stakeholders working towards to the same time objectives (which will likely require a soft close for no new investors and hard close, for no additional monies, from existing investors) and ASX support to develop a key investor information template to be used by brokers/industry to share minimum investor information.

- We also wish to avoid unnecessary costs that may arise from poor planning, forced redemptions because the mFund closure/transition is perceived to be too difficult for investors/advisers or brokers and avoid reputational damage that all stakeholders risk being exposed to if the investor experience is poor. To this extent, should the ASX proceed with closure of mFund, it will be critically important for the ASX to work with stakeholders to agree the process and timeframe for mFund closure with sufficient advance notice for this to be implemented by all stakeholders with the least disruption wherever possible.

3. mFund challenges and opportunities

With the continued growth of the exchange traded product (ETP) sector in recent years it is acknowledged that ETP offerings are increasingly seen as attractive to investors and that mFund has not received similar levels of investor interest. Feedback received however also notes that mFund provides a unique distribution channel for investment strategies and asset classes that may be better suited to unlisted funds, such as illiquid strategies, than an ETF.

Feedback received from members is that the preference is mFund service to continue and not to be closed down, however it is acknowledged that in its current form it is unlikely to play a significant role in fund manager's distribution.

3.1 mFund potential if challenges addressed

Feedback suggests that mFund take up has likely been inhibited as the underlying system infrastructure and messaging system lacks the requisite level of development, functionality and support to enable ease of use and overall integration. The following challenges have been cited as barriers to, or limitation of mFund, which limits its support and growth potential;

- **mFund message suite separate from other CHESS messages** - mFund uses a different messaging suite ("mFund Messages") to the ones used for settlement of shares and the two messaging suites are not interoperable. From an investor perspective when they update their HIN details via CHESS, this does not result in a corresponding update for their personal information with an mFund (notwithstanding that the investor may have the same HIN for CHESS and the mFund which readily enables investor identification). This means a broker would need to send a separate message via mFund, at an additional cost to the broker and also additional effort. Ease of use, efficiency and cost are factors that can either encourage or discourage use of a product offering such as mFund or ETF. In the case of mFund, feedback suggests that this has impeded support for mFund.
- **Limited broker support and availability of mFund** – Not all large brokers support mFund, with some ceasing to offer mFund due to the introduction of Design and Distribution Obligations (DDO)[1], and

[1] **FAQ on nabtrade website noted the following on why the platform was no longer offering mFund Buy orders:**

for those which offer mFund not all have invested in integrating messaging systems (specifically, those created via the CHESS 10 project for changes of email address, adviser and DRP preference with a number of data fields optional) which has flow on consequences for the investments offered or available to investors. The consequence of optionality, of system integration, critically limits system functionality and utility. It may also adversely impact the investor experience (such that key investor information, such as email addresses, is not commonly able to be updated via mFund messaging). It is also likely that investment in system integration by brokers and other stakeholders, or mFund more generally, may have slowed down following announcements in 2016 that the ASX was exploring CHESS replacement options, given the potential of existing systems becoming redundant pending a prospective replacement system.

- **Poor investor experience** – The inability to update investor information via mFund/the broker, once the investor is in mFund has been cited as a key challenge and source of client complaints. The lack of broker integration with mFund messaging, inhibits the brokers' ability to update client information via mFund messages. This can lead to a poor investor experience, which is likely to discourage adviser, broker and issuer support of mFund. The practical implications of this, may result in the investor having to contact the issuer directly to update their details and given that the issuer has limited information about the investor, the issuer will often need to request the investor provide further identification so that they can verify the identity or signature of the person they are communicating with.

We have received feedback that in its current form, mFund is unlikely to play a significant role in fund manager distribution however feedback also notes that mFund provides a unique channel for offering managed funds (with a wider range of asset classes and investment strategies suited to mFund). If system frictions were addressed and there was wider broker adoption of, and integration with, mFund there are opportunities to grow mFund.

We understand from member engagement with the ASX that a significant level of growth, from current levels, would be required for the commercial viability of mFund. This may be difficult to achieve given existing barriers, including imposition of DDO obligation on brokers and distributors for mFund and overall broker support of mFund. Notwithstanding the commercial barriers, section 3.2 below seeks to highlight what changes would be required to support mFund growth.

3.2 Changes required to support mFund

System challenges, ease of use and improving the broker and customer experience is key to making mFund an attractive distribution channel for the admission unlisted managed funds. Support for, and growth in mFund, requires system changes to remove current frictions for stakeholders.

Changes required include:

- Investing in the mFund messaging system for interoperability with messages used for settlement of shares; to enable investor information to be updated via either mFund or settlement of shares messaging systems for investors with the same HIN. This would remove the need for further broker integration with mFund messages and would reduce system frictions for stakeholders.

"The Government has introduced new Design and Distribution Obligations (DDO) from 5 October 2021 which require (amongst other things): product issuers to make, publish and review a target market determination for financial products i.e. determining who the product is appropriate for; and product distributors (like nabtrade) to take reasonable steps to distribute the financial products within that target audience. As a product distributor, nabtrade is unable to provide target determinations for all ASX mFunds available on the platform or limit distribution to only clients within that target audience. As a result nabtrade will no longer be able to accept mFund Buy orders." See https://www.nabtrade.com.au/products/investments/mfunds#accordion-cea993092a-item-95e9e1a746

- Further broker integration to enable mFund messaging system is key to supporting mFund growth. If interoperability between mFund messages and messages used for settlement of shares is not achieved, there would need to be greater broker integration with mFund messages to ensure brokers have the capability to send all CHESS messages to meet mFund Settlement Service requirements consistent with ASX mFund Settlement Service Guidance.
- Provision of key client information such as email address and mobile phone number should be mandatory not voluntary to enable issuers to contact clients.

Without wider broker support, as well as greater mFund message system integration, mFund growth and reach will be limited.

4. Closure of mFund

As noted above, mFund provide a unique distribution channel for a wide range of asset classes and investment strategies however without further investment and development to remove system frictions and facilitate ease of use, mFund are unlikely to play a significant role issuer distribution, product design and manufacturing strategies.

Should the ASX decide not to further develop and invest in mFund infrastructure and instead close mFund this will impose significant administrative, resource and cost as well as legal obligations on stakeholders ranging from product issuers, brokers/advisers and investors. If this is to be the outcome, ASX support to facilitate transition is key to minimize and best manage the significant administrative, financial and resource imposition arising from mFund closure. Member feedback recommends that there be a two year transition process from announcement that mFund will close, to enable an orderly transition. The following section identifies some of the key implications that arise from closure of mFund including:

- **Cost imposition -** Issuers are likely to incur significant costs associated with the closure of mFund which include costs associated with; each contacting a few hundred up to a few thousand investors and requesting they complete the application form and provide accompanying identity documentation, staffing and resourcing to process application forms and follow up any required information, potential costs associated with third party AML/KYC checks, mailing costs which may need to be issued multiple times to each client, costs associated with updating product disclosure statements as well as any investor education collateral developed to educate investors of the change and what it means to them. Feedback indicates that account set up and work involved with Know Your Client requirements can range from $20 - $30 per account, plus $27 for any ASIC company searches. Advisers and Brokers are also likely to incur their own time and resource costs associated facilitating closure of mFund, providing requisite information/assistance to issuers arising from closure of mFund.
- **Imposition of administrative and legal obligations** – AML and KYC checks for each investor will need to be undertaken again for investors, with this obligation presently sitting with brokers and being imposed on issuers if mFund is closed. As issuers commonly have extremely limited investor information, with more comprehensive information held by the broker, issuers will likely need to ask all investors to complete an application form (with accompanying identity documentation) for the investment the client holds. This is likely to be a significant undertaking, with some issuers having thousands of mFund clients (noting issuers are generally not resourced to undertake onboarding/processing of application forms for hundreds to thousands of investors at any one point in time and will need to resource up to facilitate mFund closure). Given low investor response rates to general investor communication (with feedback citing 5% mFund investor response rate), it is

likely that issuers will need to contact and communicate with investors a number of times to follow up and receive completed application forms to facilitate AML/KYC requirements.
- **Poor investor experience, high administrative burden or high costs could be a redemption catalyst** – if the cost or administrative burden is too high in relation to investor moving from CHESS sponsored to issuer sponsored units – on brokers, advisers or the investor, this may be a catalyst for investor redemptions out of the fund entirely, with capital invested elsewhere. It may be easier for investors to simply redeem than to complete a new application and stay in the investment once mFund closes. There could also be a range of investor impacts ranging from forced redemptions (where the issuer closes the product) or blocked accounts because of AML obligations not having been met.

Should the ASX decide to close mFund it is recommended that the following issues addressed to facilitate closure:

- **Broker and adviser support essential to facilitate mFund closure and provision of essential investor information** – Broker, and where relevant adviser, support is required to: 1. educate the investor of the change, including that they will likely need to complete an application form and provide identification material directly to the issuer; and 2. for the broker to provide essential current investor information to the product issuer to undertake requisite AML/KYC checks. At minimum current contact information is required including - name, current address including email address and mobile/phone number. The ASX should develop a standard form containing minimum level of information which brokers can use to provide this to issuers for ease of administration purposes on an industry wide basis.
- **Low investor response rates and implications for investors –** Given low investor response rates, aside from imposing a greater cost and administrative burden on issuers to follow up clients for required paperwork, there is a key risk that mFund closure will lead to a poor investor experience where the investor does not return the application form necessary for issuers to undertake KYC/AML checks, resulting in an account being blocked and the investor being unable to transact in or out of the fund until this is completed.
- **2 year transition time from decision or announcement that mFund will cease –** sufficient transition time is required for the industry to prepare and undertake requisite work involved with closure of mFund including confirming what the process is for closure of mFund with all stakeholders (such as a soft and a hard close for when there are no new clients, no new investments for existing clients) and providing enough lead time to enable investors to be educated, contacted and for issuers to request investor information and paperwork.

Further information and responses to the specific questions in the consultation paper are outlined below. If you have any questions regarding any of the matters raised in this submission we would be pleased to discuss this further with you.

Kind regards,

Bianca Richardson
Policy Director Investments and Global Markets

Questions for mFund Issuers (Fund Managers/Registries)

Question	**FSC Feedback**
Question 2.2.1: How significant is the role that mFund plays in your distribution and product design and manufacturing strategies?	Feedback received from members is that mFund in their current form do not play a significant role in fund manager's distribution, product design or manufacturing strategies. Without further investment in mFund and system integration it is likely that issuers would look to offer products as ETPs where a product is to be made available through "listed" markets, subject to the investment strategy and asset class being suitable as an ETP. Whilst ETPs are growing, and as noted in the consultation paper, not every unlisted fund is suitable to operate as an ETF, mFund offers a unique channel to enable investment into unlisted funds via a HIN. It is also provides a level of simplicity as the only real issuer to end investor 'Delivery Versus Payment' settlement service in the Australian market for unlisted funds.
Question 2.2.2: Does the increasing popularity of ETPs impact the mFund service's ability to make a meaningful impact on your distribution strategy, resourcing and capabilities?	We have received feedback that ETP offerings are increasingly seen as more attractive to investors than mFund and without further investment and development in mFund some issuers may not intend to offer new mFund investments in the future.
Question 2.2.3: Are there operational advantages or challenges in servicing mFund in comparison to other fund structures such as ETPs, Listed Investment Companies and Trusts (LIC/LITs), or other methods for accessing unlisted managed funds?	An advantage of mFund is that it presents a reasonably streamlined operational model for fund managers, as it operates in the same channel as an unlisted fund compared to other structures. Investors also see mFund as an avenue to use the CHESS HIN as an easy 'platform' to hold managed funds alongside their direct holdings and ETFs. This will be taken away if mFund closes. Feedback on the challenges with mFund has identified the inability of an mFund investor to change their details as one of the biggest challenges. Brokers have not invested in the infrastructure to send the change of details messages required for mFund and the registry has insufficient client details to be able to be sure that an investor requesting the change is the appropriate investor. This has resulted in a poor investor experience and complaints. A big challenge of mFund has also been the limited broker access offering mFund, which may have been influenced by

	announcements of a CHESS replacement system, making brokers reluctant to invest in a system which is planned to be scrapped. Integrating mFund messages with other CHESS messages i.e. not using a separate CHESS messaging suite for mFund could overcome some of these barriers for brokers. Furthermore, mFund does not receive the same treatment as ETFs for DDO purposes with additional distribution obligations imposed on brokers in relation to mFund investments compared to ETFs. As noted earlier in the submission, the introduction of DDO obligations in 2021 has resulted in reduced broker support of mFund and may more generally discourage broker use or support of mFund.
Question 2.2.4: Are you aware of, or do you anticipate, any legal, regulatory, technological or other market trends or changes which could impact the attractiveness of ETPs as opposed to mFund/unlisted managed funds?	Whilst asset classes able to be accessed via ETPs are continuing to expand, a broader range of strategies or asset classes may be suited to mFund compared to ETFs.
Question 2.2.5: Prior to the announcement of this consultation, did you have a significant pipeline of products that would be applying for admission to mFund?	Feedback received to this question is commonly no given the current system limitations. However addressing the barriers to mFund as outlined earlier in this submission could facilitate growth of, and interest in, mFund.
Question 2.2.6: Prior to the announcement of this consultation, did you expect your usage of the mFund service would increase, decrease or remain static over the short to medium term?	Feedback received for this question varies with the expectation on mFund usage ranging from static to an expectation that usage will decrease (based on mFund remaining in its current form). Some have been considering how they would withdraw from the service.
Question 2.2.7: What considerations do you take into account when deciding whether or not to offer interests in eligible managed funds via mFund? Did any specific factors significantly influence a decision not to use the mFund service?	Feedback includes the following considerations; • Client access. • Cost versus revenue earned from investors in the service as well as demand from advisers. One member has noted that they have had no requests from advisers in the past several years for funds to be added to mFund. The lack of demand suggests that the cost benefit isn't there.

Questions for all mFund Stakeholders

Question	FSC Feedback
Question 2.2.24: What is your view on the mFund service and whether ASX should continue to offer it?	Feedback received: The mFund service was a step in the evolution to what is seen as ETPs today. Whilst much of the market has now moved on to other vehicles such as ETPs feedback has noted that this

	may be influenced by current limitations surrounding mFund. Feedback received from members is that the preference is mFund service to continue and not to be closed down, however it is acknowledged that in its current form it is unlikely to play a significant role in fund manager's distribution. Feedback has suggested that the closure of mFund is likely to lead to significant administrative burden and imposition of legal obligations (in relation to KYC/AML obligations). mFund does not receive the same treatment as ETFs for DDO purposes, we are not aware of significant DDO obligations being imposed should mFund close. The ASX should work with brokers, advisers, issuers and other stakeholders to offer a pathway off mFund if the ASX decides to cease this service. See response to Question 3.2.1 for more information.
Question 2.2.25: Is ASX's observation that various industry trends have impacted the original utility for a managed fund settlement service for the Australian market consistent with your experience	Feedback received: Yes. This includes the imposition of DDO obligations on mFund which is likely a key barrier to broker support and take up of mFund. mFund system integration may also be a barrier. ETPs utilise the same messaging suite as what brokers already utilise for settlement of shares, providing a much easier path for distribution. If mFund were to utilise the same messages as settlement of shares then this could facilitate greater support.

Impact to mFund stakeholders if ASX were to close the service
Questions for mFund Issuers (Fund Managers/Registries)

Question	FSC Feedback
Question 3.2.1: What impact do you foresee on your business from the closure of mFund?	The consultation paper notes that AML/KYC forms may need to be completed in respect of converted unit holdings and that investors may need to complete questionnaires to help issuers and product distributors comply with relevant product design and distribution obligations (DDO). It is not clear what additional DDO obligations would apply with the closure of mFund on the basis that the closure of mFund would generally not change an investor's legal rights in a fund. However, we submit the ASX should obtain advice that this is correct.

	The most significant impact arises from the imposition of new KYC/AML obligations on issuers and the corresponding impact this will have on investors, mFund issuers, brokers, and possibly advisers, from an administration, resource and legal perspective. Having mFund investors complete a full application form (and associated identity document requirements) will be problematic for all parties to co-ordinate (issuers only have the investor name and address and generally no other information) - not just investors, particularly where investor response rates to mailouts are traditionally very low. The complexity and administrative burden could be a catalyst for many mFund investors (or their advisers/brokers to recommend this) to simply redeem out of the investment before the service closes. **Impact on an issuer's business** is potentially significant arising from managing any transition admin work involved with KYC/AML and DDO or having mFund investors completing a full application form. Transitioning to direct will be a poor experience for investors who sought simplicity via their HIN. mFund closure could take months as educating and seeking paperwork from investors and conducting AML/KYC will be slow when it needs to be undertaken across hundreds to thousands of investors.
Question 3.2.2: What amount of time do you believe is appropriate for the wind down and closure of the mFund service?	The time required may vary across issuers, based on how many mFund investors need to be contacted (which will also vary across funds and could range from hundreds to thousands). Feedback notes that closure of mFund could take months of investor education, obtaining further information from investors (given issuers often have limited investor information) and updating PDS documentation. Feedback suggests that 2 years would be needed from announcement of closure of mFund to facilitate the requisite work. Importantly, the timeline needs to be consistent across the industry such that brokers, registries and issuers are working towards the same timeframes.
Question 3.2.3: Does Table 1 cover the key milestones that you believe are required to minimise disruption to your business? If not, what else needs to be added?	Feedback is that providing 2 years to achieve the key milestones in Table 1 would be better. Please see also response to Q3.2.2 above.

Question 3.2.4: What (if any) considerations would you like to bring to ASX's attention regarding specific matters that need to be addressed as part of an orderly wind down process (such as unit conversions, income distributions, investor costs, AML/CTF processes, trustee duties, amendments to fund terms, tax implications, coordination in relation to cessation of application processing)?	The key considerations have been outlined at the opening of this submission. This includes; provision of key client information from broker to facilitate transition as well as investor education of the forthcoming change and the need to complete application forms with issuers to facilitate the change. **AML/KYC issue** The number one issue in relation to the potential closure of mFund is AML/KYC obligations. All clients will have been confirmed AML compliant by the broker before establishing their account/HIN. The ASX should facilitate; • a process whereby key client contact information is provided to the issuer; • an investor education campaign to raise investor awareness of mFund closure; and • that this will likely mean investors will need to complete application forms/verify their details with issuers directly **Tax** We are not aware of any tax implications that arise from the closure of mFund and conversion of CHESS sponsored to issuer sponsored units. It is recommended that the ASX obtain advice to confirm this is the case.
Question 3.2.5: Would the closure of mFund necessarily result in the termination and wind-up of a significant number of existing funds?	Feedback on this question may vary across issuers. The FSC has received feedback from some members that it is unlikely to result in termination or wind up of existing funds with mFund clients generally in ordinary classes of units that will continue. However there is a risk that this will be perceived to be administratively difficult for investors which may be a redemption catalyst.
Question 3.2.6: Would the closure of mFund require significant effort and resources to restructure funds to avoid the termination and wind up of funds admitted to the service?	See response to Q3.2.5
Question 3.2.7: Would you be willing to engage with ASX to have products removed from mFund before its closure?	Feedback received from issuers is that if ASX chooses to close mFund, they would be willing to engage with the ASX to have products removed from mFund before its closure. ASX should consider if there are ways in which it could help facilitate a smoother transition of certain mFund to an ETF, where appropriate, including by a reduction in fees for that transition.

Questions for Other Stakeholders

Question	**FSC Feedback**
Question 3.2.17: What observations do you have about the proposed mFund closure?	Our preference is that mFund is not closed, given once mFund closes this infrastructure providing greater investor access to unlisted funds will cease, however it is also acknowledged that in its current form mFund is unlikely to play a significant role in fund manager's distribution, product design or manufacturing challenges. A number of system frictions would need to be addressed to facilitate ease of use and enhance the investor experience. This also requires greater broker system integration and wider broker adoption of mFund. If the ASX however makes a decision to close mFund, ASX support, including forward planning with stakeholders, is required to facilitate an orderly transition and to help industry to best manage the significant administrative, financial and resource imposition that arises from mFund closure. Where there is an existing ETF in place which reflects the same strategy as an mFund, ASX could assist industry by seeking industry tax relief from the ATO for the transfer of investors from mFund to the corresponding ETF, to retain those investors.
Question 3.2.18: What do you think is an appropriate wind-down period for the mFund service	Member feedback recommends that there be at least a two year transition process from announcement that mFund will close, to enable forward planning and an orderly transition.