Hamilton Locke

Contact: Mr Brendan Ivers (Partner)
Mr Erik Setio (Partner)
Email: Brendan.Ivers@hamiltonlocke.com.au
Erik.Setio@hamiltonlocke.com.au
Tel: (02) 8072 8271

29 September 2023

Director
Investment Funds Unit
Retirement, Advice and Investment Division
The Treasury
Langton Crescent
Parkes ACT 2600

By email: misreview@treasury.gov.au

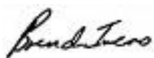
Dear Director

We welcome the opportunity to submit a response to Treasury's consultation paper: "Review of the regulatory framework for managed investment schemes", released in August 2023 (the **Paper**).

The Paper makes several enquiries in relation to the regulatory framework applicable to managed investment schemes under Chapter 5C of the *Corporations Act 2001* (Cth) (the **Act**) and relevant financial services concepts that apply under Chapter 7 of the Act.

Our submission intends to contribute to the development of the law applicable to managed investment schemes under these chapters, drawing on the significant experience of Hamilton Locke's funds and financial services team.

Yours faithfully



Brendan Ivers
Partner
Hamilton Locke

Erik Setio
Partner
Hamilton Locke

Submission Paper

In response to the Consultation Paper for the review of the regulatory framework for managed investment schemes

About Hamilton Locke - Funds and Financial Services

Hamilton Locke is Australia's fastest growing law firm, which is focused on transforming the traditional approach to corporate and commercial legal services. Hamilton Locke is a full service offering corporate law firm, and as a part of the HPX Group, delivers essential corporate services across legal, governance, risk and compliance helping businesses grow and thrive.

Our funds and financial services team specialises in advising responsible entities and promoters of managed funds, platform operators, brokers, custodians, advisors and other stakeholders in the funds management sector. We have established funds across all asset classes and scheme types, including property, equities, fixed income, commodities, private equity, hedge funds, agribusiness, credit and alternative asset schemes.

We are experts at keeping up to date with financial services laws and ASIC, APRA and AUSTRAC regulation. We also act on behalf of our clients in regulatory investigations and enforcement actions. Our approach is to form lasting partnerships with our clients, and we do this by taking the time to understand their business objectives and the drivers of their stakeholders. We have an accessible, easy to work with approach, and pride ourselves on our reputation as being lawyers who get in and get the work done, who are solutions focused and who work seamlessly with the broader team, including other advisers.

Our clients have praised us for our understanding of the specific commercial rationale for an individual transaction, as well as the legal challenges involved. Our excellent project management skills combined with the efficiencies gained from our innovative business structure, our expertise and previous legal experience and our senior bench strength allows us to deliver concise, value for-money advice.

Hamilton Locke

Submission

Chapter 1 – Wholesale client thresholds

Hamilton Locke supports updating the wholesale client thresholds and tests to ensure that the wholesale client classification remains appropriate for the current day. The wholesale client test is used to exclude certain investors (who are defined as wholesale clients under the eligibility tests under ss 761G and 761GA of the Act) from the default consumer protections that apply to retail investors in managed investment schemes. People who do not meet one of the wholesale client tests are provided financial services as retail clients, and are covered by certain consumer protections, such as prescribed disclosure, the application of the product intervention power (**PIP**) and design and design and distribution obligations (**DDO**) regimes, and access to external dispute resolution support through AFCA. The policy rationale for the differential treatment is that wholesale clients are presumed to be "better informed and better able to assess the risks involved in financial transactions" or possess the "means to acquire appropriate advice", and accordingly do not require the same and therefore do not need the same level of protection as retail clients.[1]

The current regulatory settings reflect that retail client protections are not reasonably needed to protect all investors and permit a lighter regulatory burden in such cases. Financial product and service providers may choose to engage with wholesale clients for a variety of reasons including to reduce their compliance costs or to limit the number of clients that they engage with in order to offer more bespoke services or products and offer higher quality engagement with their clients.

We believe that it is important to consider the wider context of consumer regulation that is now available to retail clients, such as the DDO regime, when considering updates or amendments to the wholesale client test. Regulatory changes should strike a balance between consumer protection, supporting the efficient flow of capital, and regulatory simplicity.

Where Treasury implements increases to threshold values in the product value test and/or individual wealth test, there will need to be consideration of how these changes will apply to investors who met the wholesale client test at the time of investment but no longer meet the requisite thresholds and wish to make a further investment. Similarly, the regime will need to account of investors who previously were considered wholesale investors at the time of investment who have been issued partly paid securities and will no longer be considered wholesale clients following the update to these thresholds. The transition period for the wholesale client test is considered in Chapter 2 regarding the scheme registration process.

Should the financial threshold for the product value test be increased? If so, increased to what value and why?

In our opinion, it is appropriate to increase the product value test such that the amount is adjusted for inflation from the date of introduction in 2001. According to the Reserve Bank of Australia's inflation calculator, $500,000 in 2001 would roughly equate to $852,931.32 in 2022.[2]

Treasury's 2011 Wholesale and Retail Clients Future of Financial Advice Options Paper proposed a regular indexation of the amount every five years for the product value test and wealth-based tests. We think that this is an appropriate time frame for the product value test to be reviewed and amended according to CPI. It would be important to consider how amendments to the product value tests would be implemented to account for changing client classifications as outlined above.

Should the financial thresholds for the net assets and/or gross income in the individual wealth test be increased? If so, increased to what value and why?

In accordance with the above, we think that the individual wealth test should be similarly indexed such that the value is adjusted for CPI growth and reviewed every five years. As outlined in the Paper, there has been a significant increase in the number of Australians who meet the individual wealth test to be classified as a wholesale client in comparison to when the threshold was introduced. In addition,

[1] Revised Explanatory Memorandum, Financial Services Reform Bill 2001 (Cth) [2.27], [6.19].
[2] https://www.rba.gov.au/calculator/annualDecimal.html

some areas in Australia have seen significant growth in property prices. Amending the threshold value of the individual wealth test as adjusted for CPI growth ensures a simple and effective means of ensuring that the individual wealth test is met by individuals with sufficient financial knowledge or means to obtain independent financial advice.

Although some assets increase in value beyond CPI growth, we do not believe that there would be meaningful benefit gained by creating complex indexation to account for the real growth of an asset. This is further discussed below in relation to the primary residence.

By increasing the threshold every five years, investors who are required to provide an accountant's certificate every two years would understand the threshold requirement needed to continue to be classified as a wholesale client, and in the event that they do not have sufficient assets, this time frame would ensure that both the licensee and the individual have sufficient time to plan for the person to either divest their interests or cease receiving the financial service.

Should certain assets be excluded when determining an individual's net assets for the purposes of the individual wealth test? If so, which assets and why?

We do not think that certain assets should be excluded from determining an individual's net assets for the purpose of the individual wealth test. Excluding certain assets from the determination of an individual's net assets for the purpose of the individual wealth test would create greater complexity and risk to the process of determining whether a client is a wholesale client. As we have noted, financial services licensees may choose to only engage with wholesale clients to decrease their regulatory costs, which allows smaller businesses to offer financial products or services. Increasing the complexity and therefore risk may impact the viability of smaller financial services licensees.

We understand concerns regarding the inclusion of the primary residence in the calculation of an individual's net assets as increase in residential property value in some areas of Australia does not match CPI growth. However, it would be remiss to assume that residential property prices across Australia will continue to maintain and increase their value in perpetuity. Property prices are influenced by a range of factors from local council planning rules to tax policy and availability of credit. If a person's primary residence was excluded from the net assets test, then Treasury should follow the SEC's approach and not exclude the equity value of the primary residence.

Consent Requirements

Consumer consent may only have limited effectiveness in producing the desired outcomes. Recent research conducted by the Office of the Australian Information Commissioner about consumer consents for Consumer Data Right found that complex consents may reduce engagement due to consent fatigue.[3] Consumer consent is not a guarantee that consumers will have an understanding of what it means to be classified as a wholesale client. The Final Report in the Quality of Advice Review characterises consumers that meet the individual wealth test as meeting it 'automatically'. However, practically, clients who use the individual wealth test are required to provide an accountant's certificate as part of the application process for an interest in a managed investment scheme. This active step requires some level active level of involvement in their investment decision that is not automatic. Consumer consents may provide assistance to some individuals to understand the consequences of being a wholesale client but is unlikely to significantly assist all individuals.

How could these be designed to ensure investors understand the consequences of being considered a wholesale client?

If wholesale client consent was implemented, it is important to ensure that it does not become another leaflet of paperwork that may be easily glossed over in favour of the client spending more time on other matters such as the investment memorandum or application form. Generally, wholesale investors in a managed investment scheme will receive an investment memorandum or other offer document which contains the key details of the fund, and an application form. Investors will need to provide the application form, which will contain their personal details to ensure that they may be verified for AML/CTF purposes as well as an accountant's certificate if the client is relying on the

[3] https://treasury.gov.au/sites/default/files/2023-08/c2023-434434-consent-design-paper.pdf page 7

individual wealth test. The addition of a pro-forma consent form may be considered additional paperwork and may not be sufficiently considered and understood.

Should the same consent requirements be introduced for each wholesale client test (or revised in the case of the sophisticated investor test) in Chapter 7 of the Corporations Act? If not, why not?

If the law is changed to implement a wholesale client consent, the consent requirements should be varied appropriately. For example, it is unlikely that a wholesale client who is a professional investor (as defined in s 9 of the Act) would benefit from a consent form. Similarly, a business that is not a small business would be unlikely to benefit from providing a consent. However, the consent required for an individual relying on the product value test, individual wealth test or sophisticated investor test should be aligned.

Chapter 2 – Suitability of scheme investments

Should conditions be imposed on certain scheme arrangements when offered to retail clients? If so, what conditions and why?

We believe that conditions should not be imposed on the scheme operators that restrict or prohibit them from investing in certain asset types or using particular investment strategies.

The Paper notes that the purpose of such restrictions would be to avoid scheme collapses like the failure of the Sterling Income Trust. However, in our view, the Sterling case involved several serious breaches of existing financial services laws by the relevant parties. Since the Sterling case, ASIC has been granted additional powers under Part 7.8A of the Act (*Design and distribution requirements relating to financial products for retail clients*) which are proving to be an effective gatekeeping mechanism for ensuring investment products are appropriately targeted towards relevant investors. On this basis, we consider that additional regulation is not required in circumstances where compliance with the existing laws would have likely limited the negative consequences that arose in this case.

Further, the Paper refers to limitations that are in force in the UK and US as examples of potential limitations that could be introduced. However, this ignores the structure of the Australian funds management landscape, which involves a high degree of participation from retail investors through self-managed super funds (**SMSFs**). As at 30 June 2022, there were an estimated 603,000 SMSFs representing over 1.123 million members and collectively holding $868.7 billion (26%) of the $3.3 trillion in super assets under management.[4] Any limitation to the types of schemes that retail SMSFs can invest in may prevent these investors from constructing diversified and balanced portfolios.

Are any changes warranted to the procedure for scheme registration? If so, what changes and why?

In our opinion, the current procedures for scheme registration are appropriate as they strike a balance between ensuring retail investors receive the required level of protection while permitting sufficient flexibility in product design to facilitate the efficient movement of capital in keeping with the overall policy design of the financial services regime.

Relevantly, s 601EB sets out the grounds on which ASIC may refuse to register a scheme including that the responsible entity is appropriately structured and licensed pursuant to s 601FA, that the constitution meets the minimum standards required by ss 601GA and 601GB, and that appropriate compliance arrangements are in place as required by ss 601HA, 601HC and 601HG.

For completeness, we note that if the wholesale client test is changed (whether in accordance with Chapter 1 of this Submission or otherwise) such that existing wholesale schemes may need to become registered schemes, sufficient transitional arrangements should be implemented to facilitate the orderly transition. We would welcome further consultation on this point to ensure that the registration process for existing wholesale schemes can be implemented efficiently and over appropriate timeframes so as not to impose overly burdensome administrative requirements on wholesale scheme operators.

What grounds, if any, should ASIC be permitted to refuse to register a scheme?

The Paper asks whether an additional ground of refusal may be required for cases where another law has been breached in relation to the scheme. It specifically identifies where a director of the proposed responsible entity has been disqualified from acting as a director. In our view, this specific issue is more applicable to enquiries into the proposed responsible entity's continued ability to hold an Australian financial services licence (**AFSL**) and is better addressed by ASIC's power to cancel the proposed responsible entity's AFSL under s 915B(3) than through a separate enquiry that exists as part of the scheme registration procedures.

[4] Australian Tax Office, "Self-managed super funds: A statistical overview 2020–2021".

Hamilton Locke

Chapter 3 – Scheme governance and the role of the responsible entity

Are any changes required to the obligations of responsible entities to enhance scheme governance and compliance? If so, what changes and why?

In our opinion, the collective legal obligations of responsible entities are sufficient in promoting a high standard of good governance and compliance. In our view, a responsible entity that is fully compliant with its regulatory obligations and implements ASIC's guidance for best practice and good governance (such as RG 132 Funds management: Compliance and oversight (**RG 132**)) maintains a high level of good governance that facilitates ongoing compliance.

As noted in the Paper, responsible entities, as AFSL holders, are subject to the general obligations under s 912A(1), further obligations under the Act (for example s 601FC), other financial services laws (for example under the *Australian Securities and Investments Commission Act 2001* (Cth)) and the obligations under the registered scheme's constitutions that the responsible entity acts for.

In practice, the effectiveness of a responsible entity to comply with its obligations is dependent on several factors including, resources, competence, leadership and corporate culture. We have observed that a culture of compliance and good corporate governance can be more effective at delivering the desired regulatory outcomes than through the imposition of further legal obligations and even the risk of regulatory action. That is, in our view, increased regulatory requirements and guidance may not have the desired outcome to produce better governance and increased compliance.

Should ASIC be able to direct a responsible entity to amend a scheme's constitution to meet the minimum content requirements, similar to the CCIV regime?

We believe that ASIC should have the power to direct a responsible entity to amend a scheme's constitution in the same way that it can direct a corporate director to amend a CCIV's constitution under s 1223C of the Act.

Currently, ASIC is empowered to deregister schemes that do not have a constitution that complies with the Act. In our opinion there should be a directive powers for ASIC to use as part of its regulatory toolbox in relation to registered schemes with non-compliant constitutions. Accordingly, we recommend an equivalent provision to s 1223C of the Act providing ASIC with the regulatory power to direct a responsible entity to amend a scheme's constitution to meet the minimum requirements under ss 601GA and 601GB.

If ASIC was granted the power to direct responsible entities to amend a scheme's constitution, then s601GC of the Act should also be amended to empower a responsible entity to unilaterally amend a scheme's constitution to comply with a direction from ASIC. This is because , the procedures required for responsible entities under s 601GC of the Act to amend a scheme's constitutions can be time and cost intensive.

As the ultimate end purpose of a constitution for both a CCIV and scheme are to set out of rights and obligations of the corporate director or responsible entity and members, the regulator's powers in regulating the constitutions of both CCIV and scheme should be no different to each other.

Are changes required to the compliance plan provisions to ensure compliance plans are more tailored to individual schemes? If so, what changes and why?

As the Paper points out, the Act does not expressly require compliance plans to be tailored to the specific scheme or mandate items other than those stated in s 601HA. However, the Act states that the compliance plan of a registered scheme must set out "adequate measures" that the responsible entity is to apply in fulfilling its responsibilities to ensure compliance with the Act and the scheme's constitution.

Notwithstanding that there is no express requirement in the Act to tailor a compliance plan, there is the expectation to tailor compliance plans according to the needs of a particular scheme. In our opinion, it is not necessary to amend the legislation to expressly state what is widely understood and accepted.

Further, other than the minimum requirements of s 601HA, responsible entities should continue to be afforded the flexibility to create compliance plans and controls according to their schemes' requirements. Consistent with our recommendation for the first question in Chapter 3, a responsible entity that promotes a culture of compliance and good governance is more likely to adopt the intent of the law than a responsible entity that does the bare minimum required by the law for the sake of demonstrating compliance.

We consider that the guidance provided by ASIC in RG 132 provides sufficiently clear commentary to inform responsible entities of the legal intent of the Act and how to tailor compliance plans accordingly.

Should auditors be legislatively required to meet minimum qualitative standards when conducting compliance plan audits? If so, what should these standards be and why?

We understand that the Auditing and Assurance Standards Board (**AASB**) has issued ASAE 3100 (Standard Assurance Engagements) that specifically covers the AASB's guidelines on conducting compliance plan audits.

As we are not auditors, we do not have an opinion as to the qualitative standards that should be required of auditors.

Should responsible entities be required to have a majority of external board members, similar to the CCIV regime?

In our opinion, the requirement for a compliance committee circumvents the need for responsible entities to also have a majority of external board members.

The function currently provided by a compliance committee achieves the intended purpose that having a majority external board membership aims to achieve, but without the obligations under s 601FD(1) imposed on external compliance committee members. Introducing a mandatory external board will present practical challenges such as finding suitable board members which would be unnecessarily burdensome for responsible entities.

Chapter 4 – Right to replace the responsible entity

Are any changes required to the voting requirements or meeting provisions that allow members to replace the responsible entity of a listed scheme? If so, what changes and why?

We do not believe that any changes are required to the current voting requirements or meeting provisions that allow members to replace the responsible entity of a listed scheme. As the Paper outlines, the requirement to pass ordinary resolutions by listed scheme members was decided in *MTM Funds Management Ltd v Cavalane Holdings Pty Ltd* [2000] NSWSC 922 and implemented by ASIC in Class Order 13/519. We maintain that the interpretation by the Court in Class Order 13/519 is appropriate.

Are any changes required to the voting requirements or meeting provisions that allow members to replace the responsible entity of an unlisted scheme? If so, what changes and why?

We recommend that the voting requirements that allow members to replace the responsible entity of an unlisted scheme are amended. We note previous comments made by CAMAC that the voting requirements of an unlisted scheme are "out of step" with general voting requirements in the Act.[5] Currently, s 601FM(1) of the Act requires members to pass an extraordinary resolution to replace the responsible entity making it very difficult for members of unlisted schemes to pass a resolution to replace the responsible entity given the stringent voting threshold.

Instead, we recommend that the voting threshold for unlisted schemes is lowered to require a simple majority of votes cast in favour of the resolution, provided that the total votes cast in favour of the resolution equate at least 40% of the votes able to be cast on the resolution. We consider this as a sensible approach that balances the interests of members seeking to change a responsible entity and the costs and disadvantages to the scheme more broadly, when a responsible entity is changed.

In what circumstances should an existing responsible entity be required to assist a prospective responsible entity conduct due diligence? What might this assistance look like?

In our opinion, we believe that the "reasonable assistance" provisions under s 601FR of the Act are appropriate and should extend to all due diligence activities required by a prospective responsible entity, noting that what is "reasonable" would depend on the circumstances.

An approach presented by the CAMAC is the requirement that reasonable assistance could be determined based on a percentage of members requesting assistance from the incoming responsible entity.[6] We do not agree that determining what is reasonable should depend on a percentage of members of the scheme asking for the assistance but a matter between the prospective and current responsible entities to determine based on the circumstances. Responsible entities are better placed to know what (if any) assistance is required in the circumstances compared with the members of the scheme who are not expected to have the knowledge and expertise of the responsible entities.

Should there be restrictions on agreements that the responsible entity enters into or clauses in scheme constitutions that disincentivise scheme members from replacing a responsible entity? If so, what restrictions may be appropriate?

We do not recommend imposing restrictions on agreements that disincentivise scheme members from replacing a responsible entity. Specifically, we believe that restricting a responsible entity's freedom to contract will have undesirable commercial consequences. One practical example is lender's use of common restrictive clauses in loan contracts which restrict a borrower's ability to undergo a change of control. These types of clauses are widely utilised and likely to apply to any financing contracts entered by a responsible entity and is likely to affect the ability of schemes to obtain finance if statutory bars are applied to a responsible entity's ability to contract with third party lenders.

More broadly, responsible entities and their counterparties should not be limited in their freedom to contract. Provided that potential investors are given the necessary disclosures to make informed

[5] CAMAC (2012), Managed Investment Schemes: Report, Australian Government, p 97.
[6] Ibid, p 91.

decisions (including the disclosure of any provisions that entrench a responsible entity for example by the trigger of a performance fee on their removal) we believe that the current provisions to protect members are adequate and limiting the freedoms of parties to contract would unnecessarily restrict commercially sensible arrangements.

Prohibiting restrictions that disincentivise members from changing a responsible entity could lead to an abuse of power by a scheme's institutional investors and other parties with significant voting power. These parties could legitimately exercise their voting rights simply to avoid having to pay a responsible entity the professional fees that have been agreed as a term of the constitution and appropriately disclosed.

Chapter 5 – Right to withdraw from a scheme

Is the definition of liquid assets appropriate? If not, how should liquid assets be defined?

The definition of liquid assets is generally appropriate, noting that liquidity mechanisms appear to be operating effectively in both the ordinary course of operating schemes as well as through periods of market dislocation.

We are aware that it is common practice for the constitution of a scheme to specify a period of up to 365 days as the relevant period within which to satisfy withdrawal requests for the purposes of s 601KA(6). The effect of this is that assets that are generally considered illiquid, such as real property assets, can count towards the liquid assets test for the purposes of s 601KA. In contrast, the assets designated under s 601KA(5) are all highly liquid kinds of assets and include money in an account or on deposit with a bank, bank accepted bills, and marketable securities (as defined in s 9).

On its face, this permissive approach to s 601KA(6) appears to subvert the purpose of the liquid/non liquid distinction, by allowing scheme operators to deem assets that are generally considered illiquid (such as real property) as liquid, alongside other highly liquid types of assets.

However, in practice this does not cause significant issues. As noted in the paper, ASIC's targeted review of how various registered schemes responded to the 2020 COVID-19 pandemic found that liquidity frameworks were generally adequate to respond to the liquidity challenges, and that market disruptions were well managed.[7]

Are any changes required to the procedure for withdrawal from a scheme? If so, what changes and why?

No changes are required to withdrawal procedures unless the liquid/non liquid scheme test in s 601KA is amended.

The permissive approach to s 601KA(6) allows scheme operators (where they have a reasonable expectation that a scheme can realise its assets for market value within the relevant period) to adopt the withdrawal procedures that have been designed for that scheme in light of its particular investment strategy under s 601KA(1).

In practice, we have seen that this allows scheme operators to offer bespoke withdrawal facilities that investors can access in the ordinary course of operating a scheme. Where the responsible entity can no longer form a reasonable expectation that it can realise assets within the relevant timeframe (for example during periods of market dislocation) investors are protected by the orderly process set out for illiquid funds in s 601KB of the Act.

However, the orderly process for illiquid funds set out in 601KB is cumbersome to implement and carries negative connotations that may accelerate withdrawal requests.

If changes to s 601KA(6) are contemplated to restrict the permissive approach to liquidity timeframes, we would suggest that either a new framework for permitting the fair and orderly withdrawal of members during the ordinary course of operating a scheme is introduced for non liquid schemes, or the existing withdrawal procedures that apply to a non liquid schemes under s 601KB are relaxed to make it more workable in the ordinary course of operating a scheme.

In particular, we would recommend that:

1. Section 601KB(3)(a) is amended to allow a more flexible timeframe within which withdrawal offers must remain open; and

2. Section 601KB(5), which requires responsible entities to lodge a copy of any withdrawal offer with ASIC, is deleted.

---

[7] ASIC (2021), 21-091MR ASIC review finds retail managed funds responded well to COVID-19 challenges in 2020, [media release], 30 April 2021, accessed July 2023.

Is there a potential mismatch between member expectations of being able to withdraw from a scheme and their actual rights to withdraw? If so, how might this be addressed?

We offer no comment on member expectations. However, to the extent that expectations are based on inaccurate disclosure, we note that responsible entities are subject to comprehensive disclosure obligations.

Chapter 6 – Winding up insolvent schemes

The legal complexities regarding scheme insolvency and winding up have re to a series of recommendations for regulatory reform. We acknowledge that the wide variety of scheme structures has created significant challenges in establishing a singular set of statutory principles for to apply to schemes. Although we recommend that there is regulatory reform in order to provide certainty for investors and creditors, we believe that it is important to ensure that regulation does not restrict the types and kind of scheme structures that may be offered to the public. Where Treasury does proceed with changes to scheme insolvency and winding up, we recommend that further additional consultation is taken to ensure that any statutory provisions are fit for purpose.

Are any changes required to the winding up provisions for registered schemes? If so, what changes and why?

We believe that the winding up provisions for registered schemes require significant changes to ensure that registered schemes have sufficient regulation to wind up in a manner that is fair, honest and efficient. The requests for regulatory change to the winding up provisions for registered schemes in the 2012 CAMAC report, 2016 Bitter Harvest report and 2022 Sterling Income Trust illustrate a steadfast industry wide desire for regulatory change.

Currently, registered schemes rely on requesting direction from the court as to how the registered scheme is to be wound up.[8] Although requesting direction from the court assists registered schemes in navigating a complex and often unclear area of law, it also provides a defence to conduct that may be challenged as not being in the interests of members.[9] Application to the court are both capital and time intensive[10] which may cause detriment to members during an insolvency.

In our opinion, the statutory provisions for winding up a registered scheme need to include greater clarity and where appropriate, align to the existing winding up provisions in Chapter 5. Due to the complex nature of winding up registered schemes, we recommend that Treasury adopts the recommendations in the 2012 CAMAC report as discussed in the 2016 Bitter Harvest report and 2022 Sterling report for consultation.

In particular, these provisions should provide clarity regarding priority of interests of creditors and fund members as beneficiaries. Other key provisions are outlined further in the question below.

Would a tailored insolvency regime for schemes improve outcomes for scheme operators, scheme members and creditors? Are there certain aspects of the existing company and CCIV insolvency regimes that should be adopted?

Where possible, the insolvency regime for registered schemes should align with the existing insolvency regime to improve outcomes for members and creditors. Alignment would assist with the transition and understanding of how rules would apply. However, it is important to ensure that rules are fit for purpose and apply appropriately to registered schemes. It is in that regard that the approach taken for the CCIV regime provides a suitable roadmap for the development of a tailored insolvency regime for registered schemes. The CCIV regime relies on translation rules to ensure that existing insolvency provisions apply appropriately to the CCIV structure. The translation rules are supplemented with specific provisions in Part 8B.6 of Chapter 8 of the Act. We suggest that translation rules may be a useful tool to adapt existing insolvency regime for companies, and where appropriate, specific rules may be implemented for registered schemes.

Another aspect of the CCIV regime that may be appropriate for registered schemes are the rules around the appointment of receivers and controllers. The CCIV regime limits the appointment of receivers and controllers to be on a sub-fund basis.[11] Similarly, a liquidator is only appointed on a sub-fund basis.[12] This principal could be adapted such that a receiver or controller may only be appointed in respect of the registered scheme and not the responsible entity. This could protect the

[8] 15.24 Bitter Harvest Report
[9] 15.35 &15.36 Bitter Harvest Report
[10] 15.43 Bitter Harvest Report
[11] s 1236B Corporations Act 2001 (Cth).
[12] s 1237N Corporations Act 2001 (Cth).

conflicts of interest identified in the Bitter Harvest Report whereby liquidators acted in the best interests of the responsible entity and not in the best interests of the members. Further, in the same manner that a CCIV's Corporate Director cannot be appointed as the receiver or controller,[13] we think it would be appropriate to ensure that the responsible entity is not appointed as the receiver or controller of the scheme. This is supported by the recommendation of CAMAC to suspend the powers of a responsible entity from operating an insolvent scheme.[14] We do, however, note that this may not be preferable given that it would require two separate receivers involved in the insolvency which may increase fees and create inefficiencies as a result of conflict between the responsible entity and the scheme.

It is, however, important to ensure that any amendments to the insolvency regime for registered schemes receives targeted consultation to ensure appropriate outcomes are achieved for both consumers and responsible entities. Although the adaptation of some provisions in the CCIV regime appears to be beneficial for registered schemes, it should be noted that there has been a pronounced lack of adoption of the CCIV structure. As such, these provisions have not been relied upon or tested in an actual wind up and their appropriateness or effectiveness is essentially conjecture.

We acknowledge that a tailored insolvency regime for schemes may create difficulties given the range of different scheme structures. For example, there would be significant complexities when applying a regime to a scheme that involves a trust against a contract based scheme with no trust created. Although alignment can create additional efficiencies and certainty, Treasury should ensure that regulation continues to facilitate the broad range of scheme structures that are available.

Should statutory limited liability be introduced to protect personal assets of scheme members in certain circumstances? If not, why not?

We do not recommend the introduction of mandatory statutory limited liability for members in schemes. An imposition of statutory limited liability may limit the types of scheme structures that may be used or the ability to design schemes. The broad definition of managed investment scheme captures a wide range of structures that may be used for collective investment. In practice, most schemes are structured as unit trusts though alternative forms of schemes are not uncommon and include strata based schemes, partnerships, and contract based schemes. The extent of member liability will be driven by the nature of the relevant scheme, and the specific terms set out in the scheme's constitution. There exist valid circumstances in which members in each type of scheme may be liable beyond their initial investment, subject to adequate disclosure as required by s 1013E. For example, the constitution of a strata based scheme may provide that members must contribute to levies payable to maintain scheme property, or beneficiaries of a trust may be liable to indemnify the trustee for liabilities or expenditure that they have authorised.[15]

The introduction of the CCIV regime provides an alternative collective investment framework with limited liability that exists alongside the managed investment scheme regime. The flexibility of the regulatory approach to managed investments schemes provides commercial advantages over the CCIV structure.

Both schemes and CCIVs should be available as alternative frameworks for collective investment. We do, however, acknowledge the need to ensure that members have sufficient protection, and we propose amendments to the current regulations such that all schemes would have limited liability unless the members' liability was included in the scheme's constitution in addition to disclosure requirements.

As an alternative to imposing statutory limited liability, we propose that all schemes have limited liability for members, unless the scheme's constitution provides otherwise. The scheme would also then have to disclose that the member's liability is not limited in the product disclosure statement. We think that this provides flexibility for schemes while maintaining consumer protections.

[13] s 1236C Corporations Act 2001 (Cth).
[14] Page 183 2012 CAMAC Report.
[15] *Vacuum Oil Co Pty Ltd v Wiltshire* (1945) 72 CLR 319 at 325; [1946] ALR 50; (1945) 19 ALJR 380; BC4600010.

Chapter 7 – Commonwealth and state regulation of real property investments

Do issues arise for investors because of the dual jurisdictional responsibility when regulating schemes with real property? If so, how could they be addressed?

Yes, there are issues that arise for investors (and property fund operators) because of the dual jurisdictional responsibility when regulating schemes with real property.

In particular, the differing Landholder Duty/Trust Acquisition Duty regimes that apply in each State and Territory make it difficult for property fund operators to acquire real property assets in certain jurisdictions.

In particular, it very difficult for property fund operators to acquire real property assets through managed investment schemes in Queensland and Victoria. As a result, investors (particularly retail investors) may miss out on opportunities to gain exposure to quality real property assets in those jurisdictions through investments in property funds.

We would welcome the opportunity to discuss this particular issue further with Treasury.

Chapter 8 – Regulatory cost savings

What opportunities are there to modernise and streamline the regulatory framework for managed investment schemes to reduce regulatory burdens without detracting from outcomes for investors?

There are significant opportunities available to modernise and streamline the regulatory framework for managed investment schemes. We believe that the principal opportunity is by removing the reliance on paper forms and using digital channels to submit forms and establish communication between ASIC and licensees. ASIC's development of the regulatory portal should continue and be bolstered to support compliance functions for managed investment scheme. Further, supporting and fostering regulatory technology platforms can help transform compliance obligations from tick-a-box exercises to genuine integration within licensees. Digital platforms and applications can provide for a more active investor engagement and greater understanding of their rights as investors.