Financial
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Review of the Regulatory Framework for Managed Investment Schemes

Consultation Paper

King Irving Submission

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King Irving

King Irving was founded in 2012 to deliver integrated legal and consulting solutions for financial services through our offices located in Sydney, Melbourne, and Brisbane. Our focus is funds management and our purpose is to provide exceptional advice to our clients, meaningful opportunities to our staff and to support the local community.

We are a dynamic and inclusive team of lawyers and financial professionals who are active partners in our clients' success. Our firm prides itself on our collaborative spirit both internally and as an extension of our clients' team.

Having a myriad of rich work and life experiences creates a culture that draws strength from the diversity of our team's knowledge and skills.

We have responded to specific questions within the Consultation Paper in this Submission.

Chapter 1 Wholesale client threshold

Q1. Should the financial threshold for the product value test be increased? If so, increased to what value and why?

Our stance asserts a resolute position against the proposition of increasing the existing threshold. This position is predicated upon examination of various factors, which collectively converge to underscore our contention that the existing threshold should remain unaltered.

Primarily, we contend that raising the financial threshold for wholesale products could potentially limit access to sophisticated investment opportunities for smaller investors. By maintaining the current threshold, a diverse range of investors can continue to access products that may offer diversification benefits to their portfolios.

Moreover, wholesale products play a significant role in capital formation for businesses and projects which may not be available through bank finance. Increasing the product value threshold could result in reduced funding options for enterprises seeking to raise capital through wholesale products. Vice versa, maintaining the current threshold encourages businesses to utilise these channels for fundraising, promoting economic growth and innovation.

Furthering this, the existing threshold has been set after careful consideration of the balance between investor protection and market efficiency. Raising the threshold could disrupt this equilibrium, potentially leading to market distortions and reduced transparency. The current threshold helps maintain a level playing field for both wholesale and retail investors and products.

Finally, wholesale products often have less regulatory oversight compared to retail products, given the assumption of higher investor sophistication. Increasing the threshold could prompt regulatory concerns about potential consumer protection issues for investors who may not meet the higher threshold but could still be vulnerable to risks associated with wholesale products.

The current threshold has been in place for a certain period, and market participants have adapted their practices and strategies accordingly. Sudden changes to the threshold could create uncertainty and impact investor and industry confidence in the regulatory environment.

However as noted below, the thresholds could be adjusted periodically to account for changes in the cost of living and the purchasing power of money.

Q2. 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?

As per our comments above, our view is that raising the financial threshold for wholesale products could potentially limit access to sophisticated investment opportunities for smaller investors. By maintaining the current threshold, a diverse range of investors can continue to access products that may offer diversification benefits to their portfolios.

We note that the current financial threshold test relies on set monetary values for net assets and gross income. However, these values can erode over time due to inflation. To address this, the thresholds could be adjusted periodically (for example, every 3 years) to account for changes in the cost of living and the purchasing power of money.

The thresholds adjustments should be achieved by linking the financial thresholds to key economic indicators such as the consumer price index. This would automatically adjust the thresholds based on the prevailing economic conditions, ensuring that the test remains relevant and consistent over time.

In conclusion, the financial threshold test for wholesale clients in Australia should remain as currently stated, with the potential to be adapted to take into account the impacts of inflation.

Q3. 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?

As per our comments above, our view is that restricting current access for wholesale products could potentially limit access to sophisticated investment opportunities for smaller investors. On this basis, no assets should be excluded from the wholesale test.

Q4. If consent requirements were to be introduced:

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

Including consent requirements by wholesale investors as part of the wholesale affirmation certification currently incorporated in applications could assist ensuring that investors fully understand the implications of their decision.

Consent requirements should be communicated in a clear, concise and easily understandable manner. The language used should avoid jargon and complex financial terminology. The goal is to make sure that investors with varying levels of financial literacy can comprehend the information provided.

Before submitting their consent, investors could be required to answer a concise set of questions (say 5 to 10) confirming their comprehension of the information presented. This may serve as a final check to ensure that the investor has understood the key points.

2. Should the same consent requirement 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 no, why not?

Introducing the same consent requirements for each wholesale client test, including the sophisticated investor test in Chapter 7 of the Corporations Act, is not a suitable approach. The reason is that the various wholesale client tests cater to different types of investors with distinct levels of financial sophistication, experience, and understanding of investment products and risks. Taking this into account, a one-size-fits-all consent requirement will not appropriately address the varying needs and concerns of these different investor categories.

Wholesale client tests in Chapter 7 of the Corporations Act include various categories such as professional investors, sophisticated investors and institutional investors. These categories encompass a wide range of investor profiles, from high-net-worth individuals to professional investment entities. Their familiarity with financial matters and ability to assess risks differ significantly.

The level of risk and complexity associated with investment products and services also varies across wholesale investor categories.

For instance, the sophisticated investor test has specific eligibility criteria that differ from other tests. Implementing a uniform consent requirement across all categories could overlook these distinctions and result in unintended consequences. Overly standardised consent requirements could lead to confusion, as the complexity of some tests.

It's important not to hinder accessibility to investment opportunities for investors who are genuinely well-versed in financial matters. Introducing overly burdensome consent requirements might deter wholesale investors from participating in certain investments.

Chapter 2 Suitability of scheme investments

Q5. Should conditions be imposed on certain scheme arrangements when offered to retail clients? If so, what conditions and why?

The financial services industry will always require an additional level of regulation enforced for the protection of retail investors, by virtue of their position of vulnerability. Unlike institutional or other professional (wholesale) investors, retail clients typically do not have the same level of access to resources or expertise to thoroughly evaluate highly complex and risky financial products and services.

While it is apparent that investments will always carry a level of risk, the industry needs to be firmly encouraged to give consideration to the asymmetrical level of sophistication of such investors.

In its Final Report on the 'Financial System Inquiry' (the FSI) in 2014, the Australian Government Treasury Department made a pertinent observation to this effect: "*Consumers have a responsibility to accept their financial decisions, including market losses, when they have been treated fairly. However, financial system participants, in dealing with consumers, should have regard to consumer behavioural biases and information imbalances.*"

When dealing with the question of the adequacy of protections, whether in place or proposed to be implemented, Regulators should ensure that the consideration towards the 'imbalance' which exists against retail investors is appropriately observed by market participants. The implementation of appropriate checks within the Managed Investment Schemes (MIS) Regime should be a key consideration to be implemented as a minimum as this is already a mechanism integrated within other financial services regimes such as the domestic Crowd-Sourced Funding (CSF) Regime, the Responsible Lending obligations imposed within the Credit Licensing Regime, and even within other robust international systems.

Proposed Regulatory Changes

The regulatory framework in Australia has made significant strides in protecting retail clients investing in MIS since 1998, when the first legislation was enacted. The emphasis, since that time, on disclosure, investor education, regulatory oversight, and liquidity risk management has enhanced transparency and regulatory defences. However, there are still further improvements which can be made to better safeguard retail clients.

It may be that some high risk products should only be distributed to a retail client where a financial planner has provided advice to that client. Alternatively, for these high risk products retail investors could benefit from undergoing a 'suitability test' which would take into account aspects of the investor's financial standing and risk tolerance if direct investing without advice.

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We wish to further comment on the recommendation from several inquiries including the Parliamentary Joint Committee Inquiry into aspects of agribusiness managed investment schemes in 2009, which was directed to potentially prohibit retail investors from investing in certain types of assets on account that certain products were potentially too complex or too risky for unsophisticated investors.

We note that, while it is crucial to implement regulations that safeguard retail investors, restricting their access to certain types of financial products or funds should be approached with caution. In the 2014

Financial System Inquiry Final Report, it was noted that: "The Inquiry also supports continuing industry and Government efforts to increase financial inclusion."

We consider that the above restrictions could inadvertently limit opportunities for individuals to diversify their portfolios and participate in potentially lucrative investment opportunities. By imposing overly stringent barriers, we risk excluding segments of the population from participating in certain financial market opportunities, which may hinder the broader goal of financial inclusion.

On the other hand, it would be likely that product innovation may also be stifled or at the least impacted because of the withdrawal.

It is therefore essential to strike a balance that protects investors while ensuring that they have the opportunity to explore a wide range of financial products, empowering them to make informed decisions and contribute to their financial well-being. Effective regulatory frameworks should, therefore, prioritise accessibility and education alongside protection to advance the overarching goal of greater financial inclusion.

Overall, the effectiveness of regulation in this area equally depends on investor awareness and behaviour as regulation of the product providers. Retail clients must actively engage with the provided disclosures, seek professional advice when necessary, and remain vigilant about their investments. Additionally, regulatory authorities should continue to adapt to the evolving market conditions and emerging risks to ensure ongoing effectiveness in protecting retail investors.

Q6. Are any changes warranted to the procedure for scheme registration? If so, what changes and why?

No, although while there are arguments in favour of increasing regulatory oversight of unregistered MISs to protect investors and maintain market integrity, there are also legitimate concerns about the potential drawbacks associated with a blanket obligation to register schemes which are not to be offered to retail clients.

Striking the right balance between regulatory oversight and market efficiency is essential. This approach can help ensure that regulatory objectives are met without unnecessarily burdening the market participants.

A core concern is in relation to investor sophistication. Registered MIS are typically marketed exclusively to retail clients and hold higher compliance requirements as a result of the position of vulnerability of retail clients. Wholesale clients on the other hand, are typically institutional or high-net-worth individuals with a higher degree of financial sophistication. These investors are generally assumed to have the ability and resources to conduct their own due diligence and negotiate directly with investment managers or obtain professional advice, reducing the need for the same level of regulatory protection as retail investors.

Imposing the same registration requirements and associated obligations would ultimately trivialise the 'wholesale' and 'retail' categories of investors which hold specific purpose in giving due consideration to protecting the interests of the more vulnerable participants of the market.

It is in light of this latter point that we do not consider it a necessity to broaden the procedure for scheme registration further. Rather, our view is that considerations around retail protections and reporting protocols for compliance measures should be evaluated further.

Q7. What grounds, if any, should ASIC be permitted to refuse to register a scheme?

Section 601EB of the Corporations Act provides the conditions under which a scheme may currently be refused registration. The test is one that, if all minimum conditions are satisfied, ASIC is obligated to register the scheme within 14 days of lodgement of the application.

In addition to these requirements, ASIC could be given a discretionary power to refuse the registration of a scheme based on 'good fame and character' checks on the responsible entity which take into account its and its officers' integrity, competence, governance and financial standing.

We believe this is sufficiently broad to empower ASIC to refuse to register schemes it considers are unsuitable for registration.

Chapter 3 Scheme governance and the role of the responsible entity

Q8. Are any changes required to the obligations of responsible entities to enhance scheme governance and compliance? If so, what changes and why?

The obligations of responsible entities in Australia currently regulated under the Corporations Act include several key items relating to scheme governance and compliance. Our view is that the main changes should relate to the regulation of constitution and compliance plans as per our answers below.

Q9. 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?

Currently, if amendments are required to be made for the scheme's constitution, such amendments can only be made if a special resolution of the scheme members is passed and if the responsible entity itself reasonably considers the change will not adversely affect the members rights.

This could be onerous on the responsible entity and the members and it may result in wasting time and resources unnecessarily.

ASIC currently has no power to direct the responsible entity to amend the scheme's constitution after registration and thus, to allow for better enhancement of scheme governance and compliance. In our view, there should be mechanisms in place to allow for special circumstances where ASIC can direct a responsible entity to amend the constitution to introduce any necessary changes to allow the scheme to operate in the best interest of its member. This may provide more efficiency for all stakeholders in terms of governance. However, it is prudent to ensure that an appropriate balance is struck between ASIC's power to direct the responsible entities and the responsible entity's control over the scheme.

Q10. Are changes required to the compliance plan provisions to ensure compliance plans are more tailored to individual schemes? If so, what changes and why?

Yes, it is our opinion that changes are required to ensure responsible entities are creating compliance plans that are more tailored to individual schemes to ensure optimal scheme governance and compliance and reduce generic off the shelf compliance plans that lack detailed procedures.

Regulations are also changing faster than ever, leaving many scheme compliance plans 'on the shelf' out of date. There should be a mechanism for the responsible entity to review the plans in order to maintain its currency and ensure appropriate governance and reducing risks of any non-compliance.

We also believe that there should be more guidance towards amending and consolidating compliance plans for entities with multiple registered schemes, reducing the need for unnecessary lengthy and overly complex documents to save all stakeholders time and costs.

Q11. 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 agree with CAMAC and the Parliamentary Joint Committee Inquiry's on the collapse of Trio Capital that there must be a better approach in governing the effectiveness of scheme compliance plans and their audits.

Generic compliance plans are common in the marketplace. With reduced quality and effectiveness of compliance plans, auditor and ASIC's assessments are limited as to whether the responsible entity has adhered to the plan. Additionally, lack of qualitative standards for the auditor may contribute to compliance plan audits not providing the regulatory oversight expected and as a result, to potentially impact negatively on scheme members.

It is our opinion that there should be a standard regulatory guidance in which auditors should check against to ensure auditors are reviewing scheme compliance plans with the highest standard and avoiding a tick-and-flick situations in order to improve the oversight and operation of compliance plans. In turn, this may also assist in the issue of generic compliance plans where responsible entities will have the need for more detail in the plans, matching the raised qualitative standards from their auditors.

However, we acknowledge that the effect of this means a more complex audit process, which would be more costly and time consuming, with a large ramification on government budget as the process of inputting all parameters to cater to all the different scheme structures means more resources are required.

Auditing process could take up to 3-4 months, with schemes potentially spending more time and resources on the audits instead of growing their funds management business, raising the inevitable question of whether this would be in the best interest of the scheme members.

If time and costs create hinderances to schemes' growth, even if the scheme's returns are good, the costs spent in auditing will reduce overall funds' performance. Additionally, having legislation to mandate tailored compliance plans and standardised audits may create too big of a hurdle for new entrants to the financial market, as well as smaller schemes to continue operating. Increased costs will restrict wholesale fund managers from entering the already costing retail market.

Q12. Should responsible entities be required to have a majority of external board members, similar to the CCIV regime?

To ensure that the best interest of the scheme members is in mind, it is of our opinion that there should be a guideline set for the qualifications and experience of the compliance committee members, the governance arrangements for the committee, and the requirement to notify ASIC of committee members, as well as ASIC's power to direct the members to further education required.

We are in agreement with ASIC *Regulatory Guide 132* that compliance committee members must have enough experience, qualifications, and competence to carry out their duties and functions, given the important role they play as gatekeepers in monitoring the responsible entity's compliance with its obligations.

However, we do not think that ASIC should adopt the same approach as CCIVs, where there are mandatory majority of external board members, for two reasons:

1. there is more oversight when there are two different groups (Board and Compliance Committee level) carrying out similar functions albeit in a slightly different structure, acting almost like two factor authentication method; and
2. if ASIC removes the role of the Compliance Committee and replaces it with a board with majority external members, there is a question of whether this is feasible in the commercial climate. If this cannot be integrated into the responsible entities' current business model, this change could pose as a risk of being counterproductive to the funds management industry.

Chapter 4 Right to replace the responsible entity

Q13. Are any changes required to the obligations of responsible entities to enhance scheme governance and compliance? If so, what changes and why?

Consultation papers such as this are at the centre of the determining whether changes are required to the obligations of responsible entities in the context of scheme governance and compliance.

It's important to note that the specific roles and responsibilities of responsible entities can vary widely depending on the level of engagement the responsible entity (**RE**) has with its managed investment schemes. To ensure the protection of investors' interests and the proper functioning of the scheme, regulators must take into consideration the operations it offers. Whilst categorising can dilute important detail, distinction and increase complexity, we see that RE's within the industry could broken into two 'types' of RE's.

Responsible Entity as a Service (RES)

The RES model are those businesses which are operate and offer to the market the service of primarily performing the role as an RE and Trustee services for external investment managers and other financial services offerings which require an RE. For example, Equity Trustees, Perpetual and other REs offer a diverse range of financial and fiduciary services for corporate clients and investment managers.

We submit that RE's who provide services primarily for external engagement and appointment should have a stricter and more transparent governance and also require higher levels of resourcing and capability. The RES model allows for greater scalability. Once an RE is established and compliant for one scheme, there is no express guidelines for how the composition of an RE should also scale and grow for further schemes. This ability for an RE to accept responsibility over multiple schemes provides an ease of entry to market for an Investment Manager. This aspect of the RES model is also coupled with a consumer sentiment that the RES model provides scheme members with greater security, assurance and oversight over the given scheme or investment manager. We submit that the balance between the number of schemes an RE covers and its resources and competence required to meet consumer expectations should be given more clarity. We believe the standards that should be met for such a model is generally demonstrated by the majority of RE's in the market.

Responsible Entity as Fund Manager (RFM)

The RFM model are those business which are only an RE for the schemes it is an investment manager for. They do not hold themselves out as RE's for other investment managers but maintain an internal expertise. Whilst the RFM model does not have the same independent oversight and scrutiny as the RES, it does require internal resources in addition to the operation of an investment manager. Whilst all retail products must meet strict disclosure requirements, it is possible to explore whether an RFM model could be differentiated in governance and resource requirements to that of the RES model.

Ultimately, the need for changes to the obligations of responsible entities would be assessed based on a careful consideration of many factors discussed in this paper and an evaluation of whether the existing regulatory framework adequately addresses current and future challenges in scheme governance and compliance. Further input from stakeholders, industry experts, and the outcomes of the regulatory review would play a significant role in shaping any potential changes this submission proposes.

Q14. 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?

The need for changes to the voting requirements or meeting provisions that allow members to replace the responsible entity of an unlisted scheme depend on various factors, including the existing legal and regulatory framework, industry practices, and the specific circumstances of the scheme. However, several considerations might prompt a review and potential changes in this area.

For example, the current required participation rate of 50% of voters entitled to vote may well be impossible to attain where platforms representing investors refuse to exercise their votes (which has been known to happen). Investors may be disengaged. A lower rate may be appropriate given the safeguards provided by the Corporations Act otherwise provided regarding REs.

Some constitution voting requirements make it excessively challenging for members to replace the RE, particularly in cases where the RE may not be acting in the best interests of investors, it may be necessary to revise these requirements to facilitate a more efficient and responsive process.

Revisions to voting and meeting provisions may be balanced by transparency in the replacement process. This can include ensuring that members receive clear and independent information about the reasons for replacing the RE.

Any changes to voting requirements or meeting provisions should strike a balance between protecting investors' interests and providing a fair and transparent process for replacing the RE. Consultation with stakeholders, including investors, industry participants, and regulatory authorities, can help identify areas for improvement and ensure that any proposed changes are well-considered and appropriate for the specific circumstances of the unlisted scheme.

Q15. 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?

A transition can occur for various reasons, such as changes in ownership, corporate restructuring, or a desire to replace the existing RE. The goal of requiring assistance from the existing RE is to ensure a smooth and orderly transition while protecting the interests of investors. We submit that this assistance is always in the best interests of the investors, and certainly any resistance should be discouraged. Assistance can take the form below:

1. **Disclosure of Documents** - The existing RE should provide access to relevant documents and records, including financial statements, investment portfolios, contracts, and legal agreements related to the scheme.
2. **Assisting with Legal and Regulatory Compliance** - Ensuring that all legal and regulatory requirements are met during the transition, including necessary filings and notifications to regulatory authorities.

3. **Co-ordinating with Service Providers** - The existing RE may facilitate communication between the scheme and service providers, such as custodians, administrators, and auditors, to ensure a seamless transition of responsibilities.
4. **Financial and Operational Summation** - Providing a comprehensive statement of the scheme's assets, liabilities, and operational procedures to identify any potential issues or risks together with working papers (in addition to the provision of lodged financial statements).
5. **Asset Valuation** – Providing the existing policy for valuation of the scheme's assets to assist in continuity.

Q16. 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?

It is vital that restrictions on agreements or clauses in scheme constitutions that disincentivise scheme members from replacing a responsible entity be removed (or not included) to ensure that the process for replacing an RE is fair, transparent, and aligned to the best interests of investors.

Prohibitions could be put in place to prevent the inclusion of clauses that impose punitive fees or costs on members who wish to initiate or support a replacement of the RE (e.g. fees based on the remaining period of an expressed term). High costs can discourage members or (investment managers) from exercising their rights.

Chapter 5 Right to withdraw from a scheme

Q18. Are any changes required to the procedure for withdrawal from a scheme? If so, what changes and why?

The concept of withdrawal from liquid investment schemes warrants a structured approach that guarantees the prompt and equitable processing of redemption requests. To address potential discrepancies between fund constitutions and statutory regulations, a dual-layered system could be implemented to ensure consistency and fairness in the redemption process.

By enacting redemption timeframes at both the constitution and statutory levels, investors' interests and expectations are safeguarded, contributing to a transparent and secure investment environment.

1. Constitution Level Redemption Timeframe:

   At the heart of this framework lies the necessity for fund constitutions to stipulate a redemption timeframe. However, this timeframe should adhere to a statutorily prescribed maximum term. This alignment between the constitution and the law guarantees that investors' rights are upheld and that no fund can impose a redemption period that surpasses the statutory limit. This level of regulation ensures that no investor is subjected to undue delays or uncertainty when seeking to withdraw their investments from a liquid scheme.

2. Statute Level Redemption Timeframe:

   In addition to the constitution's stipulated timeframe, a statute-level regulation should be established. This statutory provision will serve as a ceiling, dictating the maximum redemption period that any liquid scheme's constitution can impose on its investors. This framework acknowledges that while funds possess autonomy in crafting their internal rules, these rules must still operate within parameters defined by overarching statutory law. As such, the statute-level redemption timeframe acts as a safety net, guaranteeing that no fund can extend the redemption period beyond what is deemed reasonable and fair. Currently this is set out in *Regulatory Guide 134: Funds Management Constitutions* as 21 days (RG 134.225), we view this as not necessarily aligning with the definition of *liquid funds* set out in s601KA of the Corporations Act and likely too restrictive; a period of 30 days may be more appropriate (and aligns with APRA's standards, see for example Prudential Standard 210 applying to ADIs).

The two-tiered approach outlined above ensures that the process of redemption within liquid schemes remains transparent, clear, and equitable. This approach not only strengthens investor confidence but also provides investors with a consistent and predictable experience across different funds.

This careful balance respects the autonomy of funds to structure their operations while simultaneously protecting investors' rights. Moreover, this approach aligns with broader regulatory goals of ensuring consumer protection, market integrity, and transparency in the financial sector.

In conclusion, the establishment of redemption timeframes at both the constitution and statute levels reflects a comprehensive and thoughtful approach to managing withdrawals from liquid investment schemes. This framework aims to strike a harmonious balance between investors' interests and the operational realities faced by these schemes, ultimately fostering trust and confidence in the investment landscape.

Chapter 6 Winding up insolvent schemes

Q20. Are any changes required to the winding up provisions for registered schemes? If so, what changes and why?

We recommend adding an 'insolvency' provision to the winding up provisions, requiring the responsible entity to wind up a scheme where the scheme has become insolvent. This would create greater certainty for creditors and members of insolvent schemes. As schemes cannot currently be considered insolvent under the Corporations Act in the same manner as companies, the addition of an insolvency provision to the winding up provisions may require granting schemes a separate legal status. This would allow the schemes themselves to incur liabilities, thus allowing the schemes to be considered insolvent under the Corporations Act. Alternatively, the new insolvency provision in the winding up provisions could simply require the scheme to be wound up when the scheme's assets are no longer sufficient to indemnify the responsible entity for its liabilities (adopting the Victorian Supreme Court's definition of an insolvent scheme in *Capelli v Shepard*). The benefit of this approach is that it does not require granting schemes a separate legal status.

Q21. 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?

A tailored insolvency regime for schemes would improve clarity and certainty for operators, members and creditors of insolvent schemes. This is because a scheme's constitution, the general principles of trust law and case precedent might not offer sufficient guidance as to procedure when winding up a scheme that has become insolvent. In such cases, having a statutory procedure for winding up insolvent schemes would speed up the winding up process, leading to better outcomes for both members and creditors. In addition, this would reduce the need for responsible entities to apply to the courts for directions on how to administer the assets and liabilities of an insolvent scheme. As court involvement in the winding up of a scheme will often add significant time and costs, this should be avoided if possible. Our recommendation is therefore to adopt a tailored insolvency regime for schemes.

Q22. Should statutory limited liability be introduced to protect personal assets of scheme members in certain circumstances? If not, why not?

We recommend that statutory limited liability for scheme members be introduced. This would not only protect scheme members but also encourage investment, particularly from foreign investors who are accustomed to investment schemes which offer limited liability for investors. Additionally, introducing statutory limited liability for scheme members would also encourage domestic investment in Australian schemes, as this would help investors when deciding whether to invest in a scheme. By prescribing limited liability for members, potential investors in schemes would be able to make investment decisions without having to consider the issue of limited liability. This would simplify the decision-making process and thereby encourage investment.

Chapter 7 Commonwealth and state regulation of real property investments

Q23. Do issues arise for investors because of the dual jurisdictional responsibility when regulating schemes with real property? If so, how could they be addressed?

Under the Australian Federal system of government real property rights are governed by the laws of each individual state or territory that form the Commonwealth of Australia. These laws are a combination of common law and legislation, which slightly very in each state and territory, although they all encapsulate English property law principles.

The overlap between Commonwealth and state regulations was highlighted in the *Senate Inquiry into Sterling Income Trust Submission by ASIC (November 2021)* (the **Sterling Group case**). The Sterling Group case illustrated that issues arise for investors when there is overlap between federal and state regulation. In the Sterling Group case, the regulatory responsibility for the products and services provided by Sterling Group were shared between the Commonwealth (in the case of dealing in financial products) and the Western Australian Government (in the case of housing).

Addressing the overlap:

We are of the view that the Australian government should collaborate with State and Territory regulators to identify and remove the jurisdictional overlap that exists between State and Commonwealth regulation of schemes that pertains to investment schemes that include real property rights. The collaborative efforts will enable the Australian Government to create a database of legislation that operates concurrently with Commonwealth legislation to govern schemes that deal with real property.

Chapter 8 Regulatory cost savings

Q24. 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?

The modernisation and streamlining of the managed investment schemes regulatory framework is a complex task that would provide benefits for all those involved within the creation, operation, and conclusion of these investment structures. In considering how to best approach this task, there are multiple strategies that can be examined in further detail which could potentially provide a foundation for this reform.

1. Technology Integration

In the digital age, where technological advancements are reshaping industries across Australia, the financial sector stands poised for a transformative leap through the integration of cutting-edge technologies. The approach of technology integration within regulatory frameworks is rapidly gaining traction as a powerful means to modernise and simplify the landscape of managed investment schemes. By harnessing the capabilities of automation, data analytics, and digital platforms, regulatory bodies can revolutionise the way investment schemes are monitored, reported, and managed. This discussion delves into the potential of technology integration as a catalyst for modernisation, shedding light and how it can enhance regulatory oversight, reduce administrative burdens, and empower both regulators and industry participants within the managed investment schemes ecosystem.

The key benefits that that technology integration could bring to the managed investment scheme framework includes:

- streamlining reporting and compliance
- enhanced surveillance and monitoring
- efficient auditing and review
- reduced human error
- faster regulatory responses
- cost-reduction
- scalability and consistency
- data-drive insights
- easier compliance monitoring.

The integration of technology offers a transformative opportunity to modernise and simplify the regulatory framework for managed investment schemes. By leveraging automation, data analytics, and digital platforms, regulatory bodies can enhance their oversight capabilities, reduce administrative burdens, and foster a more efficient and transparent managed investment schemes ecosystem. As technology continues to evolve, embracing these advancements can position the financial industry for a future of streamlined operations, improved investor protection, and increased market integrity.

2. Simplified Disclosure Documents

In the intricate world of finance, where complexity often accompanies confusion, the concept of simplification has emerged as a beacon of clarity and transparency. Within the managed investment schemes framework, the adoption of simplified disclosure documents presents a promising approach to modernise and enhance the investor experience.

These documents, characterised by their clear language, concise structure, and user-friendly presentation, hold the potential to streamline the intricate web of information that investors encounter. Embracing simplified disclosure documents in the modernisation of the managed investment scheme framework gives rise to the potential opportunity to empower investors, foster trust and contribute to a more navigable and investor-friendly landscape.

The key benefits that simplified disclosure documents could bring to the managed investment scheme framework includes:

- enhanced investor understanding
- reduced information overload
- informed decision-making
- greater transparency
- efficient comparison
- compliance with regulations
- standardised formatting
- accessibility improvements
- mitigation of misunderstandings
- cost savings.

Embracing simplified disclosure documents within the managed investment schemes framework offers a transformative avenue to modernisation. Through prioritising clarity, transparency, and investor empowerment, these documents can create a more user-friendly and approachable investment landscape.

As investors gain a clearer understanding of their options and risks, market integrity is strengthened, fostering a relationship of trust between investors and investment managers. Ultimately, the adoption of simplified disclosure documents supports a more informed and confident investor community while contributing to the overall modernisation and simplicity of the managed investment schemes framework.

3. Harmonisation of Regulations

In the Australian landscape of financial markets, a variety of overlapping regulations and standards can often hinder investment activities, create inefficiencies, and impede market growth.

The concept of harmonisation of regulations emerges as a unifying force, offering the potential to streamline the complex web of rules governing managed investment schemes within Australia. Through aligning the regulatory frameworks, this approach would seek to create a cohesive and consistent environment that fosters innovation, reduces compliance burdens, and enhances investor protection.

The key benefits that harmonising regulations could bring to the managed investment schemes framework includes:

- consistency and clarity
- reduce compliance complexity
- improve efficient resource allocation for regulatory authorities
- provide enhanced investor protection
- facilitate innovation and market development in a consistent and predictable environment
- reduce regulatory arbitrage
- provide global investor confidence
- facilitate easier supervision and enforcement of regulations.

The harmonisation of regulations offers a compelling strategy to modernise and simplify the managed investment schemes framework. This has also been recently suggested by the Australian Law reform Commission within the Financial Services Legislation: Interim Reports A, B and C. By uniting the diverse regulatory landscape, this approach paves the way for a more efficient, investor-friendly, and globally integrated market ecosystem. As investment activities continue to transcend national boundaries, the adoption of harmonised regulations represents a progressive step toward creating a consistent, transparent, and resilient managed investment schemes industry that benefits investors and fosters innovation.

KING IRVING