

Property Fund News

March 2009

Shorter PDSs for property funds

Working Group

In previous editions of Property Fund News we have commented on the efforts of the Commonwealth Government's Financial Services Working Group (Working Group) in its quest for the four page product disclosure statement (PDS).

A brief review

The Working Group was established in early 2008 with the objective of tackling complexity in disclosure documents. To assist the Working Group, the government established the Industry and Consumer Advisory Panel (Advisory Panel). Andrew Shearer-Smith sits on the Advisory Panel as a representative of the Australian Direct Property Investment Association (ADPIA) and has been involved in the Working Group's monthly meetings.

The first task undertaken by the Working Group was to draft a PDS for the government's First Home Saver Account (FHSA) product. This task was completed late last year with the introduction of new legislation mandating the use of four page PDSs for these products. Each PDS must have nine sections in a set order and with prescribed headings. There is prescribed text for seven of the nine sections. We now have a very prescriptive approach to offer documents for FHSAs however, these products are relatively simple and generic.

Once work was completed on the FHSA PDS, the Working Group started considering PDSs for superannuation and managed investment products and this work is currently underway.

Shorter PDSs

To gauge the task at hand, the Working Group commissioned a number of research houses to conduct surveys of consumers, industry associations and fund managers with the aim of identifying the issues currently faced by all concerned given the length and complexity of PDSs. Not surprisingly, and consistent with all previous surveys on the topic, consumers and fund managers alike think PDSs are too long and detailed.

Given the results of the surveys, and the express wishes of the Minister for Superannuation and Corporate Law, Senator the Hon Nick Sherry, we have no doubt that a new disclosure regime will be introduced in Australia towards the end of the year. This new disclosure regime will mandate the use of much shorter PDSs.

At first, we were cynical of the idea of a four page PDS. However, shorter PDSs will be a positive for the industry. Consumers and fund managers alike comment that no-one reads PDSs. The Working Group is trying to rectify that. They want fund managers to prepare a document that investors will read and hopefully understand and we should support such a cause if it improves the investment decision process.

Exactly what the shorter PDSs will look like is still unclear. We doubt the document will be four pages, but it might be say eight or 10. To achieve this, the balance information normally included in a PDS will have to be incorporated by reference. However, we have concerns that fund managers will be exposed to greater liability because they will be providing prospective investors with less information in the PDS itself. We will be pushing for a regime that limits the liability of fund managers and places the onus on the prospective investor to seek out the additional information.

Fee disclosure

You may recall from previous editions of Property Fund News that we have been campaigning against the current fee disclosure regime introduced for property funds from 1 July 2006. It is encouraging to note that the fee disclosure regime will be revised as part of the Working Group's efforts.

Timing

Originally, Senator Nick Sherry wanted the shorter PDS work to be completed by 30 June 2009. However, this work will be delayed because of the government's new and more pressing interests in the margin lending industry. We expect progress will continue to be made but the new PDS regime will not be implemented until late this year.

Conclusion

There is much work to be done before the Advisory Panel and Working Group agree on the new disclosure regime but we will keep you posted along the way. Hopefully, as a member of the Advisory Panel, we and ADPIA will have some success in shaping an efficient, effective and balanced disclosure regime.



If you would like more information, then please contact **Andrew Shearer-Smith** by email or on 07 3239 2915.

Continuous disclosure—not just an issue for the listed sector

The focus on disclosure

In the current climate, with the A-REIT sector having been all but decimated, and financial and other pressures building on many funds, there is a renewed focus on market disclosure issues.

The industry and broader community are used to hearing about the ongoing disclosure obligations of listed companies and funds. However, there is much less awareness of the continuous disclosure obligations which apply to many unlisted entities.

ASIC is aware of this and over the last year has said it believes there is poor compliance in this area by unlisted disclosing entities. Especially given the current environment, this is an issue which is likely to receive more attention from the regulator this year.

Disclosure by unlisted funds

“Disclosing entities” include unlisted funds with 100 or more investors who invested under a PDS (as well as unlisted companies with 100 or more investors).

The relevant obligation under the *Corporations Act 2001* (Corporations Act) is to lodge a “continuous disclosure notice” with ASIC, as soon as practicable after the manager of a disclosing entity becomes aware of information that—

1. is not generally available
2. a reasonable person would expect, if it were generally available, to have a material effect on the price or value of the fund’s securities, and
3. has not been included in a PDS, supplementary PDS or replacement PDS which has been lodged with ASIC.

Failure to comply with this obligation is an offence and may attract penalties.

Issues under the current disclosure regime

In practice, this test for continuous disclosure can be problematic in the context of an unlisted property fund; and the usefulness of the current disclosure regime as a means of communicating important information has to be questioned. The following issues often arise for fund managers:

1. For an unlisted property fund, it can be difficult to decide which information could be expected “to have a material effect on the price or value” of units. Unlike securities in a listed fund, the price (and value) of units in an unlisted property fund are normally a function of the fund’s net asset value. Price is not subject to the whims and sentiment of the investor market.

However, the Corporations Act says a reasonable person will be taken to expect particular information to have a material effect on the price or value of units, if the information would, or would be likely to, “influence persons who commonly invest in securities” in deciding whether to acquire or dispose of units. Therefore, an event might not have any direct impact on the price or value of units in an unlisted property fund, but it could still be something which is likely to influence investors in making a decision whether to invest in the fund or sell their units.

Surprisingly, at present there is little guidance from ASIC about the types of information expected to be disclosed by unlisted property funds. It is hoped that in due course, ASIC will give the industry some meaningful guidance in this area.

2. The only obligation is to lodge notification of the information with ASIC. This disclosure usually just takes the form of a letter to the regulator. However, at present ASIC does not, for example, collate all continuous disclosure notices lodged by a particular fund and make them easily available to investors at a central location (or say on ASIC’s website). If an investor wants to read the disclosures made by a particular fund, then they would need to conduct a search of ASIC’s records in relation to that fund (which they would also have to pay for). The usefulness of the current disclosure regime to investors is therefore somewhat questionable. It may be that another system is eventually put in place under which information is more readily accessible to investors and the industry. However, only time will tell.

Review

It is worth taking the time to review your policies and procedures for identifying and disclosing information and events which you consider need to be disclosed under the current law. Fund managers who ignore their continuous disclosure obligations, or who have inadequate procedures in place, could risk committing an offence under the Corporations Act.

McMahon Clarke Legal can assist in the development of continuous disclosure policies and procedures, as well as provide advice on the continuous disclosure provisions.



If you would like more information, then please contact **Matthew Moses** by email or on 07 3239 2928.

BCIPA—will you be caught out?

Urgent action

In Queensland, the *Building and Construction Industry Payments Act (Qld) 2004* (the Act) is known as the “pay now, argue later” regime for people involved in construction work.

The strict time limits in the Act apply whether the claim is for as little as \$28 to as much as \$50 million. It is imperative that everyone involved in construction work in Queensland has systems in place ready to deal with a claim as soon as it is received.

Similar Acts are in force in Western Australia, Northern Territory, New South Wales and Victoria.

Payment schedule

If you receive a document with the words “This is a payment claim under the *Building and Construction Industry Payments Act (Qld) 2004*”, or words generally along those lines, then you have 10 business days (sometimes shorter) to prepare a response, called a ‘payment schedule’.

If you do not submit a response within that time frame, then the claimant can apply to the court for summary judgement for the amount claimed. You will have extremely limited grounds to defend the summary judgement application and in most cases, you will have to pay over the amount claimed and then commence separate proceedings to recover it.

The payment schedule must include every argument that you intend to rely on should the matter go to adjudication. You may want to argue legal defences, such as invalidity of the payment claim or interpretation of the terms of your contract. You may also want to argue a valuation point that may require expert reports. In every case, the payment schedule must be prepared carefully and served properly within time to escape a judgement being made in the claimant’s favour.

Adjudication

If the claimant is unhappy with your payment schedule, then they can refer the matter to adjudication, again within 10 business days of receipt of your payment schedule. This is usually when you receive the full force of their submissions about why you should pay them. Sometimes the payment claim has simply been a tax invoice, yet the adjudication application can contain folders of material and reports in support of the claim.

The adjudication response is due within five business days of receipt of the application. This can mean a very large amount of work must be done in a very tight time frame, including preparing statutory declarations, expert reports, photographs and submissions.

Adjudication decision

The adjudicator that is appointed might be a lawyer, a quantity surveyor, a builder or another suitably qualified person. You cannot ask for a person with specific qualifications to be appointed.

They will make a finding based on the adjudication application and the adjudication response within 10 business days.

There are very limited grounds of appealing an adjudicator's decision. You are limited to arguments of bad faith or a lack of natural justice.

You will have to pay the claimant the amount of the adjudication decision within five business days. If you dispute the decision you will have to commence separate proceedings to recover the amount you have been required to pay.

Conclusion

The regime imposed by the Act doesn't allow much margin for error. The process is rigid and the time frames are short.

McMahon Clarke Legal has expertise in preparing documents and defending claims under the Act. Please contact us if you need assistance.



If you would like more information, then please contact **Brit Ibanez** by email or on 07 3239 2960.

New disclosure principles—31 March 2009 deadline is approaching

In our [November 2008 issue of Property Fund News](#), we reminded readers of the timetable for compliance with ASIC's new disclosure principles for unlisted property funds.

By now, managers of "open" funds should have provided investors with updated disclosure applying the new disclosure principles. For the purpose of its disclosure principles, ASIC consider an "open scheme" to be an unlisted property fund that at any time from 30 November 2008 to 31 March 2009 gives investors withdrawal rights. The deadline for this was 30 November 2008.

Managers of "closed" funds are required to provide updated disclosure under the new principles by 31 March 2009 (unless investors need earlier disclosure, to make a decision on withdrawal rights that commence on or shortly after 31 March 2009).

Therefore, you should now be considering whether you need to prepare an information update to your investors, applying the eight new disclosure principles. Some fund managers may have already done this, perhaps through a quarterly report for the December 2008 quarter.

McMahon Clarke Legal can advise on compliance with the new disclosure principles and help in the preparation of investor updates.



If you would like more information, then please contact **Matthew Moses** by email or on 07 3239 2928.

Shareholders maintain position as creditors

Equal ranking

Aggrieved shareholders will continue to rank equally with unsecured creditors in insolvency proceedings.

The Corporations and Markets Advisory Committee (CAMAC) recently recommended in its report (Report) on the High Court decision in *Sons of Gwalia v Margaretic* [2007] HCA 1 (Sons of Gwalia) that the law should be left as it stands.

Background

The High Court found in *Sons of Gwalia* that a shareholder ranked equally with the claims of ordinary unsecured creditors where the shareholder's claim was based on non-compliance with disclosure laws, or another form of corporate misconduct. The High Court held that a claim made in these circumstances by an 'aggrieved shareholder' was not a claim in the shareholder's capacity as a member of the company. This decision reinterpreted a longstanding principle of the law, that shareholders rank behind creditors in a winding up, and has attracted much commentary and debate.

CAMAC

In their review, CAMAC considered submissions from the business community, whose views on the issue were polarised. Particularly, they acknowledged the significant implications of the decision on unsecured creditors including debt finance providers. Debt providers now need to factor in the additional risk of competing with aggrieved shareholders in any external administration, which may mean tighter credit, increased costs and difficulty in attracting investment in times of financial stress. Consequences in the area of insolvency proceedings were also noted, as the complexity of determining claims will increase and be further hampered by the increasing incidence of class action litigation.

However, despite these factors, CAMAC has recommended the government leave the law as it stands and should not postpone, cap or prohibit the rights of shareholders. While CAMAC was not unanimous in its view, “as a whole” it was not persuaded legislative change is required.

Reasoning

CAMAC reasoning was essentially based on its observation that Australian corporate regulation has undergone a ‘significant shift’ in recent years, with a stronger regime for corporate reporting and direct rights of action available for shareholders and others who suffer because of corporate misconduct. CAMAC noted the legislative intention to empower investors would be undermined if rights of recourse to aggrieved investors were curtailed. Fund managers may be interested to note that, in considering whether aggrieved shareholders claims should be postponed, CAMAC compared the position of unitholders of a managed investment scheme where the unitholders had a claim against the responsible entity. In this case CAMAC noted that it has never been in doubt that unitholders would be treated as creditors of the scheme, and CAMAC considered aggrieved shareholders should be treated in a similar way.

Report

In its Report, CAMAC proposed several related reforms to the government which include the following:

1. Various measures to assist external administrations if shareholder claims are not postponed, such as a standardised proof of debt form for aggrieved shareholders.
2. The abolition of the rule in Houldsworth’s case which would remove any distinction between a claim from a shareholder who holds subscriber shares and another who purchased the shares from a third party.
3. Legislative amendments to make clear that shareholders are not entitled to exercise voting rights in insolvency proceedings.

We look forward to the government’s response following the release of the report and will keep you updated on any further developments.



If you would like more information, then please contact **Nicole Singer** by email or on 07 3239 2906.

AML/CTF update—compliance programs and reporting

Reporting period

In January 2009, the Australian Transaction Reports and Analysis Centre (AUSTRAC) confirmed the—

1. 2008 reporting period for anti-money laundering and counter-terrorism financing (AML/CTF) compliance is 1 January 2008 to 31 December 2008, and
2. compliance reports for that period must be lodged with AUSTRAC by 31 March 2009.

Lodgement deadline

For most responsible entities of registered and unregistered managed investment schemes, the 2008 AML/CTF reporting period will be the first compliance report they have been obliged to lodge.

The previous AML/CTF reporting period was the 2007 calendar year however, responsible entities issuing interests or units in their schemes only became subject to the AML/CTF laws in January 2008 (provided they had not undertaken other services already caught by the legislation). If they have not already done so, then responsible entities must familiarise themselves with the compliance reporting procedure as soon as possible in order to meet the looming lodgement deadline.

With respect to the lodgement process, it is AUSTRAC policy that AML/CTF compliance reports be submitted electronically via AUSTRAC Online (unless a reporting entity does not have the technology to do so) with each reporting entity completing an online questionnaire before being permitted access to complete and lodge its compliance report. Details of the lodgement process can be obtained from the AUSTRAC website, www.austrac.gov.au.

AML/CTF compliance program

With the current focus on AML/CTF compliance, it is also opportune for reporting entities to revisit their AML/CTF compliance program and update it.

From 13 December 2008, reporting entities are obliged to monitor their customers and their transactions through ongoing customer due diligence and they also have obligations to report certain matters to AUSTRAC.

Customer monitoring

The ongoing due diligence obligations involve the implementation of appropriate risk-based systems and controls to—

1. determine whether and in what circumstances ‘know your customer’ (KYC) information should be updated or verified or if any *further* KYC information should be collected in respect of customers, and

2. monitor the transactions of customers to identify any suspicious transactions (i.e., implement a transaction monitoring program).

Reporting entities must also implement an enhanced customer due diligence program which applies in circumstances where the reporting entity determines, in the course of conducting its ongoing customer due diligence, that money laundering or terrorism financing risk is high. The enhanced customer due diligence program assists the reporting entity to determine what course of action to take in response to an identified risk e.g., the reporting entity may need to seek further information from a customer or re-verify the customer's identity.

The transaction monitoring program and enhanced customer due diligence program must be incorporated into Part A of a reporting entity's AML/CTF program.

Additional reporting

Reporting entities must also implement procedures for reporting "suspicious matters" and "threshold transactions" to AUSTRAC. These procedures will generally contain information which will assist a reporting entity to identify what "suspicious matters" and "threshold transactions" are and detail the information which must be contained in any reports to AUSTRAC.

Draft AML/CTF Rules

A number of draft AML/CTF Rules currently exist, some of which are relevant to managed investment schemes.

With respect to the issue of scheme interests, it is proposed the AML/CTF Rules be amended to provide a time frame pursuant to which the customer identification procedure can be carried out after the interest is issued. Currently, customers must be identified *before* the interest is issued. The proposed amendments will allow up to five business days after issuing interests in a scheme to carry out the customer identification procedure.

We will keep you informed as the AML/CTF Rules are updated.

If you require any further information or need any assistance with your AML/CTF compliance reporting obligations or AML/CTF compliance program, then please contact us.



If you would like more information, then please contact **John Lane-Mullins** by email or on 07 3239 2960.

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