

Corporate Advisor July 2010

Welcome to the July 2010 edition of *Corporate Advisor*.

In this issue of *Corporate Advisor*, we look at the simpler product disclosure regulations which have now come into force and will affect all product manufacturers of “simple managed investment schemes”. We also look at the potential liability of officers of a responsible entity to investors, and further disclosure reforms for the infrastructure and agribusiness sectors which we expect will be applied to other investment sectors.

We hope you enjoy this edition of *Corporate Advisor*.

Regards

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Simpler disclosure now law

New regulations

In the April 2010 edition of *Corporate Advisor*, we reported on the draft regulations and example product disclosure statement (PDS) for the simpler disclosure of managed investment products (http://www.mcmahonclarke.com/April_2010.cfm#1).

Following public consultation on the draft regulations, a revised version of the regulations became law on 16 June 2010.

Significant changes to the draft regulations

The final form of the regulations were significantly different to the draft regulations released at the end of 2009. The major changes between the draft regulations and the final form are as follows:

1. The draft regulations were intended to apply to registered managed investment schemes which invest at least 80 percent of their assets in “financial assets”. “Financial assets” were not defined.

This criteria has now significantly changed. The regulations will now apply to “simple managed investment schemes” which are defined as registered managed investment schemes which invest at least 80 percent of their assets—

- (a) in a bank account or in a term deposit on the basis that the money is available for withdrawal either immediately or at the end of a maximum fixed term of three months, or
- (b) the scheme invests at least 80 percent of its assets in investments which the responsible entity of the scheme can “reasonably expect to realise”, at market value, within a 10 day period.

However, the new regulations do not apply to listed registered managed investment schemes, offers of stapled securities or to platforms.

2. The new regulations have clarified that a PDS may only relate to one simple managed investment scheme. This will be a significant change for issuers who are used to preparing one PDS for multiple schemes.

3. The prescribed length of the PDS has been extended from the maximum length of six A4 pages to eight A4 pages and a lot of the proposed prescribed content of each of the mandatory sections in the PDS has been removed.
4. The information in the fees and costs table which will be required to be included in the shorter PDSs is now more closely aligned with the information required by the enhanced fee disclosure regime introduced in 2005. This addresses the numerous inconsistencies in fee disclosure contained in the draft regulations.
5. Importantly, there is no requirement to disclose an investment return objective which is spread above the rate of inflation. In addition, issuers must now include a product's specific risks rather than the proposed prescribed content about the generic risks applying to managed investment schemes.

Other significant proposals carried over

In addition, some of the more significant proposals from the draft regulations which were carried into the final form of the regulations include the following:

1. The PDS must contain a number of prescribed section headings, and each section must contain certain mandatory statements. Although the document can only be eight pages long, it must include a table of contents.
2. Additional information may be included by reference. Material can be posted to a website and a link included in the PDS. The material which is incorporated by reference is deemed to form part of the PDS.
3. Some of the mandatory disclosure includes—
 - (a) describing the role of the responsible entity and any investment manager
 - (b) statements about the type of investors for whom the product is intended to be suitable
 - (c) information about strategic asset allocation of investments, and
 - (d) statements about the investment return objective, the minimum suggested timeframe for holding the investment and the risk level of the investment.

Transitional arrangements

The regulations provide for a transitional period of two years for implementation. After the initial 12 month period, issuers have to comply with the new regime if they amend an existing PDS or offer new products requiring a PDS. After two years, all PDSs need to comply with the new regime.

Get ready to comply

All product issuers should consider how they are going to change their disclosure to meet the new regime. For most product issuers, the new regime will mean doing away with their multiple scheme single offer documents and replacing them with a shorter form PDS for each scheme.

Once again, complying with the complex fee disclosure requirements is going to be challenging, even though the fee and costs table in the shorter form PDSs should ostensibly be a summary of the current requirements.

Contact

If you need assistance to convert your current disclosure documents to the shorter form PDS, then please contact Chris Mee.



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Cutting of red tape

A new Bill (the *Corporations Amendment (Corporate Reporting Reform) Bill 2010*) has been passed by parliament and is awaiting royal assent. The Bill is intended to reduce red-tape affecting business and improve Australia's corporate reporting framework. The Bill was introduced after a two month consultation period that ended in February this year.

The key measures to reduce red-tape include—

1. significantly reducing the regulatory burden on companies limited by guarantee, which typically have a not-for profit purpose, by introducing a three-tiered differential reporting framework
2. streamlining parent-entity reporting
3. providing greater flexibility for companies to pay dividends, by replacing the profits test with a solvency-type test, and
4. allowing companies to more easily change their year-end date to minimise the burden on companies and their auditors during peak reporting periods.

Contact

For more information, please contact Emma Stapleton, a lawyer in our Funds Management team.



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Enhanced disclosure and further reforms

New regulatory policy

Further to our article in the December 2009 edition of *Corporate Advisor*, the Australian Securities and Investments Commission (ASIC) continues to expand the regime for disclosure for retail investors.

In April 2010, ASIC released Consultation Paper 133—*Agribusiness managed investment schemes: Improving disclosure for retail investors* (CP 133) and Consultation Paper 134—*Infrastructure entities: Improving disclosure for retail investors* (CP 134). ASIC intends to release a regulatory guide based on CP 133 in July 2010 (with an implementation date of 30 September 2010) and a regulatory guide based on CP 134 in September 2010.

Increased disclosure

The consultation papers build on the existing ASIC retail disclosure regime in place for mortgage schemes, unlisted property schemes and debenture issuers. The underlying principle of ASIC's retail disclosure regime is disclosure to investors on an "if not, why not" basis against a range of benchmarks determined by ASIC. That is, disclosure must be made against each benchmark and, where a product issuer does not meet a benchmark, an explanation must be given as to why the benchmark is not being met.

Benchmarks in CP 133 and CP 134 include the following:

1. Fee structure (CP 133).
2. Financial position of the responsible entity and use of funds raised (CP 133).
3. Funding, assumptions and sensitivity analysis (CP 134).
4. Portfolio diversification (CP 134).

Further changes

Given the increased rate at which ASIC is releasing consultation papers and implementing regulatory policy for disclosure to retail investors, in our view, it is only a matter of time before ASIC extends the regime to include a much wider range of financial product issuers, including equity fund managers.

It has also been our recent experience that ASIC is applying aspects of the benchmarks in CP 133 to other products. In particular, ASIC has sought further disclosure about the underlying financial position of the responsible entity in one case. As such, we consider further amendments to the existing regulatory guides on disclosure for retail investors may be imminent.

Consequences

In preparing, or updating, any disclosure document, product issuers must ensure there is effective disclosure against the benchmarks for the particular product to ensure ASIC does not query the disclosure document. Product issuers should also consider disclosing against any benchmarks which are included in regulatory policy for other products which may be relevant to retail investors.

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Australian Consumer Law—unfair terms in contracts

Timing

From 1 July 2010, the Australian Consumer Law (ACL) unfair contract terms provisions will commence. The effect of the provisions is that unfair terms in standard form consumer contracts will be rendered void.

Scope

These provisions will affect **standard form** contracts which are—

1. with an individual who has acquired the goods or services wholly or predominantly for personal, domestic or household use or consumption, and
2. contracts for—
 - (a) the supply of goods or services
 - (b) the sale or grant of an interest in land, or
 - (c) the supply or possible supply of financial products or services.

The contract need not be in writing and can include an agreement over the phone or via the internet.

Standard form

The ACL does not define 'standard form contract'. However, the Australian Competition and Consumer Commission has stated that, as a general guide, a contract which has been prepared by one party to the contract and is not subject to negotiation between

the parties (that is, offered on a 'take it or leave it basis'), will be a standard form contract. A number of industries typically use standard form contracts, for example, finance, domestic building, gyms, motor vehicles, travel, telecommunications and utilities.

Unfair

A term of a consumer contract will be unfair if—

1. it would cause a significant imbalance in the parties' rights and obligations arising under the contract
2. it is not reasonably necessary in order to protect the legitimate interests of the party who would be advantaged by the term, and
3. it would cause detriment (whether financial or otherwise) to a party if it were to be applied or relied on.

The provisions will apply to all standard form consumer contracts renewed, varied or entered into on or after 1 July 2010.

Contact

If you would like some advice as to whether the provisions will apply to the contracts used by your business or assistance reviewing the terms of your standard form consumer contracts, then please contact Kristy Dorney, an associate in our Litigation and Risk Management team.



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ASIC is coming—are you ready?

Recent visits

Over the past few months, we have become involved in two Australian Securities and Investments Commission (ASIC) surveillance visits on responsible entities.

This is not surprising in light of some significant corporate failures in the managed funds arena during the past 12 months.

When a responsible entity applies to ASIC for a licence, many representations are made, and then even more are contained in the constitutions and compliance plans for the managed investment schemes once they are lodged with ASIC. All these representations may be tested by ASIC when it carries out a surveillance visit.

Preparation

The work required to prepare for a surveillance visit cannot be underestimated. In addition to conducting enquiries to confirm compliance with scheme constitutions and compliance plans, ASIC is also investigating compliance with the *Corporations Act 2001* generally, which is obviously a very broad surveillance mandate.

The regulator is therefore asking for a raft of information and documents about compliance with statutory requirements including AFS licence conditions, professional indemnity levels, conflicts management rules and continuous disclosure laws.

It is now opportune to review all your compliance systems and procedures as well as being satisfied you are meeting the requirements of your scheme constitutions and compliance plans. In order to help you protect one of the most valuable assets a responsible entity holds—its licence—we have developed a service which provides the following benefits to responsible entities:

1. The service will prepare you for an ASIC surveillance visit, and give you confidence you are ready when ASIC arrives.

2. It will provide you with tangible evidence of your commitment to compliance.
3. It will provide you with practical recommendations on how to address deficiencies (if any) or better represent the compliance systems you are using. Often compliance systems and a compliance culture are present in an organisation, but are not visible or are not properly articulated.

Contact

For more information about this service, please contact Chris Mee.



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Funded representative actions

The Australian Securities and Investments Commission has released interim class order relief (CO 10/333) to lawyers and funders involved in legal proceedings structured as funded representative proceedings and funded claims lodged with liquidators to prove in the winding up of an insolvent company.

The relief, which will apply until 30 September 2010, is in relation to requirements under Chapter 5C and Chapter 7 of the *Corporations Act 2001*, as these arrangements would otherwise be caught by the definition of 'managed investment scheme'. It is intended that the relief will allow time for the implementation of a new legislative and policy regime that amends the definition of managed investment scheme to exclude these types of arrangements.

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Compensation from officers of responsible entities

Compensation from directors and officers of responsible entities

The Federal Court of Australia was recently asked to consider whether unitholders in a managed investment scheme could sue officers of a responsible entity for compensation for breaches of duties under the *Corporations Act 2001* (Act).

The action before the Court is a class action brought by a number of unitholders in a property trust (formerly the MFS Premium Income Fund) (Fund). The unitholders allege the officers of the responsible entity breached their duties to unitholders because they had failed to exercise reasonable care and diligence and to act in the best interests of the unitholders by allowing the responsible entity to enter into a number of transactions which depleted the Fund's assets and diminished the value of the units in the Fund.

On 14 May 2010, the court confirmed the unitholders have standing to sue the officers of the responsible entity for compensation, thereby allowing the unitholders to continue with their claim.

The law

Chapter 5C of the Act imposes duties on responsible entities and officers of responsible entities. The Act also allows a responsible entity or ASIC to seek compensation for any damage suffered by the managed investment scheme.

The unitholders in the class action are relying on a general provision in the Act which allows the court to make a compensation order against someone who has breached the Act in favour of a person who has suffered damage.

Finding

The defendant officers attempted to argue that only ASIC or the responsible entity could seek compensation directly from the officers of the responsible entity. The court rejected this argument and found the general provision on which the unitholders rely does give them standing to sue the officers directly for compensation.

Conclusion

This finding is important to all former and current officers of responsible entities as it confirms that officers of responsible entities are directly accountable to unitholders for their conduct in relation to the operation of the scheme.

It is imperative that officers of responsible entities familiarise themselves with their duties under the Act to ensure they perform those duties to the required standard and minimise exposure to potential compensation claims from unitholders. They should also ensure the responsible entity has adequate insurance in place to cover them in the event of a claim.

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For more information, please contact Allana Agnew, a lawyer in our Litigation and Risk Management team.



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Extension of hardship relief for frozen funds

The Australian Securities and Investments Commission (ASIC) has recently extended the relief which allows operators of frozen mortgage funds to permit withdrawals on the grounds of hardship to include funds that are in the process of being wound up. Previously, the relief only applied where the fund was a going concern.

The applicable hardship grounds are the same as those in the existing relief. This means the operator must be satisfied the member meets one of the following criteria:

1. The member is unable to meet reasonable and immediate family living expenses.
2. Compassionate grounds (e.g., medical costs for serious illness, funeral expenses or to prevent foreclosure).
3. Permanent incapacity.
4. The member is unemployed for at least three months, without other means of support.

Under the relief, a member is able to make up to four hardship withdrawals per calendar year to a cap of \$100,000.

To take advantage of the relief, operators of frozen funds which are in the process of winding up will need to apply to ASIC.

ASIC has also released information to better inform investors in frozen funds about their rights in relation to the freezing of funds and to confirm which entities have received relief to assist in the redemption of funds.

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McMahon Clarke Legal debt recovery services

One of the most common difficulties businesses face is managing cash flow. Too often, late payment from customers or clients cripples the ability of a business to pay its own debts.

McMahon Clarke Legal (MCL) has developed a fast, cost effective debt recovery system that can help you manage your receivables and cashflow.

Our focus

At MCL, we focus on—

- certainty of fees
- speed of delivery
- competitive rates, and
- quality of service.

Our services

If you engage our services, then—

- you will know what our fees will be before they are incurred
- your instructions will be acted on immediately, and
- you will have a solicitor in control of your matter at all times.

Our fees

We offer fixed fee arrangements with volume discounts for all recoveries where the debtor does not dispute the debt. Our fixed fees apply from sending a letter of demand to completing bankruptcy or winding up proceedings so that you know what you will pay throughout the process. We actively encourage debtors to be open about their financial capacity and we are available to you to offer sound commercial advice to assist you in your decision making in circumstances where debtors wish to enter into some form of payment plan.

Our fees (excluding GST and outlays) for sending a letter of demand start at \$40 per demand and our fees for commencing court proceedings start at \$200.

Contact

For a copy of our complete fee schedule or to discuss our services in more detail, please contact Nathan Shaw, an associate in our Litigation and Risk Management team.



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