Delete the current section 1.5 and insert the following replacement section 1.5

1.5 Further reforms

There have been a number of inquiries into the regulation of managed investment schemes since the Managed Investments Act 1998 was enacted.

The first inquiry was in 2001 which made a number of recommendations. None of the recommendations were implemented at that time.

On 1 August 2008, the Commonwealth Government released an issues paper in relation to non-forestry managed investment schemes which considered the costs and benefits of managed investment schemes from an economic, environmental and social perspective. This inquiry did not result in any specific recommendations or come to any clear conclusions.

Following a number of high-profile collapses of a number of agribusiness managed investment schemes, in May 2009, the Parliamentary Joint Committee on Corporations and Financial Services (“Joint Committee”) held an inquiry into agribusiness managed investment schemes and issued a report in September 2009. The Joint Committee made three recommendations. The only recommendation that has been implemented following this inquiry is the requirement for disclosure of the qualifications and accreditation of third parties. ASIC, in a Regulatory Guide, now requires disclosure against a benchmark on a “if not – why not” basis about the independence and qualifications of experts engaged by the responsible entity which also sets out various requirements in order to meet this benchmark.

In October 2010, the Consumer Advisory Panel (“CAP”), which represents a diverse range of consumer and investor interests with whom ASIC consults, commissioned independent research into the social impacts of consumers and investors not being fully compensated for financial loss, such loss arising from their AFS licensee’s misconduct. This included investors who had invested in managed investment schemes. One of the findings was that the loss experience of investors can have a corrosive effect on trust in the financial system. It was also a conclusion of the review into compensation arrangements for consumers of financial services that uncompensated losses associated with the failure of managed investment schemes can have serious consequences for affected retail clients and may also detract from

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5 Ibid at pp 46, 47 and 65.
6 ASIC Regulatory Guide RG 232 at paras 232.12 and 232.66 to 232.75.
their confidence in the financial services sector.\(^8\) The OECD has also identified the importance of the confidence of investors to the financial system.\(^9\)

Investor confidence was particularly adversely affected by the collapse of a number of high-profile agribusiness schemes. These failures highlighted a number of difficulties with the current structure of managed investment schemes when financial stress occurs. As a result, the Corporations and Markets Advisory Committee ("CAMAC") was given the task of undertaking a more comprehensive review of the law regulating managed investment schemes.

In June 2011, CAMAC issued a discussion paper ("Stage 1 Discussion Paper"). This paper suggested some changes that could be made to the current law which CAMAC was of the view would correct some of the problems that had occurred in practice as identified in that report.\(^10\)

After extensive consultation, CAMAC issued a report ("CAMAC Report").\(^11\) This report recommended a completely new approach to the operation of registered managed investment schemes. CAMAC named this approach the "Separate Legal Entity (SLE) Proposal" ("SLE Proposal").\(^12\) CAMAC also proposed a prohibition on enterprise schemes.\(^13\)

In March 2014, CAMAC issued a further discussion paper ("Stage 2 Discussion Paper").\(^14\) The basic tenor of the Stage 2 Discussion Paper is that the regulatory regime for managed investment schemes should be aligned with the regulatory regime for companies unless there are compelling reasons for treating schemes differently from companies.\(^15\) CAMAC was therefore, up until the time of its current proposed abolition, examining possible reforms that could be made in areas where such alignment in the regulatory regimes could be made.

The CAMAC Report, together with the Stage 2 Discussion Paper, proposes radical changes to the regulation of managed investment schemes. Even if the government could be persuaded to consider such reforms, it will be a long hard road to achieve that result. Given the lack of action in relation to an earlier Turnbull Report in 2001,\(^16\) one cannot have a lot of confidence that any legislative change will be made, despite all of the problems in the regulation of managed investment schemes thrown up by the general financial crisis. For example, the Turnbull Report recommended excluding class actions and costs paid for legal proceedings from the definition of "managed investment scheme".\(^17\) However, it took approximately 10 years for this recommendation to be implemented.\(^18\) The amendments to the law were probably only made because the government bowed to industry pressure for

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\(^10\) Ibid at para 1.6.2 and ch 3.

\(^11\) Ibid at para 1.6.1.

\(^12\) Ibid at para 1.6.1.

\(^13\) Ibid at para 1.6.1.


\(^16\) Ibid Recommendation 17 at para 5.2.3.

\(^17\) Ibid at para 1.9.2.

\(^18\) Corp Regs, reg 5C.11.01, inserted by *Corporations Amendment Regulation 2012 (No 6) (Cth)* (SLI No 172 of 2012) 12 July 2012.
reform following a decision of the Federal Court where it was held that a litigation funding scheme constituted a managed investment scheme.\(^{(19)}\)

The primary problem with changing the current legal framework for managed investment schemes is that this framework is driven by tax issues.\(^{(20)}\) The SLE Proposal will require amendments to the tax laws, in addition to amendments to the Corps Act because the primary driver of the managed investment scheme statutory construct is the “flow through” effects for taxation purposes such as is the case with trusts and agribusiness schemes.

Although CAMAC did recognise that the SLE Proposal would also require amendments to the tax laws, both to exempt the transfer of title to assets from the responsible entity to the managed investment scheme from stamp duty and other tax consequences, and to ensure the ongoing “flow through” tax treatment of schemes once they are converted to the SLE structure,\(^{(21)}\) CAMAC failed to deal with what changes would be necessary to the taxation laws to enable its proposals to work.

In addition, as part of the 2014-2015 budget, the government announced its decision to cease the operation of CAMAC and its legal committee. As a result, CAMAC is no longer operating.\(^{(22)}\) even though the Bill to effect its abolition is yet to be passed.\(^{(23)}\) This may result in the loss of impetus for reform.

Nevertheless, the Senate Economics Reference Committee has recognised the valuable contribution to the reform agenda which gives some hope for reform despite the abolition of CAMAC. In a report into agribusiness managed investment schemes, the Committee stated that it was strongly of the view that the valuable work produced by CAMAC in relation to managed investment schemes in 2010, especially in relation to the very difficult problems of dealing with managed investment schemes which are in financial stress, provides an ideal starting point for reform.\(^{(24)}\) The Committee in fact recommended “… that the government use CAMAC’s report on managed investment schemes as the platform for further discussion and consultation with the industry with a view to introducing legislative reforms that would remedy the identified shortcomings in managing an MIS in financial difficulties and the winding-up of collapsed schemes”.\(^{(25)}\)

The two major reforms proposed by CAMAC are as follows:

1.5.1 Ban on future common enterprise schemes

CAMAC has recommended that there should be a prohibition on the creation of new common enterprise schemes.\(^{(26)}\) This recommendation would prevent the raising of funds for agribusiness schemes which is an alternative source of fundraising for this sector of the economy. No alternative is proposed to replace these structures which only work from a taxation perspective because of their current structure. It is not clear from the CAMAC Report whether or not their SLE proposal is intended in some way

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\(^{(19)}\) Brookfield Multiplex Ltd v International Litigation Funding Partners Pte Ltd [2009] FCAFC 147

\(^{(20)}\) See section 19.1 herein at p 315.

\(^{(21)}\) Above n 11 at p 57.

\(^{(22)}\) CAMAC Corporate Plan, 2015, at section 1.

\(^{(23)}\) Statute Update (Smaller Government) Bill 2017 (Cth), Sch 7.

\(^{(24)}\) Senate Economics Reference Committee Report, Agribusiness Managed Investment Schemes – Bitter Harvest, 2016, at p xxvi.

\(^{(25)}\) Ibid Recommendation 20 at para 15.51.

\(^{(26)}\) See above n 11 at ch 3.
to accommodate these forms of schemes. Under current tax laws, the SLE Proposal will not allow for the current tax treatment of agribusiness schemes to apply.

When Div 394 was introduced, the government said that “[t]he objectives of the legislation is to direct investment to commercial plantation forests, to help achieve the industry’s goals as set out in Plantations for Australia: the 2020 Vision”.(27)

Also the Joint Committee said in relation to the Div 394 provisions “[a]lthough the committee recognises that there is a vigorous debate over whether the goal of trebling Australia’s plantation output by 2020 has a sound economic basis, the inherent disincentives to invest in forestry warrant the retention of the existing arrangements”.(28)

CAMAC fails to recommend any alternative to reconcile the objectives of this legislation with the proposed ban on these schemes.

Further, the recommendation is inconsistent with the Joint Committee recommendation that these provisions should be given time to work.(29)

The recommendation to ban these schemes, without offering an alternative, is a major deficiency in the CAMAC Report. While it might be possible to accommodate these provisions in the SLE Proposal with appropriate accompanying tax measures, nothing is stated in the CAMAC Report about this. Rather, the discussion around tax amendments appears to only concern passive types of investment schemes.

Arguably the Future of Financial Advice (“FOFA”) reforms contained in Chapter 7.7A of the Corps Act, particularly the prohibition on financial advisers accepting conflicted remuneration, will correct many of the problems that have arisen in relation to common enterprise schemes.

In any event, retail investors should take some responsibility for their own affairs, rather than simply investing because of the tax deductions provided by the product without consideration of the consequences of doing so. This has been recognised by the NSW Supreme Court in one decision.(30)

Further, one may have some doubts as to the claims by investors in this sector. The former Chief Justice of the NSW Supreme Court had doubts about accepting what he called “ex post facto protestations of reliance on financial representations” and the “hindsight bias of an investor who has made a loss in a tax driven scheme”.(31)

To impose an outright prohibition is to unnecessarily restrict fundraising for the agribusiness sector.

1.5.2 Separate Legal Entity (SLE) Proposal

CAMAC proposed an alternative approach to the legal framework for schemes, based on making the managed investment scheme a separate legal entity, rather than the responsible entity, the principal to agreements forming part of the scheme and the

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28 Above n 2 at para 3.125.
29 Ibid at para 3.126.
30 Tomasetti v Brailey [2011] NSWSC 1446 at [817]-[818].
holder of legal title to scheme property. It proposed this to overcome many of the
problems which it raised in its discussion paper as an alternative to reforms that
would have sought to improve, but nevertheless maintain, the current legal framework
for schemes.  

This is a radical proposal not raised in the Stage 1 Discussion Paper. There is no
doubt that ASIC had issues with enterprise schemes and in its submission to CAMAC,
ASIC separated its submissions on various issues between how the proposals
impacted on enterprise schemes and on pooled asset schemes.

However, the proposal does correct some of the problems raised in the earlier
discussion paper and, subject to overcoming the tax issues, would be a good reform.
Effectively by treating each scheme as a separate legal entity liabilities and scheme
property will be ring fenced within each particular scheme.

Constituting the managed investment scheme as a separate legal entity would still
require that separate legal entity to act through the responsible entity as its agent and
would not have a directing mind or will, or capacity to act in its own right. Accordingly,
it would not have any directors or employees.

The responsible entity’s role under the new arrangement would be to:

- act as the manager of the scheme for the purpose of operating it on a day-to-
day basis; and
- act as the agent for the managed investment scheme for the purpose of
  binding the managed investment scheme, as principal, in agreements entered
  into by the responsible entity in its managerial role.

If the SLE Proposal was adopted the following changes would occur in relation to the
legal structure of a registered managed investment scheme flowing from such a
scheme being an entity in its own right.  

32 Above n 11 at 3.2 p 46.
34 See Chapter 6 for a fuller discussion of these provisions.