



ASIC

Australian Securities & Investments Commission

REGULATION IMPACT STATEMENT

Agribusiness managed investment schemes: Improving disclosure for retail investors

January 2012

About this Regulation Impact Statement

This Regulation Impact Statement (RIS) addresses ASIC's proposed policy on agribusiness managed investment schemes (agribusiness schemes) to improve disclosure to retail investors, while maintaining the flexibility of the public fundraising process.

What this Regulation Impact Statement is about

- 1 This Regulation Impact Statement (RIS) addresses the proposed policy of the Australian Securities and Investments Commission (ASIC) on disclosure for agribusiness managed investment schemes (agribusiness schemes). This follows a consultation paper published in April 2010 setting out our proposals and supporting rationale for clarifying the content requirements for disclosure documents related to agribusiness schemes: see Consultation Paper 133 *Agribusiness managed investment schemes: Improving disclosure for retail investors* (CP 133). A summary of the submissions made in response to CP 133 and our consideration of those responses can be found in Report 273 *Response to submissions on CP 133 Agribusiness schemes: Improving disclosure for retail investors* (REP 273).
- 2 We initiated this work because we have concerns about the quality of disclosure available to retail investors in agribusiness schemes. We have reached our views based on the risks highlighted following the failure of large operators of agribusiness schemes and reviews of Product Disclosure Statements (PDSs). The conclusions that we have drawn from these is that many PDSs currently in use for agribusiness schemes do not adequately explain the way agribusiness schemes work, and the risks associated with investing in them. This has resulted in retail investors investing in these schemes without an adequate understanding of the risks.
- 3 The regulatory framework in the *Corporations Act 2001* (Corporations Act) (outlined in paragraphs 35–44) is intended to provide adequate disclosure about financial products, including the offer of interests in agribusiness schemes. In meeting this regulatory framework, a product issuer must provide information to prospective investors. We are concerned that the current disclosure practices are not resulting in documents that clearly and adequately discuss the risks associated with investing in agribusiness schemes in accordance with the law.
- 4 If investors are better informed about the risks involved in the investments they are about to make, they are better equipped to make an investment decision that suits their needs and future circumstances. We consider that better investment decisions can be made when investors receive clear, concise and effective disclosure about key risks and structural issues associated with these schemes.
- 5 The agribusiness scheme market has a value of about \$8 billion. The recent collapse of large and small responsible entities has resulted in both a monetary and a future confidence cost. Debt and equity market turbulence since late 2007 has also increased the financial stress in the agribusiness scheme sector. Together, these factors are likely to result in an increase in the cost of raising capital through agribusiness schemes (i.e. investors may demand a greater risk premium).

- 6 Our overall aim is to improve disclosure to retail investors to help them understand and assess whether these schemes are appropriate for them, while maintaining the flexibility of the public fundraising process. This aligns with ASIC's strategic priorities, including promoting:
- confident and informed investors and financial consumers; and
 - fair and efficient financial markets.
- 7 In developing our final position, we have considered the regulatory and financial impact of our proposals. We are aiming to strike an appropriate balance between:
- disclosure that assists investors to make better-informed decisions about investing in agribusiness schemes in accordance with the law;
 - not unduly interfering with the market and the flexibility of the public fundraising process; and
 - promoting efficiency in the capital markets.
- 8 This RIS sets out our assessment of the regulatory and financial impacts of our proposed policy and our achievement of this balance. It deals with:
- the likely compliance costs;
 - the likely effect on competition; and
 - other impacts, costs and benefits.

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A Introduction

Background

What is an agribusiness scheme?

- 9 For the purposes of our proposals, an agribusiness scheme is a primary production operation that pools investors' interests into a common enterprise using the legal structure defined in the Corporations Act as a 'managed investment scheme'.
- 10 Traditionally, the industry has distinguished between those agribusiness schemes that operate forestry plantations and those involved in non-forestry activities. Forestry scheme refers to plantation forestry projects which may be ready to harvest between eight and 25 years, necessitating a long period between investment and return. Non-forestry scheme activities are primarily focused on horticultural enterprises, but also include other primary industries, such as beef cattle, aquaculture and poultry. The wait for a return on investment from these schemes differs depending on the type of produce, but is less than for forestry schemes. However, these schemes are more labour and capital intensive in comparison.

The agribusiness scheme market

Role of Government

- 11 In 1997, the Government (federal and states) formed the initiative 'Plantations for Australia: The 2020 Vision' in an effort to strengthen the forestry plantations industry through industry and government commitment to plantation development. The key goals of the initiative were to increase plantation timber output to service Australia's and global demand for paper and, in so doing, provide economic benefits such as jobs and revenue. The Government recognised that the central impediment to plantation investment was that an investment in plantations would not produce revenue for between 8 and 25 years. In order to stimulate private ownership of forestry plantations, the Government established arrangements in the form of immediate tax deductibility to investments in forestry plantation projects to encourage investments. The tax benefit was only available if the project met a minimum direct investment test.
- 12 In response to government initiatives, the industry started to structure forestry investments using the managed investment scheme structure. These structures have now taken over as a leading form of plantation landownership, accounting for approximately 34% of total plantations in Australia.

Agribusiness scheme operators

- 13 We noted in our submission to the Parliamentary Joint Committee on Corporations and Financial Services' *Inquiry into aspects of agribusiness managed investment schemes* in 2009 that, at that time, 416 agribusiness schemes had been registered by 70 different responsible entities and, taking into account schemes that had been deregistered or wound up, there were 371 agribusiness schemes registered to operate in Australia. These 371 were divided as follows:
- (a) 198—forestry schemes;
 - (b) 162—horticultural schemes; and
 - (c) 11—other categories of agribusiness schemes.
- 14 We assessed the various horticultural schemes that had been registered, and the majority were involved in the production of grapes (45%), almonds (16%) and olives (14%).
- 15 We estimate that, since the introduction of the managed investments regime in 1998, agribusiness schemes have raised over \$8 billion. In the past seven years, over \$5 billion has been invested in agribusiness schemes by over 75,000 investors. Of this, forestry schemes represent \$3.7 billion and non-forestry schemes represent \$1.3 billion.
- 16 Forestry agribusiness scheme operators have sought to diversify and vertically integrate their operations. To diversify, scheme operators have commenced producing higher value timber used in construction (such as teak and mahogany). This timber has a different time profile and may take around 20 years to produce harvestable product, but investors receive revenue from trimmings at around 8–12 years into the project. Some forestry agribusiness scheme operators have also vertically integrated their operations by developing pulp-milling operations.
- 17 The first non-forestry agribusiness schemes commenced operation around 1997–98, but increased significantly in 2004 due to heavy expansion by existing agribusiness scheme operators. Non-forestry agribusiness schemes have focused on horticultural crops, such as wine grapes, almonds and olives. Other non-horticultural agricultural investments were structured to give investors exposure to livestock projects, such as cattle and chicken, and aquaculture products, such as abalone and pearls.
- 18 Like forestry agribusiness schemes, a number of these schemes were also structured around a tax benefit received at the point of initial investment, subsequent contributions, and then revenue often commencing after 4–5 years (when the crops reach maturity). PDSs are generally open for investment for a shorter period of time compared to other managed investment schemes (i.e. in the lead-up to the end of the financial year).

Agribusiness scheme investors

- 19 Research from Australian Agribusiness Group (AAG)¹ has found that fewer than 2,500 investors contributed \$103 million to agribusiness schemes in 2010—a 59% fall from the \$250 million raised in 2009. Investors contributed an average of \$67,400 (with 38% gearing) in 2010, compared with \$31,400 (and 62% gearing) in 2009. In the 2010–11 financial year, AAG estimates that the agribusiness sector raised \$36 million, representing a decrease of 65% from the previous year. Investors contributed an average of \$62,700, with 44% gearing the investment.²
- 20 In the 2010–11 financial year, there were 10 PDSs issued for new agribusiness schemes. In the past two years, approximately 46 different agribusiness schemes were promoted. We would expect the number of PDSs to increase in future years if confidence in the sector improves.

Business models of agribusiness schemes

- 21 Agribusiness schemes pose particular risks, as detailed in Table 1, because, unlike many other types of managed investment schemes, they do not generally use a traditional unit trust structure. For tax reasons, many agribusiness schemes are structured so that investors are taken to operate their agribusiness investment in their own right. Investors enter into contracts with the responsible entity or other parties to perform all the cultivation and management activities associated with the investor's agribusiness enterprise.
- 22 An investment in an agribusiness scheme is not a liquid investment. An investor cannot easily exit and therefore remains a member for the term of the scheme. Our experience also shows that the contractual nature of the investment means that the scheme's financial reports provided to investors contain less detailed performance and financial information than a traditional unit trust which has assets and liabilities that reflect the contributions of investors.
- 23 Table 1 explains the significant risks associated with an agribusiness scheme and shows how the risks associated with this type of scheme can be distinguished from common risks associated with other types of managed investment schemes. These are important because the law requires disclosure of information about significant risks.
- 24 Agribusiness scheme business models have some common features:
- (a) Investors or 'growers' enter into contracts with the responsible entity to cultivate, maintain and harvest the investors' agribusiness enterprise on their behalf. In doing so, investors acquire a right to derive profits from

¹ Australian Agribusiness Group, *Agribusiness MIS end of year round-up report 2009–10 financial year*, July 2010.

² Australian Agribusiness Group, *Agribusiness MIS end of year round-up report 2010–11 financial year*, July 2011.

agribusiness produce of the agribusiness enterprise (e.g. timber, wine grapes, olives and almonds), net of management and lease fees paid to the responsible entity, and net of rent and other expenses incurred in operating the agribusiness scheme.

- (b) Investors may also be entitled to potential tax deductions for the up-front investment and any annual fees paid to the responsible entity and its related parties, provided that they own their scheme interests for at least four years.
- (c) Fee structures differ among projects:
 - (i) Forestry schemes generally require an up-front fee from investors, and the responsible entity receives a rental and management fee out of the proceeds of the harvest (8–12 years later). Pre-2004, some forestry schemes contained annual fees to cover rent and management.
 - (ii) Horticultural schemes generally require an up-front fee from investors and either ongoing rental and management fees on an annual basis or rental and annual fees paid out of the net proceeds from harvests (available after four to five years when the crops reach maturity).
- (d) Investors often use leverage to maximise tax benefits. Finance may be originated by the responsible entity or related party, and either kept as an asset on the balance sheet of this entity or securitised to other financial intermediaries.
- (e) In some circumstances, annual sales of new agribusiness scheme products by the responsible entity provide fresh working capital to fulfil obligations to other agribusiness schemes sold in previous years and to secured creditors.

25 Critical to establishing a forestry agribusiness scheme is obtaining a product ruling from the Australian Taxation Office (ATO) to provide investors with greater certainty about the tax benefits of the scheme. In obtaining a product ruling, the responsible entity must provide the ATO with information supporting the expected profitability of the project. This includes cash flow forecasts, budgeted profit and loss statements, expert reports supporting those forecasts and proposed marketing materials for the scheme.

26 In order to ensure the agribusiness scheme makes a significant contribution to primary production, the ATO sets minimum forestry and horticultural expenditure requirements for a person's investment to obtain a tax deduction. The ATO makes an express representation in every product ruling it issues that it does not sanction or guarantee the agribusiness scheme.

27 Non-forestry agribusiness schemes are more labour and capital intensive. Non-forestry schemes will also generally provide some income before the crops are fully ready for harvest. Horticultural schemes (almonds, wine grapes and olives) are marketed in Australia as being fully income producing after five years. They then have an average revenue-producing life of up to 22 years.

Key risks of agribusiness schemes

- 28 The risks of investing in various types of agribusiness schemes have been highlighted since 2008. Six large operators of agribusiness schemes have failed³ since that time.
- 29 Before releasing CP 133, we consulted with stakeholders about the key risks for retail investors in the agribusiness scheme sector, and about the ways in which these risks might be addressed. The risks faced by retail investors in agribusiness schemes include those shown in Table 1.
- 30 The collapse of Great Southern Managers Australia Limited and, subsequently, Timbercorp Securities Limited were considered by the Parliamentary Joint Committee on Corporations and Financial Services' *Inquiry into aspects of agribusiness managed investment schemes* (PJC), resulting in a recommendation that agribusiness schemes be required to disclose the qualifications and accreditation of third parties who provide expert opinions on likely scheme performance. The proposals outlined in this RIS seek to address this recommendation.
- 31 The PJC also recommended that ASIC should impose a licence condition on responsible entities of agribusiness schemes, requiring them to have sufficient working capital to meet current obligations.
- 32 We have reviewed ASIC Regulatory Guide 166 *Licensing: Financial requirements* (RG 166)—and released a draft updated version of RG 166 (draft RG 166), which forms Appendix 1 to Report 259 *Response to submissions on CP 140 Responsible entities: Financial requirements* (REP 259)—amending the levels of financial resources required to provide financial services as a responsible entity. This work has been the subject of a separate RIS.
- 33 Our inquiries have highlighted a number of issues surrounding the structure of agribusiness schemes, and concerns have been raised about whether disclosures used to promote agribusiness schemes are robust enough to adequately protect investors' interests as required by law.
- 34 As a result of the work we have undertaken, we consider that it is appropriate to provide guidance to this sector to address the problems associated with insufficient or unclear disclosure to retail investors.

³ Environinvest Limited, Timbercorp Securities Limited, Great Southern Managers Australia Limited, FEA Plantations Limited, Rewards Projects Limited and Willmott Forests Limited.

Table 1: Key risk features of agribusiness schemes

Risk feature	What this means
Fee structures	<p>An up-front fee structure creates uncertainty surrounding the ability of the responsible entity to fulfil its obligations owed to agribusiness scheme investors well after investments are initially made.</p> <p>Liquidity may be at risk because of a mismatch between cash flows from investors and the expenses of the agribusiness scheme. This fact is not highlighted in current disclosure practices. This also creates the risk of the responsible entity becoming dependent on increasing growth in new managed investment schemes to fund operations. Generally, fee structures in unit trusts (as opposed to contract-based agribusiness schemes) enable the responsible entity to draw a fee on a regular basis from the net assets of the scheme.</p> <p>Agribusiness schemes generally have limited assets (as the investor generally owns the assets that produce the return) and therefore the responsible entity is reliant on the investor's up-front fee payment and any ongoing contributions (if any) to the scheme or its own assets to fund the operation of the agribusiness scheme.</p>
Adequacy of capital	<p>A lack of cash flow from investors for working capital purposes due to the up-front fee structure or the failure by investors to meet ongoing fee obligations increases the risk that the responsible entity will not be able to fulfil its obligations owed to agribusiness scheme investors because the scheme does not have sufficient assets from which the responsible entity can draw to operate the scheme. This risk is related to the 'fee structures' risk, and the difference between agribusiness scheme and unit trust structures is detailed above.</p>
Lack of information	<p>Some agribusiness schemes involve a significant time lag between the commencement of the scheme and the time that revenue is produced. Investors therefore need updated information on the status of the agribusiness scheme and its assets so they can assess whether performance is in line with expectations.</p> <p>Most unitised managed investment schemes will produce revenue on a more regular basis and generally report to members of the scheme while making revenue distributions. As agribusiness schemes—in particular, forestry schemes—may not realise any revenue until many years after the scheme has commenced, this risk is particularly apparent for these schemes.</p> <p>Further, financial reports for agribusiness schemes generally provide little information because there may be no assets, or negligible assets, on the balance sheet of the scheme, and investors are reliant on information outside of these reports for information on the status of their investment.</p>
Reliance on experts	<p>The success of an agribusiness scheme is dependent on a wide range of factors that the responsible entity may not have expertise in, such as soil suitability, horticultural or forestry practices, and the suitability of different varieties of produce to particular regions or for particular purposes.</p> <p>Opinions from experts with experience and knowledge of the underlying commodity, its geographical location, product yields and markets, and agricultural factors affecting the agribusiness scheme are generally provided by the responsible entity in promoting the agribusiness scheme and are relied on by investors.</p> <p>Due to the specialist nature of the underlying product, opinions of the types provided in relation to agribusiness schemes are generally not provided for other types of managed investment schemes.</p> <p>If opinions are not prepared by suitably qualified and independent experts, it is difficult to assess the level of reliance that can be placed on such opinions.</p>

<p>Service providers and related parties</p>	<p>Agribusiness schemes tend to rely on a range of service providers to carry out the agribusiness enterprise. Some agribusiness schemes transact with associated companies or businesses to provide these services. There is an increased risk that agreements entered into with an associated company by the responsible entity on behalf of the agribusiness scheme are not properly approved, nor adequately reviewed and monitored.</p> <p>Frequently, related party service providers lack accountability and are not independently assessed on a regular basis to ascertain financial strength or ability to provide the service. In some circumstances, responsible entities of these schemes have entered into transactions that appear not to be commercial or not to be on an arm's length basis.</p>
<p>Financing arrangements</p>	<p>Some responsible entities promote investors' ability to borrow funds to invest in order to attract investors, without adequately disclosing the terms and conditions. In some circumstances, responsible entities themselves provide the finance to investors to invest in a scheme.</p> <p>The finance is generally in the form of a full recourse financing arrangement, allowing the financier access to the assets of the investor. If a scheme were to collapse, an investor would generally continue to be liable under the financing arrangement. Some collapses of agribusiness schemes in recent years have resulted in no return, or only a small return, to investors.</p>
<p>Land, licences and water</p>	<p>Agribusiness schemes require access to a range of physical infrastructure and natural resources such as land, water and farming equipment. These assets are generally owned by either the responsible entity or entities other than investors. Investors or the responsible entity enter into arrangements to secure access to these resources.</p> <p>If rights to the land and water are not scheme property, there is a risk that they may not be available for use when required by the agribusiness scheme.</p> <p>Generally, other types of managed investment schemes will not be reliant on these types of contractual and legal obligations, which are specific to agribusiness schemes.</p>
<p>Counterparty risk</p>	<p>The ability of the responsible entity to fulfil its obligations to investors under the management agreement and various other contractual arrangements, and to meet its share of fees charged (if it owns interests in the agribusiness scheme), is dependent on the responsible entity's financial position. This may in turn depend on the financial position of the group to which the responsible entity belongs.</p> <p>In addition, investors are exposed to the ability of the responsible entity to continue to operate where, in some circumstances, there is limited cash flow to support its operation. In some cases, this results in the responsible entity borrowing to fund its operations or becoming reliant on other parties for financial support. In circumstances where there is insufficient cash flow from the agribusiness scheme, the responsible entity may be unable to meet its obligations under these arrangements, resulting in defaults under the various arrangements.</p>
<p>Replacement of the responsible entity</p>	<p>Investors face the risk that they may lose part or all of their investment when the agribusiness scheme's documents and contractual arrangements do not adequately provide for the responsible entity to be replaced (e.g. if the responsible entity has become insolvent or there are insufficient assets to meet the ongoing obligations of the agribusiness scheme).</p> <p>Due to the contractual obligations owed to investors in the agribusiness scheme, replacement of the responsible entity becomes a prominent risk, which is not present in a unitised managed investment scheme.</p>
<p>Liquidity</p>	<p>Investors are unable to exit the scheme until the scheme has concluded. There is no established secondary market or withdrawal procedures offered for these types of schemes, and therefore the investor is liable for their interest for the term of the scheme, which could extend over a long period of 10 years or more. The uncertainty can affect investors whose personal circumstances can change substantially over the duration of the scheme.</p>
<p>Nature of the product</p>	<p>Agribusiness schemes by their nature carry an inherent risk because they are prone to environmental factors generally beyond the control of even the best endeavours of the responsible entity. Predicting returns for growing new products can be very uncertain, both as to the crop return and the potential market for the product.</p>

Current regulation of agribusiness schemes

- 35 The offer of interests in agribusiness schemes is regulated under the Corporations Act—all sections (s), chapters (Chs) and parts (Pts) referred to in this RIS are from the Corporations Act unless otherwise stated. An interest in an agribusiness scheme is a financial product, so the obligations for the offer of financial products in Pt 7.9 apply to the offer of interests in agribusiness schemes, including the requirement to prepare a PDS for the offer of interests in the scheme, ongoing disclosure obligations and requirements on advertising and publicity for the offer of interests.
- 36 In addition, Ch 5C imposes various requirements on agribusiness schemes, including (where applicable) the requirement to be registered as a managed investment scheme, to be operated by a responsible entity that holds an Australian financial services (AFS) licence, and to have a scheme constitution and compliance plan.

PDS disclosure

- 37 The Corporations Act requires disclosure in the form of a PDS for an offer of interests in an agribusiness scheme to retail investors. The PDS must:
- (a) be worded and presented in a clear, concise and effective manner (s1013C(3));
 - (b) make specific disclosures (s1013D), including among other things about the significant risks associated with holding the product; and
 - (c) include all other information that might reasonably be expected to have a material influence on the decision of a reasonable person (when investing as a retail client) about whether or not to invest in the product (s1013E).
- 38 The general PDS content requirement in s1013E is designed to:
- (a) promote efficiency in the capital markets;
 - (b) promote disclosure of relevant information;
 - (c) reduce the likelihood of omitting important information;
 - (d) focus responsible entities on the information needs of investors; and
 - (e) be sufficiently flexible to accommodate changes in investors' information needs.

Ongoing disclosure

- 39 An agribusiness scheme operator also has obligations to provide ongoing disclosures to investors under the Corporations Act, including
- (a) disclosure of material changes and significant events (s675 and 1017B);
 - (b) notification of any material change to a matter that would be required to be specified in a PDS (s1017B); and
 - (c) periodic statements to members who acquired their interests as retail clients (s1017D).

Requirements for a compliance plan, compliance committee and compliance plan auditor

- 40 The Corporations Act requires registered managed investment schemes to have a compliance plan: s601EA. The compliance plan must set out adequate measures for the responsible entity to ensure compliance with the Corporations Act and the scheme's constitution: s601HA. The responsible entity has a duty to comply with the compliance plan: s601FC(1)(h).
- 41 A scheme must also have a compliance committee, unless at least half of the responsible entity's directors are external directors: s601JA. The functions of the compliance committee are to:
- (a) monitor the extent to which a responsible entity complies with the compliance plan and report its findings to the responsible entity;
 - (b) report any breach of the law or the scheme's constitution to the responsible entity;
 - (c) report to ASIC if the compliance committee considers that the responsible entity is not taking adequate action to deal with a matter reported to the responsible entity; and
 - (d) assess at regular intervals whether the compliance plan is adequate, to report to the responsible entity on the assessment and to make recommendations to the responsible entity about any changes that it considers should be made to the plan (s601JC(1)).
- 42 The auditor of a compliance plan must give the responsible entity a report that states the auditor's opinion on whether:
- (a) the responsible entity has complied with the compliance plan; and
 - (b) the plan continues to meet the requirements of the Corporations Act.

Restrictions on advertising

- 43 The Corporations Act provides restrictions on advertising and publicity for offers of interests in agribusiness schemes before and after interests are available for acquisition by retail clients: s1018A.
- 44 There are also general consumer protection provisions in the *Australian Securities and Investments Commission Act 2001* (ASIC Act), including prohibitions against misleading and deceptive conduct, as well as prohibitions against false or misleading representations.

ASIC's role in administering the law

- 45 We administer the law regulating agribusiness schemes, within the powers granted by the Corporations Act. This includes conducting surveillance and undertaking enforcement action in cases of any breach of the Corporations Act (as well as the ASIC Act).

- 46 While PDSs of agribusiness schemes are generally not required to be lodged with ASIC, and ASIC does not approve PDSs, we have powers to stop offers being made in a PDS if we are satisfied that:
- (a) information in a PDS is not worded and presented in a clear, concise and effective manner; or
 - (b) an offer of securities under a PDS contains a misleading or deceptive statement, or omits information from the disclosure statement that is required under the Corporations Act (s1020E).
- 47 In administering the law, we are able to exercise our regulatory powers without notice. However, it can be more effective and efficient to provide the market with specific and clear guidance on our views of the existing requirements of the Corporations Act as they apply to particular financial products. This approach informs the industry as a whole about our view of the requirements of the Corporations Act, rather than communication of these views on an individual basis, which can be disruptive to individual fundraising and inefficient for ASIC.

Identifying and assessing the problem

Retail investors' understanding of agribusiness structure and product

- 48 A combination of market dynamics, tax laws and government agricultural policy has contributed to managed investment schemes being the legal vehicle of choice for retail investment in agribusiness enterprises.
- 49 To give effect to the investment, investors enter into a number of contractual arrangements with the responsible entity and other parties to provide services in respect of their agribusiness enterprise. This is in contrast to unit trusts where scheme assets are operated in a pooled manner and divided into economic units.
- 50 Agribusiness schemes are synthetically structured around individual contracts so that investors are each allocated, for example, a designated allotment of land on which to operate their agribusiness enterprise. In substance, the responsible entities operate each investor's interest in the same manner as for all other investors, and the difference between one person's investment and another's is superficial.
- 51 Our reviews of PDSs in light of the recent collapses in the agribusiness scheme sector has highlighted to ASIC that current disclosure practices do not provide investors with sufficiently clear information about the risks associated with the contractual arrangements, structures and business models operated by responsible entities, including liquidity risks faced by the agribusiness schemes and responsible entities reliant on investors' ongoing fees to meet working capital obligations.

Sources of information

- 52 The existing regulatory framework in the Corporations Act is intended to provide adequate disclosure for the offer of interests in agribusiness schemes. This disclosure may change as the market changes and significant risks become apparent.
- 53 PDSs are not required to be lodged with ASIC, and ASIC is not required to review them before they are made available to investors. Once available to the market, the interests in the agribusiness scheme are generally only available for investment over a short time period of around four to five months. During this period, ASIC generally has a limited time to review the disclosure and, where this is considered inadequate, take further action to ensure that it is improved before the product is no longer available to the market.
- 54 Agribusiness schemes are often specific in their nature and, because of their inability to be traded and the time lags in producing returns, the PDS is likely to be the main source of information that investors receive with a degree of independence (i.e. in that responsible entities must include certain information by law). While there may be independent research reports from research houses, these are often commissioned by the responsible entities and rely on information provided by responsible entities.
- 55 In 2009, ASIC assessed the PDS for each of the 20 agribusiness schemes marketed in the lead-up to the end of the financial year. These reviews resulted in improved disclosure for 12 schemes operated by the seven largest participants in the sector. Each operator was required to provide additional disclosure of:
- (a) the risks faced by investors that their investment might be adversely affected if the responsible entity (or its ultimate parent) encounters financial difficulty;
 - (b) the risks associated with the agribusiness scheme operator's reliance on annual agribusiness scheme sales to provide working capital; and
 - (c) information about poor past performance from other similar managed investment schemes run by the operator.
- 56 In 2010, ASIC reviewed all eight PDSs issued for agribusiness schemes in the lead-up to the end of the financial year, resulting in improved disclosure for three of these schemes through the issue of supplementary PDSs in respect of:
- (a) the timing of returns from the scheme;
 - (b) the failure to adequately disclose the structure of the scheme;
 - (c) the financial position of the responsible entity and its ability to meet its obligations in relation to the scheme; and
 - (d) the commissions paid to advisers when selling the product.

- 57 In 2011, ASIC reviewed five of the 10 PDSs issued for agribusiness schemes in the lead-up to the end of the financial year. The review noted that the responsible entities had sought to address the concerns raised with them in previous years. However, there was still inconsistency between products in terms of the disclosure to investors.
- 58 Case-by-case assessment of agribusiness disclosure documents is resource intensive. It is also time-consuming for individual responsible entities to amend deficiencies in their disclosure documents, and disruptive for their fundraising.
- 59 In general, the PDSs we reviewed did not always meet our expectations of a 'clear, concise and effective' document within the meaning of s1013C(3). We do not have any evidence to suggest, however, that responsible entities are not attempting to comply with their obligations. Indeed, the length of many documents we reviewed suggests that they are attempting to include as much relevant information about the product as possible, and this is having the effect that PDSs become too long and complicated for investors to understand. Rather, we think that because the PDS content requirements (described in paragraph 37) are principles based and very broad, this is not assisting responsible entities to ensure that the information that they provide in PDSs is appropriately targeted to the needs of investors.

Our conclusions on the nature of the problem

- 60 Our conclusions are as follows:
- (a) The different structures of agribusiness schemes and the risks associated with them mean that they are significantly different from the majority of financial products offered to investors. The risks of these products are not being adequately disclosed to retail investors to ensure that they understand the products and whether the products will meet their investment needs, objectives and risk profile.
 - (b) Investors generally have ongoing obligations in relation to their investment as a result of the contractual arrangements they enter into or repayment obligations as a result of borrowing money to finance their investment, and these obligations are not always well understood by investors.
 - (c) Because most retail investors rely on the information in the PDS, it is important that information in the PDS is of high quality to address the information needs of retail investors. However, we have concerns about the general quality of PDSs relating to agribusiness schemes. There is also a general lack of independent information available about agribusiness schemes.
 - (d) The problem can be characterised firstly as one of market failure through asymmetric availability of information—investors do not have access to sufficiently clear information about agribusiness schemes

because the current product disclosure information available to them does not describe the risks of the product clearly enough. The problem is also one of legislative failure—the PDS content requirement (described in paragraph 37) is principles based and applies to all financial products, without specifically addressing the risks and characteristics of agribusiness schemes. As discussed in paragraph 59, we believe that responsible entities are attempting to comply with the law, but the law is not sufficiently clear on how to produce a good PDS for this product.

- (e) We note that the agribusiness industry is fragmented, with a large number of small, produce-specific industry representatives (e.g. the almond industry, which is represented by the Almond Board of Australia). While a number of the large responsible entities within the forestry sector are members of the Australian Forests Products Association (AFPA),⁴ there is no single peak industry body that represents both forestry and non-forestry agribusiness to drive best practice standards and monitor and enforce compliance. Without such a body, it is not possible to consider effective industry regulation in the short to medium term. In addition, there are no known moves by industry participants to establish such a body. Therefore, we consider we need to take action to improve the quality of information available on agribusiness schemes to prospective investors.

61 We consider that responsible entities that are financially sound within the agribusiness sector are likely to find it difficult to differentiate themselves from those that have failed and to signal their greater quality to investors. Although it would be possible for the remaining agribusiness schemes to disclose how they deal with the matters identified in our proposals, in the absence of providing clarification, there is still the possibility that they would not cover what ASIC considers is required by law.

62 Because we think that the problem is partly one of legislative failure, and not necessarily the lack of compliance among responsible entities, we do not think that targeting individual responsible entities is an efficient solution to the problem. Rather, a holistic solution to improve disclosure is required.

63 While the regulatory framework in the Corporations Act (outlined in paragraphs 37–46) is intended to provide adequate disclosure for the offer of interests in agribusiness schemes, there appears to be a need for clarification of the requirements of the Corporations Act to improve disclosure in PDSs to enable investors to better assess the risks of agribusiness schemes. If investors are better informed about the risks involved in the investments they are about to make, they are better equipped to make an investment decision that suits their needs.

⁴ Formed in April 2011 by the merger of the Australian Plantation Products and Paper Industry Council (A3P) and the National Association of Forest Industries (NAFI).

Our objectives

- 64 We aim to improve the quality of disclosure available to retail investors about agribusiness schemes to maximise the chance that they will make an informed investment decision about whether the product is appropriate for them.
- 65 Our proposals relate to agribusiness schemes in the retail sector. We have concentrated on the retail sector because some agribusiness schemes in which retail investors invest have recently experienced financial stress, evidenced by the collapse of large agribusiness scheme operators such as Environinvest Limited, Great Southern Managers Australia Limited, Timbercorp Securities Limited, FEA Plantations Limited, Rewards Projects Limited and Willmott Forests Limited.
- 66 We aim to strike an appropriate balance between:
- (a) disclosure that assists investors to make better-informed decisions about investing in agribusiness schemes;
 - (b) not unduly interfering with the market and the flexibility of the public fundraising process; and
 - (c) promoting efficiency in the capital markets.
- 67 The need to strike an appropriate balance between protecting investors' interests and allowing markets to operate freely is part of ASIC's mandate under the ASIC Act.

B Options

- 68 ASIC considers that the following possible options to meet the objectives:
- (a) *Option 1*: Current disclosure requirements continue to apply (status quo).
 - (b) *Option 2*: ASIC provides clarification on disclosure in PDSs, including benchmarks and disclosure principles that apply (as appropriate), and on advertising and educational material for investors (preferred option).
 - (c) *Option 3*: Current disclosure requirements continue to apply, with increased level of supervision of agribusiness scheme PDSs by ASIC.

Option 1: Current disclosure requirements continue to apply (status quo)

- 69 Option 1 is that the existing disclosure requirements under the Corporations Act continue to apply without any specific guidance for agribusiness schemes. ASIC's existing powers to take action on a case-by-case basis against defective PDSs and advertisements would also continue.
- 70 To solve the problem that we have identified, we would rely on regulatory tools already available to us—that is, we would continue to undertake a risk-based assessment approach to the review of PDSs and require responsible entities to improve deficiencies in their PDSs.
- 71 Industry would have no specific guidance on the issues likely to give rise to regulatory concerns.

Option 2: ASIC provides clarification on disclosure (preferred option)

- 72 Under this option, we would provide clarification to responsible entities on how to comply with the Corporations Act, with the goal of improving risk assessment by retail investors.
- 73 The means of achieving this would be through the benchmark and disclosure principle models of disclosure, which would include:
- (a) setting out the information that we believe should be disclosed at law to help retail investors identify the key risks and risk–reward prospects associated with agribusiness schemes;
 - (b) expecting responsible entities of agribusiness schemes to address certain standard benchmarks on an 'if not, why not' basis (see paragraph 74) and apply the disclosure principles in any PDS current at, or issued on or after, 1 August 2012 so that retail investors can assess whether responsible entities have strategies in place, where possible, to mitigate key areas of risk; and

- (c) clarifying that, from 1 August 2012, responsible entities should provide the benchmark and disclosure principle information to investors in meeting their continuous disclosure obligations under the Corporations Act;
- (d) providing additional clarification to responsible entities in relation to good practices in disclosure and advertising; and
- (e) providing additional educational material, through the release of an investor guide, to assist investors and potential investors in the agribusiness scheme sector to better understand these schemes.

The benchmark model of disclosure

- 74 This model of disclosure provides concrete standards by which retail investors can assess financial products for which there are typically few such external benchmarks.
- 75 The benchmark model of disclosure:
- (a) identifies, for a particular financial product, the key risk areas potential investors should understand before making a decision to invest;
 - (b) outlines benchmarks on how a responsible entity can address these risks in establishing its business model and compliance procedures; and
 - (c) sets out our expectation that a responsible entity will state in the PDS and other disclosures whether its agribusiness scheme meets the disclosure benchmarks and, if not, why not.
- 76 Disclosing on an ‘if not, why not’ basis means, for each benchmark, stating that a responsible entity either:
- (a) meets the benchmark; or
 - (b) does not meet the benchmark, and explaining why not.
- 77 ‘Why not’ means explaining how the responsible entity deals with the issues underlying the benchmark in another way.
- 78 Disclosure on an ‘if not, why not’ basis would be addressed:
- (a) up-front in the PDS; and
 - (b) as material changes occur—in a supplementary PDS, continuous disclosure notice, notice under s1017B or periodic reports.
- 79 In addition, the responsible entity should include the information identified by the disclosure principles described in Table 2.

The disclosure principle model of disclosure

- 80 The disclosure principle model of disclosure:
- (a) identifies, for a particular financial product, the key risk areas potential investors should understand before making a decision to invest;
 - (b) encourages a responsible entity to disclose those key risks and the details underlying the key risks, where appropriate; and
 - (c) sets out our expectations that a responsible entity will state in the PDS and other disclosures that its agribusiness scheme applies the disclosure principles.
- 81 The disclosure principle model of disclosure provides concrete standards by which retail investors are provided with key information to assess financial products for which there are typically few readily comparable products.

Benchmarks and disclosure principles for agribusiness schemes

- 82 We propose to clarify that the five benchmarks and five disclosure principles listed in Table 2 reflect the key areas of risk for retail investors in agribusiness schemes. ASIC’s view is that the information identified in the benchmarks and disclosure principles is information that is required to be disclosed under the law. No responsible entity is under the obligation to adopt the benchmark in operating its business—however, we consider the responsible entity is under the obligation to disclose whether or not the benchmark is met.

Table 2: Proposed benchmarks and disclosure principles for agribusiness schemes

Benchmark/ disclosure principle	Description of benchmark/disclosure principle
Benchmark 1: Fee structures	<p>The scheme is structured so that either:</p> <ul style="list-style-type: none"> • investors are required to pay annual fees (or contributions) to the responsible entity that are sufficient to fund the operation of the agribusiness scheme for the relevant financial year; or • the up-front fees (or contributions) investors pay when they invest is sufficient to cover the operation of the agribusiness scheme until the proceeds of sale of produce are available and this money is held on trust for the investors in that agribusiness scheme. <p>Any fees (or contributions) received by the responsible entity from investors in the agribusiness scheme are:</p> <ul style="list-style-type: none"> • held separately from the other assets of the responsible entity for the benefit of the investors in that agribusiness scheme, are only available for the operation of that agribusiness scheme and are subject to annual audit; and • only used by the responsible entity to meet any expenses that are incurred in the operation of that agribusiness scheme during the period to be covered by the payment, including the portion of the responsible entity’s fees that is proportionate to its duties that have been properly performed during that period.

Benchmark/ disclosure principle	Description of benchmark/disclosure principle
<p>Benchmark 2: Responsible entity or related party ownership of interests in the agribusiness scheme</p> <p>Note: This benchmark was Benchmark 3 in CP 133 and was called, 'Responsible entity or other group company ownership of interests in a scheme'.</p>	<p>The responsible entity and its related parties own less than 5% in aggregate by value of the interests in the agribusiness scheme except for any interests acquired through the default by a member of the agribusiness scheme.</p> <p>In reporting against this benchmark, the responsible entity should also disclose its policy on ownership of interests in the agribusiness scheme by the responsible entity or related parties.</p>
<p>Benchmark 3: Annual reporting to members</p> <p>Note: This benchmark was Benchmark 4 in CP 133.</p>	<p>The responsible entity provides members with a report at least annually that contains relevant scheme-specific information.</p>
<p>Benchmark 4: Experts</p> <p>Note: This benchmark was Benchmark 6 in CP 133 and was called, 'Qualifications of experts'.</p>	<p>Where the responsible entity engages an expert to provide a professional or expert opinion on the agribusiness scheme, and the expert opinion is disclosed to retail investors in a way that may lead them to place reliance on the expert's expertise, the responsible entity only engages an expert that is independent.</p> <p>In addition to disclosing against this benchmark, the responsible entity should disclose, with equal prominence to any expert opinion provided on the agribusiness scheme:</p> <ul style="list-style-type: none"> • a summary of the instructions to the expert; • the qualifications held by the expert and the relevance of these to the opinion; • whether the expert has experience in the commodity in the geographical location being considered or proposed ,or in any other subject matter of the opinion; • the proportion of the expert's work with the responsible entity; and • whether the responsible entity requires the expert to maintain professional indemnity insurance. <p>If the responsible entity obtains a number of expert opinions from persons who hold appropriate qualifications and are independent, the responsible entity should provide a summary of all the opinions with equal prominence when any of the opinions are provided to retail clients.</p>
<p>Benchmark 5: Appointing and monitoring service providers</p> <p>Note: This benchmark was Benchmark 7 in CP 133 and was called, 'Related party issues'.</p>	<p>The responsible entity only engages key service providers (whether directly or indirectly on behalf of the agribusiness scheme investors) necessary for the operation of the agribusiness scheme where:</p> <ul style="list-style-type: none"> • the engagement is subject to a written agreement approved by the board of the responsible entity in accordance with a documented policy; • the agreement is subject to annual review against set performance criteria or measures; and • the agreement is subject to certification by the board, at the time each agreement is entered into, that the agreement is on an arm's length basis. <p>In addition to reporting against this benchmark, the responsible entity should disclose:</p> <ul style="list-style-type: none"> • details of the parties to any agreement; • the key terms of the agreement; • the amounts payable under the agreement; and • a summary of the responsible entity's policy on appointing and monitoring service providers, including the board assessment and approval process.

Benchmark/ disclosure principle	Description of benchmark/disclosure principle
<p>Disclosure Principle 1: Investor financing arrangements</p> <p>Note: This disclosure principle was Benchmark 9 in CP 133 and was called, 'Third party financing arrangements'.</p>	<p>If the responsible entity or a related party is providing finance, or expects to receive payment for arranging finance, for investors in the agribusiness scheme to fund an investment into the scheme, the responsible entity should clearly and prominently disclose in the PDS:</p> <ul style="list-style-type: none"> • the details of the financier; • any amounts paid to the responsible entity or related party in relation to the finance; • that the investor should obtain and read the finance agreement before entering into the finance facility; and • unless the proposed finance facility is non-recourse, that the investor will remain liable to repay the amount lent or made available under the finance agreement should the scheme fail. <p>The responsible entity should also ensure that, as far as practicable, investors receive a copy of the finance documents for the financing arrangement before investing in the agribusiness scheme.</p>
<p>Disclosure Principle 2: Track record of the responsible entity in operating agribusiness schemes</p> <p>Note: This disclosure principle was Benchmark 2 in CP 133.</p>	<p>The responsible entity of an agribusiness scheme should disclose the experience and resources it has available to operate the agribusiness scheme and the agribusiness enterprise.</p> <p>Where the responsible entity has operated other agribusiness schemes, it should disclose:</p> <ul style="list-style-type: none"> • the number of agribusiness schemes it currently operates; • the types of agribusiness scheme being operated; • the period of time that it has been operating the agribusiness schemes; and • whether any of the agribusiness schemes operated by the responsible entity have produced, or are producing, positive returns net of contributions for the investors in those agribusiness schemes.
<p>Disclosure Principle 3: Responsible entity's financial position</p> <p>Note: This disclosure principle was Benchmark 5 in CP 133 and was called, 'Responsible entity's financial position and use of funds raised'.</p>	<p>The responsible entity should disclose a summary of its financial position in any PDS, including details of any known unfunded obligations in respect of the schemes it operates.</p> <p>The responsible entity should disclose if it:</p> <ul style="list-style-type: none"> • is reliant on funding from external or related parties to perform the functions and obligations to members in relation to the agribusiness scheme; • has entered into guarantees or indemnities with external or related parties; or • is a member of a tax consolidation group. <p>It should also disclose the measures it has in place to address the risks arising out of these arrangements to its financial position and its ability to meet its obligations in relation to the agribusiness scheme.</p> <p>If the responsible entity is reliant on funding from external or related parties to perform its functions and fulfil its obligations in relation to the agribusiness scheme, it should disclose the extent of this reliance.</p> <p>If the responsible entity has entered into any guarantee or indemnity with external or related parties, it should explain:</p> <ul style="list-style-type: none"> • what each guarantee or indemnity is, including the names of the parties to the guarantee; and • the potential implications of entering into these arrangements on the financial position of the responsible entity if the other parties to the guarantee are unable to meet their obligations. <p>If the responsible entity is a member of a tax consolidation group, it should disclose details of:</p> <ul style="list-style-type: none"> • whether a tax-sharing agreement is in place and the parties to the tax-sharing agreement; and • if no tax-sharing agreement is in place, the potential implications of not having this.

Benchmark/ disclosure principle	Description of benchmark/disclosure principle
<p>Disclosure Principle 4: Land, licences and water</p> <p>Note: This disclosure principle was Benchmark 8 in CP 133.</p>	<p>The responsible entity should disclose the arrangements entered into to secure rights of access or tenure to the resources and infrastructure required to operate the agribusiness scheme, including any land, licences or leases, and water required, and whether these arrangements:</p> <ul style="list-style-type: none"> • provide for access for the life of the agribusiness scheme; and • are entered into on an arm's length basis. <p>The responsible entity should disclose:</p> <ul style="list-style-type: none"> • the risks associated with these arrangements; • the consequences of a failure by the responsible entity to pay amounts due under these arrangements, and any breaches of these arrangements or agreements underlying the arrangements; and • any measures the responsible entity has implemented, or will implement, to address these risks. <p>The responsible entity should disclose the identity, where known, of the owner of the resources and infrastructure referred to above, the terms of use and whether security has been given over these assets.</p> <p>The responsible entity should disclose (where applicable) for any leases, licences, rights or infrastructure required for the operation of the agribusiness scheme:</p> <ul style="list-style-type: none"> • whether the responsible entity treats the leases and licences or rights as scheme property; • the identity of the parties to the leases, licences and/or rights; and • whether any action in relation to a lease, licence or right needed for the operation of the agribusiness scheme, which is not an obligation of the responsible entity, could endanger the relevant lease, licence or right. Disclosure should clarify the risk of this occurring and how it may affect the agribusiness scheme. <p>If land, licences or water assets are, or are proposed to be, used as security for borrowings by the responsible entity, the responsible entity should disclose the level of actual or proposed gearing, and the risks associated with this gearing, in the PDS and in the report provided to members in response to Benchmark 3.</p>
<p>Disclosure Principle 5: Replacement of the responsible entity</p> <p>Note: This disclosure principle was Benchmark 10 in CP 133.</p>	<p>The responsible entity should disclose whether there are any restrictions on the ability of any replacement responsible entity to access the resources required to continue to operate the agribusiness scheme (including but not limited to any leases, licences, land, water and money held for the purposes of operating the scheme).</p> <p>The responsible entity should disclose:</p> <ul style="list-style-type: none"> • whether the responsible entity or related parties are eligible for any payment or fee that is payable if the responsible entity is replaced, or is to be replaced, and, if so, the amount or method for calculation of this fee; • the effect of a change in responsible entity on any agreements entered into between investors and the responsible entity or other parties in relation to the agribusiness scheme; • any obligation to repay fees already paid to the responsible entity to the incoming responsible entity if the responsible entity changes; and • the risk to, and impact on, investors if the responsible entity changes.

83

We first introduced benchmark disclosure requirements for unlisted, unrated debentures in October 2007: see Regulatory Guide 69 *Debentures: Improving disclosure for retail investors* (RG 69). Since then, we have applied a similar approach to mortgage schemes and over-the-counter contracts for difference: see Regulatory Guide 45 *Mortgage schemes: Improving disclosure for retail*

investors (RG 45) and Regulatory Guide 227 Over-the-counter contracts for difference: Improving disclosure for retail investors (RG 227).

- 84 We first introduced disclosure principles for unlisted property schemes in September 2008: see Regulatory Guide 46 *Unlisted property schemes: Improving disclosure for retail investors (RG 46)*.
- 85 Our benchmarks and disclosure principles relate to matters that must be disclosed under s1013D–1013E of the Corporations Act. Issues addressed by the benchmarks are all matters that might reasonably be expected to have a material influence on the decision of a reasonable person whether to invest in this type of product when investing as a retail investor.
- 86 The purpose of the proposed disclosure benchmarks and principles is to improve the consistency and quality of disclosure by the responsible entities of agribusiness schemes and to enhance investor confidence. It is not a requirement of the law for a business to be structured to meet the benchmarks. However, we consider that the benchmark and disclosure principle information is the type of information that should be disclosed under s1013D–1013E of the Corporations Act.
- 87 We released a consultation paper in April 2010 setting out our proposals for change in the agribusiness scheme sector: see CP 133. A summary of the submissions made in response to CP 133, and our consideration of those responses, can be found in REP 273.
- 88 As result of the consultation process, we have amended our approach in relation to five of the benchmarks and replaced these benchmarks with disclosure principles. We consider that the benchmarks and disclosure principles approach will address the risks associated with agribusiness schemes, as highlighted in Table 1, as well as the submissions received in response to CP 133.
- 89 We have monitored the disclosure issued under RG 69, RG 45 and RG 46 and are of the view that benchmarks and disclosure principles are an effective means of improving the consistency and quality of disclosure, and have assisted investors to better understand the investments they are either considering or have invested in.

Clarification on advertising

- 90 To provide further context to our proposals, and to assist responsible entities in their disclosure practices, we would also provide clarification on good disclosure and advertising practices for agribusiness schemes.
- 91 We propose to clarify for responsible entities of agribusiness schemes that advertising for these schemes should ensure that:
- (a) there is disclosure that investors risk losing some or all of their principal investment;

- (b) returns on the investment are only quoted if they are accompanied by prominent disclosure that there is a risk that the investment may achieve lower than expected returns;
- (c) statements in advertisements are consistent with all corresponding disclosures on that subject in the PDS; and
- (d) if an investment rating is used, it is properly explained.

Education of investors

- 92 As a complement to the clarification provided under this option, we would address investor education needs by:
- (a) publishing an investor guide to assist investors' understanding of the risk areas and how to evaluate the responsible entity's response in connection with agribusiness schemes; and
 - (b) encouraging responsible entities of agribusiness schemes to provide investors with a copy of the investor guide with the PDS.
- 93 Educating investors would help them understand and use the benchmarks, together with the 'if not, why not' responses, and the disclosure principle information in their investment decision making.

Option 3: Current disclosure requirements continue to apply, with increased supervision

- 94 Under this option, ASIC would review all PDSs that are issued by responsible entities of agribusiness schemes to raise the standards and quality of disclosure as well as to ensure compliance with the requirements of the Corporations Act.
- 95 The existing requirements of the Corporations Act would still apply in relation to a PDS, including that the PDS must:
- (a) include any information that might reasonably be expected to have a material influence on the decision of a reasonable person, as a retail client, whether to acquire the product (s1013E);
 - (b) make specific disclosures (s1013D); and
 - (c) word and present the PDS in a clear, concise and effective manner (s1013C(3)).
- 96 The Corporations Act currently provides ASIC with the power to deal with PDSs that are defective on a case-by-case basis.
- 97 However, we do not think that this is a realistic and efficient option to address the problems identified in Section A.

C Impact analysis

Affected parties

- 98 Parties affected by the proposed policy would include:
- (a) responsible entities of agribusiness schemes (we estimate that there are currently 70 responsible entities operating approximately 371 agribusiness schemes);
 - (b) experts employed by responsible entities to provide agribusiness consultancy and opinions on the likely performance of agribusiness schemes;
 - (c) advisers of responsible entities of agribusiness schemes;
 - (d) investors who receive an offer of interests in an agribusiness scheme; and
 - (e) ASIC.

Costs and benefits of each option

Option 1: Current disclosure requirements continue to apply (status quo)

Benefits

- 99 In the short term, providing no clarification to industry would avoid imposing direct costs on industry immediately.
- 100 Investor protection would continue at least at its current level as we would continue to monitor potential issues in this area and take action on a case-by-case basis against responsible entities where PDSs or advertisements were defective.
- 101 The risk-based assessment approach to reviewing PDSs can be accommodated within ASIC's current workload.

Costs

- 102 We think that this option will impose costs on investors because it will not effectively address the problems identified in Section A of this RIS.
- 103 Maintaining the status quo is likely to impose some costs to industry. Because some agribusiness schemes have recently experienced financial stress, doing nothing is likely to mean that some potential investors would avoid agribusiness schemes and pursue other investment opportunities.

- 104 Providing no clarification also means that there may be no amelioration of the problems identified in Section A, which may dampen general confidence in the agribusiness scheme sector.
- 105 This is likely to particularly affect agribusiness schemes that are still in the market. Without any clarification of the existing law, the remaining responsible entities of agribusiness schemes are likely to find it difficult to differentiate themselves and signal their greater quality to investors. ASIC may also raise regulatory concerns and issue stop orders on the matters covered by its proposed guidance.
- 106 Over time, the lack of a regulatory response may compound the cost for industry and investors—that is, not intervening now may mean that the cost of any eventual intervention is much higher. Although it is possible that some agribusiness schemes may act on their own accord to provide investors with better disclosure addressing key risk information, we consider that it is unlikely that agribusiness schemes would anticipate all of our regulatory concerns. It is also unlikely that such an approach would provide investors with the level of comparability between agribusiness schemes that is possible through our proposals.
- 107 Failing to provide clarification forgoes the opportunity for reducing the risk of investors failing to understand the nature of these schemes and their associated risks in the future and may fail to effectively address the problems identified in Section A.
- 108 A risk-based approach to reviewing PDSs means that only PDSs that are considered to pose significant risks are identified for review. This would mean that some deficient PDSs may still remain in the market. Hence, the inconsistencies in the level of disclosure and the incomparability of different agribusiness schemes would continue.

Option 2: ASIC provides clarification on disclosure (preferred option)

Benefits

- 109 We think that this approach would effectively address the problems identified in Section A by promoting disclosure documents that better address:
- (a) the risks associated with agribusiness schemes; and
 - (b) whether the responsible entity of the agribusiness scheme has strategies in place to mitigate these risks, where possible.
- 110 We think that this will have a direct positive impact on the ability of retail investors to make informed decisions about whether to invest in agribusiness schemes.

Benefits of specific guidance

- 111 The rationale for our proposals was outlined in CP 133. While some amendments have been made to these proposals to address concerns raised during consultation, the rationale behind the proposals remains the same.
- 112 We consider that further clarification about the disclosure of relevant risk areas for agribusiness schemes would have significant benefits for investors by allowing them to more easily and effectively compare the characteristics and risks of different agribusiness schemes. Comparable disclosure documents would establish standards that help retail investors to better assess whether to invest in agribusiness schemes.
- 113 The recent collapse of a number of responsible entities has highlighted the extent to which agribusiness schemes are vulnerable to risks that may not exist in other types of schemes. While the nature and intensity of these risks vary between schemes and responsible entities, these risks are of direct concern to the investors in agribusiness schemes.
- 114 While clarifying the requirements of the law would not directly prevent agribusiness schemes from experiencing financial stress or failure, it is likely to raise governance standards for agribusiness schemes (e.g. through increased disclosure of their financial position and performance) and increase investor understanding of the key risks associated with these schemes. In addition to improving investor understanding of agribusiness schemes, our proposals are likely to encourage responsible entities of agribusiness schemes to adopt more robust and transparent business models, and improve the practices that they put in place to mitigate the risks as a result of making specific disclosures about these practices.

Benefits of the 'if not, why not' benchmark and disclosure principle approach

- 115 An additional benefit of this particular approach is flexibility. The 'if not, why not' approach means that, if a responsible entity does not meet a particular benchmark, it can explain that this is because it has alternative methods of ensuring stability and viability (e.g. because it operates a more conservative business model). The disclosure principles address key areas of potential risk for investors and would, where appropriate, ensure that investors obtain adequate information.

Benefits of giving clarification on advertising

- 116 The benefits of providing clarification on advertising include the benefits of greater transparency generally (as discussed above).
- 117 Our experience indicates that retail investors who are thinking about investing place particular emphasis on the information and impressions given in advertisements. Some of the advertisements we have observed for agribusiness schemes have not given a realistic impression of the scheme, its features and its risks.

118 We consider clarification for responsible entities when advertising their agribusiness schemes should promote investor understanding of agribusiness schemes and minimise the risk of mis-selling. Although it would be possible to deal with advertisements on a case-by-case basis, clarification for advertising of agribusiness schemes would:

- (a) provide responsible entities with greater certainty about whether an advertisement is likely to be acceptable, and a greater assurance that agribusiness scheme advertising will be regulated consistently; and
- (b) reduce the risks of misleading or deceptive advertising.

Benefits of investor education

119 The proposal to provide investor education materials would help investors to understand the information and explanations provided in disclosure documents by the responsible entities of agribusiness schemes. This would help investors better understand the products offered to them, and thus make better choices that suit their own risk tolerance.

120 We consider that ASIC would benefit from the proposals through fewer complaints resulting from investors better understanding these products, meaning that our resources can be focused on other areas.

Costs

Costs resulting from the provision of clarification

121 Our proposal represents our view on the best way for responsible entities to provide disclosure about the risks of investing in agribusiness schemes.

122 It is our experience that responsible entities do take into consideration clarification or guidance we issue about our view of the law, and given that we are likely to take this into account when enforcing the law, we would expect that responsible entities of agribusiness schemes are likely to address the disclosure benchmarks and disclosure principles in future disclosures to retail investors.

123 We expect that the clarification of the requirements of the law will result in some additional compliance and administrative (one-off and ongoing) costs. These are costs involved in complying with the law. Our guidance simply outlines our view of how the law operates. There would also be costs involved if a responsible entity chose to modify its business model in order to meet a benchmark. However, we make it clear that complying with the benchmarks is not mandatory—this is because the option provides for an ‘if not, why not’ explanation, and responsible entities may meet the area of concern underlying each benchmark using some alternative practices.

- 124 As part of our consultation process, we sought feedback on the likely impact of the proposals. On the whole, respondents did not provide detailed information on the likely compliance and administrative costs associated with implementing the proposals. Where respondents indicated that costs would be significant, we have taken steps to reduce the potential impact. Given its nature, we consider that the information identified in our proposal is already required as a result of the current disclosure regime for PDSs, and any information that the responsible entity has not made available to investors in the past would generally already be available to responsible entities of agribusiness schemes (although some system changes may be required to allow information to be collected automatically).
- 125 Although the various costs arising for responsible entities can, in principle, be quantified, they will likely vary significantly across the industry. In particular, costs will vary depending on the nature and size of the responsible entities, the types and number of agribusiness schemes being operated, the extent to which the proposed disclosure information is known, and other factors.
- 126 We have undertaken additional consultation with industry and sought details specifically in relation to the cost implications of our proposals. Feedback from a number of industry participants, including responsible entities and their advisers, was that the proposals would only result in minimal additional costs. These participants were, however, unable to provide any estimation of the costs that may be incurred.
- 127 AFPA estimates that it would cost \$170,000 in initial costs and \$90,000 on an annual basis for both closed and new agribusiness schemes to address the proposals. The estimates are based on costs associated with a portfolio of 40–50 projects operated on behalf of 15,000 investors. In the main, these costs comprise obtaining, analysing and maintaining the information required by our proposals as well as attending to inquiries from existing investors and advisers in relation to the information provided under our proposal.
- 128 AFPA also submitted that investors in closed forestry schemes (i.e. not being offered to new investors) would not derive any benefit from mandated enhanced disclosure, and any costs associated with meeting our proposals would be additional non-recoverable costs for closed schemes.
- 129 We note, in response, that we would expect that responsible entities of closed schemes would generally be expected to maintain the information outlined in the proposals to meet their continuous disclosure obligations under the law. Further, we would expect that a number of the circumstances relating to the information for investors in closed schemes would not be expected to change significantly over the life of the scheme, and that there would appear to be a limited need to collate information, particularly in respect of fee structures, experts, appointing and monitoring service providers, investor financing arrangements, land, licences and water, and replacement of the responsible entity.

- 130 Further, we note that disclosure is already required under the Corporations Act if a significant event or circumstance occurs, such as a change in the financial position of the responsible entity or the arrangements in place to secure land, licences and water.
- 131 The increased costs of issuing interests in agribusiness schemes may lead to issuers turning to other methods of raising funds—such as offering other types of securities (e.g. shares) or offering interests to wholesale rather than retail investors. Some of these methods might be more costly than issuing interests in agribusiness schemes and some might be cheaper. The method chosen will depend on the business structure and the aims of the business.
- 132 We do not consider the detriment to the market of agribusiness schemes turning to other methods of fundraising, such as issuing shares, would be significant. Those who invest in shares often have a better understanding of their investment, particularly of the risks of not getting back the principal investment.
- 133 Entering into a wholesale market might be an option, although, again, this would depend on the goals of the business. The wholesale market has fewer rules and regulations for an offer of interests, or the provision of financial services, because the clients are generally more sophisticated than retail clients. For example, the offer of interests to wholesale clients does not need a PDS.
- 134 There is a risk that the cost of issuing interests in agribusiness schemes might push issuers to less regulated areas of fundraising, such as the issue of promissory notes that do not fall within the definition of ‘debenture’. However, while this might be a risk for investors if they do not understand the investment being offered, we can oversee such issues under the general provisions of the Corporations Act and the ASIC Act. This would be done on a case-by-case basis initially. If there was a significant move to a less regulated sector, we would consider whether it was desirable to identify general standards that applied to that sector.

Costs of giving clarification on compliance plans, compliance committees and compliance plan auditors

- 135 We do not consider that the proposal would, in itself, have any significant cost impact on compliance plans, compliance committees and compliance plan auditors. This is because a compliance plan should already address issues relating to ensuring compliance with disclosure obligations under the Corporations Act. Compliance committees and compliance plan auditors would already be aware of, and need to take into account, the information required under the benchmarks and disclosure principles when examining compliance plans and effectively discharging their obligations under the current legal requirements.

Costs of giving clarification on advertising

- 136 Our proposals in relation to advertising for agribusiness schemes would have some cost to industry. Additional warnings required in advertisements might increase the cost of advertisements or result in less time or space within the advertisement being devoted to the marketing message and more devoted to the regulatory message.
- 137 Further, our proposals might discourage some responsible entities from advertising, which might have an impact on their ability to raise funds. Advertising may be less effective in attracting new investors if there are restrictions on what can be included, or if particular statements must be included in advertisements. However, we are not proposing to prohibit advertising. Rather, we are seeking to clarify the application of the law to ensure appropriate disclosure of the risks of investing in an agribusiness scheme and to prevent misleading statements.
- 138 To implement this option—including the engagement of industry over the implementation of the proposals—we consider ASIC would incur additional costs in staff, estimated at a quarter of a full-time equivalent with the current level of products (estimated to cost approximately \$25,000). This may decrease over time, however, as industry becomes more familiar with the proposals, and providing the benchmark and disclosure principle information becomes embedded in industry practice. We would expect that there would be less need to review PDSs on an ongoing basis if the proposals are implemented.
- 139 With this option, we consider that there may be some increased costs to ASIC in terms of engagement with industry over the implementation of the proposals. However, we consider the benefits for investors and certainty for industry of our approach would outweigh these costs in the medium to long term.

Option 3: Current disclosure requirements continue to apply, with increased supervision**Benefits**

- 140 This option would result in ASIC reviewing all agribusiness PDSs that are issued to ensure that the PDS deals with the requirements of Subdiv C of Pt 7.9 of the Corporations Act, particularly in addressing the key risks in a clear, concise and effective manner.
- 141 Investor protection would continue at its current level, while ASIC would become more proactive on a case-by-case basis with issuers whose disclosure documents were deficient or inadequate. Through increased enforcement, ASIC would be in a position to take action to influence disclosure and to improve disclosure of key risks in respect of these schemes on a more consistent basis.

Costs

- 142 In the short term, increasing surveillance activities by ASIC would avoid any immediate direct costs on an industry-wide basis. However, it would impose costs on investors because it would not effectively address the problems identified in Section A of this RIS. It would also result in additional costs for agribusiness issuers that we consider are not presently meeting their legal obligations (because there is a lack of clarity about those obligations).
- 143 There may be additional costs incurred by individual responsible entities in responding to concerns identified by ASIC that may result in additional disclosure being required or amendments to existing disclosure. These costs would only be borne by those responsible entities where concerns are identified in the PDS, and may include the costs associated with obtaining legal advice, drafting and issuing revised disclosure, and the effects of having to offer investors the opportunity to have their investment refunded where the document is defective under the Corporations Act.
- 144 In addition, there may be other implications. For example, investors may assume that, because we review each PDS, this means that ASIC may have in some way approved the agribusiness scheme, or responsible entities may adopt an approach that transfers their consideration of disclosure issues to ASIC, which we consider to be inappropriate.
- 145 Under this option, we expect ASIC would require additional resources to undertake PDS reviews and spend time working with responsible entities of agribusiness schemes to improve processes. To carry out reviews of all PDSs, including follow-up surveillance work at the desired level to produce effective change, ASIC would incur additional costs in staff, estimated at half a full-time equivalent with the current level of products (estimated to cost approximately \$50,000), but this would increase if the number of products in the market returned to previous levels. If this occurred, we estimate ASIC would require at least two full-time equivalents (estimated to cost approximately \$170,000 per year) to monitor the industry and effectively understand all the products and carry out reviews of all PDSs. Additional resources may be required in future years as the number of PDSs increases following recovery of investor confidence.
- 146 A further cost for ASIC associated with this option is that it would require a continuing focus on the agribusiness sector, resulting in a less efficient use of resources, where there may be greater risks arising in other sectors over time. The failure to introduce consistency through clarification of the requirements of the law may result in reduced effectiveness of disclosure in circumstances where ASIC no longer has the resources to continue to apply this approach to the sector.

147

We do not think that Option 3 would be an appropriate solution to the problems we have identified. As noted in Section A, there is no evidence to suggest that responsible entities of agribusiness schemes are not attempting to comply with their disclosure obligations, but we do think further clarification would assist responsible entities to comply. An option relying on our compliance and enforcement regulatory tools would not be as effective as a more holistic, guidance-based solution because:

- (a) given that the problem extends across the industry, targeting particular responsible entities of agribusiness schemes would not be efficient;
- (b) responsible entities would have less certainty about the disclosure that was expected;
- (c) the process for identifying the standards required would be less transparent and only emerge as issues arose on a case-by-case basis; and
- (d) investors would be less likely to be given key risk information that was readily comparable between agribusiness schemes.

D Consultation

- 148 We published CP 133 in April 2010, which set out our proposals on improved disclosure for agribusiness schemes. We invited written and oral comments on our proposals and asked for quantitative and qualitative information.
- 149 The consultation period ended on 31 May 2010. We received 17 written submissions from stakeholders, including responsible entities of agribusiness schemes, industry associations, research houses, industry professionals, accounting bodies, private law firms, government departments and forestry commissions. During the consultation period, we also met with A3P (now AFPA) to discuss the proposals and our responses to the submissions received on CP 133. Most of the submissions recognised that there was a problem and that some action was required. However, there were mixed responses to the proposals in CP 133.
- 150 The main issues raised by respondents related to:
- (a) our ‘if not, why not’ approach and, in particular, our proposed approach of ‘compliance with’ the benchmarks, as opposed to ‘disclosure against’, the benchmarks;
 - (b) whether the benchmarks should apply to all agribusiness schemes;
 - (c) whether annual fees were appropriate for all schemes;
 - (d) the financial arrangements for responsible entities;
 - (e) ownership of the land; and
 - (f) segregation of investors’ money.
- 151 We did not receive any submissions from retail investors directly. However, submissions were received from lawyers representing retail investors in failed agribusiness schemes, and individuals who operate within the agribusiness industry. These submissions generally supported action to address issues that have arisen in the agribusiness scheme sector, as identified in CP 133. Where other issues have been raised, we have considered these in determining our final position.
- 152 There was general support for the application of benchmarks, although many respondents considered some of the benchmarks should be refined. In particular, we received feedback that a number of the benchmarks indicated that ASIC was proposing a particular model of agribusiness scheme as more preferable over others (i.e. a model that has an annual fee structure) through the introduction of benchmarks involving disclosure of whether the scheme displayed the preferred characteristic.

- 153 Some submissions commented that such an approach may force responsible entities to amend the structures of their schemes and reduce the tax effectiveness of the arrangements, resulting in additional costs to responsible entities and reduced returns to investors, and that the benchmarks should not apply to existing agribusiness schemes.
- 154 Further submissions noted that the benchmarks may result in less investment being made into schemes that do not meet the benchmarks, thereby affecting competition in the agribusiness scheme sector.
- 155 We have considered these submissions (see REP 273) in determining our final proposal. We are not attempting to promote any particular model. Rather, we are clarifying for industry its existing obligations under the Corporations Act and highlighting to investors the issues that they should consider and understand before investing in a scheme.
- 156 With regard to comments that the proposals should not apply to existing agribusiness schemes, we have clarified our view of the continuous disclosure obligations that apply to responsible entities of existing agribusiness schemes under the Corporations Act, in which no interests are issued on or after 1 August 2012 (closed schemes).
- 157 We consider that, because investors in these schemes generally do not have a right to withdraw and, in some circumstances, have ongoing obligations to pay fees, investors should receive updated information on the matters outlined in our proposals because this may assist them to better understand their investment and make more informed decisions in exercising any existing rights they have as investors in the scheme. As a result, our proposals provide clarity to responsible entities that they should consider the benchmark and disclosure principle information in meeting their continuous disclosure obligations.

E Conclusion and recommended option

- 158 We recommend Option 2.
- 159 We think that implementing Option 2 will result in improved disclosure documents which better address (compared to current disclosure documents):
- (a) the risks associated with agribusiness schemes; and
 - (b) whether the responsible entity has strategies in place to mitigate these risks, where possible.
- 160 We think that this option will have a direct positive impact on the ability of retail investors to make informed decisions about whether to invest in agribusiness schemes. The investor education completes the package by helping investors to understand the additional disclosure proposed.
- 161 We consider that providing clarification to industry will bring about a more consistent, transparent and timely improvement to disclosure. In our experience, this approach assists entities in complying with their obligations, and tends to improve the overall standard of compliance more effectively than intervening on a case-by-case basis. We therefore consider it appropriate to issue the proposed clarification.
- 162 While Option 2 may incrementally increase the costs for responsible entities of agribusiness schemes, we consider that the initial and ongoing costs are outweighed by the benefit of empowering investors with the ability to better assess the merits of investing in agribusiness schemes.
- 163 The costs incurred by responsible entities in implementing Option 2 are likely to vary significantly depending on the nature and size of the responsible entity, the types and number of agribusiness schemes being operated, and the extent to which the proposed disclosure information is known. While some responsible entities and their advisers have indicated that the proposal would result in minimal additional costs, we also received a submission that our proposals would cost \$170,000 in initial costs, and \$90,000 in ongoing costs, for a responsible entity operating a portfolio of 40–50 projects.
- 164 We recognise that there will be increased compliance costs to implement Option 2. We have considered those submissions received in relation to increased costs and have made adjustments to our proposals. We also recognise that there are economies of scale in operating multiple agribusiness schemes, and that additional costs will apply to existing agribusiness schemes where investors may have already made their investment by a one-off payment. In such situations, there is either no capacity, or a reduced capacity, for responsible entities to recover these additional costs.

- 165 Submissions received generally endorsed the approach outlined in Option 2, although there were concerns about timing and particular disclosure principles, which we have addressed in finalising our approach.
- 166 Option 2 also has the benefit that it has lower expected costs for ASIC due to expected improvements in the level and consistency of disclosure, which should result in us being able to focus fewer resources on this sector in the medium to longer term.
- 167 We have also taken into account that, although it would be possible to deal with defective PDSs and advertisements on a case-by-case basis, the more general approach in Option 2 has the following advantages:
- (a) responsible entities will have greater certainty about our expectations regarding their disclosure and advertising obligations;
 - (b) the approach will apply consistently across the agribusiness scheme sector, rather than being applied in a piecemeal fashion as PDSs and advertisements raise concerns; and
 - (c) key risk information provided to investors will be more focused to increase understanding of agribusiness schemes and make them more readily comparable.

F Implementation and review

Implementing our proposals

168 Our previous experience with implementing this kind of approach would suggest that responsible entities of agribusiness schemes are likely to follow our guidance. We expect that responsible entities will implement improved disclosure for their fundraising documents, as well as for ongoing disclosure documents.

169 Our proposed transition period is as follows:

- (a) responsible entities for all agribusiness schemes will apply the advertising standards from the publication date of the final regulatory guide;
- (b) responsible entities for existing closed agribusiness schemes will be encouraged, as a matter of best practice, to provide the benchmark and disclosure principle information as part of their ongoing disclosure obligations to existing investors from 1 August 2012; and
- (c) existing fundraising documents that are still in use, as well as fundraising documents for new agribusiness schemes, will provide the benchmark and disclosure principle information from 1 August 2012.

170 We will review all fundraising documents and updated investor disclosure from 1 August 2012 for a period of six months. This review will check that the benchmark information is being adequately disclosed to investors on an 'if not, why not' basis and that the responsible entity has applied the disclosure principles.

171 We will also:

- (a) work with responsible entities to ensure that the benchmarks, disclosure principles and our disclosure expectations are understood;
- (b) discuss with responsible entities any concerns we have with their disclosure and, where necessary, seek additional disclosure from them (e.g. about the practical impact of not disclosing against a particular benchmark or applying the disclosure principles, and the associated risks for investors); and
- (c) conduct surveillance visits, as needed, to reinforce our expectations.

172 As outlined in paragraph 46, we can use our stop order powers if we consider that a PDS does not comply with the PDS content requirements. At the end of the transition period, we will continue to review the fundraising documents on a risk-based approach.

Our guidance

- 173 Our option will be implemented by publishing several documents. These will include:
- (a) a regulatory guide;
 - (b) an investor guide; and
 - (c) a report on the submissions received in response to CP 133 (REP 273).