



**ASIC**

Australian Securities & Investments Commission

## CONSULTATION PAPER 3

# **Managed investments: Change of responsible entity —effect on contracts**

June 1999



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# Managed investments: Change of responsible entity — effect on contracts

ASIC issues paper

*2 June 1999*

## What this issues paper is about

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**1** ASIC invites comment from participants in the managed investments industry and other interested persons on its proposal to adopt a policy that it will modify the Law to clarify that when a new responsible entity of a registered managed investment scheme takes office, it is not bound by contracts that the former responsible entity entered with agents of the former responsible entity.

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## **Submissions sought**

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### **ASIC invites submissions on issues related to the change of a responsible entity and its effect on contracts**

**2** To help in its consideration of the issues associated with the replacement of a responsible entity and its effect on contracts that the former responsible entity made with agents, ASIC is seeking submissions from participants in the managed investment industry and other interested persons on any of the matters referred to in this issues paper.

**3** Submissions are sought on the following issues.

- (a) Do s601FS and s601FT have the effect that a new responsible entity would be bound by contracts made by the former responsible entity with agents of the former responsible entity?
- (b) Are contracts with agents likely to include provisions that cause them to expire on change of responsible entity? Would such provisions be ineffective because of s601FS and s601FT?
- (c) Would transfer of contracts with agents under s601FS and s601FT have an advantageous or disadvantageous effect on members if a temporary responsible entity is appointed?
- (d) Could transfer of contracts with agents under s601FS and s601FT be used to diminish the accountability of a responsible entity or other persons involved in operating a scheme by making it difficult to remove them? Is this contrary to the intent of s601FM (ie, removal of the responsible entity by the members)?
- (e) Where the responsible entity intended to enter long terms contracts with agents, that a replacement responsible entity may not wish to be bound by, would the risk that it may be difficult to change the agents be required to be disclosed in a prospectus in relation to the scheme?
- (f) What would be the regulatory and financial impact of implementation of possible option for modification of s601FS and s601FT contained in this issues paper (see paragraphs 11 to 13)?
- (g) Are there any other means (including by modification of the Law by ASIC) to achieve the outcome sought by the possible option for modification of the Law contained in this issues paper (see paragraphs 12 and 13)?

**4** Submissions addressing these and any other relevant matters will be used by the ASIC to help it decide whether there is a need, and a sound policy and legal basis for modifying the relevant provisions of the Law.

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### **Your comments**

We invite your comments on this issues paper.

Comments are due by 19 July 1999 and should be sent to:

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You can contact Geoffrey McCarthy on (02) 9911 2083 or Ian Domicello on (02) 9911 2376 for further information about this issues paper.

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## **Interpretative discussion**

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### **Consideration of the effect of sections 601FS and 601FT**

**5** On one view, s601FS and s601FT may have the effect that on a change of responsible entity of a registered scheme, an incoming responsible entity is bound by contracts that the former responsible entity made with agents.

**6** Alternatively, it may be that the former responsible entity will retain a right of indemnity for any liability it has for a breach of contract with the agent arising from the termination of the appointment of the agent on the change of responsible entity.

### **Policy objectives**

**7** ASIC's present view is that the outcomes discussed in paragraphs 5 and 6 would be inconsistent with the accountability of a responsible entity that the Law intends. Under s601FM, a responsible entity may be removed by an extraordinary resolution of members. Under s601FP, the Court may appoint a temporary responsible entity. It is not appropriate that a new responsible entity should not have choice as to its agents

because the new responsible entity will be liable for the acts and omissions of the agents.

**8** ASIC considers that s601FS and s601FT were not intended to apply to contracts of a responsible entity with its agents. The application of those sections to agents would be inconsistent with Parliament's intention that the responsible entity should be accountable for the operation of a registered scheme.

**9** ASIC has considered that excluding the operation of s601FS and s601FT in relation to agents, may not benefit the members in some circumstances. For instance, as a result of the possible option for modification (see paragraphs 11 to 13), some agents may be less willing to contract with a responsible entity. Further, a new responsible entity may have to negotiate new terms with agents. In some cases, that may mean that the members will be disadvantaged because of increased payments to indemnify the new responsible entity for agents' fees. If sections 601FS and 601FT do not apply there may also be some increased administrative costs associated with effecting transfers or contracts that have been entered with agents.

**10** However, if the modification applies only in relation to those contracts in relation to which an incoming responsible entity seeks it, then these disadvantages will be minimised. An incoming responsible entity could seek the modification in relation to all contracts of the responsible entity with its agents in relation to a particular scheme or as to only specified contracts relating to the scheme.

## Options

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### Form of possible modification

**11** ASIC is considering adopting a policy that it will on application by an incoming responsible entity make a declaration under s601QA(1)(b) that on the change in responsible entity is appointed that applies to either:

- (a) all the contracts then in force with agents of the former responsible entity in relation to a registered scheme; or
- (b) contracts specified by the incoming responsible entity.

**12** The declaration would be that Chapter 5C applies to the relevant contracts as if:

- (a) a new s601FS(2)(e) were added:

[...the following rights and liabilities remain rights and liabilities of the former responsible entity:]

...

“(e) rights and liabilities of the former responsible entity in relation to any agent or the engagement of any other person to do anything the former responsible entity was authorised to do in connection with the scheme.”;

(b) a new s601FS(3) were added:

“The former responsible entity does not have any right against the new responsible entity, the scheme property or the members to be indemnified against any liability of the former responsible entity to an agent or other person engaged to do anything the former responsible entity was authorised to do in connection with the scheme where that liability comes into existence on or after the change in responsible entity.”

**13** The modification proposed in paragraph 12(b) prevents the former responsible entity making a claim if it is liable to the agent as a result of the agency terminating when the responsible entity changes.

**14** The possible modifications described in paragraph 13 would not be available to the initial assumption of the responsible entity role under the transitional provisions (ie, where s1462 applies).

## **Rely on disclosure**

**15** In the alternative, ASIC could rely on an interpretation that investors will be informed about the potential for contracts with agents to make it difficult to remove a responsibility entity of a particular scheme in the scheme’s prospectus.

## **Key terms**

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**16** In this issues paper, a reference to:

“agent” includes any person engaged to do anything a responsible entity is authorised to do in connection with a registered scheme;

“ASIC” means the Australian Securities and Investments Commission;

“Law” means the Corporations Law; and

“s601ED” (for example) is to a section of the Law.