



ASIC

Australian Securities & Investments Commission

CONSULTATION PAPER 4

Managed investments: Protection of underlying land in primary production managed investment schemes

June 1999

What this issues paper is about

1 ASIC invites comment from participants in the managed investments industry and other interested persons on ASIC's interim policy referred to in Policy Statement 130 *Managed investments: Licensing* at [PS 130.23A]. The interim policy applies where an offer of interests in a primary production managed investment scheme is made with an offer of rights regarding land on which the primary production activities of the scheme will occur. The interim policy is to insert the following condition in the licence issued to the responsible entity of a primary production managed investment scheme:

“The licensee must ensure (in relation to each scheme) that an interest that confers the right, for the purpose of and for the duration of the scheme, to use the land on which any primary production will occur in the operation of the scheme:

- (a) is registered as soon as possible after receipt of application moneys, in the name of the member, licensee or custodian (as appropriate) under State or Territory land titles law; and
- (b) is registered such that it can not be adversely affected by any existing or subsequent mortgagee, secured creditor or transferee (other than in connection with a borrowing or other transaction that is entered into by the licensee in accordance with the constitution of the scheme).

Contents

What this issues paper is about ... 2

Submissions sought

ASIC invites submissions regarding the imposition of the licence condition ... 3

The features of a primary production managed investment scheme ... 5

Interpretative discussion

Licensee's duty to perform duties efficiently, honestly and fairly ... 5

Responsible entity's duty to act honestly, exercise care and diligence and act in the best interests of members ... 6

The power to impose licence conditions ... 6

General interpretation of the provisions ... 7

Scope of provisions ... 8

Interim policy ... 8

Submissions sought

ASIC invites submissions regarding the imposition of the licence condition

2 ASIC invites submissions from participants in the managed investment industry and other interested persons on any of the matters referred to in this issues paper. Where possible, submissions should consider the following issues:

- (a) Does the condition assist in ensuring that the licensee performs its duties as a holder of a dealers licence authorising it to operate a managed investments scheme efficiently, honestly and fairly as required of it by the Corporations Law?
- (b) Does the condition assist in ensuring that the licensee in performing its duties as a responsible entity operating a registered scheme acts honestly, exercises care and diligence and gives priority to members' interests over its own interests?
- (c) Is the licence condition unduly onerous on the licensee?
- (d) Are there any practical problems which arise because of the licence condition?
- (e) Are there circumstances where the imposition of such a condition may adversely effect the position of members in the scheme?
- (f) In circumstances where there are stapled securities (being an members interest in the scheme and an equivalent proportional shareholding in the land owning company) is the imposition of such a condition inappropriate?
- (g) Are there other mechanisms available which could protect member's interests in land to the same extent as the licence condition?
- (h) Does the proposed condition adversely effect the opportunity for a member to claim taxation deductions?

3 ASIC is seeking submissions so we can:

- (a) assess the implications that the imposition of the condition has for promoters of primary production managed investment schemes and members; and
- (b) determine whether there is a policy basis for continuing the interim policy.

Your comments

We invite your comments on the interim policy and matters contained in this issues paper.

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

Darren Mc Shane
Director,
Managed Investments, NSW,
Australian Securities & Investments Commission
GPO Box 9827, Sydney NSW 2001
facsimile (02) 9911 2369
darren.mcshane@asic.gov.au

You can also contact Graeme Plath on (02) 6250 3832 for further information about this interim policy.

The features of a primary production managed investment scheme

4 In many primary production managed investment scheme, the member contracts with the responsible entity to set up and maintain the project and harvest and market the proceeds. The underlying land usually remains the property of the responsible entity or an associate and reverts to them at the conclusion of the project. The member is given rights to use a part of the land for the duration of the project.

5 If members are not protected by a registered interest in the land that is paramount and cannot be adversely effected by any existing or subsequent mortgagee, secured creditor or transferee, the risks to the members include the following:

- (a) the landowner may have used, or may use, the land as security, and if there is a default, the mortgagee or similar secured creditor may be able to rely on the security and disregard the interests of the members, and
- (b) the landowner (or a liquidator of the landowner) may transfer the land (or an interest in the land) to a transferee who is not under an obligation to recognise the rights of the members regarding the land.

6 In such schemes the intention is that the member's participation will be for the duration of the scheme and that the member's rights to use a part of the land will not be alienated for the duration of the project.

Interpretative discussion

7 The relevant parts of the Corporations Law are set out below:

Licensee's duty to perform duties efficiently, honestly and fairly

- (a) s784(1) and 784(2)(d) state that:
 - (1) *This section has effect where a body corporate applies for a licence.*
 - (2) *The Commission shall grant the licence if:*
 - (d) *the Commission has no reason to believe that the applicant will not perform efficiently, honestly and fairly the duties of a holder of a licence of the kind applied for;*

(b) s826(1)(j) and (k) state that:

(1) *Subject to section 837, the Commission may, by written order, revoke a licence if:*

(j) *the Commission has reason to believe that the licensee has not performed efficiently, honestly and fairly the duties of a holder of a dealers licence or an investment advisers licence, as the case requires; or*

(k) *the Commission has reason to believe that the licensee will not perform those duties efficiently, honestly and fairly.*

Responsible entity's duty to act honestly, exercise care and diligence and act in the best interests of members

(c) s601FC(1)(a), (b) and (c) state that:

In exercising its powers and carrying out its duties, the responsible entity of a registered scheme must:

(a) *act honestly; and*

(b) *exercise the degree of care and diligence that a reasonable person would exercise if they were in the responsible entity's position; and*

(c) *act in the best interest of the members and, if there is a conflict between the members' interests and its own interests, give priority to the members' interest;*

The power to impose licence conditions

(d) s601FA states that:

The responsible entity of a registered scheme must be a public company that holds a dealers licence authorising it to operate a managed investment scheme.

- (e) s601FB(1) states that:
 - (1) *The responsible entity of a registered scheme is to operate the scheme and perform the functions conferred on it by the scheme's constitution and this Law.*
- (f) s780(2) states that:

A dealers licence may authorise a person to do either or both the following:

 - (a) *to carry on a securities business*
 - (b) *to operate:*
 - (i) *a managed investment scheme; or*
 - (ii) *managed investment schemes of a particular kind.*
- (g) s786(1) states that:
 - (1) *A licence is subject to:*
 - (a) *such conditions and restrictions as are prescribed; and*
 - (b) *subject to section 837, such conditions and restrictions as the Commission imposes when granting the licence or at any time when the licence is in force.*

General interpretation of the provisions

8 Section 784(2)(d) and s826(1)(j) and (k) require that a responsible entity granted a dealers licence authorising it to operate a registered scheme is required to perform its duties under the licence efficiently, honestly and fairly.

9 Sections 601FC(1)(a), (b) and (c) require that a responsible entity, in operating a registered scheme is to act honestly, exercise care and diligence and is to give priority to members' interests over its own interests.

10 Sections 601FA, 601FB(1) and 780(2) have the effect that a responsible entity can not operate a registered scheme unless a dealers licence authorises the responsible entity to operate the registered scheme. The dealers licence issued to a responsible entity may be one that only allows the responsible entity to operate a registered scheme and does not allow the responsible entity to carry on a securities business (s780(2)).

11 Section 786(1) permits the imposition of conditions and restriction in a licence. Such a licence may be a dealers licence that only allows the responsible entity to operate a registered scheme and does not allow the responsible entity to carry on a securities business. Accordingly the conditions and restrictions imposed pursuant to s786(1) could be conditions and restrictions that only have a nexus to the operation of the registered scheme and do not have a nexus to the carrying on of a securities business.

Scope of provisions

12 When the responsible entity is the entity that grants to the member rights to use a part of the land, the duties of a responsible entity as set out in s601FC(1)(a)(b) and (c) require that the responsible entity not deal with land inconsistently with the rights, not to create any security over the land and not to default on an existing security.

13 A primary production managed investment scheme will only be operated efficiently, honestly and fairly, and therefore consistently with the duties imposed by s784(2)(d) and s826(1)(j) and (k), if the member's rights to use a part of the land is not alienated.

14 The imposition of the condition in a dealers' licence issued to responsible entity authorised to operate a primary production managed investment scheme:

- (a) ensures compliance by the responsible entity with the duties of the responsible entity; and
- (b) ensures that the scheme will operate efficiently, honestly and fairly.

Interim policy

15 Pending consideration of the issues set out in this issues paper, ASIC will impose the proposed condition in dealer licences issued to responsible entities of primary production managed investment scheme where an offer of interests in the scheme is made with an offer of rights regarding land on which the scheme will occur.