



ASIC

Australian Securities & Investments Commission

REPORT 545

Response to submissions on CP 280 ASIC class order on wholesale equity schemes

September 2017

About this report

This report highlights the key issues that arose out of the submissions received on Consultation Paper 280 *ASIC class order on wholesale equity schemes: Licensing relief for trustees—[CO 07/74]* (CP 280) and details our responses to those issues.

About ASIC regulatory documents

In administering legislation ASIC issues the following types of regulatory documents.

Consultation papers: seek feedback from stakeholders on matters ASIC is considering, such as proposed relief or proposed regulatory guidance.

Regulatory guides: give guidance to regulated entities by:

- explaining when and how ASIC will exercise specific powers under legislation (primarily the Corporations Act)
- explaining how ASIC interprets the law
- describing the principles underlying ASIC's approach
- giving practical guidance (e.g. describing the steps of a process such as applying for a licence or giving practical examples of how regulated entities may decide to meet their obligations).

Information sheets: provide concise guidance on a specific process or compliance issue or an overview of detailed guidance.

Reports: describe ASIC compliance or relief activity or the results of a research project.

Disclaimer

This report does not constitute legal advice. We encourage you to seek your own professional advice to find out how the Corporations Act and other applicable laws apply to you, as it is your responsibility to determine your obligations.

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A Overview/Consultation process

- 1 A 'wholesale equity scheme' is essentially an unregistered managed investment scheme that primarily invests in securities of unlisted companies and whose members are all wholesale clients. Wholesale equity schemes are usually structured by the manager using a multiple unit trust structure with separate corporate trustees that are related bodies corporate of the manager. This ensures consistent and equal tax outcomes for all investors, in line with global standards.
- 2 We made Class Order [CO 07/74] *Wholesale equity schemes: Licensing relief for trustees* to remove impediments in the venture capital and private equity industry by allowing wholesale equity schemes to hold equities in small, unlisted, closely held private equities. [CO 07/74], which was due to expire on 1 October 2017, has provided relief to trustees of wholesale equity schemes from the requirement to obtain an Australian financial services (AFS) licence to provide 'wholesale equity financial services' by:
 - (a) dealing in investment products that form part of the trust property of the wholesale equity scheme; and
 - (b) providing a custodial or depository service in relation to the investment products of the trust.
- 3 In 2013, as part of our wider review of the financial and custody requirements applicable to AFS licensees, we strengthened the requirements for responsible entities and custodial and depository service providers, imposing new financial requirements and minimum standards (or custody requirements) to address risks associated with the provision of these services.
- 4 The financial requirements for responsible entities and custodial and depository service providers relating to net tangible assets (NTA), cash flow projections and liquidity are outlined in [Regulatory Guide 166 Licensing: Financial requirements](#) (RG 166) and implemented through [Class Order \[CO 13/760\] Financial requirements for responsible entities and operators of investor directed portfolio services](#) and [Class Order \[CO 13/761\] Financial requirements for custodial or depository service providers](#).
- 5 The custody requirements for custodial and depository service providers are outlined in [Regulatory Guide 133 Managed investments and custodial or depository services: Holding assets](#) (RG 133) and implemented through [Class Order \[CO 13/1410\] Holding assets: Standards for providers of custodial and depository services](#).
- 6 [CO 07/74] has not reflected these financial and custody requirements.

- 7 In [Consultation Paper 280](#) *ASIC class order on wholesale equity schemes: Licensing relief for trustees—[CO 07/74]* (CP 280), we consulted on proposals to either:
- (a) repeal [CO 07/74] if it no longer forms a useful part of the legislative framework; or
 - (b) remake [CO 07/74], without significant changes, if it still forms a useful part of the legislative framework, in the form of draft ASIC Corporations (Wholesale Equity Scheme Trustees) Instrument 2017/849, which was attached to CP 280, updated with minor amendments to:
 - (i) align the relief with [\[CO 13/760\]](#), [\[CO 13/761\]](#) and [\[CO 13/1410\]](#), which have come into force since the introduction of [CO 07/74]; and
 - (ii) provide transitional provisions to continue the relief under [CO 07/74] until the end of the financial year of the trustee.
- 8 This report highlights the key issues that arose out of the submissions received on CP 280 and our responses to those issues.
- 9 This report is not meant to be a comprehensive summary of all responses received. It is also not meant to be a detailed report on every question from CP 280. We have limited this report to the key issues.

Responses to consultation

- 10 We received four confidential and two non-confidential responses (with one respondent providing two submissions) to CP 280 from entities operating wholesale equity schemes, and from other stakeholders, including an industry body representing these entities and two law firms advising these entities. We are grateful to respondents for taking the time to send us their comments.
- 11 All of the respondents expressed the view that the relief in [CO 07/74] continues to form a useful regulatory purpose and were supportive of the changes proposed in CP 280, although:
- (a) one respondent queried the need for the financial and custody requirements to apply to trustees because they already apply to the manager; and
 - (b) one respondent submitted that the definition of ‘wholesale equity scheme’ should be amended.
- 12 For a list of the non-confidential respondents to CP 280, see the appendix. Copies of these submissions are currently on our website under [CP 280](#).

B Continuation of relief for wholesale equity schemes

Key points

After considering the submissions to [CP 280](#), we have remade the relief for wholesale equity schemes in a new instrument, updated with minor amendments, to:

- reflect current drafting practice;
- align it with [\[CO 13/760\]](#), [\[CO 13/761\]](#) and [\[CO 13/1410\]](#), which have come into force since the introduction of [\[CO 07/74\]](#); and
- provide transitional provisions to continue the relief under [\[CO 07/74\]](#) until the end of the financial year of the trustee.

Relief continues to form a useful part of the legislative framework

- 13 In [CP 280](#), we advised that if we formed the view that [\[CO 07/74\]](#) no longer forms a useful part of the legislative framework that we would repeal [\[CO 07/74\]](#) and provide transitional relief in the form of [\[CO 07/74\]](#) for a period of 12 months beyond its sunseting date. To help us form a view, we asked entities that relied on the relief to provide details about the wholesale equity schemes operated and about their compliance with their lodgement requirements.
- 14 All respondents submitted that the relief in [\[CO 07/74\]](#) continues to provide a useful regulatory purpose and should be remade without significant changes. Some respondents advised that they continue to rely on the relief. Others advised that even though they do not currently rely on the relief, it remains a useful part of the legislative framework.
- 15 Some respondents submitted that it would be disproportionately onerous to require each trustee to obtain an AFS licence to provide wholesale equity financial services, and that the costs associated with obtaining and maintaining an AFS licence or appointing a third party licensed trustee would be prohibitive to many wholesale equity schemes. One respondent submitted that a trustee relying on [\[CO 07/74\]](#) would save upwards of AUD35,000 in initial legal fees in connection with an AFS licence application and upwards of AUD15,000 in annual legal costs associated with maintaining an AFS licence.
- 16 One respondent submitted that if [\[CO 07/74\]](#) were to be remade with amendments, there would be regulatory impacts and costs associated with ensuring compliance with the new instrument, with legal costs associated with understanding the amendments and how they affect the business

estimated at approximately AUD10,000. Ongoing costs would depend on the nature of the changes required for the affected entities.

ASIC's response

We consider that the relief in [CO 07/74] continues to form a useful part of the legislative framework. We have remade the class order—see [ASIC Corporations \(Wholesale Equity Scheme Trustees\) Instrument 2017/849](#) and [ASIC Corporations \(Amendment and Repeal\) Instrument 2017/848](#)—without significant changes, and updated the relief with minor amendments, to:

- reflect current drafting practice;
- align it with [\[CO 13/760\]](#), [\[CO 13/761\]](#) and [\[CO 13/1410\]](#), which have come into force since the introduction of [CO 07/74]; and
- provide transitional provisions to continue the relief under [CO 07/74] until the end of the financial year of the trustee.

Definition of ‘wholesale equity scheme’

- 17 In [CP 280](#), we did not specifically consult on the definition of ‘wholesale equity scheme’ used in the draft instrument attached to CP 280, but invited respondents to make submissions more generally about whether [CO 07/74] is currently operating effectively and efficiently.
- 18 ‘Wholesale equity scheme’ was defined in section 4 of the draft instrument to mean a trust that is operated under a managed investment scheme to which all of the following apply:
- (a) the scheme is not registered; and
 - (b) all of the trust property (other than incidental property) consists of investment products; and
 - (c) at all times the value of investment products which are quoted on a financial market does not exceed 20% of the trustee’s reasonable estimate of the market value of the trust property; and
 - (d) no interests in the scheme have been issued to a person as a retail client.
- 19 One respondent submitted that ASIC’s policy objective for continuing to impose the 20% limit on investment products which are quoted on a financial market as part of the definition of ‘wholesale equity scheme’ was unclear. They submitted that this requirement should be removed on the basis that it can place trustees in technical breach and may preclude the orderly exit of investments on a financial market or prevent compliance with requirements in the ASX Listing Rules in relation to restricted securities. No other submissions were received on this point.

- 20 In May 2007, we released [Consultation Paper 82](#) *Wholesale equity venture capital schemes: Trustee licensing* (CP 82) to consult on providing ongoing AFS licensing relief to wholesale equity venture capital schemes. We included consultation on whether the proposed 20% limit on investments in quoted products was appropriate. We received no submissions about this proposed limit and continued to impose a 20% limit in [CO 07/74].
- 21 We have not received breach reports or applications for individual relief from entities relying on [CO 07/74] to suggest that this 20% limit has proved problematic or that the relief in [CO 07/74] is not operating effectively and efficiently.

ASIC's response

We consider that it is appropriate to retain the 20% limit for investment products which are quoted on a financial market in the definition of 'wholesale equity scheme', having regard to:

- our policy rationale for providing relief from the AFS licensing provisions to remove impediments in the venture capital and private equity industry by allowing wholesale equity schemes to hold equities in small, unlisted, closely held private equities;
- our consultation in [CP 82](#) and [CP 280](#), and the absence of any submissions about the 20% limit from all the other respondents; and
- the absence of breach reports or applications for individual relief from entities relying on [CO 07/74] to suggest that this limit has been problematic.

Aligning financial and custody requirements for trustees

- 22 In [CP 280](#), we proposed to align the relief provided to trustees of wholesale equity schemes in [CO 07/74] with the financial and custody requirements that were introduced in 2013 to address risks associated with the provision of these services.
- 23 Under [CO 07/74], a trustee must:
- (a) be able to pay all its debts as and when they become due and payable under condition 13(a) of [Pro Forma 209](#) *Australian financial services licence conditions* (PF 209);
 - (b) have total assets that exceed total liabilities or adjusted assets that exceed adjusted liabilities under condition 13(b) of PF 209;
 - (c) meet the cash needs requirement under condition 13(c) of PF 209; and
 - (d) lodge an audit report under condition 28 of PF 209.

- 24 Under the relief proposed in [CP 280](#), a trustee, as a custodial and depository service provider, would (subject to the transitional relief discussed in paragraphs 31–32 below) need to comply with:
- (a) conditions 13(a) and 13(b) of [PF 209](#);
 - (b) the tailored cash needs requirement implemented through [\[CO 13/761\]](#) instead of the cash needs requirement under condition 13(c) of [PF 209](#) imposed under [\[CO 07/74\]](#);
 - (c) the requirement to lodge an audit report opinion on its compliance with the tailored cash needs requirement implemented through [\[CO 13/761\]](#) instead of an audit report under condition 28 of [PF 209](#) imposed under [\[CO 07/74\]](#); and
 - (d) the custody requirements for providers of custodial and depository services implemented through [\[CO 13/1410\]](#).
- 25 However, under the proposed relief, a trustee, as a custodial and depository service provider, would not need to meet the NTA requirements or lodge an audit report opinion on its compliance with the NTA requirements in [\[CO 13/761\]](#).
- 26 One respondent queried the need for the financial and custody requirements to apply to trustees because they already apply to the manager, but agreed with our proposal that the NTA requirements not apply to trustees on the basis that trustees would often struggle to satisfy NTA requirements.
- 27 All of the remaining respondents supported aligning the conditions imposed on trustees under [\[CO 07/74\]](#) with the financial and custody requirements.

ASIC's response

Subject to the transitional relief discussed in paragraphs 31–32, we have imposed a condition that trustees comply with the equivalent requirements for licensed providers of custodial and depository services implemented through:

- [\[CO 13/761\]](#) (excluding the NTA requirements and the audit requirements insofar as they relate to compliance with the NTA requirements) as outlined in [RG 166](#); and
- [\[CO 13/1410\]](#) as outlined in [RG 133](#).

We consider that it is appropriate to align the conditions imposed on trustees with the financial and custody requirements to address risks associated with the provision of these services and to promote consistency and the informed participation of investors.

Aligning financial requirements for managers

- 28 In [CP 280](#), we proposed to:
- (a) align the requirement contained in paragraph 5(a)(C) of [CO 07/74] that managers treat the assets, liabilities, cash inflows and cash outflows of the trustee as though they were included in the assets, liabilities, cash inflows and cash outflows of the manager with the financial requirements in [\[CO 13/760\]](#) and [\[CO 13/761\]](#); and
 - (b) achieve this outcome through the Declaration in Part 3 of the draft instrument to avoid requiring AFS licence variations for all managers.
- 29 As an AFS licensee, the manager must already meet the financial requirements implemented through [\[CO 13/760\]](#) and [\[CO 13/761\]](#) and outlined in [RG 166](#), subject to the authorisations on the manager's AFS licence.
- 30 The submissions received were supportive of this proposal.

ASIC's response

[ASIC Corporations \(Amendment and Repeal\) Instrument 2017/848](#) amends s912AA and 912AC (as notionally inserted by [\[CO 13/760\]](#) and [\[CO 13/761\]](#)) so that the manager must treat the assets, liabilities, cash inflows and cash outflows of the trustee as though they were included in the assets, liabilities, cash inflows and cash outflows of the manager for the purposes of [\[CO 13/760\]](#) and [\[CO 13/761\]](#).

This has the same effect as the proposed Declaration, but consolidates the amendments to s912AA and 912AC in the instruments under which they were originally inserted. A note has been included under paragraph 5(a)(C) of [ASIC Corporations \(Wholesale Equity Scheme Trustees\) Instrument 2017/849](#) explaining how s912AA and 912AC (as notionally inserted by [\[CO 13/760\]](#) and [\[CO 13/761\]](#)) apply to managers.

Transitional relief

- 31 In [CP 280](#), we proposed to:
- (a) repeal [CO 07/74] on the same date as we would make a new legislative instrument preserving the effect of [CO 07/74] beyond the sunset date of 1 October 2017; and
 - (b) provide transitional relief in the new legislative instrument to a trustee that relied on the relief in [CO 07/74] immediately before its repeal to enable the relief under [CO 07/74] to continue until the end of the financial year of the trustee (if the repeal does not occur at the end of

the financial year of the trustee) to simplify the preparation of financial reports and the audit process.

- 32 One respondent submitted that the transitional relief proposed would provide sufficient time to meet the new financial and custody requirements, which would require manager and trustee entities to review and make changes to their financial requirements and asset holding arrangements. The other respondents did not object to the transitional relief proposed.

ASIC's response

We have:

- repealed [CO 07/74] on the same date that we made [ASIC Corporations \(Wholesale Equity Scheme Trustees\) Instrument 2017/849](#), preserving the effect of [CO 07/74]; and
- provided transitional relief to a trustee that relied on the relief in [CO 07/74] immediately before its repeal to enable the relief under [CO 07/74] to continue until the end of the financial year of the trustee (if the repeal does not occur at the end of the financial year of the trustee).

We consider that the transitional relief available under the new legislative instrument provides sufficient time for alternative arrangements to be made and simplifies the preparation of financial reports and the audit process.

Appendix: List of non-confidential respondents

- Allens Linklaters
 - Australian Private Equity & Venture Capital Association Limited (AVCAL)
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