

ATTACHMENT A: OVERVIEW OF THE MANAGED INVESTMENT SCHEME REGULATORY FRAMEWORK

Summary

1. This attachment sets out a summary of the managed investment scheme (MIS) regulatory framework as it applies to MIS and the operators of MIS. For the most part, the framework is contained in Chapter 5C and Chapter 7 of the *Corporations Act 2001* (Corporations Act).¹

Definition of a MIS

2. A MIS is defined in the Corporations Act as a scheme having the following key features:²
 - (a) people contribute money or money's worth to acquire rights to benefits produced by the scheme;
 - (b) contributions are pooled, or used in a common enterprise, to produce financial benefits, or benefits consisting of rights or interests in property, for members of the scheme; and
 - (c) members do not have day-to-day control over the operation of the scheme.

Types of MIS

3. MIS cover a wide variety of structures. Some examples of MIS include:
 - (a) unitised trust based MIS;
 - (b) common enterprise (contract based) MIS;
 - (c) platform arrangements such as IDPS; and
 - (d) managed discretionary accounts.
4. The categories of investment are also very broad and include:
 - (a) Financial asset MIS, such as cash management trusts, Australian equity (share) MIS, international equities MIS and exchange traded funds (ETFs);
 - (b) property MIS;
 - (c) mortgage MIS;
 - (d) commodities MIS;
 - (e) crypto-asset MIS;
 - (f) litigation funding MIS;
 - (g) agricultural MIS;
 - (h) horse-breeding and horse racing MIS;
 - (i) time-sharing MIS;³ and
 - (j) management rights and serviced strata MIS.

¹ Relevant obligations are found in other Chapters the Corporations Act, such as financial reporting requirements (Part 2M.3) and continuous disclosure obligations (Chapter 6CA).

² *Corporations Act 2001* (Cth) (Corporations Act) s 9.

³ Time-sharing schemes are specifically included in the definition of an MIS in s 9 of the Corporations Act

5. MIS may be listed, where units in the fund are available for purchase on an exchange, or unlisted, where units are not listed on an exchange and must be purchased from an adviser, platform or directly from the fund manager.
6. Interests in MIS are financial products⁴ and, as such, operators are required to hold an Australian Financial Services (AFS) licence and are subject to conduct and disclosure obligations under Ch 7 of the Corporations Act.

ASIC's role in relation to regulating MIS

7. ASIC's role in regulating MIS includes:
 - (a) assessing Australian financial service AFS licence applications submitted by entities seeking to be operators of registered and unregistered MIS;
 - (b) assessing applications for registration of MIS;
 - (c) exercising ASIC's administrative powers in relation to AFS licences and disclosure;
 - (d) providing guidance to industry;
 - (e) providing relief from provisions of the Corporations Act where necessary and appropriate;
 - (f) undertaking proactive and reactive supervision and surveillance activities into operators' conduct and disclosure obligations; and
 - (g) taking regulatory action in response to non-compliance with the laws administered by ASIC.

Registration of a MIS

8. Generally, a MIS offered to retail clients must be registered with ASIC if it has more than 20 members or is promoted by a person in the business of promoting a MIS. MIS only offered to wholesale clients are not required to be registered and are referred to as 'unregistered MIS' or 'wholesale MIS'.
9. Under the Corporations Act, ASIC *must* register a MIS within 14 days of lodgement of an application, unless it appears to us that:
 - (a) the application does not comply with the requirements of the Corporations Act;
 - (b) the proposed responsible entity (RE) is not a public company that holds an AFS licence that authorises it to operate the MIS;
 - (c) the MIS's constitution does not meet the requirements of the Act;
 - (d) the MIS's compliance plan does not meet the requirements of the Act;
 - (e) the copy of the compliance plan lodged with the application is not signed by all of the directors of the RE; or
 - (f) arrangements are not in place that will satisfy the Act in relation to the audit of compliance with the MIS's compliance plan.
10. There is no prescribed form for the constitution or the compliance plan. However, the application must state which provisions of the constitution address the matters in ss601GA and 601GB of the Corporations Act.

⁴ Corporations Act s 764A(1)(b) and (ba).

11. The constitution of a registered MIS must be legally enforceable between the RE and members and must make adequate provision for:
 - (a) the consideration to be paid to acquire an interest in the MIS;
 - (b) the powers of the RE in relation to making investments of, or otherwise dealing with, MIS property;
 - (c) the method for dealing with member complaints;
 - (d) any rights of members to withdraw from the MIS; and
 - (e) winding up of the MIS.
12. If the RE is to have any rights to be paid fees out of MIS property, or to be indemnified out of MIS property for liabilities or expenses incurred in relation to the performance of its duties, those rights must be specified in the constitution and must be available only in relation to the proper performance of those duties.
13. A compliance plan must set out adequate measures to ensure that the MIS complies with the Corporations Act and the MIS constitution.
14. The RE must engage an auditor to audit compliance with the MIS compliance plan. The auditor must, within three months of the end of the financial year of the MIS, audit the RE's compliance with the compliance plan during the year and provide a report to the RE. The RE must then lodge the compliance plan audit report with ASIC at the same time it lodges the financial report for the MIS.
15. ASIC does not have a residual discretion to refuse to register a MIS where the above statutory requirements are satisfied.

Key roles in relation to a MIS

The RE

16. The RE of a registered MIS is required to be a public company and must operate the MIS and perform the functions conferred on it by the constitution and the Corporations Act. A RE can appoint an agent to undertake its functions, for example a custodian to hold MIS property or an external investment manager. However, the RE remains responsible for the acts of its agents.
17. REs are subject to the following duties in Chapter 5C of the Corporations Act. In exercising its powers and carrying out its duties, the RE must:
 - (a) act honestly;
 - (b) exercise a reasonable degree of care and diligence;
 - (c) act in the best interests of the MIS members;
 - (d) treat the members who hold interests of the same class equally and members who hold interests of different classes fairly;
 - (e) not make use of information acquired through being the RE in order to gain an improper advantage or cause detriment to the members of the MIS;



- (f) ensure that MIS property is clearly identified and held separately from other property
- (g) ensure that the MIS property is regularly valued; and
- (h) ensure that all payments out of the MIS property are made in accordance with the MIS constitution and the Corporations Act.

Wholesale trustee

18. The operator of a wholesale MIS is known as a 'wholesale MIS operator' or 'wholesale trustee'. Wholesale trustees must generally hold an AFS licence authorising them to issue interests in the unregistered MIS but are not required to be a public company. A wholesale MIS may use a similar structure to that used by a registered MIS.

Investment managers vs fund managers

19. The terms 'investment manager' and 'fund manager' are often used interchangeably. However, the term 'investment manager' best describes the entity responsible for the asset selection and portfolio management for a MIS whereas 'fund manager' refers more broadly to the entity (including RE or wholesale trustee) responsible to investors for the MIS.

20. A fund manager can also act as the investment manager for a MIS. This can provide efficiency in the provision of funds management services to investors but may also lead to conflicts as the fund manager is entitled to act in its own interests in its capacity as investment manager but is required to act in the best interests of investors in its capacity as fund manager.

21. REs and wholesale trustees must hold an AFS licence authorising them to issue interests in, and operate, any relevant MIS. As AFS licensees, MIS operators are subject to general conduct obligations set out in s912A of the Corporations Act, including the obligation to:

- (a) provide financial services efficiently, honestly and fairly;
- (b) maintain the competence to provide the financial services;
- (c) comply with the conditions on the licence;
- (d) comply with the financial services laws;
- (e) have adequate arrangements for the management of conflicts of interest;
- (f) take reasonable steps to supervise its representatives;
- (g) have adequate financial, technological and human resources; and
- (h) have adequate risk management systems.

22. ASIC must grant an AFS licence to anyone who applies, in accordance with s913B of the Corporations Act, where:

- (a) all required documents were submitted by the applicant;
- (b) ASIC has no reason to believe that the applicant is likely to contravene the obligations that will apply under s912A if the licence is granted;
- (c) ASIC is satisfied that there is no reason to believe that the applicant, or in the case of a body corporate its responsible officers, is not of good fame or

- character or that the applicant's ability to provide the financial services covered by the licence would nevertheless not be significantly impaired;
- (d) the applicant has provided ASIC with any additional information ASIC has requested; and
 - (e) the applicant meets any other relevant requirements prescribed by regulations.

23. REs are also subject to additional conduct obligations under the Corporations Act. They must hold adequate professional indemnity insurance and maintain internal dispute resolution procedures and membership of an external dispute resolution scheme (generally the Australian Financial Complaints Authority). These requirements do not apply to wholesale trustees.
24. The Corporations Act imposes duties on officers and employees of the RE in relation to the MIS. These duties override any conflicting duty they may have under Chapter 2D.1 of the Corporations Act as an officer or employee of the RE.
25. If less than half of the directors of a RE are external directors, the RE of a registered MIS must establish a compliance committee. The compliance committee must have a majority of external members.
26. The role of the compliance committee is to monitor the RE's compliance with the Corporations Act, the financial services laws and the conditions of its AFS licence.
27. The RE of an MIS can be changed. A RE may retire, members may remove the RE at a member meeting or, where there is not a RE for the MIS that meets the requirements of the Corporations Act, the current RE, members or ASIC may apply to the court for the appointment of a temporary RE.
28. The role of a temporary RE is to take steps to appoint a new RE. The temporary RE must call a meeting of members within 3 months of its appointment to vote on the appointment of a new RE.
29. Where the RE of the MIS changes:
- (a) the former RE must give any books relating to the MIS and provide reasonable assistance to the new RE; and
 - (b) the rights, obligations and liabilities of the former RE in relation to the MIS become rights, obligations and liabilities of the new RE.

Key aspects of operating and closing a registered MIS

Members' right to withdraw from a MIS (MIS Liquidity)

30. The constitution of a registered MIS may make provision for members to withdraw when the MIS is liquid or illiquid. The RE must not allow a member to withdraw from the MIS:
- (a) if it is liquid, otherwise than in accordance with the MIS constitution; or

(b) if it is not liquid, otherwise than in accordance with the MIS constitution and the non-liquid provisions of the Corporations Act.

31. A registered MIS is liquid where 80% of its assets are liquid. Liquid assets are defined in the Corporations Act as being any of the following kinds of assets unless it is proved that the RE cannot reasonably expect to realise them within the period specified in the constitution for satisfying withdrawal requests while the MIS is liquid:

- (a) money in an account or on deposit with a bank;
- (b) bank accepted bills;
- (c) marketable securities;
- (d) property of a prescribed kind; or
- (e) any other property is a liquid asset if the RE reasonably expects that the property can be realised for its market value.

32. The Corporations Act sets out a process for REs to make withdrawal offers to members of non-liquid MIS. The RE must make an offer in writing to all members of the MIS or all members of a class of the MIS. Only one offer is to be open at a time and the RE may cancel the offer. The RE must pro-rata amounts paid if it receives withdrawal offers that exceed the amount available in the MIS to meet withdrawals under the terms of the withdrawal offer.

Effect of contraventions (civil liability and voidable contracts)

33. A member of a registered MIS who suffers loss or damage because of the conduct of the MIS's RE that contravenes a provision of Chapter 5C may recover the amount of the loss or damage by action against the RE whether or not the RE has been convicted of an offence or has had a civil penalty order made against it, in respect of the contravention. An action must be begun within 6 years after the cause of action arises.

34. If a MIS is:

- (a) being operated in contravention of the requirement for it to be registered and offers of interests are made or issued for an interest in the MIS; or
 - (b) a PDS was not issued when required,
- a contract entered into to subscribe for the interest as a result of the person accepting the offer, or of the acceptance of an offer made by the person in response to the invitation, is voidable at the option of that person by notice in writing to the offeror.

Winding up

35. A MIS can be wound up:

- (a) under the terms of the constitution;
- (b) pursuant to a direction of members voting at a member meeting;
- (c) where the RE considers the purpose of the MIS has been accomplished or cannot be accomplished; or
- (d) under order of the court.

36. The following parties can apply to the court for an order for the winding up of a registered MIS:
- (a) the RE;
 - (b) a director of the RE (or a creditor);
 - (c) a member of the MIS; or
 - (d) ASIC.
37. The RE must ensure that the MIS is wound up in accordance with the constitution and any court orders.
38. If, on completion of the winding up of a registered MIS, there are unclaimed or undistributed money or other property that was part of the MIS property, these must, as soon as practicable, be paid or transferred to ASIC to be dealt with as unclaimed monies.

Deregistration

39. A registered MIS can be deregistered on the application of the RE where:
- (a) the MIS has less than 20 members and is not required to be registered; or
 - (b) the MIS is not required to be registered and all the members agree the MIS should be deregistered or the scheme is not an MIS.
40. ASIC can initiate the deregistration of a MIS where:
- (a) the MIS does not have a RE;
 - (b) the MIS does not have a constitution that meets the requirements of the Act;
 - (c) the MIS does not have a compliance plan that meets the requirements of the Act;
 - (d) the property of the MIS is not being clearly identified as MIS property, and held separately from property of the operator and property of any other MIS, in accordance with the fund's compliance plan;
 - (e) the response to a return of particulars given to the operator of the MIS is at least 6 months late, no other documents have been lodged by or on behalf of MIS in the last 18 months and ASIC has no reason to believe the MIS is being operated;
 - (f) the review fee for the MIS in respect of a review date has not been paid in full at least 12 months after the due date for payment; or
 - (g) the MIS has been wound up.
41. ASIC may reinstate the registration of an MIS if ASIC is satisfied that it should not have been deregistered or if the defect that led to it being deregistered has been remedied. A court can also order ASIC to reinstate the registration of an MIS.

Key aspects of operating and closing an unregistered MIS

42. Wholesale trustees are not subject to the requirements of Chapter 5C in operating and closing a wholesale MIS and these matters will be determined by the trustee and outlined in the trust deed for the MIS.



MIS disclosure obligations

43. A Product Disclosure Statement (PDS) must be provided to a retail client who wishes to acquire a financial product, such as an interest in a MIS. The PDS must contain sufficient information so that the consumer may make an informed decision about whether to purchase the financial product, including information about fees payable and the risks, benefits and significant characteristics of the product.
44. Retail clients must also be provided with any new material information via a supplementary or new PDS, and periodic statements containing prescribed information that the issuer reasonably believes the client needs to understand their investment in the financial product. Retail clients must also be notified of any material change or significant event that affects a matter that would have been required to be specified in the PDS for the MIS.
45. If a registered MIS is a 'disclosing entity', it is subject to continuous disclosure obligations. A disclosing entity includes certain listed MIS and unlisted MIS in which 100 or more people hold an interest in the MIS because of offers that required a PDS. Listed MIS will also need to comply with the relevant listing rules.
46. Unlisted MIS are required to make such information available to investors as soon as practicable after becoming aware of the information, either by lodging it with ASIC or publishing material on its website.
47. The operator of a wholesale MIS is not required to provide a PDS (or ongoing disclosures) to wholesale investors.

Financial reporting

48. Registered MIS are subject to financial reporting and audit obligations under the Corporations Act. This means the RE must prepare annual audited financial statements for the MIS. These statements must be lodged with ASIC and sent to members. If a registered MIS is also a 'disclosing entity', it must also prepare and lodge half-yearly reports.
49. AFS licensees are subject to financial reporting obligations under Chapter 7 of the Corporations Act. REs are also subject to their own financial reporting obligations under Chapter 2M.

Surveillance and enforcement of MIS

50. The fact that a MIS operator is licensed, or a MIS is registered, does not mean that ASIC has closely considered the desirability, robustness, or risk profile of the products being offered. Licensing and registration should be understood as imposing legal obligations on AFS licensees, with ASIC undertaking risk-based surveillance to enforce compliance with those obligations.

51. Whilst ASIC's surveillance work tends to focus on REs of registered MIS and protection of retail clients, we also, from time to time, undertake surveillances of wholesale trustees to ensure that they are complying with their obligations as AFS licensees.

Surveillance of conduct

52. ASIC takes a risk-based approach to surveillance. A surveillance may be triggered by:

- (a) the reporting of a 'reportable situation' (previously, a breach notification) by the MIS operator;
- (b) a report from a compliance plan auditor or compliance committee;
- (c) a person reporting misconduct;
- (d) periodic reporting by an RE (such as qualified financial statements); or
- (e) our proactive targeted surveillance of entities or sectors.

53. Where an entity is targeted for surveillance, our approach to that entity varies with the circumstances. ASIC will generally approach an RE to seek voluntary assistance with our surveillance, however, we do also use our information gathering powers under the Corporations Act and ASIC Act where it is considered appropriate.

54. Where ASIC has received sufficient information to become concerned that a MIS is not being run in the best interest of members, or the RE is not complying with its other conduct obligations, ASIC may take regulatory action, including administrative action (such as suspension or cancellation of the AFS licence) or enforcement action (such as civil or criminal proceedings including to wind-up the MIS).

55. ASIC typically considers the following factors when selecting matters for formal investigation and possible enforcement action:

- (a) areas of significant harm (e.g. actual or potential harm to vulnerable consumers or investors, particularly if the behaviour is predatory);
- (b) broader public benefit (e.g. enforcement action that is likely to influence other entities by sending an effective deterrence message to the industry);
- (c) issues specific to the case (e.g. the nature of the misconduct – such as whether it was dishonest or deliberate; the impact of the misconduct – including the amount of money lost; and the time elapsed since the misconduct occurred); and
- (d) alternatives to formal investigation (i.e. whether it is more efficient and effective to address the matter using other regulatory tools).

Surveillance of disclosure

56. ASIC does not review a PDS before it is issued. An RE is not required to lodge a copy of a PDS with ASIC unless the MIS is listed or will be listed on an exchange. In all other cases ASIC is merely 'notified' that a new PDS has been issued.



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57. ASIC may undertake a risk-based targeted review of PDSs and marketing materials at any time. Where we identify compliance issues, we may request amended disclosures and/or use our stop order powers to address our concerns.

ASIC's Exemption and modification powers

58. ASIC has powers to exempt a person from various provisions of the Corporations Act or declare that provisions apply to a person as if specified provisions were omitted, modified or varied as specified in the declaration.