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Trustee Corporations Association of Australia

26 June 2009

Dr Shona Batge
Committee Secretary
Parliamentary Joint Committee
on Corporations and Financial Services
PO Box 6100
Parliament House
CANBERRA ACT 2600

Dear Dr Batge

Inquiry into Agribusiness Managed Investment Schemes

The Trustee Corporations Association (TCA) is the peak representative body for the trustee corporations industry in Australia.

It represents 17 organisations, comprising all 8 regional Public Trustees and the great majority of the 10 private statutory trustee corporations.

We appreciate the opportunity to provide comments in relation to the Committee's inquiry into Agribusiness Managed Investment Schemes.

Background

Statutory trustee corporations provide a wide range of financial services to individual, family and corporate clients.

Their core 'traditional' services include:

- estate planning
- preparing wills
- acting as executor / administrator of deceased estates
- establishing and administering personal and charitable trusts
- preparing and administering Powers of Attorney

- acting as guardian or financial manager, usually under Court or Tribunal order, for persons unable to look after their own affairs

A number of TCA members also provide various 'corporate' trust services, including acting as Responsible Entity (RE) and / or custodian for managed investment schemes (MIS).

Prior to the introduction of the *Managed Investments Act 1998* (MIA), several TCA members were very active as trustees for what were then called 'collective investment schemes', monitoring the activities of the scheme managers.

At the time of the MIA's introduction, the TCA expressed strong concerns that the new regime would seriously weaken the investor protection afforded to the billions of dollars held in those schemes for superannuation and other purposes.

We noted that, following some problems in the industry a few years earlier, caused in large part by the dramatic collapse of commercial property values, the substantial amounts of money recovered by investors came mostly from the trustees and their insurers rather from the managers (who had few assets).

Our concerns were subsequently restated in the TCA's submissions to the 'Turnbull' review in 2001, and to Treasury and the Joint Committee on Corporations and Financial Services' assessment of Turnbull's report in 2002.

Comments

The recent difficult economic conditions, which have included sharp falls in various asset prices, have presented the first serious 'stress test' of the new MIS regime since its introduction.

While agricultural schemes have some distinctive structural and operational features, we feel that the comments we previously put forward, as noted above, continue to apply in respect of MIS generally.

<u>Shortcomings of the MIA</u>

The MIA has fundamental structural flaws, ie:

- there is an inherent conflict of interest within the RE structure that can expose scheme members to unacceptable risk of loss.
- there is a lack of independence due to the fact that an RE's 'external' directors or Compliance Committee members are appointed by, paid by, and may be removed by the RE.
- timely compliance monitoring is not undertaken by a body independent of the RE.
- 'hindsight' monitoring has been an important contributing factor in a number of corporate failures, eg the losses suffered by investors in relation to the HIH, Enron, Commercial Nominees and the solicitors' mortgage scheme debacles.

- there is a lack of appropriate accountability to investors by the RE.
- scheme property is not required to be held by an independent custodian.
- schemes have insufficient financial underpinning - REs with Net Tangible Assets (NTA) of only $5 million (the maximum required) and $5 million of insurance (the maximum required) can, and do, hold at risk many billions of dollars of investors' funds.
- Where a Receiver is appointed to the Responsible Entity, the Receiver is appointed by the Secured Creditors. Whilst the Receiver owes a duty to the investors in the scheme, it also owes a duty to the Secured Creditors, and these duties may conflict. ASIC might be left as the only party protecting the interests of the investors.
- ASIC found breaches and compliance failures in 83% of REs inspected in 2000/01[we are not aware of any more recent data].

Recommendations

We believe that a more robust MIS structure would entail:

- clearly defining the roles and liabilities of all parties involved in the running and oversight of MIS. These include the financial auditor, custodian, compliance monitor, and any other service providers.

  Importantly, the RE should have full responsibility for the operation of a scheme, and be solely responsible for the prudence of investments (and hence the performance of the scheme).

- eliminating the Compliance Committee and expanding the present function of the compliance plan auditor to encompass:
  - more frequent and timely monitoring the RE's performance in relation to its obligations under the MIA, and each scheme's constitution and compliance plan.
  - monitoring related party dealings.
  - reporting periodically, say quarterly, to the RE and, as necessary, to ASIC on the RE's compliance procedures and the conduct of the scheme.
  - potentially acting as 'investor champion' if action against the RE is required.

  Consideration might be given to appointing a party with a similar role to that of a Security Trustee in wholesale schemes. This Security Trustee could either be involved on an ongoing basis (cf a Debenture Trustee receiving and reviewing reports), or be appointed to act where a Receiver is appointed.

- widening access to the compliance monitoring role - allowing other qualified professionals to take on this work would introduce more competition in this area and could be expected to place downward pressure on costs.

- strengthening the financial underpinnings of MIS - the regulatory framework should mandate a more meaningful level of capital and insurance for REs and all commercial service providers which has regard to the size of funds under management and is not capped at a level as low as $5 million.

  Such an approach would provide more substantial means of compensating investors, with less likelihood of the need to draw on the public purse, in the event of losses due to maladministration, negligence or fraud.

We would be pleased to provide any further information that the Committee might require.

Yours faithfully

Tony Keywood

Manager Operations