

EXPOSURE DRAFT OF AMENDMENTS TO THE CORPORATIONS REGULATIONS 2001 RELATING TO TRUSTEE COMPANIES

MARCH 2010

COMMENTARY

Background

The *Corporations Legislation Amendment (Financial Services Modernisation) Act 2009* (the Modernisation Act) received Royal Assent on 6 November 2009. Schedule 2 of the Act inserts Chapter 5D (Licensed trustee companies) into the Corporations Act and makes adjustments to the financial services regime in Chapter 7 to accommodate traditional trustee company services. Schedule 2 also inserts a number of regulation making powers into the Corporations Act to specifically deal with trustee company matters.

In brief, the provision of a traditional trustee company service by a trustee company constitutes the provision of a financial service. The trustee company providing this service as part of its business will need an Australian financial services licence. Trustee companies will thus be subject to the consumer protection and disclosure requirements of the Act and the *Australian Securities and Investments Commission Act 2001*. Licensed trustee companies will be subject to new Chapter 5D which addresses, among other things, fees, duties of officers, limits on control of trustee companies and transfer of business if a trustee company's Australian financial services licence is cancelled.

An earlier draft of the regulations was released for public consultation on 21 August 2009. The consultation period closed on 18 September. Five submissions were received and the comments made in them have been taken into account.

It is proposed that Schedule 2 of the Modernisation Act commence on 1 May 2010.

OUTLINE OF THE DRAFT REGULATIONS

Listing of trustee companies

- The regulations insert a list of trustee companies that will be required to hold an Australian financial services licence (AFSL) covering the provision of traditional trustee company services. Further, the regulations state that a State or Territory Public Trustee must only be listed if the State or Territory asks the Commonwealth Minister to list the trustee, and the Minister agrees.

Traditional trustee company services

- The regulations clarify the ambit of 'traditional trustee company services' by specifically excluding certain conduct from this concept.

Ambit of legislation with respect to guardianship matters

- The regulations provide that matters relating to the role of trustee companies as administrators of estates under the State and Territory guardianship legislation will remain subject to State

and Territory laws and tribunals. In this role, trustee companies will however be supervised by ASIC in relation to their AFSL conditions, their charging of fees and certain other matters.

Annual information return

- The regulations create a requirement for a licensed trustee company to provide an annual information return when requested by certain specified persons. The regulations also specify the content.

Retail and wholesale clients

- The regulations provide two exceptions to the general rule that clients receive traditional trustee company as retail clients.

Persons taken to be provided with a traditional trustee company service

- The regulations prescribe certain persons to whom a traditional trustee company service is taken to be provided. They are: a person entitled to request an annual information return (other than a beneficiary); and a person who requests the preparation of a will, a trust instrument, a power of attorney or an agency agreement.

Rights of beneficiaries

- The regulations provide that beneficiaries are covered by the licensed trustee company's dispute resolution and compensation arrangements

Common funds

- The regulations include provisions regulating the establishment and operation of common funds of trustee companies.

Exception from 'dollar disclosure' rules

- The regulations provide trustee companies with an exception from the normal requirement to disclose fees, commissions and other charges as a dollar amount. The regulations permit the remuneration, commission or other benefits to be stated as a percentage of the income or the capital value of the estate.

Transitional provisions

- The Regulations include transitional provisions in relation to services which are the subject of capped fees and which are being provided at the time of commencement, and in relation to existing common funds.

Details of the Regulations appear in the Attachment.

As indicated in the draft Regulations, further instructions are to be provided to the drafter to address:

- transitional provisions (possibly a deemed Australian financial services licence for a limited period covering only traditional trustee company services) for those trustee companies which do not hold an Australian financial services licence; and
- the list of State and Territory Acts and provisions to be included in the regulations to be made for the purpose of subsection 601RAE(4).

COMMENTS

You may wish to comment on the following issues:

1. If those trustee companies which do not currently have an AFSL are provided with a transitional deemed licence, would they have difficulty meeting the requirements of Part 7.8 of the Act?

2. Will trustee companies have difficulty in the short term in complying with paragraph 912A(1)(g) (dispute resolution arrangements) and section 912B (compensation arrangements) in relation to traditional trustee company services?
 - If so, should the date of effect of these requirements be delayed?
3. Which provisions of State and Territory legislation do you consider should be specified in the regulations made for the purpose of subsection 601RAE(4)?
 - Note that the States and Territories have also been asked to provide lists for this purpose.
4. Does your company currently provide some or all of the information required to be included in the annual information return?
5. Would your company have difficulty in complying with the common fund provisions from 1 July 2010?
6. Do you have any comments on the timing requirements in the common fund provisions?
 - Is the requirement for a monthly valuation of common fund assets appropriate?
 - If not, what period do you suggest?
7. Is there a need to recognise existing valuation methodologies for common funds?

Note that the regulations no longer include provision for the voluntary transfer of a trustee company business within a corporate group. This follows advice on the limits of the regulation-making power.

The Regulations are a legislative instrument for the purposes of the *Legislative Instruments Act 2003*.

Regulations 1-4 and Schedule 1 of the Regulations will commence on 1 May 2010. Schedule 2 of the Regulations will commence on 1 July 2010.

Details of the Corporations Amendment Regulations 2010 (No.)

Regulation 1 – Name of Regulations

This regulation provides that the title of the Regulations is the *Corporations Amendment Regulations 2010 (No.)*.

Regulation 2 – Commencement

This regulation provides for regulations 1 to 4 and Schedule 1 of the amending regulations to commence on the same day as Schedule 2 of the Modernisation Act (1 May 2010). Schedule 2 of the amending regulations will commence on 1 July 2010.

Regulation 3 – Amendment of Corporations Regulations 2001

This regulation provides that the *Corporations Regulations 2001* (the Principal Regulations) are amended as set out in Schedules 1 and 2.

Regulation 4 – Transitional

This regulation addresses the situation where, as at 1 May 2010, a trustee company is providing a service to an existing client and the fee for that service is specified or capped by State or Territory law in force immediately before that date.

This transitional provision does not apply to fees for being a trustee or manager of a charitable trust. Division 4 of Part 5D.3, which was inserted by the Modernisation Act, addresses the fees payable in relation to new and existing client charitable trusts.

Regulation 5 – Application to established common funds

This Regulation addresses common funds which were established before 1 July 2010, the date on which Schedule 2 of the Regulations will commence, and continue to operate after that day. In brief, it adjusts the timing of the application of the requirement in Schedule 2 of the Regulations about making a decision on the details of the operation of such funds.

**SCHEDULE 1 – AMENDMENTS COMMENCING ON COMMENCEMENT OF THE
*CORPORATIONS LEGISLATION AMENDMENT (FINANCIAL SERVICES
MODERNISATION) ACT 2009***

Item [1] – Chapter 5D

Item 1 inserts new Chapter 5D into the Principal Regulations.

Part 5D.1 Preliminary

Regulation 5D.1.01 Meaning of *trustee company*

Subsection 601RAB(1) of the Act states that a trustee company is a company: (a) that is a corporation to which paragraph 51(xx) of the Constitution applies; and (b) that is prescribed by the regulations as a trustee company for the purpose of this Act. Subsection 601RAB(2) states that companies may (for example) be prescribed by setting out a list of companies in the regulations.

Subregulation (1) provides that a company is prescribed as a trustee company if the company is listed in proposed Schedule 8AA.

Subregulation (2) provides that a Public Trustee of any State or Territory must only be listed in Schedule 8AA if: (a) the State or Territory requests the Commonwealth Minister to prescribe the company as a trustee company; and (b) the Minister agrees to the request.

Regulation 5D.1.02 Meaning of *traditional trustee company services and estate management functions*

The concept of ‘traditional trustee company services’ is central to the reforms embodied in Schedule 2 of the Modernisation Act. Subsection 601RAC(1) lists a series of ‘traditional trustee company services’, including performing ‘estate management functions’ (a concept which is elaborated in subsection 601RAC(2)). Subsection 601RAC(3) makes clear that certain services provided by a trustee company are not ‘traditional trustee company services’. They include operating a registered scheme, acting as a receiver of property of a corporation under Part 5.2 and acting in any other capacity prescribed by the regulations for the purpose of paragraph 601RAC(3)(f).

This regulation lists further capacities for the purpose of paragraph 601RAC(3)(f). This means that conduct in carrying out this function is not regarded as a ‘traditional trustee company service’.

The capacities listed acting include as custodian for a responsible entity of a registered scheme, as trustee for the holders of debt securities, as a person named in a will as an executor when not actively providing a service or function.

Some of the terms used in subregulation 5D.1.02(1) are defined in subregulation 5D.1.02(2). They include ‘custodian’ and ‘debt security’. The term ‘mortgage-backed security’ which is used in paragraph 5D.1.02(1)(b) is defined in regulation 5D.1.03.

Regulation 5D.1.03 Meaning of mortgage-backed security

This regulation defines the term ‘mortgage-backed security’. This term is used in paragraph 5D.1.02(1)(b).

In brief, the effect of the provisions is to exclude from the concept of ‘traditional trustee company services’ the conduct of the trustee company as trustee of a trust established for purposes that include issuing mortgage-backed securities or managing the assets of such a trust.

Regulation 5D.1.04 Interaction between trustee company provisions and State and Territory laws

The purpose of this regulation is to ensure that matters relating to the role of trustee companies as administrators of individuals’ estates under the State/Territory guardianship legislation listed in Schedule 8AB remain subject to State and Territory laws and tribunals. However, under Commonwealth law the trustee company would still:

- have to fulfil its general AFSL obligations (except in relation to dispute resolution – see 7.6.02(6));
- be prohibited from engaging in unconscionable conduct;
- be regulated in relation to common funds that contain relevant moneys;
- be regulated in relation to fees charged to clients who are subject to an order under the State/Territory guardianship legislation); and
- be subject to the general duties of officers and employees.

Paragraph 601RAE(4)(b) of the Act states that the regulations may provide that the trustee company provisions (as defined in subsection 601RAE(1)) are intended not to apply to the exclusion of prescribed State and Territory laws, or prescribed provisions of State or Territory laws.

This regulation provides that the trustee company provisions are intended not to exclude the State and Territory laws listed in Schedule 8AB. Schedule 8AB contains a list of laws which deal with guardianship and administration of estates (on behalf of persons not fully able to manage their own affairs).

As indicated in the draft Regulations, other particular State and Territory laws are expected to be prescribed so that they can operate together with the new Corporations Act trustee company regime.

Part 5D.2 Powers etc. of licensed trustee companies

Division 2.1 Annual Information Returns

Regulation 5D.2.01 Obligation on licensed trustee company to provide an annual information return if requested

Section 601SAB of the Act states that the regulations may prescribe (amongst other things) additional powers, functions, liabilities and obligations of licensed trustee companies.

This regulation creates a requirement for a licensed trustee company to provide an ‘annual information return’ to a person who is entitled to request such a return. Those persons include a settlor or appointor of a trust, and a beneficiary of a deceased estate or (in some circumstances) of a testamentary trust.

The annual information return must be provided within 30 days of the request, and then annually.

The regulation specifies the various means by which the annual information return must be provided – for example, in writing or by email.

The annual information return relates to a particular financial year.

Regulation 5D.2.02 Information to be included in the annual information return

This regulation specifies the required content for an annual information return. In general terms this includes:

- details of income and expenses and the net value of the trust’s assets, and
- if required under the terms of the trust – a copy of the trust’s audit report and financial statements for the year.

Part 5D.3 Regulation of fees charged by licensed trustee companies

Regulation 5D.3.01 Modification of section 601TAB of the Act: disclosure to clients of changed fees

Section 601YAB empowers the making of regulations which may, for example, provide that Chapter 5D applies to a person or class of persons as if specified provisions were omitted, modified or varied as specified in the declaration.

This regulation is made for the purpose of subsection 601YAB(2).

It modifies section 601TAB, which relates to disclosure to clients of changed fees, where the client or agent required to be notified is uncontactable.

Item [2] – Regulation 7.1.17B Retail clients: traditional trustee company services

The provision of a traditional trustee company service is a financial service (subsection 766A(1A) which is inserted by Item 19 of Schedule 2 of the Modernisation Act).

Section 761G defines the terms ‘retail client’ and ‘wholesale client’. A number of the protections included in Chapter 7 apply only when the financial service is provided to a retail client.

Subsection 761G(6A) (which is inserted by Item 16 of Schedule 2 of the Modernisation Act) provides that a traditional trustee company service is provided to a person as a retail client unless the regulations made for the purpose of this subsection provide otherwise.

This regulation provides two situations in which the traditional trustee company service is not provided to a person as a retail client. They are where the service is provided to a business that is not a small business and where it is provided to a professional investor.

This is consistent with paragraphs 761G(7)(b) and (d).

The term ‘small business’ is defined in subsection 761G(12) and the term ‘professional investor’ in section 9.

Item [3] Regulation 7.1.28A Circumstances in which a person is taken to be provided a traditional trustee company service

New subsection 766A(1B) of the Act states that the regulations may, in relation to a traditional trustee company service of a particular class, prescribe the person or person to whom a service of that class is taken to be provided. These are:

- a person entitled to request an annual information return under regulation 5D.2.01(3); and
- a person who requests the preparation of a will, a trust instrument, a power of attorney or an agency arrangement.

A comparable amendment is proposed to be made to the *Australian Securities and Investments Commission Regulations 2001* – see the draft Australian Securities and Investments Commission Regulations 2010 Schedule 1, item [1].

Item [4] - Subregulation 7.6.02(6) Alternative dispute resolution systems

Subject to transitional arrangements, trustee companies listed in Schedule 8AA will be required to have an Australian financial services licence covering traditional trustee company services.

A financial services licensee is required to have a dispute resolution scheme complying with subsection 912A(2) if it provides financial services to retail clients (paragraph 912A(1)(g)).

A class of persons may be exempted from this requirement by regulations (subsection 926B(1)(a)).

Item [4] will make such a regulation – 7.6.02(6). In brief, this provides that the requirement for dispute resolution arrangements will not apply where the complaint is about the administration of an estate by an individual if complaints about such services may be made under a State or territory law listed in Schedule 8AB (particularly guardianship legislation).

Items [5] and [8] – Subregulation 7.7.04(3) and 7.7.07(3) Financial Services Guide

Division 2 of Part 7.7 imposes the requirement for a Financial Services Guide to be provided to a retail client and the contents of that Guide.

Regulation 7.7.04(3) and 7.7.07(3) require disclosure of remuneration if it is ascertainable at the time the Financial Services Guide is provided to the client.

The proposed amendments to these subregulations provide trustee companies with an exception from the normal requirement to disclose fees, commissions and other charges as a dollar amount. The regulations permit the remuneration, commission or other benefits to be stated as a percentage of the income or the capital value of the estate, in recognition of the normal practice followed by trustee companies.

Items [6], [7], [9] and [10] – Subregulations 7.7.04(4) and (5) and 7.7.07(4) and (5)

These subregulations correct a technical error in the regulations.

Item [11]

Schedule 8AA Trustee companies

This item inserts a list of trustee companies into the regulations. Each company listed will be a trustee company for the purposes of the Act. This is ensured by Regulation 5D.1.01 which is described above.

Schedule 8AB Prescribed State and Territory laws

This item also inserts a list of prescribed State and Territory laws which are not excluded by the trustee company provisions. The prescribed laws deal with guardianship matters. This Schedule is referred to in 5D.1.04 (which relates to interaction of the Commonwealth provisions with State/Territory provisions) and 7.6.02(6) (which relates to the need for alternative dispute resolution schemes where there is a route for making complaints under the relevant State/Territory legislation).

SCHEDULE 2 AMENDMENTS COMMENCING ON 1 JULY 2010

Item [1]

Division 2.2 Common funds

Regulation 5D.2.03 Common funds

Division 3 of Part 5D.2, which is inserted by the Modernisation Act, deals briefly with common funds. It addresses, for example, the pooling of estate money in a common fund and prohibits

putting estate money into a common fund if doing so is contrary to an express provision of the conditions subject to which the estate money is held.

Section 601SCC empowers the making of regulations relating to the establishment and operation of common funds.

The proposed regulations for this purpose are included in Schedule 2 of the regulations.

This regulation refers to the power in section 601SCC to make the regulations.

Regulation 5D.2.04 Establishment of common funds

This regulation addresses the establishment of accounts within a common fund and the possibility that not all money being put into the common fund is held on trust.

Regulation 5D.2.05 Deciding details about common funds

The regulation requires the licensed trustee company, when deciding to establish a common fund, to make a decision about a list of matters, including investment strategy and fees (5D.2.05(1)).

This decision needs to be provided to ASIC, published on its website and made available to certain persons on request (5D.2.05(2)).

Regulation 5D.2.06 Operation of common funds

This regulation addresses such issues as withdrawals, investments, derivatives, investments and the valuation of investments.

Regulation 5D.2.07 Register of investments

This regulation requires that a licensed trustee company maintain a register of investments for each common fund. The matters to be contained in the register are specified.

Regulation 5D.2.08 Financial reports

The regulation addresses the accounting and auditing requirements in connection with common funds. It also provides a means for requesting a copy of certain information about common funds.

Regulation 5D.2.09 Arm's length transactions

This regulation applies to common funds which are not registered schemes. It addresses related party transactions and uses the exceptions described in section 210.

Item [2]

Regulation 7.6.02AI Modification of subsection 912A(1) of the Act: extension of dispute resolution to beneficiaries

This regulation ensures that a beneficiary of a trust or estate has the right to access internal and dispute resolution mechanisms.

As a result of the trustee company provisions being inserted into the Act, paragraph 912A(1)(g) of the Act, which requires financial services licensees to have a dispute resolution system that

complies with subsection 912A(2), will ensure that clients of trustee company services will have access to dispute resolution. However, there is a need to make special provision for beneficiaries.

The regulation provides that a licensed trustee company must have a dispute resolution system that complies with the normal requirements for such systems and that provides for complaints by beneficiaries.

Specifically, beneficiaries may make a complaint against a financial services licensee if the complaint relates to an alleged breach of the *financial services law* as defined in section 761A of the Act.

Regulation 7.6.02AJ Modification of subsection 912B(1) of the Act: extension of compensation to beneficiaries

This regulation ensures that a licensed trustee company must have compensation arrangements that cover beneficiaries of an estate.

Section 912B of the Act provides that, if a financial services licensee provides a financial service to persons as retail clients, the licensee must have arrangements for compensating those persons for loss or damage suffered because of breaches of obligations under Chapter 7. While this provision will cover clients of licensed trustee companies, special provision needs to be made for beneficiaries.

Item [3]

Schedule 8AC Relevant State and Territory provisions

Regulation 5D.2.06(7) provides that a licensed trustee company commits an offence if it invests money committed to its administration or management, and the investment is not, among other things, made in a manner in which trust funds may be invested by a trustee under the relevant State or Territory provisions.

The relevant State and Territory provisions are listed in Schedule 8AC.