

Enlightenment From Property Trust Regime in Australia

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Outline

- Brief introduction of Property Trust in Australia
- Legal Regime of Managed Investment Scheme (MIS) in Australia
- Australia's Regulatory Bodies and Governing Law
- Governing Laws and Regulations in PRC and The Main Changes
- The Restriction on Trust Sector
- Suggestions

Property Trusts in Australia

- Globally known as “Real Estate Investment Trusts” (REITs)
- There are 71 listed property trust until April of 2007 in Australia, which makes Australia the second largest LPTs market in the world following the U.S.
- Most of property trusts in Australia are in form of managed investment scheme

Taxation Preferences

- Some of the tax associated with the rental income earned by the LPT is deferred
- The tax-deferred component is generally between 15% and 100% of the total income distribution
- The tax-deferred portion is passed through to investors

Listed Property Trusts

- As at April 2007

	Apr-05	Apr-06	Change	Apr-07	Change
Market Cap (\$b)	86	105	22.2%	141	33.9%
Number listed (actual)	53	63	18.9%	71	12.7%
12 month avg trades	84,312	135,213	60.4%	251,578	86.1%
12 month avg value (\$b)	5.54	6.43	15.9%	8.73	35.9%

Listed Property Trusts (cont'd)

- Allow investors to purchase an interest in a diversified and professionally managed portfolio of real estate
- Property trust investors gain exposure to both **the value of the real estate the trust owns, and regular rental income generated from the properties.**
- The fund manager selects the investment properties and is responsible for all maintenance, administration, rentals, and improvements
- Most yield is between 5 - 9% per annum
- LPTs are one of the largest sectors on ASX and currently make up 12% of the world's listed real estate assets

The types of trusts currently available

- Industrial
- Office
- Hotel/Leisure
- Retail
- Diversified
- International

Structures of Property trusts

- Stand-alone trusts or companies providing investors pure exposure to the underlining real estate portfolio
- Stapled securities providing investors exposure to a funds management and/or property development company in addition to a real estate portfolio (25 stapled listed property trusts listed on ASX)

Stapled Securities

- Stapling is an arrangement under which different securities are quoted jointly
- Joint quotation has the effect that the stapled securities cannot be traded separately, as the stapled securities are treated as one unit
- ASX provides joint quotation of stapled securities
 - issued by different entities (eg, shares issued by a company and units issued by a trust)
 - a "twin" structure or
 - a "parent/child" structure
- Different classes of securities issued by the same entity (eg: shares and debentures)
- Joint quotation of more complex combinations of stapled securities (eg: units issued by a trust stapled to shares and debentures issued by a company)

Stapled Securities

Listed Stapled Security

UNITS

Stapled Securities

SHARES

ABC Trust

ABC Funds Management

Assets eg Xyz Tower

Asset management
and/or development

Managed Investment Scheme (MIS)

- Most of property trusts in Australia are in form of managed investment scheme
- **Managed investment scheme** is used in Corporations Act to refer to certain **collective investment arrangements**

What is “Managed Investment Scheme (MIS)”?

- People contribute money to acquire an interest in the scheme
- Any of those contributions are pooled to produce financial benefits for members of the scheme
- Members (or investors) do not have day-to-day control over the operation of the scheme

Exclusion under the definition of MIS

- A body corporate
- A franchise
- Statutory funds under the Life Insurance Act 1995(Cth)
- Funds under the Superannuation Industry (Supervision) Act 1993(Cth)
- A scheme operated by some Australian financial institutions in the ordinary course of their business
- Debentures or convertible notes issued by a body corporate
- Some partnerships, barter schemes, retirement village schemes and co-operative arrangements are also excluded

Popular MIS

- Cash management trusts
- Property trusts
- Australian equity (share) trusts
- Many agricultural schemes (eg horticulture, aquaculture, commercial horse breeding)
- International equity trusts
- Some film schemes
- Timeshare schemes
- Some mortgage schemes
- Actively managed strata title schemes

Registration of an MIS

- Generally, an MIS will have to be registered with the ASIC
- Each MIS is allocated an ARSN (short for Australian registered Scheme Number)
- An MIS does not have to be registered if:
 - A PDS (Product Disclosure Statement) is not required in relation to issues of interests in the MIS, (eg: offers to investors of at least A\$500,000)
 - Non-professional schemes with fewer than 20 members

Structure



The Responsible Entity (RE)

- An MIS must have a RE, who is the scheme's operator
- Requirements
 - Must be a public company
 - Hold an Australian Financial Services (AFS) (the requirements for an AFS licence are demanding, ASIC sets a high standard for people and systems of a RE. There are also financial requirements)
- Duties
 - Statutory duties
 - Exclusive responsibility and authority for operating the MIS
 - Hold scheme property on trust as trustee for scheme members
 - Delegate or contract out its powers and responsibilities but remains liable to members for the actions of others
 - The duty to report breaches to ASIC

Responsible Entity (cont'd)

- Compliance Plan
 - A RE will be required to have a compliance plan for each scheme that it operates
 - Should be signed by all the directors of the RE
 - Must be lodged with ASIC
 - It is a statement of the measures the RE will adopt to ensure that it complies with the Corporations Act and the Scheme's constitution
 - Performance of the compliance plan must be audited annually
- Contents
 - Identification of and valuations for scheme property
 - Independent audit of compliance with the plan
 - The keeping of records for the scheme
 - Arrangements for the operation of the compliance committee (if any)
- Amendment
 - The RE can change the plan
 - ASIC can require the RE to change the plan

Responsible Entity (cont'd)

- External Directors
 - Half of the directors of a RE must be external directors. Otherwise, the RE must have a compliance committee for each MIS it operates
- Compliance Committee
 - A majority of the committee's members must be external members
 - Members of a compliance committee have director like duties and liabilities to the scheme's investors
 - Compliance committee's function:
 - Monitor the RE's compliance with the compliance plan
 - Assess whether the compliance plan is adequate
 - Report any breach to RE or even to ASIC

The Constitution

- Contents must be addressed:
 - What must be paid to acquire an interest in the scheme
 - Investment powers of the RE
 - The borrowing and other fundraising powers of the RE
 - How members' complaints will be dealt with
 - Withdrawal rights and procedures if any
 - The RE's right to fees and any right of indemnity
 - Winding up the scheme
- The constitution of a registered scheme must be contained in a document that is legally enforceable as **between the members and the RE**

Listed on ASX (Listing Rules)

- Admission
 - Structure and operations must be appropriate for a listed entity
 - Must have a constitution, which must be consistent with the listing rules
 - Product Disclosure Statement (PDS) must be issued and lodged with ASIC
 - Need a “sufficient spread” of shareholders: eg, at least 500 holders each having a parcel of main class of securities worth at least \$2,000
 - Must satisfy either:
 - A profit test; or
 - A assets test
 - If the entity is a trust, it must be a registered managed investment scheme and the responsible entity must not be under an obligation to allow a security holder to withdraw from the trust

Disclosure Obligations

- It is required to have a Product Disclosure Statement (PDS)
- Continuous disclosure
 - Immediate notice of material information
 - Notice of specific information
- Periodic disclosure (half-year and annual disclosure)

Wholesale v Retail

- A wholesale fund can draw on high net worth individuals with experience in investment and risk without requiring registration as a MIS
 - Offers to investors of at A\$500,000
 - Offers to high net worth individuals
 - The client is a business which is not a small business
 - Offers to professional investors
- Retail unit trusts are unit trusts
 - required to be registered by the Corporations Act
 - FSR provides for different disclosure requirements for retail and wholesale clients
 - It will be necessary for the manager of the Fund to be a RE and to meet all relevant regulatory requirements
 - Need to create liquidity

Withdrawal Rights

- If members are to have a right to withdraw from the scheme, that must be provided for in the constitution
- The position differs depending upon whether the scheme is liquid:
 - A liquid scheme will have no restrictions on its withdrawal arrangements
 - The RE if a non-liquid scheme may offer members an opportunity to withdraw but must first identify the amount of scheme funds available to satisfy withdrawal requests

Winding Up

- The constitution of a registered scheme must make adequate provision for winding up the scheme
 - Winding up at direction of members (by an extraordinary resolution directing the RE to wind up)
 - Winding up if RE consider scheme's purpose accomplished or can not be accomplished by giving the members and ASIC a explaining notice
 - Winding up ordered by court where is thinks it is just and equitable
- The property need to be carefully identified
- The person appointed to windup a scheme may like a liquidator of a company, be given power to continue to carry on the business of the scheme, but only for the limited purpose of collecting and realising its assets
- After winding up RE may apply to ASIC for deregistration of a scheme

Australia's Regulatory Bodies

<u>ASIC</u>	<u>ACCC</u>	<u>APRA</u>	<u>RBA</u>	<u>ASX</u>
<p>Australian Securities & Investments Commission</p> <p>Monitors and promotes market integrity and consumer protection, the provision of financial services and the payment system</p>	<p>Australian Competition & Consumer Commission</p> <p>Ensures compliance with Commonwealth fair trading and consumer protection laws</p>	<p>Australian Prudential Regulation Authority</p> <p>The prudential regulator of banks, insurance companies, superannuation funds, credit unions, building & friendly societies</p>	<p>Reserve Bank of Australia</p> <p>Regulates monetary policy, maintains financial system stability, promotes the safety & efficiency of the payments system</p>	<p>Australian Securities Exchange</p> <p>Operates Australia's primary stock exchange for derivatives, equities and fixed interest securities</p> <p>(merger Aust Stock Exchange and Sydney Futures Exchange in July 2006)</p>

Features of Australia's Regulatory Regime

- Multiple, functional regulators
 - ASIC and APRA: Twin-peaks
 - ASIC and ASX: dual regulation and supervision of market participants
- Principles-based regulation
 - Rather than telling you how to meet your obligations, a principles-based approach simply tells you what your obligations are
 - Policy Statement

Governing Law

- Corporation Act 2001
- Corporation Regulations 2001
- ASIC Act 2001
- ASIC Regulations 2001
- ASX Listing Rules (listed trust only)
- The financial Services Reform Act 2001(FSR)

Governing Laws and Regulations in PRC

- *The Trust Law of the People's Republic of China* came into effect on October 1,2001
- *Trust Companies Administration Measures* issued by China Banking Regulatory Commission (CBRC) came to effect on March 1 this year
- *Trust Companies Collective Investment Scheme Administration Measures* issued by CBRC came to effect on March 1 this year
- **The Notice of the CBRC on implementing *Trust Companies Administration Measures* and *Trust Companies Collective Investment Scheme Administration Measures*** on February 14,2007.
- *Guidelines on Trust Companies Governance* issued by CBRC on January 22,2007
- *Provisional Administrative Rules on Overseas Wealth Management Business of Trust Companies* jointly issued by the CBRC and the SAFE on March 12,2007

The main functions of the CBRC

- Formulate supervisory rules and regulations governing the banking institutions
- Authorize the establishment, changes, termination and business scope of the banking institutions
- Conduct on-site examination and off-site surveillance of the banking institutions, and take enforcement actions against rule-breaking behaviours
- Conduct fit-and-proper tests on the senior managerial personnel of the banking institutions
- Compile and publish statistics and reports of the overall banking industry in accordance with relevant regulations
- Provide proposals on the resolution of problem deposit-taking institutions in consultation with relevant regulatory authorities
- Responsible for the administration of the supervisory boards of the major State-owned banking institutions
- Other functions delegated by the State Council

The Main Changes

- The organisations formerly known as trust and investment companies, now become simply “trust companies”, thereby emphasising the trust role
- The lifting of geographical limits on development
- The new capital requirement for trust companies remains at RMB 300 million
- Clarify the definition of qualified investors
- Abolished the restriction of 200 entrustment contracts for each collective entrusted fund. But the number of individual investors in a fund cannot exceed 50

The restriction on Trust Sector

- Domestic banks, insurers and securities companies are currently prohibited from investing directly in trust companies
- Foreign investment in trust companies is limited to 25% with any individual foreign investor limited to less than 20%

Suggestions

- Set up the registration system for collective investment scheme
- There should be more disclosure obligations to the trust companies
- More chances should be provided with the retail investors after the risk control system is more advanced
- The Stock Exchange should build up a platform for the liquidity of the interest in the funds
- Tax concessions should be entitled to collective investment scheme to encourage the new financial product

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