



Australian Government

Australian Government response to the
Senate Economics References Committee Report:

Agribusiness Managed Investment Schemes. Bitter
Harvest

November 2016

Senate Economics References Committee

Inquiry into Forestry Managed Investment Schemes (MIS)

Government Response

Recommendation 1

- The committee recommends that the ATO undertake a comprehensive review of its product rulings to obtain a better understanding of the reasons some investors assume that an ATO product ruling is an endorsement of the commercial viability of the product. The results of this review would then be used to improve the way in which the ATO informs investors of the status of a product ruling.
- The committee recommends that the ATO and ASIC strengthen their efforts to ensure that retail investors are not left with the impression that they sanction schemes, including the use of disclaimers prominently displayed in disclosure documents including PDS.

- The Government notes this recommendation.
- ATO product rulings carry a disclaimer. The disclaimer states that the ruling only sets out the tax consequences of investing in a particular product, and does not guarantee the commercial or financial viability of the product.
- The ATO has recently completed the review recommended by the committee. The ATO is implementing a range of initiatives to combat retail investor misunderstanding of ATO product rulings, including:
 - introducing a requirement to prominently feature its customary disclaimer about product rulings in all scheme documents given to investors, including the product disclosure statement, promotional and other marketing material;
 - requiring that retail sellers sign a declaration stating that they:
 - understand that a product ruling is not an endorsement of commercial viability;
 - will advise buyers that a product ruling is not an endorsement of commercial viability; and
 - will encourage buyers to seek independent advice with regard to commercial viability.
 - requiring the provider of an agribusiness MIS to obtain a signature from applicants on a separate section of the form, to ensure retail investors' attention is drawn to the disclaimer and that they understand what the disclaimer means.
- The ATO anticipates these changes will be introduced by the end of 2016.

- ASIC recognises the importance of retail investors not having the impression that ASIC sanctions or endorses MIS. ASIC will consider how best to strengthen the message where appropriate in its communications to retail investors.
- ASIC's current communications practice involves warning consumers that it does not 'approve' any form of investment, including into agribusiness MISs products, through media releases, consumer warnings, its consumer website (MoneySmart), speeches, media commentary and other public statements. ASIC reviews, modifies and enhances its communications with retail investors where needed.
- ASIC also acts promptly to correct any statements to retail investors which misrepresent ASIC's role, including statements suggesting ASIC has "endorsed" or "approved" a product. In flagrant cases, ASIC's remedial action extends to prosecutions of the parties responsible for making such statements.

Recommendation 2

- The committee recommends that ASIC be vigilant in monitoring the operation of the FOFA legislation and to advise government on potential or actual weaknesses that would allow any form of incentive payments to creep back into the financial advice sector.
- The Government notes this recommendation is primarily a matter for ASIC. However as part of the Improving Consumer Outcomes in Financial Services package announced on 20 April 2016, ASIC will dedicate \$57 million to ongoing surveillance and more intensive enforcement action in respect of financial advice, responsible lending, life insurance and breach reporting.

Recommendation 3

- While noting the 1 July 2016 expiry of the 'accountants' exemption' under Regulation 7.1.29A of the Corporations Regulations 2001, the committee recommends that the Treasury look closely at the obligations on accountants or tax agents providing advice on investment in agribusiness MIS (or similar schemes). The intention would be to identify any gaps in the current regulatory regime (or the need to tighten-up or clarify regulations) to ensure retail investors are covered by the protections that exist under FOFA and that the level of regulatory oversight of tax agents or accountants providing advice on agribusiness MIS (or similar schemes) does not fall short of that applying to licensed financial advisers.
- The Government notes this recommendation.
- ASIC will monitor compliance with the new regime following the expiry of the accountants' exemption from 1 July 2016. Any gaps identified will be referred to Treasury.

Recommendation 4

- The committee agrees with the view that financial literacy has 'got to get aggressive' and recommends that the Australian Government explore ways to lift standards. In particular, the government should consider the work of the Financial Literacy Board in this most important area of financial literacy to ensure it has adequate resources.
- Drawing on the lessons to be learnt from the evidence on the need to improve financial literacy in Australia, the committee also recommends that the Australian Government in consultation with the states and territories review school curricula to ensure that courses on financial literacy are considered being made mandatory and designed to enable school leavers to manage their financial affairs wisely. The course content would include, among other things, understanding investment risk; appreciating concepts such as compound interest as friend and foe; having an awareness of what constitutes informed decision-making; being able to identify and resist hard sell techniques; and how to access information for consumers such as that found on ASIC's website. Financial literacy should be a standing item on the Council of Australian Governments' (COAG) agenda.

- The Government notes this recommendation.
- The Australian Government Financial Literacy Board is a purely advisory board. This is because the primary responsibility for financial literacy rests with ASIC. The Government values the advice provided by the Board on strategies aimed at lifting financial literacy standards across the community.
- ASIC is working closely with the States and Territories to build capacity in teachers to deliver financial literacy as part of the new Australian schools curriculum, through ASIC's MoneySmart Teaching program. Financial literacy is to be embedded in the new Australian Curriculum which States and Territories will be implementing from 2017.
- The Government notes that ASIC, as the principal agency responsible for development, implementation and leadership of the National Financial Literacy Strategy, produces and delivers a number of literacy initiatives. These include ASIC's MoneySmart website and the MoneySmart Teaching program referred to above. The National Financial Literacy Strategy also identifies a set of strategic priorities, providing a practical framework for action by stakeholders across the government, financial services, education, community and not-for-profit sectors.
- The Government considers that ASIC's existing resources and funding (that were increased as part of the package announced on 20 April 2016) are adequate to continue these initiatives.

Recommendation 5

- The committee recommends that the government gives high priority to developing and implementing a code of ethics to which all financial advice providers must subscribe.
- The Government supports this recommendation. The reforms announced by the Government to raise the professional standards of financial advisers is expected to include the development of a code of ethics, which all advisers will be required to comply with. The Government intends to introduce legislation as soon as possible.

Recommendation 6

- The committee recommends that the government consider the banning provisions in the licence regimes with a view to ensuring that a banned person cannot be a director, manager or hold a position of influence in a company providing financial services or consumer credit.
- The Government notes this recommendation and will consider this issue when addressing recommendation 24 of the Financial System Inquiry (FSI) (reviewing ASIC's powers to ban individuals from the management of financial firms) and recommendation 29 of the FSI (dealing with the review of ASIC's enforcement regime).
- The ASIC enforcement review is also being accelerated as part of the Improving Consumer Outcomes in Financial Services package announced on 20 April 2016.

Recommendation 7

- The committee recommends that the government consider legislative amendments that would give ASIC the power to immediately suspend a financial adviser or planner, subject to the principles of natural justice, where ASIC suspects that the adviser or planner has engaged in egregious misconduct causing widespread harm to clients.
- The Government notes this recommendation and will consider this issue when implementing recommendation 24 of the FSI (dealing with ASIC's powers to ban individuals from the management of financial firms) and recommendation 29 of the FSI (dealing with the review of ASIC's enforcement regime).
- The ASIC enforcement review is also being accelerated as part of the Improving Consumer Outcomes in Financial Services package announced on 20 April 2016.

Recommendation 8

- The committee recommends that, based on the agribusiness MIS experience, the Australian Government consult with industry on ways to improve the presentation of a product's risks in its respective PDS. The intention would be to strengthen the requirements governing the contents and presentation of information, particularly on risks associated with the product. This measure should not result in adding to the material in these documents. Indeed, it should work to further streamline the contents but at the same time focus on information that an investor requires to make an informed decision with particular attention given to risk.
 - With this objective in mind, the committee also recommends that the Government consider expanding ASIC's powers to require additional content for PDSs for agribusiness MIS.
 - The committee recommends further that ASIC carefully examine the risk measures used in Europe and Canada mentioned by the FSI and prepare advice for Government on the merits of introducing similar measures in Australia.
 - In conjunction with the above recommendation, the committee recommends that the government consider the risk measures used in Europe and Canada mentioned by the FSI to determine whether they provide a model that could be used for Australian PDSs.
-
- The Government notes this recommendation. It supports industry-led initiatives to improve the disclosure of risk to consumers in PDSs and is considering removing regulatory impediments to innovative product disclosures as part of the implementation of recommendation 23 of the FSI.
 - ASIC has previously engaged with industry around disclosure for agribusiness schemes, unlisted property schemes, mortgage schemes and infrastructure schemes. This resulted in the release of a number of ASIC regulatory guides describing the information it considers should be disclosed to investors for these types of schemes to help them better understand the risks associated with the products. ASIC has also issued investor guides to assist investors to understand risks and information contained in PDSs. In addition, ASIC has reviewed compliance with its guidance and noted that the PDSs for recent agribusiness offerings are compliant.
 - The Government announced in its response to the FSI that it will review the MIS framework, and as part of this, will deal with the recommendation about expanding ASIC's powers to require issuers of MIS, including agribusiness schemes, to further improve PDS disclosures. Similarly the Government's proposed product intervention power and related obligations to be imposed upon issuers and distributors, announced in response to the FSI, should also assist in future to prevent a recurrence of the issues identified in respect of agribusiness scheme products and offer documents.

Recommendation 9

- The committee recommends that the government consider not only renaming general advice but strengthening the consumer protection safeguards around investment or product sales information presented during promotional events.
- The Government notes this recommendation and will address the issue of strengthening consumer protection safeguards when implementing recommendation 40 of the FSI. Further, the Government will introduce more accountability in relation to the distribution of financial products (including through promotional events) and provide ASIC with a product intervention power as part of the implementation of recommendations 21 and 22 of the FSI.
- The implementation of recommendations 21 and 22 is being accelerated as part of the Improving Consumer Outcomes in Financial Services package announced on 20 April 2016.

Recommendation 10

- The committee recommends that ASIC strengthen the language used in its regulatory guides dealing with general advice. This would include changing 'should' to 'must' in the following example:
- “You must take reasonable steps to ensure that the client understands that you have not taken into account their objectives, financial situation or needs in giving the general advice”.
- The Government notes that this recommendation is a matter for ASIC. The Government is aware that ASIC periodically reviews and updates its regulatory guidance based on need (for instance, following the identification of gaps in regulation or compliance or receipt of Court judgements concerning misconduct in the financial system) and notes that ASIC has responded to the Committee on the outcome of its consideration of this recommendation.

Recommendation 11

- In light of the concerns about the lack of understanding of the role that referral networks had in selling agribusiness MIS without appropriate consumer protections, the committee recommends that the government's consideration of 'general advice' also include the role of referral networks and determine whether stronger regulations in this area are required.
- The Government notes this recommendation and will introduce more accountability in relation to the distribution of financial products (including through referral networks) when implementing recommendation 21 of the FSI (dealing with strengthening product issuer and distributor accountability).

- The implementation of recommendation 21 is being accelerated as part of the Improving Consumer Outcomes in Financial Services package announced on 20 April 2016.

Recommendation 12

In respect of research houses and subject matter experts providing information or reports to the market on financial products such as agribusiness MIS, the committee recommends that the government implement measures to ensure that IOSCO's statement of principles governing integrity and ethical behaviour apply and have force. In particular, the committee recommends that the government consider imposing stronger legal obligations on analysts, and/or firms that employ analysts to rate their product, to act honestly and fairly when preparing and issuing reports and applying ratings to a financial product.

- The Government notes this recommendation.
- Entities releasing research on financial products to the market are currently subject to the Australian Financial Services Licencing regime, which requires them to act efficiency, honestly and fairly and have in place arrangements to manage conflicts of interest. The Government has announced that it will strengthen financial services and credit licensing regimes in addressing recommendation 29 of the FSI.

Recommendation 13

- The committee recommends that Korda Mentha continue, through its hardship program, to resolve expeditiously outstanding matters relating to borrowers who are yet to reach agreement on repaying their outstanding loans from Timbercorp Finance.
- The committee recommends that spokespeople for HNAB–Action Group consult with Korda Mentha and the independent hardship advocate on implementing measures that would help to restore confidence, faith and good-will in the hardship program.

- The Government notes this recommendation is a matter for Korda Mentha and the HNAB – Action Group.

Recommendation 14

- The committee recommends that Bendigo and Adelaide Bank support the appointment of an independent hardship advocate to assist borrowers resolve their loan matters relating to Great Southern.

- The Government notes this recommendation is a matter for Bendigo Bank and Adelaide Bank.
- However, as part of the Improving Consumer Outcomes in Financial Services package announced on 20 April 2016, the Government has established a panel of eminent persons to review the role, powers and governance of all of the financial system's external dispute resolution and complaints schemes and to assess the merits of better integrating these schemes to improve the handling and outcomes of consumer complaints. This Panel will produce its final report to Government in March 2017.

Recommendation 15

- The committee recommends that the Australian Government initiate discussions with the states and territories on taking measures that would lead to the introduction of national legislation that would bring credit provided predominantly for investment purposes, including recourse loans for agribusiness MIS, under the current responsible lending obligations. The provisions governing this new legislation would have two primary objectives in respect of retail investors:
 - oblige the credit provider (including finance companies, brokers and credit assistance providers) to exercise care, due diligence and prudence in providing or arranging credit for investment purposes; and
 - ensure that the investor is fully aware of the loan arrangements and understands the consequences should the investment underperform or fail.

- The Government notes this recommendation. Implementation of this recommendation would require either a referral of powers from the States or a co-operative legislative scheme, similar to what existed previously with the Corporations Law.
- The Government will consider the level of consumer protections associated with MIS, including any related credit arrangements, as part of its announced review of the MIS framework (FSI Recommendation 42).

Recommendation 16

The committee recommends that the Australian Government consider ways to ensure that borrowers are aware that they are taking out a recourse loan to finance their agribusiness MIS and also to examine the merits of imposing a maximum loan-to-valuation limit on retail investors borrowing to invest in agribusiness MIS.

- The Government notes this recommendation. The Government will consider the level of consumer protections associated with MIS, including any related credit arrangements, as part of its announced review of the MIS framework (FSI Recommendation 42).

Recommendation 17

- The committee recommends that the Banking Code of Conduct include an undertaking that the banks adhere to responsible lending practices when providing finance to a retail investor to invest. This responsibility would apply when the lender is providing finance either directly or through another entity such as a financing arm of a Responsible Entity.

- The Government notes this recommendation is a matter for the Australian Bankers' Association, given its responsibility for the Banking Code of Conduct.
- On 21 April 2016, following the Government's announcement of the Improving Consumer Outcomes in Financial Services package, the Australian Bankers'

Association announced, that as part of its 6-Point Plan, it will review the Code of Banking Practice by the end of this year.

Recommendation 18

- The committee recommends that the Victorian Legal Services Commissioner and Legal Services Board thoroughly review the conduct of the lawyers who provided advice to retail investors in collapsed agribusiness MIS to cease repayments on outstanding debts and the circumstances around this advice.
- The intention would be to determine whether the profession needs to take measures to ensure it maintains high ethical standards and that its members adhere to best interest obligations towards their clients. The investigation would include making recommendations or determinations on:
 - remedies available to investors belonging to the class actions who have suffered considerable financial loss as a result of following advice to cease repayments on their outstanding loans;
 - whether disciplinary action should be taken against the lawyers who provided the advice to stop repayments;
 - whether the matter warrants any form of compensation; and
 - whether the matter should be referred to any appropriate disciplinary body.

- The Government notes this recommendation is a matter for the Victorian Legal Services Commissioner and Legal Services Board.

Recommendation 19

- To augment ASIC's product intervention power, the committee recommends that the government review the penalties for breaches of advisers and Australian Financial Services Licensees' obligations and, under the proposed legislation governing product issuers, ensure that the penalties align with the seriousness of the breach and serve as an effective deterrent.
- The Government notes this recommendation and will consider this issue as part of the review of ASIC's enforcement regime (announced as part of the response to the FSI recommendation 29).
 - This review is being accelerated as part of the Improving Consumer Outcomes in Financial Services package announced on 20 April 2016.

Recommendation 20

- The committee recommends that the government use CAMAC's report on managed investment schemes as the platform for further discussion and consultation with the industry with a view to introducing legislative reforms that would remedy the identified shortcomings in managing an MIS in financial difficulties and the winding-up of collapsed schemes.
- The Government supports this recommendation and agrees that an enhanced regulatory framework for MIS is required, drawing on the CAMAC's report (as part of the implementation of recommendation 42 of the FSI).
- As part of the 2016-17 Budget, the Government announced that it would introduce the framework for two new collective investment vehicles (CIVs) (a corporate model and a partnership model) which would, once implemented provide alternate investment vehicles to the MIS. As part of this reform there will also be a number of features in the regulatory framework which will be examined in response to the CAMAC's report and this Senate Inquiry.
- The Government's review of MIS will commence following the introduction of the CIVs regime to ensure there is policy consistency across investment fund frameworks from a retail investor perspective.

Recommendation 21

- The committee notes that neither the ATO nor Treasury have undertaken a comprehensive review of the tax incentives for MIS and whether they had unintended consequences, such as diverting funds away from more productive enterprises; inflating up front expenses; or encouraging poorly-researched management decisions (planting in unsuitable locations). The committee recommends that Treasury commission a review to better inform the policy around providing tax concessions for agribusiness MIS.
- The Government notes this recommendation.
- Currently, there are only three providers offering forestry MIS arrangements. The ATO, as part of the range of initiatives it is implementing to combat retail investor misunderstanding of ATO product rulings, will be monitoring compliance by the remaining forestry MIS to include, from late 2016, a prominent disclaimer, to obtain a retail seller declaration, and to require a retail investor acknowledgement concerning any applicable product rulings in each case.
- Any new forestry and other agribusiness MIS providers will be required to approach the ATO for a product ruling if they wish to access the tax concession. This provides an opportunity for the ATO to scrutinise their promotion arrangements. Those operating without a product ruling will generally be identified as part of the ATO's normal risk management processes. Therefore, rather than commissioning a review, the Government agrees to continue to monitor the operation of the scheme through the ATO's product ruling processes.

Recommendation 22

- The committee recommends further that the proposed review consider the approach to the incentives offered to investors in agribusiness ventures by other countries such as the United Kingdom to inform the review's findings and recommendations.

- The Government notes this recommendation and will consider the experience of other jurisdictions such as the United Kingdom in this area, as part of its announced MIS review.

Recommendation 23

In addition to the above recommendation, the committee recommends that the government request the Productivity Commission to inquire into and report on the use of taxation incentives in agribusiness MIS. As part of its inquiry, the Productivity Commission should identify the unintended adverse consequences, if any, that flowed from allowing tax deductions for agribusiness MIS. For example:

- the potential for mis-selling financial products on the tax concessions;
- the incentive for retail investors to borrow, sometimes unwisely, to fund their investment;
- whether the taxation concessions:
- became an end in themselves rather than the business model;
- showed up as subsidies to higher cost structures, operations and/or returns to the operators of the schemes; and
- distorted land values and diverted high value farmland into passive monoculture such as Blue Gums.
- The main purpose of the inquiry would be to draw not only on the experiences of the failed MIS but also the successful schemes to determine whether there is merit in reforming the system of tax incentives and, if so, what those reforms.

- The Government does not support this recommendation.
- Rather than the Productivity Commission undertaking a separate review on the use of taxation incentives in agribusiness MIS, the ATO and ASIC will continue to test and monitor these arrangements as the regulators best placed by expertise and powers to address these issues.

Recommendation 24

The committee recommends that ASIC review the complaints made against advisers and accountants, licensed or unlicensed, who engaged in alleged unscrupulous practices when recommending that their clients invest in agribusiness MIS. The review would identify any weaknesses in the current legislation that impeded ASIC from taking effective action against those who engaged in such unsound practices. This review would also examine the adequacy of the penalties available to ASIC to impose on such wrong doers. In particular, ASIC should consider the adequacy of penalties that apply to those who were unlicensed or have since become unlicensed. Banning in such cases is redundant.

The committee also recommends that as part of this review, ASIC consider the practice of advisers using bankruptcy as a means to avoid recompensing clients who have suffered financial loss as a result of their poor financial advice and any possible remedies.

The committee recommends that ASIC provide its findings to the committee.

- The Government notes this recommendation is a matter for ASIC.
- ASIC previously gave consideration to these matters, when investigating a range of individuals and entities involved in agribusiness failures such as Great Southern and Timbercorp.
- The regulatory landscape for advisers, including in respect of advice that may be given on agribusiness MIS, has been reformed since the Government's implementation of FOFA. Those reforms included new powers to seek civil penalties or administrative sanctions against AFS licensees and advisers who accept conflicted forms of remuneration or do not act in the best interests of their clients. ASIC will continue to be vigilant in monitoring compliance with the reforms and in taking action to enforce them.
- ASIC's enforcement tools are the subject of the review which the Government announced as part of its response to the FSI. This review is being accelerated as part of the ASIC reform package announced on 20 April 2016. Penalties are also being considered as part of this review.
- The Government has established a panel of eminent persons to review the role, powers and governance of all of the financial system's external dispute resolution and complaints schemes. This Panel has been asked to make observations on the establishment of a statutory compensation scheme of last resort. This Panel will deliver its final report to Government in March 2017.

Nick Xenophon's recommendation

That a compensation scheme of last resort for victims of 'Forestry Managed Investment Schemes' be established with a combination of Government funding and a contribution from financial institutions. This should be established in parallel with stricter requirements for insurance for financial planners as part of an ongoing compensation scheme for prospective failures of financial advice.

- The Government notes the recommendation. The Government has established a panel of eminent persons to review the role, powers and governance of all of the financial system's external dispute resolution and complaints schemes. This Panel has been asked to make observations on the establishment of a statutory compensation scheme of last resort. This Panel will produce its final report to Government in March 2017.
- The Government will consider this recommendation in light of the observations of the Panel.

Green's recommendation 1

That the Government establish a Royal Commission to examine misconduct within the financial services sector.

- The Government does not support this recommendation because a Royal Commission will not benefit consumers and will delay important reforms which the Government is currently implementing.
- There have already been several Senate committee and other inquiries into the financial system including an inquiry into the conduct of the Commonwealth Bank of Australia's financial planning divisions, and the Australian Securities and Investments Commission. In addition, the Senate Economics References Committee is currently conducting an inquiry into the scrutiny of financial advice.
- The Government commissioned the FSI, and has now accepted 43 recommendations from that review. In addition, the Government has added an additional 5 measures to its FSI response, bringing the total commitment to 48 actions.
- The Government has made substantial progress towards developing legislation that will lift the education, training, ethical and professional standards of financial advisers and has commissioned an important review into the financial system's external dispute resolution framework.
- In addition, in April 2016, the Government provided additional funding to ASIC to enhance its surveillance and enforcement activities, to better identify misconduct. The Government also announced that it would accelerate work already underway to assess the regulatory tools available to ASIC to protect consumers and punish wrongdoing, such as increasing penalties and giving ASIC new powers to ban the distribution of harmful financial products.

- The Government's focus is now on implementing the reforms that will strengthen our financial system — a Royal Commission would indefinitely delay this important work.

Green's recommendation 2

That the Government should legislate to require investment in forestry MIS to be treated as investment in capital, and for tax deductions to be spread across the life of the asset.

- The Government notes this recommendation.
- The ATO will continue to monitor the tax treatment of agribusiness MIS and provide advice to Government on any issues, as they arise.

Green's recommendation 3

That the Government legislate such that only limited recourse loans are able to be provided for investment in complicated financial products.

- The Government notes this recommendation.
- The Government has legislated significant reforms that improve the protections for people investing in complicated financial products, including the Future of Financial Advice reforms.
- In addition, the Government is progressing reforms to introduce more accountability in relation to the distribution of financial products in implementing recommendation 21 of the FSI (dealing with strengthening product issuer and distributor accountability). The implementation of recommendation 21 is being accelerated as part of the Improving Consumer Outcomes in Financial Services package announced on 20 April 2016.
- The Government considers these measures more appropriately deal with issues around the distribution of complex financial products.