
Proposed Australian Corporate Collective Investment Vehicle - Part II

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In brief

Our first legal talk alert on corporate collective investment vehicles (**CCIVs**) issued 31 October 2017 introduced the basic features of the CCIV regime, and explored some of the issues raised by the current form of CCIV proposed by the new legislation's Exposure Draft – in particular, the role of the Corporate Director under the CCIV's hybrid corporate trust in a box (managed investment scheme (**MIS**)) model, and some of the structural anomalies this hybrid structure creates when compared to a conventional body corporate. Please refer to our prior [alert](#) for more detail.

This second alert considers the proposed duties of the CCIV's corporate director (**Corporate Director**) in greater depth, as well as some matters for consideration with respect to the insolvency regime to be released for this new breed of investment vehicle.

In detail

Duties borrowed from the registered MIS regime

The Exposure Draft includes specific duties applicable to the Corporate Director of a retail CCIV, which are substantially those that apply to a responsible entity (**RE**) of a registered MIS. Some of the duties are aligned with the general law fiduciary duties of a trustee (honesty, care, to act in the best interests of members). Others are functionary; a duty to comply with the CCIV's constitution, or to ensure that the assets of a sub-fund are valued at regular intervals. These duties are apparently not duties owed to the retail CCIV, or at least not only to the CCIV. In particular, mirroring the duties of an RE of a registered scheme, the Corporate Director is required to act in the best interests of the members of the CCIV, as distinct from the CCIV itself. These statutory duties do not extend to the Corporate Director of a wholesale CCIV.

The *officers* of the Corporate Director of a retail CCIV also owe specific statutory duties, in substantially similar terms to the duties of the officers of an RE of a registered MIS. Officers of the Corporate Director have fiduciary duties also expressed to be for the benefit of retail CCIV members, and those officers must take reasonable steps to ensure that the Corporate Director complies with the Corporations Act, its Australian financial services licence conditions, the CCIV's constitution and the compliance plan. No such provisions apply to the officers of the Corporate Director of a wholesale CCIV.

This cascading set of duties among persons and entities within the retail CCIV structure may seem foreign for those accustomed to traditional principles of company law. In parallel to duties of officers of REs of retail MIS, the Exposure Draft provides that duties of the Corporate Director of a retail CCIV to CCIV members override any conflicting duty of an officer or employee of the Corporate Director to the Corporate Director. Similarly, the duty of an officer of the Corporate Director of a retail CCIV to that CCIV overrides any conflicting duty that the officer owes to the Corporate Director. Again, these are parallel to the requirements that apply to an RE of a registered MIS. Again, there are no such requirements for persons similarly involved with a wholesale CCIV.

Differences between duties

The Explanatory Memorandum states: “The registered scheme duties are preferred over the duties of company directors, officers and employees as they are better tailored to the nature of a managed fund”. It also notes, somewhat confusingly and without further explanation: “The corporate director owes duties to the members of the CCIV and these will take precedence over the duties the corporate director owes to its shareholders.”

This position does not accommodate the fundamental differences between the nature of the fiduciary relationship of a director of a company and the nature of the fiduciary relationship of a trustee of a trust. The Exposure Draft specifies that neither the Corporate Director nor the CCIV is a trustee of the assets of the CCIV’s sub-funds, yet many of the features of the duties imposed on the Corporate Director mirror those of a trustee of a managed fund.

It may be that the Corporate Director is actually not a “director” as traditionally understood in company law. The Exposure Draft is unclear on this topic – while it indicates that the current statutory duties of directors to the CCIV under Ch2D.1 may not apply to the Corporate Director (at least of a retail CCIV), it does not expressly address how those duties will be administered in practice and what jurisprudence will apply to company directors of the Corporate Director (whether of a retail or wholesale CCIV). The Exposure Draft does not comment at all on duties in the context of a wholesale CCIV, creating a body governed by persons with no statutory duty, and whom the Exposure Draft specifically excludes from consideration as a trustee. If the duties of the Corporate Director of a wholesale CCIV are a matter for company law (by force of the Corporations Act and/or the general law), a different duty regime would apply to a Corporate Director depending on whether it is the Corporate Director of a wholesale CCIV or a retail CCIV.

Development of duties for officers of a fund manager

As far back as 1995, the Courts concluded¹ that a higher standard of care applied to the duties of officers of a professional trustee company. In general terms, the directors were held to have the same liability as the trustee if those directors knowingly concerned or recklessly assisted in the trustee’s breach of its duties.

In 2013 Murphy J in *ASIC v Australian Property Custodian Holdings Limited (Receivers and Managers appointed) (in liquidation) (Controllers appointed) (no3)* [2013] FCA 1342 took this concept further, concluding that the duties of officers of REs under Chapter 5C of the Corporations Act (**Chapter 5C Duties**) were owed to MIS members directly and members may therefore seek direct orders against officers of the RE - this assessment has been followed in more recent cases².

¹ *Australian Securities Commission v AS Nominees Limited & Ors*, a 1995 decision (13 ACLR 1822)

² *Wigney J in Trilogy Funds Management Limited v Sullivan (No 2)* [2015] FCA14

Given that the language of the Exposure Draft in relation to duties of the officers of Corporate Director of a retail CCIV mirrors the language of current legislation applicable to the duties of the officers of the RE of an MIS, will the above law applicable to the duties the officers of the RE of a registered MIS, developed in the context of trust duties and responsibilities, apply to the officers of the Corporate Director of a retail CCIV? If so, consequential amendments to the Exposure Draft will surely be needed to fill the current vacuum in relation to the duty regime applicable to the wholesale CCIV.

Effective operation: asset allocation and capital management

Asset allocation to CCIV sub-funds

The CCIV has beneficial ownership of its assets, but all assets and liabilities of the CCIV must be allocated to its “sub-funds”. The CCIV must have a least one “sub-fund” and sub-funds must be notified to ASIC when established, even though they are not separately registered. No sub-fund is an entity separate from the CCIV, but instead is to constitute a modified version of the “protected cell” regimes in other jurisdictions for the purposes of the assets and liabilities held. The mechanics to ensure this isolation of sub-fund assets is to be released in the next instalment of the legislation.

Asset protection, security for lenders, insolvency

The CCIV provides considerably greater commercial flexibility for fund managers and investors under a single structure than is possible with an MIS, but it does present structural difficulties to lending, security and enforcement for financiers to a sub-fund. It also assumes that the activities of a sub-fund can be successfully isolated from impacting any other sub-fund of the CCIV, or the Corporate Director itself.

The insolvency regime applicable to the CCIV has not yet been released. Company receivership, liquidation and administration are concepts connected to a whole corporate entity, and the mechanics of applying those ideas to discrete baskets of assets and liabilities and investors within a single corporate entity poses interesting drafting challenges.

Greater clarity is also required to enable lenders to deal comfortably in relation to discrete sub-funds within a CCIV. Not yet seen is how a single portfolio is proposed to be secured as collateral. Under the *Personal Property Security Act 2009 (PPSA)* a general security agreement (**GSA**) relates to and is registered at entity level. A lender in respect of a single CCIV portfolio could not be secured by a GSA unless the assets of the portfolio were shares in a company that could give a GSA, creating potential issues for the proposed isolation of assets and liabilities by sub-fund.

Competitive disadvantages may flow to the CCIV if financiers to the CCIV are required to impose more stringent and costly security structures on the basis of perceived greater risk and complexity.

Corporate Director risk

A CCIV (whether wholesale or retail) may consist of a number of sub-funds and the one Corporate Director of that CCIV may also be the one Corporate Director of a number of CCIVs. This potentially creates a different risk profile to an MIS for an investor, and highlights the critical importance of legislation which does not confuse identification of the capacity in which a Corporate Director acts and also avoids insolvency contagion between sub-funds and between CCIVs.

Unlike with the CCIV, there will be no quarantining of the assets of an insolvent Corporate Director by reference to the CCIVs that it services. Except for secured assets, the assets of the Corporate Director form one general fund for its unsecured creditors. The assets of a Corporate Director of a number of CCIVs will include the right to indemnity from each. It remains to be seen whether creditors arising from the operation of one CCIV (where there has been a breach of duty by the Corporate Director) might access the

unimpaired right of indemnity from another CCIV. One might reasonably assume that disclosure in relation to the offer of investments of a CCIV must therefore also include all information that investors might reasonably require to make an informed assessment of the assets and liabilities of the Corporate Director.

The proposed legislation specifically provides that any shares of the CCIV held by the Corporate Director are its personal rights and obligations. Worthy of consideration are circumstances where those shares have been issued or are potentially to be issued to the Corporate Director under a performance incentive. Extension of concepts such as “bad leaver” clawbacks might be applied to any Corporate Director receiving a share performance incentive. The Exposure Draft currently provides only for redemption of shares at the option of the holder. Thought should be given to cancellation of performance incentive shares following member approval in limited circumstances.

The takeaway

The CCIV is intended to be comparable to and competitive with structures in other jurisdictions attracting international investment funds. It is to sit alongside, rather than replace, the Australian MIS regime.

The core framework in the Exposure Draft is promising. Its provision of a corporate structure eliminates many of the conceptual uncertainties of the MIS. Further, it is a funds management framework importing words and concepts familiar to investors domestically and offshore.

Under the current Exposure Draft, the CCIV is, in practice, a hybrid: a body corporate with the operating features of a trust. Many aspects of MIS regulation have been transposed for application to a company, so creating significant ambiguity and risking importation of trust structure shortcomings that have previously dissuaded international investors. The potential for regulatory uncertainty at this stage must be pre-empted through additional legislation to avoid current issues apparent with the MIS regime involving a considerable volume of ASIC regulatory guidance, legislative instruments and similar fixes.

The fiduciary framework in which the Corporate Director of a CCIV and its officers function would also benefit from greater clarification, both in the interests of the Corporate Director and all who deal with Corporate Directors and CCIVs.

ASIC is already [consulting](#) on some of the procedural aspects of funds management that will affect the CCIV. The regulator has released its new suite of proposed updated regulatory guidance on funds management (including CCIVs) in relation to registration of funds, requirements for constitutions, compliance and oversight, asset holding, and how ASIC will use its discretionary powers for relief. This procedural guidance does not, however, resolve the structural issues identified above. We look forward to further detail on the consequential amendments to the Exposure Draft, as well as information on the proposed tax treatment of CCIVs, so that the industry can best prepare for this new breed of investment vehicle.

Let's talk

For a deeper discussion of how these issues might affect your business, please contact:

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