



T-RUN

TAILORED REGULATORY UPDATE NEWSLETTER

AUSTRAC Issues Draft Guidance Note on 'No Action' Letters

Some of you will be familiar with 'no action' letters that ASIC can issue when the regulator has determined that, despite some potentially unlawful conduct by the licensee, it will take 'no action' in relation to that particular conduct.

Now AUSTRAC has followed in these footsteps by issuing draft guidance on how it intends dealing with applications from reporting entities for it to take no action in relation to particular conduct.

But there is one major difference. Under the Corporations Act, licensees are required to report significant breaches of the financial services laws to ASIC. However, reporting entities under the AML/CTF Act have no mandatory requirement to report breaches, significant or not, to AUSTRAC. AUSTRAC's guidance needs to be viewed in that light.

Requests for no-action letters must be in writing and contain 'all information that may be pertinent to the issue of a no action letter'.

You should be aware that, according to the draft guidance:

- AUSTRAC may at any time withdraw or revise a no-action letter;
- AUSTRAC reserves the right to take any action it considers appropriate, particularly if there has been incomplete disclosure;
- no-action letters should not be relied on as a precedent;
- while any information provided in relation to an application for no-action is treated confidentially, it may be passed to the ATO and/or a relevant designated agency (eg ASIO, ACCC, AFP, APRA, and ASIC), pursuant to the AML/CTF Act; and
- information cannot be provided on a 'without prejudice' basis.

We suggest you should assess each instance on a case-by-case basis and seek advice prior to applying to AUSTRAC for a no-action letter.

Also, keep in mind that the guidance is only in draft form at this stage. We will notify you of developments.

You can find the draft guidance at http://www.austrac.gov.au/files/gn_noactionletter.pdf

Beware Instalment Warrants

We have heard several instances of financial planners wanting to take advantage of the new rules that effectively allow gearing in SMSFs, by recommending instalment warrants as an investment tool for trustees to use.

However, licensees and representatives need to be careful about what type of financial product the instalment warrant is, if it is in fact a financial product at all.

We have heard of instalment warrants being defined variously as mortgage products (not a financial product), derivatives, securities and miscellaneous financial products.

It is vital to know what type of product a particular instalment warrant is, for two primary reasons:

1. to ensure you can take advantage of the SMSF gearing rules; and
2. to ensure that you are authorised to advise in relation to the particular type of product.

We therefore recommend that you seek a legal opinion on the type of instalment warrant you are wanting to offer, prior to recommending it to clients.

Margin Lending to be a Financial Product?

The Productivity Commission recently released a draft report on Australia's consumer policy framework, recommending that the regulation of consumer credit be transferred to ASIC.

In response, ASIC lodged a submission with the Productivity Commission suggesting that certain credit-related activities (margin lending in particular) could be covered by Chapter 7 of the Corporations Act.

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Currently, credit is not a “financial product” for the purposes of licensing. The Productivity Commission is looking to release its final report in April 2008. We will monitor developments.

Rudd Reform Agenda Kicks Off

In our last issue of T-RUN we let you know that a new Financial Services Working Group has been established. Since then, the Minister for Superannuation and Corporate Law, Senator Nick Sherry, has opened the first session of the working group.

Ostensibly set up to ‘simplify’ financial services, especially regarding disclosure obligations, the working group has said its initial focus will be to develop a short-form disclosure document for the First Home Saver Account.

We expect a raft of recommendations that will affect the broader financial services industry to follow.

Also, the Assistant Treasurer, Minister for Competition Policy & Consumer Affairs, Chris Bowen, addressed IFSA recently and gave hope that relaxed withholding rates are on the way for managed funds.

As part of a push to make Australia’s financial services industry a ‘hub’ of the Asia Pacific, the Minister spoke of allowing the financial services industry to ‘compete on a level playing field’ internationally, with a view to making investment in Australia more appealing and helping to make the export of our financial services more attractive.

To this end, the Government has asked the Board of Taxation to review the taxation of managed funds.

ASIC Action

Well, ASIC certainly hasn’t been sitting on its hands over the Easter period. Here’s some of the regulatory action taken over the last few weeks.

- After initially freezing funds in November 2006 in an illegal foreign currency scheme, ASIC has now obtained orders

to close the illegal managed investment scheme. Operated by an unregistered NZ company, investors paid at least \$14.5m into the scheme with promised returns of 4.23% per month.

- In a long-running matter, ASIC has been granted orders against a Melbourne financial planner, restraining the planner and other parties from dealing with the assets of a number of alleged unregistered managed investment schemes.
- Three financial operators have been nabbed by ASIC. One, who worked as an authorised representative, allegedly used clients’ funds to satisfy personal debts, and has been permanently banned from providing financial services. Two others pleaded guilty to operating an unregistered managed investment scheme.
- A North Queensland man is facing charges for operating an unlicensed investment scheme and embezzling more than half a million dollars from clients.
- An unregistered managed investment scheme with more than \$10m is being liquidated.

In other action, ASIC has announced that it will be targeting heavily traded securities in the wake of market volatility. ASIC’s inquiries relate particularly to conduct that could involve the spreading of false or misleading rumours or predatory trading, which could amount to market manipulation or insider trading.

New Report Counts the Cost of Compliance

ASIC has released Report 123, titled “A Report on Costs of Financial Services.” The report was prepared by a market research firm who interviewed 64 financial services organisations. It identifies the major costs of compliance and an expectation that costs could increase 15-20% per year.

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Major cost components of compliance were identified as staff costs, training, documentation, IT, outsourcing, procedures, monitoring and recording, and opportunity costs.

Interestingly, while most respondents recognised the costs of compliance as high, there was almost no knowledge of total compliance costs. Consequently, very few respondents reported to their Board on compliance costs.

While the report indicated a general maturity and acceptance of the need for regulation in the financial services industry, several disadvantages of the current regime were identified, including:

FSR overly prescriptive, excessive documentation, increased costs, ineffective consumer protection, staffing issues (some respondents stated that it is now difficult to attract high quality staff as potential staff are deterred by high levels of paperwork and perceived low productivity), legislation too complex, and duplication across regulators.

The report makes for interesting reading. It is available at:

[http://www.asic.gov.au/asic/pdf/lib.nsf/LookupByFileName/REP_123_A_Report_on_Costs_of_Financial_Services_2007.pdf/\\$file/REP_123_A_Report_on_Costs_of_Financial_Services_2007.pdf](http://www.asic.gov.au/asic/pdf/lib.nsf/LookupByFileName/REP_123_A_Report_on_Costs_of_Financial_Services_2007.pdf/$file/REP_123_A_Report_on_Costs_of_Financial_Services_2007.pdf)

Well, I'll be blogged

Have your voice heard, and hear what your colleagues in the financial services sector are saying about the latest hot topics.

Our new Financial Services Blog is designed to help industry engage with each other and share views, experiences and approaches to tackling common problems.

Check it out at

<http://www.holleynethercote.com.au/HN/AFSLBlog.aspx> and have your say on the things that are important to you. The success of this initiative will depend on clients and other participants not being shy and letting their views and experiences be known.

Current topics include P.I. Insurance and SOAA versus SOAs – Incorporated by Reference. Topics close to many people's hearts at the

moment. If you want another topic added, just ask.

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This newsletter is current as at **March 2008**.

For a list of useful FSR articles, go to www.holleynethercote.com.au, an associated law firm website.

This newsletter briefly summarises a complex area of law and one that is very dependent upon the precise facts that would apply. It is not a substitute for legal advice.