

ASIC Corporations (Serviced Apartment and Like Schemes) Instrument 2016/869

EXPLANATORY STATEMENT

Prepared by the Australian Securities and Investments Commission

Corporations Act 2001

The Australian Securities and Investment Commission (**ASIC**) makes *ASIC Corporations (Serviced Apartment and Like Schemes) Instrument 2016/869* under subsection 601QA(1), 926A(2), 951B(1), 992B(1) and 1020F(1) of the *Corporations Act 2001 (the Act)*.

Subsection 601QA(1) provides that ASIC may declare that Chapter 5C of the Act applies to a person as if specified provisions were omitted, modified or varied as specified in the declaration.

Paragraph 926A(2) provides that ASIC can exempt persons in relation to the provisions of Part 7.6, licensing of providers of financial services. This does not include the power to exempt a person from the provisions in Divisions 4 or 8 of the Act.

Paragraph 951(B)(1) provides that ASIC may exempt persons, financial products or classes of persons or financial products from any provision of Part 7.7 of the Act or modify the application of the Part to any person or financial product or classes of persons or financial products as if specified provisions were omitted, modified or varied as specified in the declaration.

Paragraph 992B(1) provides that ASIC may exempt persons or a class of persons, a financial product or a class of financial products from a provision of Pt 7.8 of the Act.

Subsection 1020F(1) provides that ASIC may exempt a person or class of persons from specified provisions of Part 7.9 of the Act or declare that Part 7.9 of the Act applies in relation to a person as if specified provisions were modified.

1. Background

The instrument remakes the following class orders which are due to sunset under the *Legislation Act 2003*:

- ASIC Class Order [CO 99/463] *Serviced Strata Scheme Valuations ([CO 99/463])* gives conditional relief to the responsible entity of a serviced strata scheme from the obligation to value property under 601FC(1)(j), which will sunset on 1 April 2018;
- ASIC Class Order [CO 02/185] *Sale of Strata Units for \$500,000 or more ([CO 02/185])* gives relief from managed investment, product disclosure and hawking provisions of the Act when strata units are sold for \$500,000 or more, which will sunset on 1 April 2018;
- ASIC Class Order [CO 02/245] *Closed Schemes ([CO 02/245])* gives relief to operators of Serviced strata schemes that are ‘closed schemes’ as at 6 October 1998 from the managed investment, licensing and hawking provisions which will sunset on 1 April 2017;
- ASIC Class Order [CO 02/303] *Management Rights Schemes – amendment ([CO 02/303])* gives conditional relief to operators of managed investment schemes involving registered proprietors of strata title units, community title or similar property interests who make their units available for use as a serviced apartment hotel or resorts in the circumstances described in the instrument from the managed investment, licensing and hawking provisions, which will sunset on 1 October 2017;

- ASIC Class Order [CO 02/304] *Management Rights Schemes (ICO 02/304)* gives operators conditional relief from the managed investment, some AFS licensing and hawking provisions which will sunset on 1 October 2016;
- ASIC Class Order [CO 02/305] *Management Rights Schemes (ICO 02/305)* gives operators conditional relief the managed investment, some AFS licensing and hawking provisions which will sunset on 1 October 2016; and
- ASIC Class Order [CO 07/189] *Management Rights Schemes where the Strata Unit cannot be used as a Residence (ICO 07/189)* exempts an operator of a management rights scheme from the requirement to register the scheme under the Corporations Act 2001 where ASIC issues a Pro Forma 187 instrument, which will sunset on 1 October 2017.

This instrument provides certain managed investment, licensing, hawking and disclosure relief in relation to managed investments schemes that are strata schemes or management rights schemes.

Strata Schemes

Typically, a strata scheme is a managed investment scheme under paragraph (a) of the definition of ‘managed investment scheme’ in section 9 of the Act. Generally, a member of a strata scheme contributes:

- (a) a right to occupy the strata unit (e.g. a lease or licence); or
- (b) a right to let or license the strata unit (i.e. as an agent of the strata unit owner).

By making available these rights to their strata unit, the retail client is making a contribution to acquire interests in the scheme.

Management Rights Schemes

The term ‘management rights’ schemes refers to the practice of buying a strata unit that is part of the complex that has the fittings and location that enable it to function as a front office for the complex. Management rights schemes are a subset of serviced strata schemes. A typical management rights scheme involves an operator who resides in a holiday accommodation complex and who:

- (a) provides short-term leases or licences to visitors;
- (b) markets the complex;
- (c) manages the common property;
- (d) provides an office and caretaking facilities;
- (e) collects the rent or licence fees; and
- (f) pays expenses out of the rent or licence fees collected and then pays the proceeds to the owner.

Management rights schemes are managed investment schemes under section 9 of the Act.

Obligations of operators of strata schemes and management rights schemes

Without relief, the operator of strata schemes and management rights schemes would be required to comply with the managed investment, licensing, disclosure and hawking provisions of the Act. This requires the operator of a scheme to be a public company and hold an Australian Financial Services (*AFS*) licence. The operator must also register the scheme with ASIC and give disclosure relating to the issue of interests in the scheme.

The managed investment provisions of Chapter 5C set out the requirements for registering a managed investment scheme if the scheme has more than 20 members or had been promoted by a person who was in the business of promoting managed investment schemes. AFS licensing and hawking provisions of the Act may also have applied to strata schemes and management rights

schemes. This instrument provides relief from these provisions, as the cost of compliance for operators of serviced strata schemes and management rights schemes is unreasonably burdensome.

2. Purpose of the instrument

The purpose of the *ASIC Corporations (Serviced Apartment and Like Schemes) Instrument 2016/869* is to:

- a. continue the effect of ASIC Class Orders [CO 99/463], [CO 02/185], [CO 02/245], [CO02/303], [CO 02/304], [CO 02/305], [CO 07/189] and incorporates the requirements of ASIC Pro Forma 187- *Management rights schemes where the strata unit cannot be used as a residence (PF 187)* into the instrument;
- b. Update the name of the legislative Instruments;
- c. Reflect current drafting practices and update the format of the current document;
- d. Simplify the drafting to give greater clarity;
- e. Update legislative references and definitions.

ASIC has continued relief for strata schemes and management rights schemes because it considers compliance with all aspects of managed investment, AFS licensing, disclosure and hawking provisions would be an unreasonable burden as the schemes are usually small and there would be limited benefit in requiring registration or licensing.

3. Operation of the instrument

Exemption for management rights schemes

Section 5 of the principal instrument provides for the exemption for operators of a strata scheme from the requirement to register the scheme, hold a financial services licence and comply with the hawking provisions, in circumstances where all conditions and obligations listed in subsection 5(2) and (3) are satisfied.

The conditions in subsection 5(2) are:

- (a) either each strata unit to which the scheme relates can either lawfully used as a residence or the operator has provided ASIC with a written statement from an independent real estate agent that in relation to each strata unit to which the scheme relates, that agent can let the unit at a reasonable rate having regard to the value of the unit, and that there would be a reasonable degree of occupancy of the unit at that rate;
- (b) investors and operators may withdraw from the scheme on no more than 90 days' notice;
- (c) an investor who withdraws from the scheme will not be bound after the 90 days' notice has expired to allow the use of their strata unit except for the occupation of the unit by a person other than the operator or an associate of the operator and under an agreement that the operator made before the notice was given;
- (d) if an investor withdraws from the scheme, they may appoint another person to manage their strata unit;
- (e) if the operator managing the letting of the strata units has not agreed after the commencement of the section 5 to make payments to investors whether by guarantee or otherwise, or cover or reimburse payments in whole or in part, that are made by any other person to investors in relation to the use of strata units of investors after the operator withdraws from the scheme;
- (f) an investor is not required to make payments to participate in the scheme, other than:
 - (i) a payment to buy the strata unit; and
 - (ii) payments for the purchase of furniture, fittings and equipment for the strata unit where the maximum amount of the payments and items of furniture, fittings and

- equipment are set out in the written agreement to be entered into between the operator and each investor as described in paragraph 5(2)(h); and
- (iii) payments of the investor's reasonable proportion of the operator's fees and expenses with respect to the management of the scheme where:
 - (A) in any three month period, the total of such payments relate to a period of no more than 3 months and is reasonably commensurate with the work done or to be done, or the expenses incurred or likely to be incurred by the operator during the period to which the payments relate; and
 - (B) where a FFE fund has been established for the investor, no payment is used for the replacement, repair or refurbishment of furniture, fittings and equipment of the strata unit in relation to the period to which the payment relates unless all money in the Fund has first been expended; and
 - (iv) where a FFE Fund has been established for the investor- payments into the Fund where:
 - (A) each payment made by deduction from rental income of the scheme that would otherwise be paid to the investor in relation to a period set by the operator does not exceed 3% of the gross rent attributable to the investor for the period ; and
 - (B) the balance of the fund is no more than \$10,000 for each strata unit available for use as part of the scheme;
 - (g) the purchase of the strata unit was not conditional on participation in the scheme whether by way of a term of the contract of sale, as a result of an interest (for example, a lease) that the strata unit is subject to immediately after the purchase or otherwise;
 - (h) if the operator is managing the letting of the strata units, the operator has entered into a written agreement with each investor which includes provisions relating to the procedures for transferring management rights as set out in section 10;
 - (i) either;
 - (i) on 1 March 2000 there was no person who had brought or agreed to buy a strata unit in relation to the scheme and who, before agreeing to buy, had been offered an interest in the scheme; or
 - (ii) a majority of scheme members have agreed in writing that the operator may rely on the exemption;
 - (j) the operator has not failed to comply with condition 7 in relation to the strata scheme, unless ASIC has notified the operator in writing after the failure that that this paragraph does not apply in relation to the breach the subject of the failure.

Subsection 5(3) provides that in working out if there is a majority of scheme members for the purposes of subparagraph (2)(i)(ii), the operator and its associates are not to be counted and a majority is based on the entitlement of scheme members to vote at body corporate meetings if there is a body corporate for the property to which the scheme relates, and otherwise is based on each member having one vote.

Section 6 describes the general conditions operators, other than operators who only operate the scheme as a promoter developers, must comply with. These conditions provide for how operators must deal with cash that is scheme property, and how cash received for FFE funds must be treated when the investor is a retail client, including when any funds must be returned to a retail client. The conditions further describe how often the operator, when it is managing the letting of the strata units, must provide retail clients of the scheme with a written statement for the reporting period, detailing any transactions in relation to the investor's interest in the scheme and how the reporting period is to be determined, including that a reporting period is not to exceed one year. Section 6 also requires that if the operator is managing the letting of the strata units, it must operate the scheme in accordance with condition 5(2)(h) in this Instrument.

Section 7 provides that an operator that becomes aware of matters that give that operator reason to believe that the operator has failed in a material respect to comply with the conditions in section 6

must give ASIC full particulars of the failure within 15 business days of becoming aware of it. This section does not apply to an operator who only operates the scheme as a promoter developer.

Section 8 provides an exemption to real estate (selling) agents who is not a financial services licensee or representative of a financial services licensee, the operator of a strata scheme or an excluded person, from the requirement to hold an AFS licence to provide the financial services listed in the section in relation to interests in a strata scheme that the real estate (selling) agent reasonably believes are covered in section 5 of this instrument.

ASIC Corporations (Effect of Licensing Exemptions) Instrument 2015/1115 provides relief from subsection 911B(1) of the Act in relation to persons acting on behalf of a person who does not need an AFSL because of an exemption under section 926A of the Act.

Section 9 provides an exemption for other persons from the prohibition on hawking.

Section 10 sets out procedures and the terms to be included in the agreement between the operator and each investor, referred to in paragraph 5(2)(h) in relation to the transfer of management rights including how a majority is to be arrived at for voting purposes.

Valuation of property of registered serviced apartment schemes.

Section 11 provides relief so that the responsible entity of a registered strata scheme does not have to comply with paragraph 601FC(1)(j) of the Corporations Act in relation to the scheme.

Paragraph 601FC(1)(j) provides that in exercising its powers and carrying out its duties, the responsible entity of a registered scheme must ensure that the scheme property is valued at regular intervals appropriate to the nature of the property.

To rely on this exemption, the responsible entity must value the scheme property as soon as practicable after the responsible entity has grounds to believe that valuation of the item is in the best interests of the member or is needed for the scheme to operate in a manner fair to all members.

Modification for strata scheme where all strata units are sold for over \$500,000

Section 13 provides relief from from managed investment, product disclosure and anti-hawking provisions for operators of certain types of strata schemes. The relief applies where all the interests are offered to investors so they will have strata units for which they have paid, or will pay, \$500,000 or more (taking into account any associated furniture and costs).

The threshold of \$500,000 is intended to reflect the policy of reg 7.1.18(2) of the Corporations Regulations 2001.

Reg 7.1.18 relates to arrangements about the price for the provision of an investment-based financial product. Under paragraph 761G(7)(a) of the Act, if a financial product, or a financial service provided to a person it is provided to the person as a retail client unless the price for the provision of the financial product, or the value of the financial product to which the financial service relates, equals or exceeds the amount specified in regulations made for the purposes of that paragraph as being applicable in the circumstances. If a client pays over \$500 000 to acquire or be issued with the financial product, the client will be a wholesale client in respect of the product.

Reg 7.1.18 (2) states that for paragraph 761G(7)(a) of the Act, the amount applicable in relation to an investment-based financial product is \$500 000.

The relief modifies regulation 7.1.18(3) of the Corporations Regulations so that the price paid for the strata unit associated furniture, fittings and equipment will be taken into account in

determining whether the \$500,000 threshold is satisfied (meaning that the investor will be treated as a wholesale client). The relief applies for the purpose of Pts 7.6 (except Divs 4 and 8) 7.7, 7.8 and 7.9 of the Corporations Act.

Subject to limited exceptions, the declaration will also apply to subsequent purchasers of a strata unit in a strata scheme where all the strata units were sold for \$500,000 or more (taking into account any associated furniture and costs).

The declaration will only apply if the price for each interest in the scheme (taking into account the price of the strata unit and associated furniture and costs) is at least \$500,000.

Transitional arrangements for closed non-complying schemes

Sections 14 to 16 deal with transitional provisions for schemes covered by ASIC Class Orders [CO 02/245], [CO 02/303], [CO 02/304], [CO 07/189] and schemes covered by ASIC Pro Forma 186 and ASIC Pro Forma 187.

ASIC has given closed and certain well-advanced schemes conditional relief from the managed investment, AFS licensing (for advice and dealing only), some product disclosure provisions and hawking provisions.

'Closed schemes' are serviced strata schemes where all the strata units in the scheme were sold, and no primary offers to join the scheme were made, after 6 October 1998

A 'well advanced' scheme is a serviced strata scheme established before 6 October 1998.

4. Documents incorporated by reference

Pro Forma 187

Legislative Instrument *ASIC Corporations (Serviced Apartments and Like Schemes) 2016/869* incorporates by reference ASIC Pro Forma 187 *Management rights schemes where the strata unit cannot be used as a residence*, which exempts a financial product that is an interest in a management rights scheme being operated in relation to a specific serviced apartment, hotel, motel or resort complex, from various provisions of Chapter 7 of the Act. It is intended to operate in conjunction with ASIC Class Order [CO 07/189], which exempts an operator of the management rights scheme from the requirement to register the scheme under Chapter 5C of the Act.

Pro Forma 186

Legislative Instrument *ASIC Corporations (Serviced Apartments and Like Schemes) 2016/869*, incorporates by reference Pro Forma 186.

Pro forma 186 has been withdrawn, however it continues to have ongoing relevance under transitional provisions contained in *ASIC Corporations (Serviced Apartments and Like Schemes) 2016/869*.

These pro formas can be found at www.asic.gov.au/pro-formas.

5. Consultation

ASIC consulted with industry stakeholders on its proposal to remake to remake ASIC Class Orders [CO 99/463], [CO 02/185], [CO 02/245], [CO 02/303], [CO 02/304], [CO 02/305], [CO 07/189] and the incorporation of the requirements of PF 187 into the instrument in CP 250

Remaking ASIC class orders on property, strata and management rights schemes published on 8 February 2016.

The feedback received was broadly supportive of the proposals in the Consultation Paper.

Statement of Compatibility with Human Rights

Prepared in accordance with Part 3 of the Human Rights (Parliamentary Scrutiny) Act 2011

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The instrument is compatible with the human rights and freedoms recognised or declared in the international instruments listed in section 3 of the *Human Rights (Parliamentary Scrutiny) Act 2011*.

Overview of the legislative instrument

ASIC Corporations (Serviced Apartment and Like Schemes) Instrument 2016/869 continues the effect of ASIC Class Orders [CO 99/463], [CO 02/185], [CO 02/245], [CO02/303], [CO 02/304], [CO 02/305] and [CO 07/189]. The instrument continues to provide relief from certain managed investment, licensing, hawking and disclosure provisions under the Corporations Act 2001, in relation to managed investment schemes that involve owners of strata units making their unit available for use as part of a serviced apartment, hotel, motel or resort complex.

Human rights implications

This legislative instrument does not engage any of the applicable rights or freedoms.

Conclusion

This legislative instrument is compatible with human rights as it does not raise any human rights issues.