

Consultation Paper on the Review of Managed Investment Scheme Rules

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Call for submissions

The Legal Services Council (**Council**) invites public comment on recommended options for addressing key issues that have emerged from the review of rules 91A to 91D (**MIS Rules**) of the Legal Profession Uniform General Rules 2015 (**General Rules**). Submissions can be sent to the Council by email to: submissions@legalservicescouncil.org.au on or before 31 January 2020, and will be published on the Council's website.

Executive summary

This consultation paper sets out the findings of the review by the Council of the MIS Rules. Rules 91A - 91D were introduced on the commencement of s 258 of the *Legal Profession Uniform Law (Uniform Law)* on 1 July 2018. The paper is based on submissions received and consultation conducted during October 2019 with industry associations and regulators in Victoria and New South Wales. In this review, the Council was also assisted by Professor Hanrahan who was appointed as an expert adviser on technical legal issues.¹

Three issues have emerged from the review:

1. The purpose and operation of s 258 of the Uniform Law is not well understood across the profession. Even the bodies consulted had trouble identifying situations in which s 258 would apply and what mischief it is intended to address. A short statement to stakeholders by the Council explaining the purpose of the restrictions and their relationship with the Legal Profession Uniform Law Australian Solicitors' Conduct Rules 2015 (**Solicitors' Conduct Rules**) may assist. This could be supported by technical guidance on the operation of the provisions, with examples.
2. Whether r 91B should be amended to address what is seen as an unnecessary compliance burden on law practices. Most bodies consulted supported an amendment to r 91B to limit the operation of s 258(3) to situations where an associate's interest in a managed investment scheme or operator of a managed investment scheme gives rise to a conflict. The intention of the proposed change is to remove the perceived risk that a law practice cannot comply with s 258(3) unless it engages in a burdensome process of collecting information about all such interests from all associates on an ongoing basis.
3. Whether r 91C should be amended to overcome a lack of clarity in the existing drafting. That lack of clarity has resulted in uncertainty for law practices, and for regulators attempting to provide guidance, as to when the prohibition in s 254(4) of the Uniform Law applies.

¹ Professor Pamela Hanrahan is a Professor in the School of Taxation and Business Law at UNSW Sydney, a solicitor member of the Law Society of New South Wales and a member of the executive of the Business Law Section of the Law Council of Australia.

This consultation paper explains these issues and sets out some recommended options. The recommended options are:

1. Provide stakeholders with:
 - a. a short statement of the purpose of s 258 (that it operates to protect individual clients and community confidence in the legal profession by restricting the involvement of law practices in certain forms of financial intermediation), and
 - b. an explanation of the relationship of s 258 with the Solicitors' Conduct Rules (that it is wider than the prohibitions on individual solicitors operating MISs or engaging in mortgage financing as part of their practice, or acting for a client when they personally have a conflict).
2. Provide industry bodies and regulators with revised technical guidance (including examples) to assist law practices in applying s 258 in practice, once any revisions to the MIS Rules are agreed. The industry bodies may be requested to provide examples to be included in the revised guidance.
3. Revise r 91B to permit a law practice to provide legal services in relation to an MIS, in circumstances where an associate of the law practice has an interest in the MIS or MIS operator but there is no conflict between the associate's interest and the duty to act in a client's best interest.
4. Request that industry bodies propose practical steps that law practices will take to ensure compliance with s 258(3) of the Uniform Law.
5. Redraft r 91C to make the restriction in s 258(4) easier to interpret, apply and enforce.

Introduction

This consultation paper sets out the findings of the review being conducted by the Council into rules 91A – 91C of the General Rules. The MIS Rules address aspects of s 258 of the Uniform Law. Section 258 of the Uniform Law came into force on 1 July 2018.

The review is being conducted by the Council according to the terms of reference (**TOR**) attached to this consultation paper at Annexure A. The TOR are limited to the efficacy of the MIS Rules and do not include a review of s 258 itself. The organisations that provided written submissions to the review are listed at Annexure B.

For ease of reference, the full text of s 258 of the Uniform Law is extracted at Annexure C to this consultation paper. The existing MIS Rules are extracted at Annexure D.

Background

Section 258 of the Uniform Law has a long history. The legislative history is explained in the Inquiry Report to the Council dated 20 October 2017.² For several decades, legislation regulating lawyers in New South Wales and Victoria has restricted lawyers' involvement in various forms of financial intermediation, particularly mortgage financing. When these legislative restrictions were first imposed, lawyers were exempt from many of the Commonwealth laws that regulate the provision of financial services, but these exemptions are no longer available.

Section 258 of the Uniform Law and the MIS Rules are complicated and honeycombed. The general pattern is that s 258 imposes broad restrictions on law practices and their related entities, which are then relaxed by the MIS Rules. This leads to complexities in the drafting that are particularly apparent in r 91C.

Section 258 and the MIS Rules interact with restrictions imposed on individual solicitors by the Solicitors' Conduct Rules and with the financial services laws contained in the *Corporations Act 2001* (Cth) (Corporations Act) and the *Australian Securities and Investments Commission Act 2001* (Cth). The main restrictions imposed by the Uniform Law, the MIS Rules and the Solicitors' Conduct Rules are summarised (in very general terms) in Table 1.

MIS is defined in s 9 of Corporations Act. Section 6 of the Uniform Law adopts this broad definition.³ Mortgage financing is defined in s 6 of the Uniform Law.⁴

² See Section 2.1 of Pamela Hanrahan, *Report of an Inquiry for the Legal Services Council into Section 258 of the Legal Profession Uniform Law* (Legal Services Council, 20 October 2017) (2017 Report), Available at <http://www.legalservicescouncil.org.au/Documents/news/LSC%20-%20MIS%20inquiry%20-%20Final%20Report.pdf>.

³ The statutory definition is very broad. Only a subset of managed investment schemes (as defined) is regulated under the Corporations Act.

⁴ Mortgage financing means facilitating a loan secured or intended to be secured by mortgage by (a) acting as an intermediary to match a prospective lender and borrower; or (b) arranging the loan; or (c) receiving or dealing with payments for the purposes of, or under, the loan; but does not include providing legal advice or preparing an instrument for the loan.

Table 1: Uniform Law and Rules restrictions

Source of the restriction	Nature of the restriction	Entity or individual to which it applies
Rule 41.1 of the Solicitors' Conduct Rules	Must not operate an MIS or engage in mortgage financing as part of their law practice	A solicitor
Sections 258(1) and (1A) of the Uniform Law	Must not promote or operate an MIS (other than a private MIS connected to the internal management or operation of the law practice)	A law practice or a related entity ⁵
Rule 12.1 of the Solicitors' Conduct Rules	Must not act for a client where there is a conflict between the duty to serve the best interests of a client and the interests of the solicitor or an associate of the solicitor	A solicitor
Section 258(3) of the Uniform Law and r 91B of the General Rules	<p>Must not provide legal services in relation to a managed investment scheme if any associate⁶ of the law practice has an interest in the scheme or the responsible entity⁷ for the scheme, unless:</p> <ul style="list-style-type: none"> • the services are provided to the MIS operator, or • no associate has a substantial interest,⁸ or • no principal of the law practice knows or ought reasonably to know that an associate has a substantial interest 	A law practice
Section 258(4) of the Uniform Law and r 91C of the General Rules	Must not act for a client who is a private lender ⁹ in respect of a mortgage if the lender was introduced to the borrower by the law practice or an associate, agent or appointee of the law practice as part of mortgage financing engaged in by the person who made the introduction	A law practice or a related entity

⁵ Related entity is defined in s 6 of the Uniform Law (for law practices that are companies) and r 91A of the General Rules (for all other law practices).

⁶ Associate of a law practice is defined in s 6 of the Uniform Law and means a person who is one or more of the following: (a) a principal of the law practice; (b) a partner, director, officer, employee or agent of the law practice; (c) an Australian legal practitioner who is a consultant to the law practice.

⁷ Responsible entity is not defined but is taken to mean the operator of the MIS.

⁸ Substantial is defined in r 91B(2) of the General Rules.

⁹ That is, a lender that is not a financial institution as defined in r 91D of the General Rules.

As noted, the restrictions on individual solicitors, law practices and related entities of law practices operate in conjunction with the Commonwealth laws that govern the provision of financial services.¹⁰ These include laws to the following effect:

- A person must not operate a registrable MIS¹¹ unless the person is a public company that holds an appropriate Australian financial services (AFS) licence issued by the Australian Securities and Investments Commission (ASIC) and the MIS is registered with ASIC under s 601EB of the Corporations Act. Until 2018, some solicitors' mortgage practices operated under an exemption from this requirement, but that exemption has now ceased.¹²
- Usually, a person must not operate a wholesale MIS¹³ unless the person holds an AFS licence or is a representative of an AFS licensee.
- A person must not carry on a business of providing financial services unless the person holds an AFS licence; this includes a business of giving financial product advice or dealing in financial products. Financial product includes, for this purpose, an interest in a registrable MIS or wholesale MIS. A person can provide financial services as a representative of an AFS licensee if the statutory requirements are met.
- Financial product advice means a 'recommendation or a statement of opinion, or a report of either of those things, that:
 - is intended to influence a person or persons in making a decision in relation to a particular financial product or class of financial products, or an interest in a particular financial product or class of financial products; or
 - could reasonably be regarded as being intended to have such an influence'.¹⁴
- 'Dealing' for this purpose includes issuing a financial product, and arranging for another person to apply for, acquire or dispose of a financial product,¹⁵ but does not include giving financial product advice.

¹⁰ See generally, Pamela F Hanrahan, *Background Paper 7: Legal Framework for the Provision of Financial Advice and Sale of Financial Products to Australian Households* (Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, 5 April 2018). Available at <https://financialservices.royalcommission.gov.au/publications/Pages/default.aspx>.

¹¹ A registrable MIS is an MIS that must be registered with ASIC because of s 601ED of the Corporations Act. Section 601ED is to the effect that an MIS must be registered with ASIC if two conditions are met. The first is that the MIS: (a) has more than 20 members; or (b) was promoted by a person or an associate of a person, who was, when the scheme was promoted, in the business of promoting managed investment schemes; or (c) is one of a group of related schemes as determined by ASIC and the total number of all the schemes to which the determination relates exceeds 20. The second is that no issue of interests in the scheme that have been made that would have required the giving of a Product Disclosure Statement under Division 2 of Part 7.9 if the scheme had been registered when the issues were made.

¹² See Australian Securities and Investments Commission, *ASIC Corporations (Mortgage Investment Schemes) Instrument 2017/587*. The small industry-supervised mortgage schemes that previously operated under in Victoria under this exemption have now terminated. See 2017 Report, n 2, [4.1].

¹³ An MIS is a wholesale MIS if the first condition but not the second condition in n 11 is met.

¹⁴ This definition appears in s 766B of the Corporations Act. Subsection 766B(5) excludes, among other advice: (a) advice given by a lawyer in his or her professional capacity, about matters of law, legal interpretation or the application of the law to any facts; (b) except as may be prescribed by the regulations – any other advice given by a lawyer in the ordinary course of activities as a lawyer, that is reasonably regarded as a necessary part of those activities'.

The review has identified the following issues:

1. The general view is that the purpose of the restrictions is not clear from the legislation, and that law practices may not understand what is restricted or the rationale for applying special rules relating to financial intermediation to solicitors, law practices and their related entities. This lack of understanding may affect compliance.
2. Rule 91B may impose an unreasonable burden on law practices by requiring them to inquire into the personal financial affairs of all their associates.
3. The drafting of r 91C may benefit from review and refinement.

Options for the Council to address these issues include publishing guidance and amending the MIS Rules.

Issue 1: Clarifying the intention

The review suggests that the rationale for s 258 of the Uniform Law and the MIS Rules is not well understood. This may be contributing to a low level of awareness among the profession of the potential scope of s 258 and the MIS Rules.

The discussions with stakeholders suggest that most solicitors understand the effect of Solicitors' Conduct Rule 41.1 – that an individual solicitor must not operate an MIS or engage in mortgage financing as part of his or her law practice. They also understand that, if they were to operate an MIS separately from their law practice, they would need to meet applicable ASIC licensing and registration requirements.

There may not be the same level of understanding that s 258(1) extends the prohibition on operating an MIS from the individual solicitor to the law practice as a whole and to all its related entities, and applies even where the MIS is operated separately from the law practice. This would extend, for example, to a related entity of the law practice operating an MIS even if that entity is managed independently and is licensed by ASIC.

There may also be a low level of awareness that the restriction extends to law practices and their related entities *promoting* an MIS, even if they do not operate it. The meaning of 'promoting' is discussed in the Inquiry Report of 17 October 2017. (By way of contrast, the restriction in r 41 of the Solicitors' Conduct Rules only prohibits operating a scheme.)

Solicitors understand that Solicitors' Conduct Rule 12 prohibits an individual solicitor from acting for a client if there is a conflict between the duty to serve the best interests of a client and the commercial or other interests of the solicitor or an associate of the solicitor. However, ss 258(3) and (5) contain

¹⁵ See s 766C of the Corporations Act.

broader restrictions that apply at the level of the law practice as a whole and, in the case of s 258(5), to related entities also. These restrictions are not limited to situations where r 12 applies.

Some firms are aware that s 258(3) currently prohibits the firm from acting for a client (other than for the MIS operator) in respect of an MIS where an associate of the firm has a substantial interest in the MIS or the operator of the MIS and a principal of the firm is aware or ought reasonably to be aware of that interest. This may require the firm to take proactive steps to ascertain whether any associate of the firm has such an interest before agreeing to act in a matter involving a MIS. Other firms may not have focused as closely on this restriction.

Most solicitors know they cannot engage in mortgage financing as part of their law practice. However, some may not realise that the law practice and its related entities cannot do the legal work on a mortgage for a client who is a private lender if the lender and the borrower were introduced by an associate, agent or appointee of the law practice that was engaged in mortgage financing.

Understanding, and therefore compliance, may be improved by a clear statement of the purpose of s 258 of the Uniform Law and its relationship with the relevant Solicitors' Conduct Rules. This is different from technical guidance about s 258 and the MIS Rules, which is intended to explain how s 258 and the MIS Rules should be applied by law practices, giving examples. There is also scope to improve the current technical guidance provided to law practices once any changes to the MIS Rules recommended by this review are finalised.

As to purpose, the Council may consider a short statement such as:

Sometimes clients look to their lawyers for guidance or assistance in financial matters. Section 258 of the Uniform Law protects individual clients, and broader community confidence in the legal profession, by restricting the involvement of law practices in creating or promoting certain investment arrangements including private mortgage financing. The restrictions extend beyond situations where that involvement would create a conflict for the individual solicitor concerned.

Law practices and their related entities cannot promote or operate managed investment schemes (MIS), and law practices may be restricted in acting for a client in a matter concerning an MIS if an associate of the practice has a [substantial] interest in the MIS or the operator of the MIS [that causes a conflict].

Also, a law practice cannot assist a client who is a private lender with their mortgage if the lender and the borrower were introduced by an associate, agent or appointee of the law practice that was engaged in mortgage financing. This operates alongside the rule that prohibits individual solicitors from engaging in mortgage financing as part of their law practice.

(The language in square brackets relates to the recommended option in relation to Issue 2.)

This general statement of principle should be supported by revised technical guidance, to explain to law practices the precise operation of s 258 and give practical examples of its application. The content of that technical guidance can be settled once any changes to the MIS Rules are finalised.

Recommended options for consultation

1. Provide stakeholders with a short statement of:
 - a. Council's understanding of the purpose of s 258 (that it operates to protect individual clients and community confidence in the legal profession by restricting the involvement of law practices in certain forms of financial intermediation); and
 - b. the relationship of s 258 with the Solicitors' Conduct Rules (that it is wider than the prohibitions on individual solicitors operating MISs or engaging in mortgage financing as part of their practice, or acting for a client when they personally have a conflict).
2. Provide industry bodies and regulators with revised technical guidance (including examples) to assist law practices in applying s 258 in practice, once any revisions to the MIS Rules are agreed. The industry bodies may be requested to provide examples to be included in the revised guidance.

Issue 2: Reducing the compliance burden of s 258(3)

The restriction imposed by s 258(3) is very broad. Rule 91B is intended to narrow that restriction so that it prevents a law practice from acting 'in relation to' an MIS only where it is necessary to do so in the public interest.

During the consultation a suggestion was made that the restriction should only apply where the law practice would, by virtue of an associate's interest in an MIS or MIS operator, have a conflict. To that end, a change to r 91B which is supported by the other industry bodies and the regulators is proposed.

Before commenting on that proposal, it is worth repeating the structure of s 258 of the Uniform Law and r 91B. Section 258(3) provides that:

Except as permitted by or under the Uniform Rules, or as approved by the designated local regulatory authority, a law practice must not provide legal services in relation to a managed investment scheme if any associate of the law practice has an interest in the scheme or the responsible entity for the scheme.

Rule 91B relaxes that restriction. The existing r 91B and the proposed amendment are set out in Table 2.

Table 2 – Rule 91B

Current r 91B	Proposed r 91B
<p>(1) For the purposes of section 258(3) of the Uniform Law, a law practice is permitted to provide legal services in relation to a managed investment scheme, despite an associate of the law practice having an interest in the scheme or the responsible entity for the scheme, if:</p> <ul style="list-style-type: none"> (a) those legal services are provided to the operator of the scheme, or (b) no associate of the law practice has a substantial interest (within the meaning of subr (2)) in the scheme or the responsible entity for the scheme, or (c) one or more associates of the law practice has a substantial interest (within the meaning of subr (2)) in the scheme or the responsible entity for the scheme, but no principal of the law practice either: <ul style="list-style-type: none"> (i) knows of any of those interests, or (ii) ought reasonably to know of any of those interests. <p>(2) For the purposes of subr (1), an associate has a substantial interest in a managed investment scheme or responsible entity if the associate:</p> <ul style="list-style-type: none"> (a) is entitled, at law or in equity, to an interest in the assets of the managed investment scheme or responsible entity which is significant or of relatively substantial value, or (b) exercises any material control over the conduct and operation of the managed investment scheme or responsible entity, or (c) has an entitlement to a share of the income of the managed investment scheme or responsible entity which is substantial, having regard to the total income which is derived from it. 	<p>For the purposes of section 258(3) of the Uniform Law, a law practice is permitted to provide legal services in relation to a managed investment scheme, despite an associate of the law practice having an interest in the scheme or the responsible entity for the scheme, if the provision of those legal services does not give rise to a conflict between the duty to serve the best interests of a client and the interests of the solicitor or an associate of the solicitor.</p>

The main concern appears to be that the current r 91B creates an unreasonable compliance burden because it requires law practices to take proactive steps to ascertain whether any associate has a substantial interest, as defined in r 91B(2), before agreeing to act for anyone other than the operator in any matter involving an MIS. If the proposed amendment is adopted, the proponents' intention is that normal conflicts checking procedures, adopted to ensure compliance with Solicitors' Conduct Rule 12, would suffice to unearth any conflicts that would trigger the operation of s 258(3).

This raises two separate issues for Council to consider. The first is whether it agrees with the basic policy argument – that the restriction on a law practice acting in relation to an MIS where an associate of the law practice has an interest in the MIS or the MIS operator should only apply where the law

practice has a conflict. The second is whether the proposed amendment to r 91B achieves that policy outcome and is workable in practice.

The policy point

All those consulted for the purposes of the review agreed that the law practice should only be prevented from acting if it (that is, the law practice) has a conflict. However, the nature of the relevant conflict, and how it might arise, was not clear. This lack of clarity may be because s 258 (and therefore r 91B) operates at the level of the law practice rather than the individual legal practitioner, and because it involves a duty-interest conflict rather than the more common duty-duty conflicts faced by law practices.¹⁶

Assuming the policy – that a law practice acting in relation to an MIS should only be prohibited from so acting if an associate’s interest creates a conflict – is agreed, how and when should the restriction operate?

An individual solicitor should be (and is) precluded from acting ‘where there is a conflict between the duty to serve the best interests of a client and the interests of the solicitor or an associate of the solicitor’,¹⁷ by Solicitors’ Conduct Rule 12.1. Presumably a conflict exists for the purposes of r 12.1 only if a ‘reasonable man looking at the relevant facts and circumstances of the particular case would think that there was a real sensible possibility of conflict’.¹⁸ If the solicitor’s or associate’s interest is insignificant,¹⁹ or if the solicitor acting is unaware of another solicitor’s or associate’s interest, a reasonable person is unlikely to think that the solicitor’s duty to serve the best interests of the client would be affected or compromised by it. A significant commercial or other interest of a solicitor will generally create a conflict for that solicitor - how that conflict can be ‘managed’ is a separate question. Whether a significant interest held by an associate creates a conflict for a solicitor depends on factors, including who the associate is and the work they might do that touches on the matter. Under Solicitors’ Conduct Rule 12.1, this always involves a judgment call for the solicitor concerned.

As noted, the prohibition in s 258(3) operates at the level of the law practice. What if one solicitor in a law practice is precluded from acting by their (or an associate’s) interest – does this mean the law practice must not act? The American Bar Association’s *Model Rules of Professional Conduct* deal with a broadly analogous question by specifying, in r 1.10(a)(1), that ‘While lawyers are associated in a firm, none of them shall knowingly represent a client when any one of them practicing alone would be prohibited from doing so by [the conflict rules] unless ... the prohibition is based on a personal interest of the disqualified lawyer and does not present a significant risk of materially limiting the representation of the client by the remaining lawyers in the firm’.²⁰ The Australian rules do not spell this out. Again,

¹⁶ The way in which large law firms manage duty-duty conflicts is usefully discussed in Ian Dallen, ‘The rise of the information barrier: Managing potential legal conflicts within commercial law firms’ (2014) 88 ALJ 428.

¹⁷ Under Solicitors’ Conduct Rule 12.1, the problem cannot be cured by obtaining the client’s informed consent. In fiduciary law, consent does not do away with a conflict; it is a defence: *Blackmagic Design Pty Ltd v Overliese* (2011) 191 FCR 1; 276 ALR 646; [2011] FCAFC 24 at [108].

¹⁸ *Boardman v Phipps* [1967] 2 AC 46 at 124.

¹⁹ A small unit holding in a listed A-REIT that a person holds as part of a diversified investment portfolio would be an example of an insignificant interest. One-third ownership of an AFS licensed entity that operates a retail or wholesale MIS would be an example of a significant interest.

²⁰ The notion of ‘materially limiting the representation of the client’ here corresponds to our notion of not being able to discharge the duty to serve the best interests of the client.

deciding whether a personal interest of a disqualified lawyer would affect the representation of the client by others in the firm involves a judgement call and ought usually to be resolved conservatively.

It is important to note that if a conflict arises, it is not possible for the law practice to act even if it obtains the client’s informed consent to act despite the conflict. Consent does not remove the conflict.

Table 3 captures the differences between the existing position and what is proposed, if a person (A) who is an associate of a law practice has an interest in an MIS or the operator of an MIS.

Table 3: Existing and proposed r 91B

Section 258	Section 258 and the existing r 91B	Section 258 and the proposed r 91B
The law practice cannot act	The law practice can act for the MIS operator	The law practice can act if A’s interest does not conflict with the duty to serve the client’s best interests
	The law practice can act if A’s interest is not substantial (as defined)	
	If A’s interest is substantial (as defined), the law practice cannot act if any principal knows or ought reasonably to know of A’s interest	

Unlike the existing r 91B, the proposed r 91B leaves it up to the law practice to decide when A’s interest gives rise to a conflict. The Council would be interested in submissions by industry bodies as to what practical steps should be taken by a law practice to ensure it complies with s 258(3). It would be helpful if industry bodies proposed steps for this purpose; regulatory practice indicates that compliance is increased if the regulated entities engage in this way.

The steps should be robust, scalable and workable. Appropriate steps may include requiring a law practice to ask any solicitor or associate working on the matter to confirm that they have no interest and are unaware of any other associate having an interest that could give rise to a conflict, before agreeing to act for any party in a matter involving an MIS. This request could be accompanied by examples of interests that the law practice considers would be likely to create a conflict, at least until law practices become accustomed to operating under the rule.

The drafting point

The Council will consider whether a revised rule should refer to ‘the interests of an associate of the law practice’ rather than referring to ‘the interests of the solicitor or an associate of the solicitor’.

Recommended options for consultation

3. Revise r 91B to permit a law practice to provide legal services in relation to an MIS, despite an associate of the law practice having an interest in the MIS or MIS operator, if there is no conflict between the associate's interest and the duty to act in a client's best interest.
4. Request that industry bodies propose practical steps that law practices will take to ensure compliance with s 258(3) of the Uniform Law.

Issue 3: Clarifying rule 91C

The complex drafting of s 258(4) of the Uniform Law and r 91C of the General Rules makes them difficult to interpret, apply and enforce. An apparently common error is to assume that, because an individual solicitor is prohibited by Solicitors' Conduct Rule 41.1 from engaging in mortgage financing as part of his or her legal practice, r 91C leaves s 258(4) with no practical application. This is incorrect.

Section 258(4) is concerned with situations where a law practice (or a related entity) acts for a lender or contributor in connection with a mortgage. In practice, it only applies where the lender or contributor is not a financial institution as defined.

The combined effect of s 258(4) and r 91C is that a 'law practice (or a related entity) must not, in its capacity as the legal representative of a lender or contributor, negotiate the making of or act in respect of a mortgage' unless the mortgage falls into one of the categories in Table 4.

Table 4: Categories of mortgages where the law practice can act

A mortgage where:	the borrower is not a person introduced to the lender or contributors by the law practice or by an associate or agent of the law practice or a person engaged by the law practice for the purpose of introducing the borrower to the lender or contributors	AND the lender or contributors nominate the borrower	Section 258(4)(b) of the Uniform Law
			Section 258(4)(c) and r 91C(1)(b)
	the borrower is a person introduced to the lender or contributors by the law practice or by an associate or agent of the law practice or a person engaged by the law practice for the purpose of introducing the borrower to the lender or contributors	AND the introduction occurred other than as part of mortgage financing engaged in by the practice or person who made the introduction	Section 258(4)(c) and r 91C(2)(b) and (c)

The layered application of the legislation is driven by the structure of s 258(4) of the Uniform Law. The intention behind r 91C was to limit what would otherwise be a broad prohibition.

The Council is aware that the current drafting has led to the prohibition being misinterpreted. The current prohibition is accurately stated as:

A law practice (or a related entity) must not, in its capacity as the legal representative of a lender or contributor, negotiate the making of or act in respect of a mortgage if:

- (1) the lender or contributor is not a financial institution; and
- (2) the borrower was introduced to the lender or contributors by:
 - (a) the law practice, or
 - (b) an associate or agent of the law practice, or a person engaged by the law practice for the purpose of introducing the borrower to the lender or contributors,as part of mortgage financing engaged in by the practice or the associate, agent or person.

The Council may consider issuing a statement explaining what s 258(4) and r 91C prohibits, and their relationship with Solicitors' Conduct Rule 41. Another option may be to revisit the drafting of r 91C to see whether it can be clarified.

Recommended option for consultation

5. Consider redrafting r 91C to make the restriction easier to interpret and apply.

Annexure A: Terms of Reference

The purpose of the Review is to assess the operation of rr 91A - 91D of the Legal Profession Uniform General Rules 2015 (MIS Rules) that support s 258 of the Legal Profession Uniform Law (Uniform Law).

The Review will not consider or re-visit the scope of s 258 of the Uniform Law.

The Review will consider and report on the effectiveness and regulatory impact of the MIS Rules in relation to the legal profession, consumers and regulators, having particular regard to:-

- (i) The extent to which the MIS Rules are meeting the objective of consumer protection
- (ii) The nature and extent of any regulatory activity in respect of the MIS Rules, and
- (iii) The nature and extent of any impact on law practices and regulated entities.

The Review will make recommendations for amendments to the MIS Rules or to the LSC Information Sheet, if considered necessary.

The Review will consult with the Legal Services Council, the Designated Local Regulatory Authorities, the Law Institute of Victoria, Law Firms Australia, ASIC, relevant mortgage fund industry participants and other relevant stakeholders.

The Review will report to the Council by 31 January 2020.

Annexure B: Written submissions

The Council received written submissions on the Terms of Reference from the following organisations:

1. Madgwicks
2. Andrew & Holmes Lawyers
3. Office of the Legal Services Commissioner
4. Law Council of Australia
5. Law Firms Australia
6. Victorian Legal Services Board and Commissioner
7. Law Society of New South Wales

Annexure C: Uniform Law

258 - Prohibited services and business

(1) A law practice (or a related entity) must not--

- (a) promote or operate a managed investment scheme; or
- (b) provide a service or conduct a business of a kind specified in the Uniform Rules for the purposes of this section.

Civil penalty: 250 penalty units.

(1A) Despite subsection (1), a law practice (or a related entity) may promote or operate a managed investment scheme if--

- (a) the scheme is connected with or related to the business structure or ownership of the law practice; or
- (b) the scheme is connected with or related to the operation of the law practice and no person who is not an associate of the law practice has an interest in--
 - (i) the scheme; or
 - (ii) the responsible entity for the scheme; or
- (c) the scheme is of a kind specified in the Uniform Rules for the purposes of this paragraph.

(2) Despite subsection (1), an associate of a law practice may promote or operate a managed investment scheme if, in the event of an insolvency or administration of the managed investment scheme, the associate is appointed as--

- (a) an administrator, liquidator, receiver, receiver and manager, agent of a mortgagee or controller of the managed investment scheme in respect of the insolvency or administration; or
- (b) a controller or external administrator of an entity acting in a similar capacity as a responsible entity where a managed investment scheme does not have a responsible entity in respect of an insolvency or administration.

(3) Except as permitted by or under the Uniform Rules, or as approved by the designated local regulatory authority, a law practice must not provide legal services in relation to a managed investment scheme if any associate of the law practice has an interest in the scheme or the responsible entity for the scheme.

Civil penalty: 250 penalty units.

(4) A law practice (or a related entity) must not, in its capacity as the legal representative of a lender or contributor, negotiate the making of or act in respect of a mortgage, other than--

- (a) a mortgage under which the lender is a financial institution; or
- (b) a mortgage under which the lender or contributors nominate the borrower, but only if the borrower is not a person introduced to the lender or contributors by the law practice who acts for

the lender or contributors or by an associate or agent of the law practice, or a person engaged by the law practice for the purpose of introducing the borrower to the lender or contributors; or

(c) a mortgage, or a mortgage of a class, that the Uniform Rules specify as exempt from this prohibition.

Civil penalty: 250 penalty units.

(5) In this section--

"borrower" means a person who borrows, from a lender or contributor, money that is secured by a mortgage;

"contributor" means a person who lends, or proposes to lend, money that is secured by a contributory mortgage arranged by a law practice;

"contributory mortgage" means a mortgage to secure money lent by 2 or more contributors as tenants in common or joint tenants, whether or not the mortgagee is a person who holds the mortgage in trust for or on behalf of those contributors;

"financial institution" means--

(a) an ADI; or

(b) a corporation or other body, or a corporation or body of a class, specified in the Uniform Rules for the purpose of this definition;

"lender" means a person who lends, or proposes to lend, a borrower money that is secured by a mortgage.

(6) To the extent that this section applies to an incorporated legal practice, this section is declared to be a Corporations legislation displacement provision for the purposes of section 5G of the Corporations Act.

Annexure D: Uniform General Rules

91A Related entities for purposes of section 258

(1) This rule specifies, for the purposes of section 258 of the Uniform Law, who is to be a **related entity** in relation to a law practice to which this r applies.

Note. In section 6 (1) of the Uniform Law, paragraph (b) of the definition of **related entity** provides that these Rules may specify who is to be a related entity in relation to certain persons.

(2) This rule applies to a law practice that is:

- (a) a sole practitioner, or
- (b) a law firm, or
- (c) a community legal service that is not a company, or
- (d) an incorporated legal practice that is not a company, or
- (e) an unincorporated legal practice.

(3) If the law practice is a body corporate, another body corporate is a **related entity** if the two are related bodies corporate.

(4) If the law practice is not a body corporate, a body corporate is a **related entity** to the law practice if any of the following paragraphs describes the relationship between the law practice and either the body corporate or a holding company of the body corporate:

- (a) the law practice controls the composition of the board of the body corporate or holding company, or
- (b) the law practice is in a position to cast, or control the casting of, more than one-half of the maximum number of votes that might be cast at a general meeting of the body corporate or holding company, or
- (c) the law practice holds more than one-half of the issued share capital of the body corporate or holding company (excluding any part of that issued share capital that carries no right to participate beyond a specified amount in a distribution of either profits or capital), or
- (d) if there is a committee of, or other body having management of, the law practice, the body corporate or holding company controls the composition of that committee or other body, or
- (e) if the law practice has meetings at which persons constituting the law practice vote on matters concerning the management of the law practice, the body corporate or holding company is in a position to cast, or control the casting of, more than one-half of the maximum number of votes that might be cast at such a meeting.

(5) In this rule:

holding company has the same meaning as it has in the Corporations Act.

related body corporate has the same meaning as it has in the Corporations Act.

91B Managed investment schemes

(1) For the purposes of section 258(3) of the Uniform Law, a law practice is permitted to provide legal services in relation to a managed investment scheme, despite an associate of the law practice having an interest in the scheme or the responsible entity for the scheme, if:

- (a) those legal services are provided to the operator of the scheme, or
- (b) no associate of the law practice has a substantial interest (within the meaning of subr (2)) in the scheme or the responsible entity for the scheme, or
- (c) one or more associates of the law practice has a substantial interest (within the meaning of subr (2)) in the scheme or the responsible entity for the scheme, but no principal of the law practice either:
 - (i) knows of any of those interests, or
 - (ii) ought reasonably to know of any of those interests.

(2) For the purposes of subr (1), an associate has a **substantial** interest in a managed investment scheme or responsible entity if the associate:

- (a) is entitled, at law or in equity, to an interest in the assets of the managed investment scheme or responsible entity which is significant or of relatively substantial value, or
- (b) exercises any material control over the conduct and operation of the managed investment scheme or responsible entity, or
- (c) has an entitlement to a share of the income of the managed investment scheme or responsible entity which is substantial, having regard to the total income which is derived from it.

91C Mortgages

(1) For the purposes of section 258(4)(c), a mortgage is exempt from the prohibition in section 258(4) if:

- (a) the lender is not a financial institution, and
- (b) neither the law practice, nor any associate, agent or appointee of the law practice, introduced the borrower to the lender.

(2) For the purposes of section 258(4)(c), a mortgage is exempt from the prohibition in section 258(4) if:

- (a) the lender is not a financial institution, and
- (b) the borrower was introduced to the lender by:
 - (i) the law practice, or
 - (ii) an associate, agent or appointee of the law practice, and
- (c) that introduction occurred other than as part of mortgage financing engaged in by the practice or person who made the introduction.

91D Financial institutions

For the purposes of paragraph (b) of the definition of **financial institution** in section 258(5) of the Uniform Law, the following classes of body are specified:

- (a) a body that is a professional investor within the meaning of the Corporations Act,
- (b) a body that holds an Australian credit licence within the meaning of the *National Consumer Credit Protection Act 2009* of the Commonwealth,
- (c) a body:
 - (i) whose ordinary business includes the lending of money, and
 - (ii) whose consolidated gross assets have a value of more than \$10 million,
- (d) a related body corporate, within the meaning of section 50 of the Corporations Act, to a body of a class specified in any other paragraph of this rule.