Victorian Legal Services
BOARD + COMMISSIONER

Level 5, 555 Bourke Street Melbourne Vic 3000
GPO Box 492 Melbourne Vic 3001 DX 185 Melbourne
T 03 9679 8001 T 1300 796 344 (local call) F 03 9679 8101
E admin@lsbc.vic.gov.au W www.lsbc.vic.gov.au

4 October 2019

Megan Pitt
Chief Executive Officer
Legal Services Council
Level 3, 19 O'Connell Street
Sydney NSW 2000

By email: submissions@legalservicescouncil.org.au

Dear Megan

Managed Investment Schemes Rules Review

Thank you for the opportunity to assist the Legal Services Council (LSC) to conduct its review of the effectiveness and regulatory impact of Rules 91A-91D of the *Legal Profession Uniform General Rules* 2015 (the General Rules), relating to Managed Investment Schemes (the MIS Rules, the Rules).

You have indicated that the focus of the review will be on:

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 of the MIS Rules on law practices and related entities.

Consumer protection and regulatory activity
Our letter to you of 26 June 2019 (attached) reported that, as a DLRA, we had not yet had any practical experience in applying the MIS Rules. Since that time, we have had cause to investigate one law practice for engaging in mortgage financing. In this instance, the issue came to our attention through a routine audit rather than because of a consumer complaint. The law practice had not been part of the Law Institute of Victoria's ASIC exempted scheme at the time of the complaint (or at any prior time). It was therefore prohibited by Rule 41 of the *Legal Profession Uniform Law Australian Solicitors' Conduct Rules* 2015 (the Solicitors' Conduct Rules) from engaging in any type of mortgage financing. The law practice was educated and cautioned to wind down their activities to bring them into compliance, and will be audited again in 6-12 months' time. The law practice was cooperative, the conduct occurred through ignorance and there was no detrimental effect on any of the clients involved.

Impact on law practices and related entities
After the introduction of the MIS Rules, we engaged Damien McAloon of Counsel to advise us on the Rules, and draft a guidance document to assist the legal profession to comply with them. We have shared our guidance document with the NSW Law Society. This work was done in order to enable clear DLRA advice to law practices on a number of issues raised in relation to the practical application of the MIS Rules by Law Firms Australia, particularly issues relating to the application of Rule 91B. The guidance, which is yet to be released, uses illustrative scenarios to compliment the LSC Information Sheet.

In terms of the general impact of the MIS Rules on the profession, despite having a dedicated email address for MIS matters, we have only received one other enquiry from a law practice as to how the Rules apply to their particular

LEGAL PROFESSION
Uniform Law

Board ABN 82 518 945 610 Commissioner ABN 66 489 344 310

activities. We have not had any requests to consider approving a particular law practice to provide legal services in circumstances otherwise subject to the prohibition under section 258(3) of the Uniform Law.

Our previous submissions to the LSC on the development of the MIS Rules have noted the complexities and lack of clarity in the drafting. Despite the low levels of regulatory intervention, the MIS Rules would benefit from greater clarity. Clearer provisions will maximise the ability of law practices to comply with the relevant requirements and therefore promote greater consumer protection.

Issues for the review
In our view, there are opportunities for the review to examine the following issues:

- The expiration of the ASIC Class Order exemption in September 2018 for the professional association mortgage financing schemes should be considered in reviewing Rule 91C(2), as that Rule may be now of little practical value.

- The review should encompass how the LSC proposes to resolve the current lack of clarity about the interaction of the MIS Rules with Rule 41 of the Solicitors' Conduct Rules. We understand the Law Council of Australia is currently reviewing these rules. We suggest that a better outcome would be for the General Rules to encompass the entirety of matters for law practices to consider in relation to the prohibitions contained within section 258.

- The definition of 'related entity' in the MIS Rules. The interaction between this definition and the definition of that term in section 6 of the Uniform Law remains complex. As currently drafted, the definition in the MIS Rules makes arbitrary distinctions between types of practice and business structure and is narrowly construed. We acknowledge this is likely due to the drafting of the section 6 definition (which we understand is outside the scope of the review) but suggest that consideration be given to how this complexity could be resolved in the future.

- The concerns of the LFA. Ensuring that law firms can easily interpret the MIS Rules reduces firms' reliance on DLRAs to approve MIS arrangements. Individual approvals are resource-intensive for both the DLRA and the law firm concerned.

We have attached both our Counsel's advice and draft guidance for the benefit of this review. We also ask that our previous submissions to the development of the MIS rules be considered as part of the review, being our letters of 18 May and 20 June 2018, as attached.

Yours sincerely

Fiona McLeay
Board CEO & Commissioner

Attachments

D-18-173905 - Letter - 2018-06-20 - VLSBC to LSC - Managed investment schemes - definition of related entity
D-18-121290 - Letter - 2018-05-18 - VLSBC to LSCouncil - Submission on amendments to Uniform Rules - MIS

Victorian Legal Services
BOARD + COMMISSIONER

Level 5, 555 Bourke Street Melbourne Vic 3000
GPO Box 492 Melbourne Vic 3001 DX 185 Melbourne
T 03 9679 8001 T 1300 796 344 (local call) F 03 9679 8101
E admin@lsbc.vic.gov.au W www.lsbc.vic.gov.au

20 June 2018

Ms Megan Pitt
Chief Executive Officer
Legal Services Council
Level 40, MLC Centre
19 Martin Place
Sydney NSW 2000

Dear Ms Pitt

Proposed amendment of the Legal Profession Uniform General Rules – Managed Investment Schemes

Further to our letter to you of 18 May 2018, I write to provide further comments on the proposed amendments to the *Legal Profession Uniform General Rules* 2015 (Uniform Rules) relating to the new managed investment schemes (MIS) regime.

The comments we made in our letter of 18 May were in response to the fourth draft of the proposed rule issued by Parliamentary Counsel. The comments below relate to the fifth draft of the proposed rule which was released by the Legal Services Council for public consultation (draft rule). I understand the public consultation phase is due to close on 20 June 2018.

We are concerned about the definition of 'related entity' contained in the draft rule. In summary our concerns are:

- The draft rule will not deliver a consistent definition of 'related entity' for the purposes of section 258 of the Legal Profession Uniform Law.
- The lack of a consistent definition of related entity will create problems for the Victorian Legal Services Board and the Law Society of New South Wales in communicating the changes to the profession and in enforcing the ban created by section 258.

Our view is the definition of related entity in the draft rule is problematic for the following reasons:

- It does not cover all the forms of law practice as it is limited to law practices that meet the definition of a person under the *Interpretation of Legislation Act* 1984 (Vic). The draft rule will not apply to law firms, community legal services that are not incorporated, and unincorporated legal practices. If the rule is adopted in this form it will create inconsistent application depending on the type of law practice (see table).
- It is broader than the definition that applies to law practices that are registered companies. It goes beyond the concepts of holding companies and subsidiaries without a clearly articulated policy rationale for this. In addition, it therefore goes beyond Professor Hanrahan's recommendation that the definition of related entity should be consistently applied. We appreciate that there may be difficulties in mirroring these concepts for unincorporated law practices. However, it is our view that the concept of control within the meaning of section 50AA of the *Corporations Act* goes beyond the relationship that comes with those concepts. We are concerned that there is no clear policy rationale for this distinction which seems to turn solely on whether the law practice is incorporated.

LEGAL PROFESSION
Uniform Law

Board ABN 82 518 945 610 Commissioner ABN 66 489 344 310

We also note the draft guidance to the profession circulated with the draft rule does not explain these definitional issues, exacerbating the difficulties we foresee in communicating the new regime to the profession.

It is our understanding that the Legal Services Council may be asked to decide between the two versions of the draft rule. To that end the following table sets out what we believe will be the practical implications for related entities of implementing either of the draft rules.

The table below demonstrates our understanding of how the definition will apply for related entities for each rule draft.

Law Practice type	Related entity for draft rule	
	Fourth Draft of the Rule	Fifth Draft of the Rule
Law practices that are registered companies	Holding companies and subsidiaries	Holding companies and subsidiaries
Law practices that are body corporates	Holding companies and subsidiaries	Holding companies and subsidiaries
Law practices that are individuals (likely to be sole practitioners that are not companies or body corporates)	Concept of control applies	Concept of control applies
Law practices that are not registered companies or covered by the scope of the rule (law firms, unincorporated legal practices, community legal services that are not companies or incorporated)	Concept of control applies	No related entities defined therefore the ban does not extend beyond the law practice itself.

In closing it is our strong preference that the Council consider removing the definition from the rule and amending section 258 to provide a direct definition for 'related entity' that applies to all law practices in relation to managed investment schemes. This will ensure a clear definition that sets out what a related entity means for law practices specifically in relation to the ban on managed investment schemes, as it will not distinguish between types of practice or business/legal structure and will be easy to explain and enforce once in place.

We are aware such an amendment cannot be done before 1 July 2018 and that in the meantime the definition in section 6 will apply to law practices that are registered companies only. We accept this is not a perfect solution. However, it is our preference that a definition be put in place that has a clear policy rationale and does not present enforcement issues.

Yours sincerely

Fiona McLeay
Board CEO & Commissioner

Victorian Legal Services
BOARD + COMMISSIONER

Level 5, 555 Bourke Street Melbourne Vic 3000
GPO Box 492 Melbourne Vic 3001 DX 185 Melbourne
T 03 9679 8001 T 1300 796 344 (local call) F 03 9679 8101
E admin@lsbc.vic.gov.au W www.lsbc.vic.gov.au

18 May 2018

Ms Megan Pitt
Chief Executive Officer
Legal Services Council
Level 40 MLC Centre
19 Martin Place
Sydney NSW 2000

Dear Ms Pitt

Proposed amendment of the Legal Profession Uniform General Rules 2015

Thank you for the opportunity to comment on the proposed amendments to the *Legal Profession Uniform General Rules* 2015 (Uniform Rules) relating to the new managed investment schemes (MIS) regime.

We appreciate that you have also provided to us a draft Information Sheet and Frequently Asked Questions (FAQs) for comment.

We note the purpose of the draft Rules is to amend the Uniform Rules to prescribe certain matters for the purposes of section 258 of the *Legal Profession Uniform Law* (Uniform Law) which is due to take effect on 1 July 2018. Section 258 imposes prohibitions on the promotion or operation of managed investment schemes by law practices. In providing our comments below, we note we have now had an opportunity to consider the full report of Professor Pamela Hanrahan of October 2017, which we received from the Legal Services Council (LSC) secretariat on 27 March 2018.

Comments on Draft Rules

Rule 5. *New Rule 6A inserted*

General comments – application of rule 6A definition to law practices only
The new rule 6A limits the definition of ***related entity*** under section 6(1)(b) of the Uniform Law to *law practices* only. We assume this new definition is intended to be limited to section 258 only as this is consistent with Professor Hanrahan's recommendations.

However, as you would be aware, the definitions of ***related entity*** under sections 6(1)(a) and 6(1)(b) of the Uniform Law are not limited to law practices and therefore have broader implications outside of section 258, specifically for corporate legal practitioners. The definition of ***corporate legal practitioner***, under section 6 of the Uniform Law, means an Australian legal practitioner who engages in legal practice only in the capacity of an in-house lawyer for their employer *or a related entity.*

Given this, there may be benefit in clarifying in the rule itself that it is limited to related entities under section 258 only, perhaps by making reference to section 258 in the title to regulation 6A or by the insertion of a note under the new rule. This would avoid any potential for confusion that the rule may have a wider application.

LEGAL PROFESSION
Uniform Law

Board ABN 82 518 945 610 Commissioner ABN 66 489 344 310

Need for definition of related entity for corporate legal practitioners
We would also like to add that there remains a gap in the Uniform Law regarding the definition of related entity for the purposes of section 6(1)(b) as it applies to corporate legal practitioners. We have received queries from corporate practitioners employed by persons who are not companies (examples include educational institutions and churches) about the extent to which they can act for related entities. This draft rule will not address that issue and there remains a need for this issue to be further considered by the LSC. We have been discussing this issue with the Law Society of NSW and would welcome an opportunity to engage in further discussions on this issue with the Law Society and the LSC.

In making this suggestion, we appreciate the need for a definition of related entity for the purposes of section 258 to be clarified urgently ahead of the prohibition coming into operation on 1 July 2018. We also appreciate that it may be difficult to reach consensus on a singular definition for ***related entity*** given the section 258 provisions are prohibitive, (which may favour a tighter definition of related entity), whereas the definition as it applies to corporate legal practitioners is permissive and a tight definition may be overly restrictive.

Therefore, we believe it would be worthwhile examining whether the definition of related entity under section 6(1)(a) as it relates to companies is appropriate for the purposes of the definition of corporate legal practitioner. We note that these issues were not considered by Professor Hanrahan given her remit was to only examine section 258. We also think there would be merit in consulting specifically with ACCA on the broader question of the definition of related entity as it applies to corporate legal practitioners.

Our preference would be to discuss a range of potential solutions including broadening the definition to, for example, 'associated entity' as defined in s 50AAA of the *Corporations Act*. Another option could be to remove ***related entity*** altogether from the definition of corporate legal practitioners, leaving the parties to the employment contract to determine to whom the in-house counsel may give advice. We would invite discussion and consideration of these options by the LSC in the future given time does not now allow.

Drafting of Rule 6A
With respect to specific drafting matters, Professor Hanrahan has suggested that for consistency a related entity to a person should be the same no matter who the 'person' is. Therefore she concluded that 6(1)(a) of the Uniform Law, which adopts the definition in section 50 of the *Corporations Act* should be as closely aligned with a definition prescribed for the purposes of section 6(1)(b) of the Uniform Law. We support the policy rationale behind this conclusion.

The proposed rule 6A appears to go beyond the *Corporations Act* concepts of subsidiary and holding company, particularly the concept of control introduced in sub clauses (d) and (e) which appear to be more reflective of the definition of associated entity in section 50AAA of the *Corporations Act*.

We also note that in relation to clause (4) that it appears to only cover a situation where a law practice (that is not a body corporate) has a related entity that is a body corporate but not situations where the related entity is not a body corporate. We assume that this is not the intention.

Our preference would be for consistency in relation to the definition of related entity for the purposes of enforcing the prohibition under section 258. We do not believe there is any policy justification for applying a broader definition (and therefore, expanding the breadth of the prohibition) on the basis that a law practice is not a company. Therefore, we support the drafting of a rule that mirrors the definition under section 6(1)(a) of the Uniform Law for the purposes of section 6(1)(b) provided that rule was limited to the prohibition under section 258. We believe this represents the position recommended by Professor Hanrahan.

Board ABN 82 518 945 610 Commissioner ABN 66 489 344 310

Rule 6. *New Division inserted in Part 4.6*

We have a concern with the definition of ***mortgage financing*** proposed to be inserted by new rule 91C(3). The definition references the definition of mortgage financing in the Legal Profession Uniform Conduct Rules (Solicitors) 2015. Firstly, the reference to the Rules in the draft rule is incorrect. Secondly, as there is a definition of mortgage financing in section 6 of the Uniform Law, we believe this definition is unnecessary and confusing. We suggest clause (3) be removed.

Guidance material
We appreciate the LSC has provided the intended guidance material in advance for our review. We are of the view the guidance material is clear and will allow smoother implementation. Subject to the matters we have raised as to the draft amendments pertaining to the effect on corporate legal practitioners and referencing to other sets of rules, we are satisfied with the guidance material.

Yours sincerely

Fiona McLeay
Board CEO & Commissioner

Board ABN 82 518 945 610 Commissioner ABN 66 489 344 310