AUSTRALIA

Investment rules of the world

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At DLA Piper, we have one of the largest finance and projects teams in the world with more than 600 dedicated lawyers and an established local law firm network. We share knowledge and skills in debt instruments, debt securities, funds, derivatives and portfolios, as well as energy, infrastructure and other projects, across Europe, the Middle East, Africa, Asia Pacific and the Americas.

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Investment Rules of the World

With input from across our global network, this guide covers key legal topics for different financial activities and projects and gives you an overview of the points you may consider when initially looking at financing or investing in particular jurisdictions. Please contact us if you would like to discuss any legal issues or solutions for your business. We also welcome your feedback about this guide via investmentrules@dlapiper.com.

Australia

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Capital markets and structured investments

Issuing and investing in debt securities

Are there any restrictions on issuing debt securities?

The general position under the *Corporations Act 2001* (Cth) is that debt securities may only be offered and sold in Australia if they are accompanied by a disclosure document prepared in accordance with the *Corporations Act 2001* (Cth). Disclosure documents must be lodged with ASIC.

There are exceptions to the requirement to prepare a disclosure document which are outlined below.

The *Corporations Act 2001* (Cth) also imposes a general prohibition on the advertising or publicity of offers of securities that require a disclosure document. There are further prohibitions on 'hawking' (i.e. unsolicited meetings or telephone calls).

If debt securities are listed on the Australian Securities Exchange, there are additional disclosure requirements and continuing obligations that will apply – these are contained in the Listing Rules of the Australian Securities Exchange.

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What are common issuing methods and types of debt securities?

The debt securities market in Australia includes stand-alone bonds and bond programs (e.g. Medium-Term Note programs) issued by large corporations and financial institutions.

Bonds may be issued in wholesale and retail formats. Wholesale issues do not require a prospectus or other disclosure document, and are rarely listed.

Many different types of debt securities are offered in the Australia, including guaranteed and asset-backed securities, high yield bonds, covered bonds, hybrid securities (including convertible notes and preference shares), derivative securities and green bonds.

Parties that are not resident in Australia may issue 'Kangaroo Bonds' (i.e. bonds issued in Australian dollars). In many cases, these issues are driven by favorable Australian dollar terms in the cross-currency swap markets.

Wholesale debt securities can be cleared through Austraclear, the Australian domestic clearing system. In order to be eligible, the securities must be issued in Australian dollars.

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What are the differences between offering debt securities to institutional / professional or other investors?

Offers of debt securities can generally be made to institutional/professional investors without a disclosure document. Offers of debt securities to retail investors require a disclosure document prepared in accordance with the Corporations Act 2001 (Cth).

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When is it necessary to prepare a prospectus?

The general position under the Corporations Act 2001 (Cth) is that debt securities may only be offered and sold in Australia if they are accompanied by a disclosure document prepared in accordance with the Corporations Act 2001 (Cth).

Offers of debt securities can generally be made to institutional/professional investors without a disclosure document.

Offers of debt securities to retail investors will require a disclosure requirement, most commonly in the form of a prospectus.

Even where a prospectus is not required by law, an information memorandum is commonly used for marketing purposes.

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What are the main exchanges available?

The Australian Securities Exchange is the main exchange in Australia.

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Is there a private placement market?

It is certainly possible to issue bonds through private placement in Australia, although domestic demand for such bonds is generally lower than in the US and Europe, due in part to a relative lack of liquidity. Many corporate issuers prefer to issue bonds in overseas jurisdictions.

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Are there any other notable risks or issues around issuing or investing in debt securities?

Issuing debt securities

Issuers are required to take responsibility for disclosure documents for debt securities. Liability may arise for breach of statute for statements that are misleading or deceptive, or omit any required information. In addition to the issuer, directors, underwriters, and other parties making statements in a defective disclosure document may also be liable for the damage arising from such defective disclosure.

Investing in debt securities

Debt security terms and conditions typically contain provisions which may permit their modification without the consent of all investors and confer significant discretions on the trustee, which depending on the terms of issue may be exercised with or without the consent of investors and without regard to the individual interests of particular investors. The conditions also provide for meetings of investors to consider matters affecting the investors interests. These provisions typically permit defined majorities to bind all investors including investors who did not attend and vote at the relevant meeting and investors who voted against the majority.

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Establishing and investing in debt / hedge funds

Are there any restrictions on establishing a fund?

Generally

The Australian funds management industry is mature and heavily regulated. An Australian hedge or debt fund is usually structured as a unit trust and would ordinarily fall within the definition of a 'managed investment scheme' in the Corporations Act 2001 (Cth). That Act imposes a wide range of obligations and requirements on the operators of managed investment schemes. Managed investment schemes are regulated by ASIC

Managed investment schemes

The following key restrictions apply when establishing a managed investment scheme:

- managed investment schemes, particularly those offered to 'retail clients' (as that term is defined in the Corporations Act 2001 (Cth)), are subject to relatively heavy regulatory requirements which may impose a significant compliance burden on the operators of such schemes;
- the operator of the managed investment scheme (which is called the 'Responsible Entity') must hold an Australian Financial Services License (AFSL) issued by ASIC (or be an authorized representative of another entity's AFSL) which authorizes it to act as the Responsible Entity of managed investment schemes;
- a managed investment scheme which is offered to retail clients must be registered with ASIC;
- if a managed investment scheme is structured as a unit trust (as is usually the case), general trust law will apply to the operation of the trust; and
- the offer of interests in a managed investment scheme to retail clients will require the preparation of a detailed disclosure document, the contents of which is heavily regulated.

Managed investment schemes may also be listed on the Australian Securities Exchange, provided that a range of regulatory requirements are met.

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What are common fund structures?

Unit trust

As noted above, the most common fund structure in Australia is a unit trust, where each investor holds units representing a beneficial interest in the assets of the fund.

Unit trusts are usually managed so they can be treated as 'flow through' vehicles for tax purposes (similar to a partnership) so that the fund itself is not subject to taxation. Investors are taxed on their share of the net income and capital gains earned by the fund.

Certain units trusts that are managed investment schemes for Corporations Act 2001 (Cth) purposes may also qualify for tax concessions as a managed investment trust.

Collective investment vehicles

The Australian Government has been working on the introduction of an Australian collective investment vehicle (CIV) regime, which will introduce two alternatives to the current Australian unit trust structure. The new vehicles will be a corporate CIV and a limited partnership CIV, which will be similar to the equivalent structures which are commonly used in foreign jurisdictions.

The Australian Government is still conducting a consultation process (which began in 2017) with the most recent pieces of draft legislation outlining the proposed regime released in January 2019.

Asia Region Funds Passport

The Asia Region Funds Passport was implemented in Australia in 2018 with the Corporations Amendment (Asia Region Funds Passport) Act 2018 (Cth). It allows Australian fund managers to offer interests in qualifying funds to investors across multiple participating economies in the Asian region with limited additional regulatory requirements. Similarly, fund managers in other participating economies

will be able to market their qualifying funds to Australian investors using the more streamlined regulatory process.

However, the uptake of the Asia Region Funds Passport will largely depend on how the corresponding tax reforms and the CIV regime will look once enacted by Parliament.

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What are the differences between offering fund securities to professional / institutional or other investors?

Distinction between retail and wholesale investors

An investor is deemed to be a 'wholesale' investor for Australian law purposes where it has invested AUD500,000 or more in a particular fund. There are numerous other criteria for an investor to qualify as a 'wholesale' investor for Australian law purposes. For example, where an investor can produce a copy of a certificate given within the preceding two years by a qualified accountant that confirms that it has net assets of at least AUD2.5 million or has a gross income for each of the last two financial years of at least AUD250,000. Further, a person who has or controls gross assets of AUD10 million (including any assets held by an associate or under a trust that that person manages) is deemed to be a wholesale investor no matter what the size of its investment.

All investors that are not wholesale investors are considered to be retail investors.

Retail funds

Funds offered to retail investors must be registered with ASIC. The offer of interests in retail funds must be accompanied by a PDS, which must contain specific information as prescribed by the Corporations Act 2001 (Cth) (for example, information about the Responsible Entity, the fees and costs payable, the risks and benefits and significant characteristics of the fund). A PDS must also contain all other information that might reasonably be expected to influence the decision of a retail investor considering whether to invest in the fund.

Institutional/professional funds

Funds which are offered exclusively to wholesale investors do not need to be offered using a PDS. However, it is usual to provide another disclosure document, such as a private placement memorandum or information memorandum, when offering interests in such funds. Any such disclosure document must not be misleading or deceptive.

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Are there any other notable risks or issues around establishing and investing in funds?

Establishing funds

As noted above, in order to establish a fund in Australia, the operator of the fund must usually hold an AFSL (or be an authorized representative of an AFSL holder) with appropriate license authorizations.

In addition, where the fund is a managed investment scheme (which is usually the case for retail funds), a Responsible Entity must be appointed. In order for an entity to act as a Responsible Entity, it must:

- be an Australian public company;
- hold an AFSL (or be an authorized representative of another AFSL holder) authorizing it to provide the various financial services relevant to the operation of the fund; and
- either have a majority of directors who are external directors or have a compliance committee (to oversee the retail fund's compliance requirements) with a majority of 'external members'.

It is common for investment managers who do not satisfy the requirements for being a Responsible Entity to enter into an arrangement with an external or 'professional' Responsible Entity, which will operate the fund according to the investment strategy which the investment manager may set.

As mentioned, managed investment schemes may also qualify for tax concessions if they qualify as a “managed investment trust” under Australian tax laws. For a wholesale unit trust fund to qualify as a “managed investment trust”, the trust must be operated or managed by an AFSL licensee or by an authorised representative of such licensee.

Investing in funds

As noted above, most investment funds in Australia are structured as unit trusts. These funds are subject to the general law of trust. In addition, usually:

- The investors in a fund have no power to influence the fund's investment strategy, or any of the decisions or operations of the fund, solely by virtue of being a unit holder.
- The investors in the fund do not have a specific right to any particular assets of the trust.
- The investors in the fund will rank behind the fund's creditors in the event of insolvency.
- The fund operator will usually be entitled to an indemnity from the assets of the fund for any liabilities it may incur in performing its duties, and will usually limit its liability to the amount by which it is actually indemnified.

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Managing and marketing debt / hedge funds

Are there any restrictions on marketing a fund?

The marketing of a fund in Australia will normally constitute providing 'financial product advice' and so will be a 'financial service' for the purposes of the Corporations Act 2001 (Cth). That Act provides that, generally, all providers of financial services must hold an AFSL (or be appointed as an authorized representative of another AFSL holder) with an authorization to provide the relevant financial service.

When offering interests in retail funds it is also generally necessary to prepare a PDS.

Exemptions

There are a number of very limited exemptions from the need to obtain an AFSL or to act under an authorization from another AFSL in order to market a fund in Australia. These exemptions generally only apply when the fund is marketed solely to wholesale investors. For example:

- Certain foreign financial services providers who are regulated in jurisdictions that ASIC considers to have a regulatory framework sufficiently similar to the Australian regime (such as the UK, US, Singapore, Hong Kong and Germany) may be eligible to apply for relief from licensing to enable them to market funds to Australian 'wholesale' investors[2].
- An exemption applies where the marketing is done in Australia to a prospective investor which itself holds an AFSL and is not acting as a trustee or on behalf of another person (as Australian superannuation funds and Australian fund managers offer their products to their Australian investors through trusts, this limits the exemption to true proprietary investors which commonly do not have an AFSL as they are not usually required to hold one).
- An exemption applies where a prospective Australian investor makes enquiries of a foreign fund manager without any prior solicitation by the foreign fund manager, and the foreign fund manager does not during this time actively solicit persons in Australia in respect of the relevant fund (other than in response to the enquiry initiated by the Australian investor or by the Australian investor's agent).

[2] ASIC is currently conducting a consultation process to formalise this exemption into a foreign financial services licence for foreign financial services providers. ASIC has proposed a prospective commencement date of 1 April 2020, however this is subject to the finalisation of the draft instruments proposed by ASIC.

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Are there any restrictions on managing a fund?

Australian-domiciled funds will usually fall within the definition of 'managed investment scheme' in the Corporations Act 2001 (Cth). The Responsible Entity of a managed investment scheme (which is the operator of the fund) is typically required to hold an AFSL (or be an authorized representative of an AFSL holder) which authorizes it to provide the various financial services necessary to operate the fund, including a specific authorization to act as the Responsible Entity of a managed investment scheme.

As noted above an entity wishing to act as the Responsible Entity of a managed investment scheme must also:

- be an Australian public company; and
- either have a majority of directors who are external directors or have a compliance committee (to oversee the retail fund's compliance requirements) with a majority of 'external members'.

An investment manager which is not able to act as a Responsible Entity may enter into an arrangement with an external or ‘professional’ Responsible Entity, which will operate the fund according to the investment strategy which the investment manager may set. In those situations, from a strictly legal perspective, it is the Responsible Entity of a retail fund that engages the investment manager and is responsible for the acts of the investment manager, and the Responsible Entity will bear any liability for the mismanagement of the fund. Such external Responsible Entities will therefore typically charge a significant fee for their service.

If a managed investment scheme is to be offered to retail investors, it must be registered with ASIC and will be subject to a further layer of regulatory requirements. For example, a registered managed investment scheme must have a 'constitution' which is compliant with the Corporations Act 2001 (Cth) and must also maintain a 'compliance plan' which sets out the measures which the Responsible Entity must take to ensure compliance with the constitution and the Corporations Act 2001 (Cth).

The offer of interests in a managed investment scheme to retail investors will also generally require certain disclosure documents, including a PDS, to be prepared in accordance with the content requirements mandated by the Corporations Act 2001 (Cth) and by ASIC.

As mentioned, managed investment schemes may also qualify for tax concessions if they qualify as a “managed investment trust” under Australian tax laws. For a wholesale unit trust fund to qualify as a “managed investment trust”, the trust must be operated or managed by an AFSL licensee or by an authorised representative of such licensee. For a managed investment trust that seeks the 15% concessionally withholding tax rate for its fund payments, a substantial proportion of its investment activities must also be carried out in Australia.

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Entering into derivatives contracts

Are there any restrictions on entering into derivatives contracts?

Unless an exemption or exclusion applies, a person issuing derivatives as part of its financial services business is deemed to be dealing in financial products, which requires an AFSL under the Corporations Act 2001 (Cth) and the Corporation Regulations 2001 (Cth). If a person issues derivatives without an AFSL, the counterparty would be entitled to rescind any agreements in relation to that product and the relevant agreements will be unenforceable. There are specific financial requirements for a person authorized to issue derivatives, which differ from requirements in relation to other financial products, which recognize the exposure of the licensee to counterparties arising from entering into derivatives.

For these purposes, a 'derivative' is broadly defined as an arrangement that has a future liability element and a derived value element, and is sufficiently wide to cover all commonly-regarded types of derivative contracts, including futures agreements and forwards, options, swaps and contracts for difference. Under the relevant legislation, certain arrangements are specifically excluded as derivatives including:

- arrangements for mandatory physical delivery of tangible property;
- a contract for the future provision of services; and
- anything that falls within one of the other categories of financial product (such as a security).

AFSL licensees have ongoing obligations under the Corporations Act 2001 (Cth) in terms of their conduct, including to:

- notify the ASIC of breaches or likely breaches of certain significant licensee obligations;
- quote their AFSL number in documents;

- comply with stipulated procedures when dealing with clients' money; and
- keep financial records.

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What are common types of derivatives?

Derivative contracts are entered into in Australia for a range of reasons including hedging, trading and speculation.

Derivatives may be traded over-the-counter or on an organized exchange.

All of the main types of derivative contract are widely used in Australia, including futures agreements and forwards, options, swaps (including credit default swaps) and contracts for difference. Underlying assets commonly include equities, fixed income instruments, commodities, foreign currencies and credit events.

The gross notional outstanding for interest rate derivatives in Australia is worth in excess of AUD10 trillion, the majority of which are denominated in AUD. There is also a sizeable FX swap market, with average daily turnover in excess of AUD100 billion.

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Are there any other notable risks or issues around entering into derivatives contracts?

Since the global financial crisis in 2007-to-2008, and the G20 summit in 2009 the derivatives market has been subject to a significant amount of new regulation, and this has led to substantial compliance costs for market participants.

In January 2013, ASIC introduced the ASIC Derivative Transaction Rules (Reporting) 2013, together with the ASIC Derivative Trade Repository Rules 2013. Among other things, these Rules introduced mandatory reporting requirements for derivative transactions for the majority of derivatives users. These rules were subsequently softened by the ASIC Derivative Transactions Rules (Reporting) Amendment 2015 (no 1).

Other recent regulatory changes of note include the requirement for certain standardized over-the-counter derivative trades to be subject to clearing with a prescribed Central Clearing Counterparty, as implemented through the Corporations (Derivatives) Amendment Determination 2015 (No 1), and the requirement for reporting of certain trades to a licensed Trade Repository, as implemented through the Derivative Transaction Rules (Reporting) 2013 (both regulations have been subject to subsequent amendment).

The Prudential Standard CPS 226 (Margining and risk mitigation for non-centrally cleared derivatives), as published by the APRA in 2016, establishes the requirement for the posting and collection of variation and initial margin in transactions which include a covered entity (for example, deposit-taking institutions that are authorized under the Banking Act 1959 (Cth)).

In addition, it is important to note that the approach to market misconduct is generally the same for securities and for derivatives (including market manipulation and insider trading) although compensation orders for damages do not apply to derivatives.

Finally, the ATO has recently issued guidelines setting out risk factors applicable to cross-border related party derivatives.

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Debt finance

Lending and borrowing

Are there any restrictions on lending and borrowing?

Lending

While there are no general restrictions on lending, a lender may need to comply with various codes or regulations if engaging in certain lending practice, particularly if lending to individuals or consumers. The most important to note are as follows:

- The National Credit Code applies to credit contracts entered into by natural persons or strata corporations, for personal domestic or household purposes or the purposes of residential improvement. The National Credit Code imposes a range of regulatory requirements on the lender that do not apply to loans that fall outside its scope. Those outside its scope generally include loans to companies and loans predominately for business or investment purposes.
- The Banking Code of Practice (BCOP) of the Australian Banking Association (ABA) came into effect on 1 July 2019. It is effectively a complete rewrite of the previous 2013 Code of Banking Practice. Although the BCOP is voluntary, each ABA member bank with a retail presence in Australia is required to subscribe to the BCOP as a condition of its ABA membership. The BCOP is binding and the BCOP rules form part of the contractual relationship between the bank and its customer. The BCOP applies to specified banking services provided to individual customers, small businesses[1] and guarantors and prospective guarantors in respect of a loan to an individual or small business. Affected "banking services" include bank accounts, term deposits, credit and debit cards, home and personal loans, overdrafts, bill facilities, consumer credit insurance and payment and forex services. However, "banking services" expressly excludes shares, bonds and securities, as well as financial products and services provided to wholesale customers.
- An Australian credit license must be held by any person engaging in the provision of consumer 'credit activities' (including supplying goods on credit). Licensees must comply with a number of general conduct obligations and responsible lending guidelines.
- The Banking Act 1959 (Cth) and various legislative and prudential requirements must be adhered to for a lender to be a 'bank' or to operate as a deposit taking institution. A person must not hold itself out to be a 'bank' unless authorized to do so.

[1]A business is a "small business" if at the time it obtains the banking service all of the following apply:

a) it had an annual turnover of less than AUD10 million in the previous financial year; and

b) it has fewer than 100 full-time equivalent employees; and

c) it has less than AUD3 million total debt to all credit providers including:

i. any undrawn amounts under existing loans;

ii. any loan being applied for; and

iii. the debt of all its related entities that are businesses.

Borrowing

While borrowers are generally not regulated, it is advisable for a borrower to consider whether the National Credit Code or the BCOP apply to his, her or its activities, in which case various protections may be available.

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What are common lending structures?

Lending in Australia may be structured in a number of different ways to include a variety of features, depending on the commercial aims of the parties.

A loan may be provided on a bilateral basis (a single lender providing the entire facility), a syndicated basis (multiple lenders each providing a portion of the overall facility) or a club basis (multiple lenders lending bilaterally in parallel).

Syndicated facilities by their nature involve more parties (such as an arranger, an agent and a security trustee which each carry out a specific role for the syndicate banks), are more highly structured and involve more complex documentation. Large financings will typically be done on a syndicated basis, with one of the syndicate taking the lead in coordinating and arranging the financing.

Club facilities involve multiple lenders lending bilaterally to the borrower in parallel to each other on materially similar terms. Club facilities usually do ot involve a facility agent (at least for payment purposes) and they lack syndication terms which dictate funding mechanics, payment distribution, sharing provisions and lender voting regimes. A club facility may be documented in a variety of ways, including by:

- a deed of common provisions which are adopted wholly or in part by each lender under its facility agreement;
- individual, but largely identical, bilateral loan agreements; and

- a single document similar to syndicated loan agreement, but without a payment agent or syndication terms.

Loans will be structured to achieve the borrower's specific funding objectives. For example, they may be term loans, revolving credit facilities, working capital loans, equity bridge facilities, project facilities and letter of credit facilities, to name a few.

Loan durations

Typically, the Australian banking market accommodates commercial loan tenors of three to five years. Longer-term debt may be available in limited circumstances.

The duration of a loan may also be determined by its type. For example, typically:

- a term loan is provided for an agreed period of time but with a short availability period;
- a revolving credit facility is provided for an agreed period of time with an availability period that extends nearer to the date of its maturity. It may be redrawn if repaid;
- an overdraft is provided on a short-term basis to solve short-term cash flow issues;
- a standby or a bridging loan is intended to be used in exceptional circumstances when other forms of finance are unavailable. It often attracts a higher margin; or
- a cash advance, provided on a short-term basis to cover short-term cash flow issues and often attracting a higher margin.

In Australia, bill facilities are also used sometimes and they operate with bills maturing and 'rolling over' at set intervals (usually 30, 60, 90 or 180 days). Historically, loan note facilities have also been made available for stamp duty or income withholding tax purposes.

Loan security

A loan may be either secured, unsecured (including on a 'negative pledge' basis) or guaranteed.

Loan commitment

A loan may be:

- committed, meaning that the lender is obliged to provide the loan if certain limited conditions are fulfilled. Conditions precedent will be set out in the loan agreement; or
- uncommitted, meaning that the lender has discretion whether or not to provide the loan.

No conditions precedent will be set out in the loan agreement.

Loan repayment

A loan may be repayable:

- on demand,
- on an amortizing basis (that is, in instalments over the life of the loan or as may be scheduled); or
- upon maturity (commonly referred to as a 'bullet loan').

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What are the differences between lending to institutional / professional or other borrowers?

Consumer and small business lending is generally heavily regulated, requiring necessary licenses and compliance obligations.

By contrast, lending to institutional or professional borrowers is subject to less regulatory oversight and is less burdensome from a compliance perspective.

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Do the laws recognize the principles of agency and trusts?

Yes, both principles are recognized under Australian law. Relationships based on the principles of agency and trust are commonly found in Australian financing transactions.

For example, in a syndicated financing, the syndicate will appoint an agent (usually the arranging bank) to act on behalf of the syndicate banks.

The agent will coordinate activities relating to the loan repayments, correspondence between the borrower and the syndicate banks and other matters. The syndicated loan documentation will typically contain provisions defining the nature of the agent's appointment and the scope of its authority and liabilities.

In a secured syndicated financing, the security will be granted in favor of a security trustee which will hold the security on trust for the benefit of the banks.

Borrowers are also commonly trustees, particularly in the real estate investment sector.

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Are there any other notable risks or issues around lending?

Generally

Loan agreements and other finance documents are subject to general statutory, contractual and common law principles.

Australian courts will not enforce a penalty in a loan agreement. Lenders muat therefore be careful when determining the rate of default interest and the amount of any cancellation, prepayment or similar fees.

A lender should be aware that, even if it is rightfully exercising its rights under the loan agreement, the Australian Securities and Investments Commission Act 2001 (Cth) (ASIC Act) prohibits persons from engaging in unconscionable conduct or morally wrong behavior. In determining what constitutes unconscionable conduct, the court will consider the bargaining power of the parties, the parties' respective abilitiesto understand the documents and the lender's disclosure of certain risks.

Unfair contract legislation

The Australian Consumer Law and the ASIC Act regulate unfair contract terms found in standard form contracts entered into or renewed after 12 November 2016 where:

- it is for the supply of goods or services or the sale or grant of an interest in land;
- at least one of the parties is a small business (employs less than 20 people, including casual employees employed on a regular and systematic basis); and
- the upfront price payable under the contract is no more than AUD300,000 or AUD1 million if the contract is for more than 12 months.

A standard form contract is a contract that is prepared by one party where the other party has little or no scope to negotiate the terms of the contract. If a court declares a term of a standard form contract to be unfair, the term will be void and the contract will continue to operate unless it is inoperable without the void term. Consumers and Australian Consumer Law regulators are able to claim for damage incurred as a consequence of the unfair contract term.

In the context of financing transactions, the unfair contract legislation will be primarily relevant to home loans and small to medium sized commercial loans documented on the lender's standard form documentation.

Specific types of lending

ACQUISITION FINANCE

An Australian company may not provide financial assistance to a person to purchase shares in the company itself or its holding company (even if that holding company is incorporated outside of Australia) unless the financial assistance:

- does not materially prejudice the company, its shareholders or its ability to pay its creditors (the ‘no material prejudice’ exception);
- has been approved by the company’s shareholders in accordance with the 'whitewash' procedure prescribed by the Corporations Act 2001 (Cth); or
- falls within a specified exemption. A common example of prohibited financial assistance is the granting of a guarantee or security by a company whose shares are being purchased in support of a loan advanced by a financier to the purchaser to fund the share acquisition.

Companies and their financiers do not generally rely on the ‘no material prejudice’ exception and the specified exemptions are only sometimes relevant. Instead, the common practice in Australia (and the prudent approach) is for the company to obtain shareholder approval of the financial assistance by way of the whitewash procedure. The whitewash procedure in Australia can be more time consuming and complex to implement than equivalent procedures in other jurisdictions.

A breach of the financial assistance prohibition will not affect the validity of the transaction, but may result in civil and criminal sanctions.

THE PERSONAL PROPERTY SECURITIES ACT 2009 (CTH) (PPSA)

The PPSA came into effect on 2012 and it comprehensively overhauled the laws then in force for taking security over personal property in Australia. The PPSA has been modelled on the equivalent Canadian and New Zealand statutes and it bears much resemblance to Article 9 of the US Uniform Commercial Code.

The PPSA adopts a substance-over-form definition of 'security interest', which captures not only traditional forms of security, such as charges and mortgages, but also quasi-security arrangements, such as turnover trusts and retention of title. The PPSA also deems certain other arrangements to be security interests, such as leasing or bailment interests and the interests in assigned receivables. Each of these types of 'security interests' should be perfected, most commonly by registration on the Personal Property Securities Register, to ensure that it operates effectively upon the grantor’s insolvency or liquidation. It is important to give careful consideration to whether a registrable form of ‘security interest’ under the PPSA arises in the relevant transaction.

Standard form documentation

Most syndicated finance transactions in Australia are documented on the basis of recommended form Australian law documentation published by the Asia Pacific Loan Market Association (APLMA). This documentation has been modelled on the recommended forms produced by the Loan Market Association in London.

Less complex and usually bilateral transactions are generally documented on bank standard form documentation prepared in-house or on bespoke facility documentation prepared by the advising solicitors.

The Banking & Financial Services Law Association (BFSLA) has produced standard templates for legal opinions in financing transactions and these are generally followed in the Australian market.

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Are there any other notable risks or issues around borrowing?

There are limited restrictions on borrowing in Australia. However, depending on the nature of the transaction, the following issues may need to be considered:

- foreign investment approval;
- superannuation funds general prohibition from borrowing money;
- financial assistance;
- loans to directors;
- corporate benefit rules; and

- related party transaction provisions applying to public companies; and
- compliance with the Australian income tax laws (such as thin capitalisation rules which limit the gearing level of inbound and outbound structures, debt/equity rules and transfer pricing rules) and the ATO's enhanced scrutiny of cross-border related party debts.

Many of these issues are discussed elsewhere in this guide.

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Giving and taking guarantees and security

Are there any restrictions on giving and taking guarantees and security?

Some of the key areas affecting the giving and taking of guarantees and security are as follows.

Corporate benefit

A transaction may be voidable if there is no corporate benefit to the entity. The presence of corporate benefit is a factual matter.

Corporate benefit is a particular issue for guarantees. Each director owes a duty to the company to act for the benefit of the company in its best interests, with due care and diligence, in good faith and for a proper purpose. Each director must also avoid any conflict between his or her personal interests and those of the company. These duties must be observed when it is proposed that a company grants a guarantee of the obligations of another.

In deciding whether to grant a guarantee (or provide third party security), the directors may consider both direct and indirect benefits flowing to the company. For example, in the context of a corporate group, the granting of a guarantee might indirectly benefit the guarantor if it is a requirement for the support of a related company and benefits flow back to the guarantor. Note that corporate benefit must be assessed at the level of the individual company – i.e. it is not sufficient that the guarantee benefits the group as a whole.

A director of a wholly-owned subsidiary may take into account the best interests of its holding company so long as the company's constitution permits him or her to act in the best interests of the holding company and the subsidiary is solvent.

It may be possible to address concerns regarding the presence of corporate benefit by obtaining shareholder approval for the transaction.

A guarantee that does not benefit the company commercially may be voidable. Further, the guarantee could be held to be an unfair preference or uncommercial transaction. The directors could be subject to civil and criminal penalties and personal liability.

Insolvency and voidable transactions

If a lender enters into a secured transaction shortly before the company becomes insolvent, unsecured creditors may be able to challenge the security on the basis that the grant of security constituted an unfair preference or an uncommercial transaction. Unfair preferences and uncommercial transactions are both voidable. If the unsecured creditors are successful, the lender will not be able to have recourse to the purportedly secured assets and they will be distributed amongst all creditors, including the unsecured creditors. The rules are technical and the following is a simplified outline.

Unfair preferences arise where one creditor is unfairly preferred over others.

Uncommercial transactions do not involve creditors as such, but aim to recover any disposals of assets at an undervalue.

The transaction must have been entered into while the company is insolvent, or the company must have become insolvent as a consequence of the transaction. It must also have been entered into during the period ending on the 'relation-back day', but on or before the winding up process began. For unfair preferences, the period is six months, and for uncommercial transactions, it is two years. In each case, the period is four years in the case of related parties and 10 years if the transaction was entered into to avoid the rights of creditors. The relevant period is known as the 'hardening period'.

After the end of the hardening period, the transaction is no longer vulnerable to being voided.

Financial assistance

An Australian company may not provide financial assistance to a person to purchase shares in the company itself or its holding company (even if that holding company is incorporated outside of Australia) unless the financial assistance:

- does not materially prejudice the company, its shareholders or its ability to pay its creditors ('no material prejudice' exception);
- has been approved by the company's shareholders in accordance with the 'whitewash' procedure prescribed by the Corporations Act 2001 (Cth); or
- falls within a specified exemption.

A common example of prohibited financial assistance is the granting of a guarantee or security by a company whose shares are being purchased in support of a loan advanced by a personfinancier to the purchaser to fund the share acquisition.

Companies and their financiers do not generally rely on the 'no material prejudice' exception and the specified exemptions are only sometimes relevant. Instead, the common practice in Australia (and the prudent approach) is for the company to obtain shareholder approval of the financial assistance by way of the whitewash procedure. The whitewash procedure in Australia can be more time consuming and complex to implement than equivalent procedures in other jurisdictions.

A breach of the financial assistance prohibition will not affect the validity of the transaction, but may result in civil and criminal sanctions.

Related party transactions

Chapter 2E of the Corporations Act 2001 (Cth) is intended to preserve and maintain the assets or resources of public companies by requiring that, in simple terms, financial benefits passed to related parties that might diminish or adversely affect those assets or resources are disclosed and approved by a general meeting of the public company beforehand.

The provisions are detailed, but essentially a public company (or an entity controlled by a the public company) may only give a financial benefit to a related party of the public company if:

- the benefit falls within one of the seven categories of exempted financial benefit (e.g. arm's-length terms, pursuant to a court order); or
- if the benefit is of any other kind, the public company has obtained the approval of its members to give the benefit or to enter into a contract to give the benefit.

Failure to comply with the related party transactions laws will not affect the validity of the transaction, but it may render any person involved liable for a civil or criminal penalty.

National Credit Code

The National Credit Code applies to credit contracts entered into on or after 1 July 2010 where:

- the lender is in the business of providing credit;
- a charge is made for providing credit;
- the debtor is a natural person or strata corporation; and
- the credit is provided for personal or domestic use or to purchase, renovate or improve residential property for investment purposes or refinance credit previously provided for this purpose.

There are certain confined exemptions (e.g. for low cost short term credit). The Code does not apply to business loans.

Where the National Credit Code applies there are restrictions on the guarantees that a lender may obtain from a customer. For example, a guarantee from an individual must be limited (in terms of the amount the lender can recover) to the amount of the relevant loan plus interest, charges, costs and expenses. There also are various disclosure and other obligations that the lender must comply with. Failure to

comply may render the guarantee or security unenforceable.

Banking Code of Practice

The restrictions noted above apply in a similar manner under the 2019 BCOP, the ABA's voluntary code of practice which is mandatory for retail banks to adopt as a condition of their membership of the ABA and which is enforceable by law. Similar to the National Credit Code, a bank that is a signatory to the BCOP may only accept a guarantee which is limited to (a) a specific amount or category of amounts (such as all amounts owing under a specific loan) plus other amounts (such as interest and recovery costs) or (b) the value of a specified property or other asset under a specified security at the time of recovery.

Foreign lenders

There are technical restrictions on the foreign ownership of Australian assets and companies set out in Australia's foreign investment legislation, namely the Foreign Acquisitions and Takeovers Act 1975 (Cth). Foreign lenders and foreign entities taking the benefit of security over Australian assets should consider the possible application of this legislation, which is administered by FIRB. Notification to FIRB and FIRB approval may be required in some cases before a foreign entity takes or enforces security. Particular issues arise for foreign government investors upon enforcement.
There is a fairly broad 'moneylender' exemption for lenders. In simplified terms, if security over Australian assets is held in the ordinary course of carrying on a business of lending money and solely by way of security for the purposes of a 'moneylending agreement', the moneylender exemption will generally apply. This exemption also applies to the acquisition of an interest in an Australian asset arising by way of enforcement of a security interest held solely for the purposes of a moneylending agreement.

A moneylending agreement is defined as:

- an agreement entered into in good faith, on ordinary commercial terms and in the ordinary course of carrying on a business (a moneylending business) of lending money or otherwise providing financial accommodation, except an agreement dealing with any matter unrelated to the carrying on of that business; and
- for a person carrying on a moneylending business, or its subsidiary or holding entity, an agreement to acquire an interest arising from a moneylending agreement as described above.

Where the exemption applies, notification and FIRB approval are not required when taking or enforcing the security.

There are limits on how long the foreign government investors may hold onto an interest upon enforcement. For these investors, the moneylender exemption requires in effect that, if its interest is acquired by way of enforcement of a security, that interest must disposed of, or a genuine sale process commenced, within six months of the acquisition (or 12 months in the case of an authorised deposit-taking institution). If this does not occur, separate FIRB approval is required. The concept of 'foreign government investor' is broadly defined and potentially easily triggered. For example, it could include a trustee of a trust in which a foreign government holds a substantial interest and general partner of a limited partnership in which a foreign government holds (alone or with associates) at least a 20% interest (or 40% or more where there is more than one foreign government).

Failure to obtain FIRB approval, if required, could give rise to penalties, an unwinding of the transaction or an order for the disposal of assets.

Critical infrastructure

If the security is taken over a 'critical infrastructure asset', which includes approximately 200 electricity, gas, water and port assets, then a secured creditor may have reporting obligations under the Security of Critical Infrastructure Act 2018 (Cth) if it is in a position to directly or indirectly influence or control the asset.

Last modified 3 Dec 2019

What are common types of guarantees and security?

Common types of guarantees

Guarantees may take a number of forms, including the following.

GUARANTEES AND INDEMNITIES

Guarantees taken in support of loan facilities typically include both guarantee and indemnity provisions (albeit the document may be described simply as a 'guarantee'). A guarantee is a promise by the guarantor to ensure that the borrower fulfils its obligations under the facility agreement (primarily to repay the loan) and a promise by the guarantor to fulfil those obligations if the borrower fails to do so. The borrower's obligations are primary and the guarantor's obligations are secondary. A guarantee is contingent on the borrower's primary obligation remaining valid, so that if for any reason the borrower's obligations are set aside, the guarantee will also fall away. An indemnity is also a promise to be responsible for another's loss. However, unlike a guarantee, it is a primary obligation given by the indemnifier in favour of the beneficiary. It is not contingent on the borrower's obligations remaining on foot. Therefore if the borrower's obligations are set aside for any reason, the indemnifier will remain liable under the indemnity.

This category may include a parent guarantee and indemnity, whereby a parent company or sponsor promises to be accountable for its subsidiary's obligations. A parent guarantee and indemnity is sometimes limited by its terms or operation.

PERFORMANCE GUARANTEES

A guarantor's promise to be accountable for the performance of an act or contractual obligation of another individual. For example, a completion guarantee ensuring that completion of the project occurs on a specified date. This is distinct from a traditional guarantee only in so far as the guarantee usually is limited to performance obligations (rather than payment obligations) and, with the exception of damages, the guaranteed beneficiary's recourse is limited to demanding performance (rather than payment).

BANK GUARANTEES

An unconditional and irrevocable undertaking by a bank in favour of a named beneficiary to make a payment upon receipt of a complying demand from the beneficiary. The bank will then seek reimbursement from its customer under the terms of the indemnity contained in the facility agreement between the bank and the customer.

PERFORMANCE BONDS

An irrevocable undertaking by a financial institution to pay an amount on demand or, in some cases, on the condition that the performance obligations of its customer are not met.

Common tyes of security

Security may be granted over almost all types of assets in Australia, subject to any contractual or statutory restrictions. The most commons forms of security are as follows.

MORTGAGES OVER LAND

State and Territory real property legislation applies. Mortgages of real property must be registered with the land titles office of the State or Territory in which the land is situated. Mortgages of leasehold interest in land must also (in most cases) be registered with the relevant land title office.

Mandatory electronic lodgement of land dealings, including mortgages, is currently being rolled out across Australia.

SECURITY OVER PERSONAL PROPERTY

The following forms of security over personal property are governed by the Personal Property Securities Act 2009 (Cth) (PPSA):

- a general security agreement, where the collateral is all of a grantor's personal property; and
- a specific security agreement, where the collateral is specific personal property of a grantor, such shares, book debts, plant or motor vehicles.

The PPSA adopts a substance-over-form definition of 'security interest', which captures not only traditional forms of security, such as charges and mortgages, but also quasi-security arrangements, such as turnover trusts and retention of title. The PPSA also deems certain other arrangements to be security interests, such as leasing or bailment interests and the interests in assigned receivables. Each of these

types of 'security interests' should be perfected, (most commonly by registration) on the Personal Property Securities Register, to ensure that it operates effectively upon the grantor's insolvency or liquidation. It is important to give careful consideration to whether a 'registrable form of 'security interest' under the PPSA arises in the relevant transaction.

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Are there any other notable risks or issues around giving and taking guarantees and security?

Guarantees

In most Australian States and Territories, a guarantee must be in writing and be signed by the guarantor.

Parties should be careful not to inadvertently discharge the guarantor from its liabilities under the guarantee when making variations to the underlying loanfacility agreement. A guarantor may be released from its guarantee if the underlying facility agreement is varied, save if the variation is immaterial or incapable of prejudicing the guarantor. This is the case even if the guarantor (a) agrees in the guarantee to variations being made to the underlying facility agreement without its consent and (b) is aware of the variations being made. The guarantor should acknowledge the variations to the loan agreement at the time they are made and affirm that its liabilities under the guarantee remain in full force.

Security

MORTGAGES OF REAL PROPERTY

Mortgages of real property must be registered with the land titles office of the State or Territory in which the land is situated. Failure to register may result in the mortgagee losing priority to prior registered interests. Priority between registered interests is generally determined in order of registration. Accordingly, mortgagees should not delay in registering.

SECURITY OVER PERSONAL PROPERTY

Where the PPSA applies, security interests in personal property should be 'perfected'. Security interests may be perfected by registration or, in some circumstances, by control (e.g. for certain financial assets) or possession (e.g. for goods and some intangible rights) of the collateral. Registration on the Personal Property Securities Register is the most common method of perfection.

It is not mandatory to perfect a security interest under the PPSA. However, if a security interest is not registered or not registered within an applicable timeframe (and not otherwise perfected), then (a) it may vest in the grantor immediately upon the grantor being wound up or entering into voluntary administration, a deed of company arrangement or bankruptcy or (b) a third party may acquire an interest in the collateral free from the security interest.

Registration is also relevant to the priority of security interests. A security interest that is not registered (or otherwise perfected) will lose priority to a security interest that is perfected. Generally, priority between security interests perfected by registration (that are otherwise equal in priority) is determined by the order of registration. Therefore it is important for secured parties to register as soon as, if not before, the security agreement is executed. Certain types of security interests are given 'super priority'. An example is a supplier's security interest in goods that it has delivered to a customer (the grantor) on a retention of title basis. This is called a 'purchase money security interest' (PMSI) and, if perfected, has priority over non-PMSIs. This applies also to the interests of lessors or bailors. A PMSI must be specifically registered as a PMSI to be effective in this manner.

The registration requirements under the PPSA are very prescriptive. Failure to register correctly orand errors in a registration, (for example, in a grantor's details,) canmay render a registration ineffective.

The broad definition of 'security interest' under the PPSA means that the rules regarding registration and perfection apply to many arrangements that, prior to the PPSA, were not considered security interests. Failure to recognizerecognise the existence of, and in-turnto perfect, security interests can have significant consequences for the transacting parties.

A secured creditor has better rights on enforcement if it has a charge over the whole or substantially the whole of the grantor's property. During an administration period, subject to certain exceptions, the Corporations Act 2001 (Cth) imposes a statutory moratorium that prevents security from being enforced against the company's assets, save with the administrator's written consent or with the court's leave. The main exception to the moratorium is that a secured creditor with a charge over the whole, or substantially the whole, of the company's property may enforce it during the 'decision period' (being 13 business days from the time notice of the administrator's appointment is given to the charge, or from the time the administration starts). It is therefore common practice for a lender to obtain security over all or substantially all of the company's assets so as to avoid the risk of moratorium on enforcement of security during an administration. A featherweight charge also addresses administration risk.

‘Ipso facto’ stays

The recent ‘ipso facto’ reforms in Australia may impact on the ability of a lender to enforce upon certain insolvency events occurring in respect of the borrower. From 1 July 2018, new provisions in the Corporations Act 2001 (Cth) have imposed a stay on the enforcement of ‘ipso facto’ clauses against a company if it becomes subject to certain insolvency procedures, namely a substantial receivership or controllership, a voluntary administration or a scheme of arrangement.

An ‘ipso facto’ clause enables a party to terminate a contract or exercise other rights by virtue of the fact the other party becomes insolvent or subject to an insolvency process. An example in a typical facility agreement would be an event of default triggered by the appointment of a receiver to all of the borrower’s assets. The new stay on the enforcement of ipso facto clauses is intended to give companies the space to recover from insolvency without the threat of major contracts being terminated. A party will not be able to enforce an ipso facto clause if the reason for doing so is because (a) the company has entered into the relevant insolvency procedure (b) the company’s financial procedure during the procedure (c) a reason prescribed by regulations or (d) a reason that, in substance, is contrary to the stay (this being an anti-avoidance measure). The stay also extends to rights that arise automatically without a party taking action (known as ‘self-executing’ rights).

There are a number of exceptions and carve-outs. Most relevantly, it does not apply to (a) syndicated loans or bonds, (b) variations to contracts made prior to 1 July 2018, (c) enforcement by a secured creditor holding security over the whole or substantially the whole of the company’s assets (d) enforcement against guarantors and third party security providers (e) drawstops under a facility agreement, meaning that the lender is not obliged to advance new monies (f) arrangements entered into during the relevant procedure and (g) a right exercised with the consent of the court or the administrator, scheme administrator, liquidator or other relevant officer.

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Financial regulation

Law and regulation

What are the main laws and regulations that apply to entities that are involved in finance and investments generally?

Generally

Australian Securities and Investments Commission Act 2001 (Cth)
Australian Securities Exchange Listing Rules
Australian Prudential Regulation Authority Act 1998 (Cth)
Banking Act 1959 (Cth)
Banking Code of Practice
Competition and Consumer Act 2010 (Cth)
Corporations Act 2001 (Cth)
Customer Owned Banking Code of Practice
ePayments Code
Financial Sector (Collection of Data) Act 2001 (Cth)
Financial Sector (Shareholdings) Act 1998 (Cth)
Financial Sector (Transfer and Restructure) Act 1999 9 (Cth)

Financial Services Reform Act 2001 (Cth)
Foreign Acquisitions and Takeovers Act 1975 (Cth)
Payment Systems (Regulation) Act 1998 (Cth)
Payment Systems and Netting Act 1998 (Cth)
Reserve Bank Act 1959 (Cth)

Consumer credit

Banking Code of Practice
Competition and Consumer Act 2010 (Cth)
National Consumer Credit Protection Act 2010 (Cth)

Mortgages and other security interests

Banking Code of Practice
National Consumer Credit Protection Act 2009 (Cth)
Personal Property Securities Act 009 (Cth)

Corporations

Corporations Act 2001 (Cth)
Superannuation Act 1976 (Cth)
Superannuation Industry (Supervision) Act 1993 (Cth)

Taxation

Income Tax Assessment Act 1997 (Cth)
Income Tax Assessment Act 1936 (Cth)
Income Tax Assessment Act 1953 (Cth)

Funds and platforms

Corporations Act 2001 (Cth)

Other key market legislation

Anti-Money Laundering and Counter-Terrorism Financing Act 2006 (Cth)
Privacy Act 1988 (Cth)

NB Reference to an Act refers to all regulations under that Act.

Last modified 26 Feb 2020

Regulatory authorization

Who are the regulators?

Regulation of the financial services sector is split between the Reserve Bank of Australia (RBA), the Australian Prudential and Regulation Authority (APRA) and the Australian Securities and Investments Commission (ASIC).

The RBA is Australia's central bank and responsible for the overall stability of financial markets and monetary policy.

APRA has the responsibility of supervising Australia's Authorized Deposit Taking Institutions (ADIs), with the primary task to ensure that organizations in the banking and financial services sector manage their risk appropriately.

ASIC has responsibility for the supervision of operators of financial markets, clearing and settlement facilities, and market participants. It advises the Australian government on licensee operating rules as well as on new market and clearing and settlement facility operators. ASIC's other main role is to regulate consumer protection in the financial sector.

Other regulators to note are:

- the Australian Transaction Reports and Analysis Centre (Austrac); and
- the Australian Competition and Consumer Commission (ACCC).

Austrac is the regulator and specialist financial intelligence unit responsible for regulation of anti-money laundering and counter-terrorism financing.

The ACCC is the national agency responsible for enforcing the Competition and Consumer Act 2010 (Cth)(CCA), Australia's key legislation in respect of trade practices. The ACCC regulates anti-competitive and unfair market practices, mergers or acquisitions of companies, consumer protection (including product safety) and third-party access to facilities of national significance.

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What are the authorization requirements and process?

Australian Financial Services (AFS)

If an entity wishes to carry on a financial services business, it will have to apply to the ASIC for an AFS license or have the benefit of an exemption. Financial services include advice and dealing in respect of financial products such as investment products, non-cash payment facilities and arrangements for the management of financial risk.

To apply for a license, the entity is required to lodge an application form and a suite of proof documents (i.e. business descriptions, organizational structures, people proofs and financial statements). In some cases, ASIC may require additional information, and request the entity lodge further proof documents or answer specific questions in relation to the documents submitted with ASIC.

When evaluating an application for an AFS License, ASIC will assess if the entity:

- is competent to carry on the type of financial services indicated in the application;
- has sufficient resources to carry on the business; and
- can meet the obligations of an AFS licensee (i.e. training, compliance, insurance and dispute resolution).

The application fee depends on the type of application application and, as at December 2019, ranges from AUD899 (i.e. paper lodgement for a request to cancel a body corporate AFS license), AUD3,721 (i.e. online application for a body corporate AFS license for retail clients and low complexity products) to AUD11,305 (i.e. paper lodgement for a body corporate AFS license for retail clients and high complexity products).

The application process takes around five to eight months in total, depending on the type of application lodged.

Firms which hold AFS Licenses are listed on the ASIC register.

Australian Prudential and Regulation Authority

If an entity wishes to carry on a banking business in Australia it is required to be authorized by APRA as an 'authorized deposit-taking institution' (ADI) or have the benefit of an exemption.

To apply for authorization, the applicant must:

- engage in a preliminary consultation with APRA to discuss the applicant's intention to engage in banking business in Australia;
- lodge an application and required documentation with APRA; and
- arrange meeting(s) with APRA to complete an onsite review.

The application fee depends on the type of application and ranges from AUD30,000 to AUD80,000.

The time required to process an application is dependent on the nature of the application and the supporting documents required to be provided to APRA. APRA states that generally the overall licensing process could take from three to twelve months.

Institutions classified as ADIs are listed on the APRA website.

Engagement with APRA prior to an application being made is recommended.

Credit

Credit providers and intermediaries require an Australian Credit License to provide credit or financial broking services (unless they are exempt). The credit licensing system is based on the AFS licensing concepts and requirements as ASIC is now the national regulator for consumer credit and finance broking.

To apply for a license, the entity will be required to lodge an application, answer questions in relation to proposed credit activities, provide supporting documents regarding employees and operations and provide a declaration the entity will comply with set obligations if granted a credit license.

To be granted a credit license, you will need to be able to comply with the general conduct obligations under the National Consumer Credit Protection Act 2009 (Cth), and be a 'fit and proper' person to engage in credit activities.

The application fee is determined by reference to a calculation method prescribed in the relevant regulatory guide and information sheets published by ASIC, and the relevant tiered scale. Depending on the calculation and scale, the application fee can range AUD450 to AUD26,250.

ASIC aims to decide whether to grant a credit licence within 60 days. However, the the time required to process an application is dependent on the nature of the application, and the supporting documents required to be provided to ASIC.

Australian Transaction Reports and Analysis Centre

The Anti-Money Laundering and Counter-Terrorism Financing Act 2006 (Cth) imposes legal obligations on certain financial services providers, including the obligation to register with the Austrac if providing designated services, such as deposit-taking, currency exchange, loan, life insurance, securities and derivatives market services.

To register an entity with Austrac, the entity must complete and lodge an Austrac business profile form.

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What are the main ongoing compliance requirements?

Australian Financial Services (AFS)

AFS Licenses carry a range of financial solvency and risk management requirements. Current general obligations include, but are not limited to:

- ensuring the financial services covered by the license are provided honestly and fairly;
- ensuring adequate arrangements are in place for managing conflicts of interests;
- complying with financial services laws and conditions of the license;
- employing adequate resources (e.g. financial, technological and human resources) to carry out the services covered by the license;
- maintaining the skills and competence to provide the financial services covered by the license;
- employing a dispute resolution and risk management system; and
- ensuring employees are adequately trained and competent to provide the financial services.

The time and resources required for a new license and to maintain ongoing compliance with an AFS License can be significant depending on the required AFS License authorizations. Some of the more time-consuming requirements concern the preparation of licensing proofs on topics such as risk management, compliance, information technology processes and capabilities.

AFS licensees are required to notify ASIC of any 'significant' breach (or likely breach) of their obligations or financial services laws as soon as practically possible, and in any event within ten business days of becoming aware of the significant breach (or likely breach). Failure to report a significant breach is an offence and may result in penalties.

Australian Prudential and Regulation Authority

APRA requires all ADIs to comply with its prudential requirements relating to governance, audit, risk management and capital adequacy from the commencement of their banking operations.

APRA's current prudential requirements include but are not limited to:

- maintaining sufficient capital adequacy (namely the prudential capital ratio (PCR));
- ensuring substantial shareholders are 'fit and proper' in the sense that they are financially sound;
- ensuring persons who hold key positions within the ADI are 'fit and proper';
- providing evidence of adequate risk management and internal control systems, business continuity management and information security standards;
- providing evidence of adequate compliance systems and processes;
- employing accounting systems that maintain secure, up-to-date records of all transactions and commitments undertaken by the ADI; and
- engaging in adequate internal and external audit procedures and arrangements.

If APRA authorizes an entity to be deemed an 'authorized deposit-taking institution' this does not automatically allow the ADI to refer to itself as a 'bank' unless special provision has been made. APRA will generally permit an ADI to refer to itself as a 'bank' in its trading name and advertising if the ADI holds at least AUD50 million in Tier 1 capital.

Depending on the nature of the breach, if an APRA-regulated institution becomes aware that it has breached (or will breach) a prudential requirement and that breach is 'significant', a breach of a prudential requirement must be reported immediately, or within 10 business days after the institution becomes aware a breach has occurred. Failure to report such a breach is an offence and may result in penalties.

A corporation may also be required to register with APRA as a registered financial corporation under the Financial Sector (Collection of Data) Act 2001 (Cth). In general, this Act applies to any corporation which engages in the provision of finance in the course of carrying on business in Australia. Provision of finance includes but is not limited to:

- the lending of money, with or without security;
- carrying out of activities, whether directly or indirectly, that result in the funding of originating loans or other financing;
- the supplying of goods by way of hire-purchase;
- purchase of debentures or other securities (other than shares) issued by a corporation; and
- acquisition of debts due to another person.

Intra-group financing activity between corporations that are related to one another does not constitute provision of finance.

There are some exemptions, including that this Act does not apply to corporations whose:

- sum of assets in Australia, consisting of debts due to the corporation resulting from transactions entered into in the course of the provision of finance by the corporation, does not exceed AUD50 million in aggregate value; and
- sum of the values of the principal amounts outstanding on loans or other financing, as entered into in a financial year, does not exceed AUD50 million in aggregate value.

Under this Act, APRA collects data from registered financial corporations. Corporations may be required to submit the appropriate forms on a monthly or quarterly basis, as confirmed by APRA upon registration.

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What are the penalties for failure to be authorized?

A person undertaking a regulated activity without being authorized, licensed or exempt, commits a criminal offence and may be liable to imprisonment.

For example, engaging in financial services without an Australian Financial Services license, attracts a criminal penalty under the Corporations Act 2001 (Cth) of five years' imprisonment, and, in the case of a body corporate, a maximum 6,000 penalty units (having a monetary value of AUD1.26 million). The court may also declare a maximum pecuniary civil penalty.

A person who engages in consumer credit activity without an Australian Credit License is, in the case of a body corporate, subject to a civil penalty of up to 5,000 penalty units (having a monetary value of AUD1.05 million) and a criminal penalty fine of up to AUD504,000, or in the case of an individual, two years' imprisonment.

If a corporation should be registered with APRA as a registrable financial corporation, and fails to provide APRA with the relevant documents within 60 days of becoming a corporation that should be registered with APRA, the corporation is subject to a fine of 50 penalty units (having a monetary value of AUD10,500) for every day that it does not comply with the reporting requirements.

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Regulated activities

What finance and investment activities require authorization?

Generally

To carry on banking business an entity must be authorized by APRA to be an ADI.

All financial activity requires regulatory authorization by ASIC when it is carried on by way of financial services or consumer credit business in Australia.

The following activities are likely to require authorization, if they have sufficient connection with Australia:

- providing financial services, such as advice and dealing in respect of financial products, investment products, non-cash payment facilities, arrangements for the management of financial risk, derivatives, shares and managed investment schemes;
- engaging in Australian financial securities activities, such as arranging and underwriting services in 'financial products' in the wholesale markets;
- providing deposit-taking services, such as accepting deposits; and
- engaging in consumer credit activities, relating to consumer leases, consumer credit contracts, credit assistance and securing payment obligations.

Financial Sector (Shareholdings) Act 1998

Acquisitions of shareholdings are covered by the Financial Sector (Shareholdings) Act 1998 (Cth) (FSSA). The FSSA restricts individual shareholdings in financial sector companies to a 20% stake. A financial sector companies is:

- an authorised deposit-taking institution; or
- an authorised insurance company; or
- a holding company of an authorised deposit-taking institution or an authorised insurance company.

The Treasurer may approve a higher percentage stake limit if it is in the national interest to do so or the person is a fit and proper person and the company is new or recently establish, with assets below a certain threshold amount.
If a person obtains practical control of the Australian company, as declared by the Treasurer, then steps will need to be taken to end the practical control.

Foreign Investment Policy

The Australian government's regulation of foreign investment has two main aspects. The first is the Foreign Acquisitions and Takeovers Act 1975 (Cth) (FATA) and the regulations made under FATA. The second consists of various ministerial statements and policy guidelines issued from time to time.

The Treasurer, assisted by the Foreign Investment Review Board (FIRB), administers this regulation. The Australian government has the power to block notifiable proposals determined to be contrary to the national interest or may impose conditions on an approval.

FIRB is a non-statutory body to advise the Treasurer and the Australian government on Australia's foreign investment policy and its administration. FIRB examines foreign investment proposals and advises the Treasurer whether or not they comply with the policy. It also generally advises the Australian government on foreign investment matters and can assist foreign investors to ensure their proposals (and their associates) confirm with government policy.

For business acquisitions, foreign persons should obtain approval for the acquisition of:

- a substantial interest in an Australian corporation or in an offshore company having Australian assets; or
- control of an Australian business, the value of which exceeds the prescribed limits.

A substantial interest exists if the foreign person (and any associates) has 20% or more or several foreign persons (and any associates) have 40% or more of the share capital or voting power in the corporation. Different thresholds apply for designated sectors such as agribusiness.

Foreign persons will require approval for the acquisition of interests in certain types of Australia real estate, depending on its value.

All foreign government investors must obtain approval before making a direct investment in Australia, starting a new business or acquiring interests in land regardless of the value of those acquisitions. Foreign government investors includes bodies politic, entities in which foreign governments or their agencies and related entities have an interest of 20% or more (or such entities from more than one foreign country having an aggregate interest of 40% or more) and entities that are controlled by foreign governments or their agencies or related entities.

Notification and approval of foreign investment will differ depending on the type of transaction and the type of investor (ie. private sector or foreign government investor). Applications are typically considered within 30 days and a further 10 days to notify the applicant, however this period may be extended, and in the case of the Treasurer making an interim order, by up to a further 90 days.

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Are there any possible exemptions?

ASIC, APRA and the ACCC have the power to grant a large variety of exemptions in relation to authorisation and licensing requirements.

ASIC may exempt an individual or entity from the requirement to hold an Australian Financial Services license under the Corporations Act 2001 (Cth). For example, product providers are not required to hold an Australian Financial Services (AFS) license when providing general financial product advice on their own products. It must be noted that when an individual or entity relies on this exemption they must disclose to the recipient that the provider does not hold an AFS license. There are a wide variety of other exemptions that may apply.

APRA has the power to grant exemptions to certain institutions (such as charitable, religious and other registered entities) to engage in 'banking business' without violating the Banking Act 1959 (Cth).

The ACCC may exempt an individual or entity from the requirement to hold a Credit License under the National Consumer Credit Protection Act 2009 (Cth). For example, a public body or authority constituted under legislation, is not required to hold a credit license for any credit activities they engage in.

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Do any exchange controls or other restrictions on payments apply?

Generally, banks are authorized to deal in foreign exchange and can operate foreign currency accounts. The RBA maintains general

oversight of dealers in the foreign exchange market and sets conditions and prudential standards, but does not impose general restrictions on the import and export of funds in and out of Australia.

The flow of currency into and out of Australia is monitored through a reporting system. Under this system, designated cash dealers and individuals are required to report significant transactions – those involving AUD10,000 (other the foreign currency equivalent) or more – to Austrac. This report is due within 10 business days after the date of the transaction.

The RBA's express approval may be required to complete some foreign exchange transactions that are real-time gross settlement (RTGS) systems (being RITS, Austraclear and CHESS) and multilateral netting arrangements. For example, the RBA has restricted foreign exchange transactions with governments and nationals of countries subject to United Nations sanctions.

There may also be anti-money laundering and tax considerations to take into account.

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What are the rules around financial promotions?

Chapter 7 of the Corporations Act 2001 (Cth) outlines various criteria which must be met when issuing promotional material relating to financial products and financial services. The Australian Securities and Investments Commission Act 2001 (Cth) also prescribes other requirements such as consumer protection provisions.

Any promotional material relating to financial products must not include the use of restricted titles, words or expressions unless strict criteria are met, or the scope of an Australian financial services license permits the provider to do so. For retail clients, advertising materials for financial products are often required to specify the issuer and seller of the product, and inform the client to consider the Product Disclosure Statement (PDS) when making a decision about the financial product.

In addition, tax promoter penalty laws prohibit the promotion of tax avoidance schemes and schemes implemented directly to the way it has been described in a tax product ruling approved by the ATO.

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Entity establishment

What types of legal entity are generally used to undertake financial or investment activity?

Generally

The type of legal entity used to undertake financial or investment activity in Australia will to a degree depend on the nature of that investment or activity.

COMPANIES

A company is a separate legal entity capable of holding assets and being sued in its own name. The most common types of companies are proprietary companies limited by shares (denoted by 'Proprietary Limited' or 'Pty Ltd' appearing at the end of the company's name) and public companies limited by shares (denoted by 'Limited' or 'Ltd').

A key advantage of undertaking financial or investment activity through a company limited by shares is that the liability of the shareholders for the company's liabilities is limited to the company's assets and unpaid share capital.

A public company may also be listed on the Australian Securities Exchange, subject to compliance with additional regulatory requirements that apply to listed entities.

PARTNERSHIPS

Partnerships involve two or more individuals or companies carrying on a business, generally pursuant to a partnership agreement. Most partnerships are limited to no more than 20 partners, unless the partnership applies to a particular profession (e.g. an accountancy

practice). A partnership is not a separate legal entity. Its partners are jointly and severally liable for the partnership's liabilities. In certain states limited liability partnerships can be registered with State regulatory authorities. An incorporated limited partnership is a special kind of limited partnership. Limited partnerships are far less common than ordinary partnerships.

JOINT VENTURES

A joint venture is usually a contractual arrangement entered into by two or more parties to carry out a specific commercial endeavour. A joint venture may be incorporated or unincorporated. An incorporated joint venture operates through a company, which is a separate legal entity. An unincorporated joint venture is a purely contractual arrangement between the joint venturers, and they will directly engage in the activities of the joint venture.

TRUSTS

A trust is an arrangement where one person, the trustee, holds property for the benefit of another person, the beneficiary. The trustee holds legal title to the property and must deal with the property for the benefit of the beneficiary. The trustee may be an individual or a company. The trustee is liable for any obligations it incurs as trustee, but it generally has a right to be indemnified out of the trust property.

Common types of trusts are discretionary trusts, unit trusts and bare trusts. The trustee of a discretionary trust may determine which of the beneficiaries are to receive distributions from the trust. The beneficiaries of a unit trust hold units in the trust and their respective entitlements to distributions from the trust isare determined by the number and class of units held. The trustee of a bare trust simply holds the property without having any active duties in relation to it, except to convey the property on demand to the beneficiaries or to deal with the property as they direct.

Funds

An Australian hedge or debt fund is usually structured as a unit trust and would ordinarily fall within the definition of a 'managed investment scheme' in the Corporations Act 2001 (Cth). That Act imposes a wide range of obligations and requirements on the operators of managed investment schemes. Managed investment schemes are regulated by the ASIC. Managed investment schemes may also qualify for tax concessions if they qualify as a "managed investment trust" under Australian tax laws.

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Is it possible to conduct lending or investment business through a branch or establishment?

Yes.

Foreign companies wishing to carry on business in Australia through a branch need to register as a foreign company with ASIC. To apply, a company must lodge an application form with ASIC, along with certified copies of the company's certificate of registration and constituent documents.

To be registered, the foreign company must have a registered office in Australia and a local agent to act on its behalf.

Registered foreign companies are required to lodge annual financial statements with ASIC and comply with certain notice obligations. The local agent will be responsible for acts, matters and things that the company is required to do under the Corporations Act 2001 (Cth) and may be held personally liable for any penalties imposed should a company contravene the Corporations Act 2001 (Cth).

Australia is in the process of transitioning to a new licensing framework for foreign financial service providers with Australian wholesale clients. ASIC has issued Consultation Paper 301: Foreign financial service providers (June 2018) and Consultation Paper 315: Foreign financial service providers: Further consultation (July 2019). The new regime is expected to commence on 1 April 2020, alongside transitional arrangements.

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FinTech

FinTech products and uses

What are the most common technology products and FinTech applications used or being developed in the finance and investment marketplace?

Peer-to-peer funding platforms and marketplace lending

Australia has seen substantial growth in active FinTech businesses in sectors such as lending (including peer-to-peer (P2P) and marketplace lending), personal and business finance and payment management. There is no strict definition for marketplace lending given the wide variety of entrants and financing techniques involved. The principal characteristics of new marketplace lenders, however, would include:

- operating from or through a non-bank lending platform established as a specialist corporate or special purpose vehicle (SPV) based structure;
- applying technology to leverage and optimize the lending platform and user experience; and
- connecting borrowers and lenders through the platform rather than applying funding arising from a wider deposit-based relationship.

Marketplace lending is available to address most forms of traditional bank funding products. Recently products have included:

- virtual credit cards;
- consumer loans;
- student lending products;
- small and medium-sized enterprises (SME) lending; and
- residential property and commercial property mortgage lending.

It is likely that the volume of lending in these product areas as well as further and additional product areas will significantly increase over the coming years, as financing becomes more readily available to support the marketplace lending sector.

HOW ARE MARKETPLACE LENDING PLATFORMS FUNDING THEMSELVES?

Marketplace lending includes P2P-type structures often operated through an electronic platform provider as well as crowdfunding and also direct-to-retail financing mechanisms. The increase in demand for credit through these marketplace platforms has also been appealing to larger pools of available capital, such as private equity and venture capital funds as well as institutional sponsors. Funding platforms will now often be backed by institutional finance in addition to, or increasingly rather than, individual investors on a traditional P2P basis.

ISSUES FOR START-UP MARKETPLACE LENDERS

Following the initial incorporation and start-up funding for a new marketplace lending business, there will be a need to establish funding lines which can accommodate growth of the ongoing lending activities of the platform. As the start-up lender will not have an established track record, deposit base or asset pools, the funding structure will often follow the format of a warehouse securitization structure. Origination of new assets will be funded through drawings on a note issuance facility backed by security over the new assets. Each of the new assets will be subject to eligibility criteria determined by reference to the nature of the underlying asset. In order to provide an efficient financing structure, the assets will typically be held through an SPV with origination and servicing provided by the marketplace lender. In order to cover expected losses on the asset pool, the senior facility will be subject to the lending platform maintaining sufficient subordinated capital in the form of equity, or a combination of equity and subordinated debt.

Blockchain, smart contracts and cryptocurrencies

WHAT IS BLOCKCHAIN?

Blockchain provides a new approach to holding and authenticating data. It is a database operating through distributed ledger technology in which data is recorded on computers, by way of a P2P mechanism, based on pre-agreed consensus algorithms in the applicable

participating network. It is a form of database where data is stored in the chain in either fixed structures called 'blocks' or algorithm functions called 'hashes'.

Each block includes unique features such as its unique block reference number, the time the block was created and a link back to the previous block. Each block is reviewed by a number of nodes and the block is only added to the database if the node reaches consensus that the block only contains valid transactions. Content includes digital assets and instructions which reflect the transactions and parties to those transactions. The ability to track previous blocks in the chain makes it possible to identify transactions back to the first ever transaction completed, enabling parties to verify and establish the authenticity of the assets in the latest block. This makes blockchain exceptionally accurate and secure.

Specialist users on the system apply advanced computing software to identify time stamped blocks, verify the accuracy of the block using sophisticated algorithms and add the verified block to the chain. As the number of participants increases, the replication of the data over a wider base makes it harder for any person to alter the data in the chain. Any attempted addition or modification to the information on a block needs to be approved by all users in the network and verification of any block can only happen through a 'proof of work' process.

As a result, the data is identified and authenticated in near real-time, providing a permanent and incorruptible database sufficiently robust to operate as a store of value (e.g. in the case of cryptocurrencies such as bitcoin) or providing an indisputable record for example relating to securities transfer.

Blockchain is a decentralized system, created and maintained by users of the network rather than being dependent on any central or third party intermediary. It may be public and open ('permissionless' or 'unpermissioned') or structured within a private group ('permissioned').

Permissionless blockchains include bitcoin and ethereum, in which anyone can set up a node that once authorized, can validate, observe and submit transactions. The identities of the participants are not known (other than the unique and random identities known as an 'address'). Permissioned ledgers restrict participation in the network and only the specific participants are given access and are known within the network. The network is private, and only organizations that have been authorized can participate and view transactions.

WHAT ARE SMART CONTRACTS AND DECENTRALIZED AUTONOMOUS ORGANIZATIONS (DAOS)?

Developments in blockchain are also providing an ability to transfer and rely on instructions verified within the electronic system in the form of so called 'smart contracts'. These contracts have been converted into code and are then executed and enforced by the blockchain network on the occurrence of an event. This reduces the need for intermediaries to collect, store and act on communicated information.

Smart contracts are essentially pre-written computer codes which are stored and replicated on distributed ledger platforms such as blockchain. Execution takes place over the network, eliminating the need for intermediary parties to confirm the transaction, leading to self-executing contractual provisions. These contracts can be as simple as moving a balance from one account to another or advanced, more-complex interactions with the outside world using so called 'Oracles'. With Oracles, the contract code consults with a service outside of the blockchain network to make a decision. This may entail receiving a confirmation that an event has occurred, such as payment, which automatically executes a further step in the contract, such as the transfer of an asset, which might be in digital form or by delivering instructions to a person or warehouse to release the asset for delivery.

DAOs are essentially online, digital entities that operate through the implementation of pre-coded rules. These entities often need minimal to zero input into their operation and they are used to execute smart contracts, recording activity on the blockchain. DAOs can be particularly challenging to regulate depending on: their software engine, the nature of transactions they are completing or other unique features. Questions of ownership and responsibility for resulting acts of DAOs can also be brought to question if any technical issues arise with their operation.

WHAT IS A CRYPTOCURRENCY?

The European Central Bank definition of a cryptocurrency is that it is a digital representation of value that is neither issued by a central bank or public authority nor necessarily attached to a fiat currency, but is issued by natural or legal persons as a means of exchange and can be transferred, shared or traded economically. The oldest and best-known cryptocurrency is bitcoin (itself based on the bitcoin platform) although many other cryptocurrencies now exist. For example, the most widely-known alternatives to bitcoin include ether based on the ethereum platform and litecoin (these cryptocurrencies are now actively traded with a large developing infrastructure for holding, pricing and exchanging currency).

The ATO has published guidance setting out its views that trading cryptocurrencies are generally subject to Australia’s capital gains tax and the use of cryptocurrencies in businesses may give rise to Australian goods and services tax implications.

Initial coin offerings and token-based products

WHAT IS AN INITIAL COIN OFFERING (ICO)?

ICOs are a form of digital currency or token using blockchain technology. ICOs are often a means by which funds are raised for a new blockchain or cryptocurrency venture (the market for ICOs is currently booming). ICOs come in a wide variety of forms and may be used for a wide range of purposes. Some forms of ICOs may be directed at customers or suppliers as a form of loyalty program or a form of access or purchasing power (preferential or otherwise) in respect of assets of the issuer's business. Other forms may be more focused on raising initial funding. It is essential to examine the legal and regulatory basis for any ICO as an unauthorized offering of securities is illegal and may result in criminal sanctions in a number of jurisdictions. Legal analysis of the underlying token will determine if it should be treated as a specified investment or form of regulated security or is more appropriately a form of asset that is not itself subject to the regulatory regime.

Typical attributes provided by tokens will include:

- access to the assets or features of a particular project;
- the ability to earn rewards for various forms of participation on the platform; and
- prospective return on the investment.

Key aspects to consider will include the:

- availability and limitations on the total amount of the tokens;
- decision-making process in relation to the rules or ability to change the rules of the scheme;
- nature of the project to which the tokens relate;
- technical milestones applicable to the project;
- basis and security of underlying technology;
- amount of coin or token that is reserved or available to the issuer and its sponsors and the basis of existing rights;
- quality and experience of management; and
- compliance with law and all regulatory requirements.

The nature of the business and the purpose and structure of the token offering will typically be set out in a white paper available to potential purchasers.

Artificial intelligence and robo advisory systems

Automated financial advice tools, also known as 'robo advisors' are software tools driven by artificial intelligence (AI) that provide a variety of investment advice services, from portfolio selection to personal finance planning. The systems are generally operated on a platform/personal dashboard basis; a user can input a set of personalized data to be processed by the AI algorithms which produce optimized outcomes around specified parameters. Although generally of application in the asset management sector, AI and automated advice tools also impact in the banking and private wealth advisor sectors; the implications include decreased human involvement, although recent trends have included a growth in popularity of hybrid structures which combine AI and human inputs.

Data analysis and cloud computing

Cloud computing enables delivery of IT services through internet-based tools and applications, rather than direct connection to a physical server. Cloud-based storage makes it possible to save masses of data to remote servers, accessible through the internet rather than by way of a physical connection. With the vast data processing and storage capabilities offered by cloud computing technology and virtually no infrastructure barriers to entry, there are a number of applications in building and running FinTech businesses and the technology has had a significant impact in recent years.

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Are there any restrictions, specific laws, regulations or procedures that apply to FinTech products?

General financial regulatory regime

ASIC is the financial services regulator in Australia.

GENERAL

To conduct a financial services business in Australia, businesses must hold an AFSL issued by the ASIC. Most FinTech services are captured in the definition of financial services and financial products in the Corporations Act 2001 (Cth) and unless an exemption applies, FinTech companies will require an AFSL. There are limited statutory exemptions available to foreign entities who conduct financial services in Australia.

Additionally, an Australian credit license (ACL) issued by ASIC is required for a business engaging in consumer credit activities in Australia which are captured in the National Consumer Credit Protection Act 2009 (Cth), unless an ASIC exemption applies.

NATIONAL INNOVATION AND SCIENCE AGENDA

In December 2015, the Australian Government introduced the National Innovation and Science Agenda (NISA) to facilitate the development of FinTech. NISA, among other things:

- encourages investment in FinTech companies through tax incentives for early-stage investment;
- enables crowdsourced equity funding of public companies (described further below); and
- establishes the FinTech Advisory Group to advise the Treasurer and the ASIC Innovation Hub.

The ASIC Innovation Hub assists FinTech startup companies to navigate the Australian financial regulatory system by engaging with FinTech businesses and providing information to streamline the licensing process.

Electronic payments platforms and regulation of peer-to-peer lenders

ELECTRONIC PAYMENT PLATFORMS

The New Payments Platform (NPP) is an industry initiative to develop a new national infrastructure for fast, versatile, data-rich payments in Australia between financial institutions and their customers. The NPP will connect to all financial institutions and, as a result, to businesses and consumers, allowing funds to be accessible almost immediately upon receipt of a payment.

PEER-TO-PEER LENDERS

Peer-to-peer lending involves a financial service provider (the lending platform) acting as the intermediary between investors and borrowers. Lending platforms are generally set up as managed investment schemes, meaning the platform operator must have an AFSL that allows them to run the scheme. Accordingly, these transactions will be caught by the Corporations Act 2001 (Cth) and must comply with the regulatory regime.

Where the borrower is an individual and not a business, the loan will be a consumer credit contract and the platform operator will be required to comply with the National Consumer Credit Protection Act 2009 (Cth), in addition to holding an AFSL.

Regulation of payment services

THE RESERVE BANK OF AUSTRALIA

RBA is responsible for the designation and regulation of systems facilitating the transfer of funds in Australia under the Payment Systems (Regulation) Act 1998 (Cth) and the Payment Systems and Netting Act 1998 (Cth). The RBA has established the Payment Systems Board to take responsibility for the payments system policy. The powers of the RBA include designating a payment system as being subject to regulation, imposing an access regime to establish rules of participation in a payment system and setting standards for payment systems to promote safety and efficiency.

To this end, the RBA has established a number of standards for compliance and access regimes applicable to participants in payment systems.

EPAYMENTS CODE

Consumer electronic payment transactions in Australia are regulated by the ePayments Code, administered by ASIC. The ePayments Code applies to voluntary subscribers, including banks, credit unions and building societies.

The Code, among other things:

- requires subscribers to give consumers clear and unambiguous terms and conditions;
- stipulates how terms and conditions changes (such as fee increases), receipts and statements need to be made;
- sets out the rules for determining who pays for unauthorized transactions; and
- establishes a regime for recovering mistaken internet payments.

Application of data protection and consumer laws

The Privacy Act 1988 (Cth) regulates the use of personal data within Australia. Where a FinTech business provides credit or handles information relevant to credit, the Privacy Act will apply. The Australian Privacy Principles that are set out in the Privacy Act outline the obligations on the collection, use, disclosure and management of personal information. Where a business undertakes an act outside Australia and there is some link to an Australian citizen or organization, or where it carries out business in Australia, the Privacy Act will apply.

The Office of the Australian Information Commissioner (OAIC) is the body responsible for administering the Privacy Act and has the power to investigate non-compliance.

Money laundering regulations

The Anti-money Laundering and Counter-terrorism Financing Act 2006 (Cth) establishes a regime to target and deter money laundering and terrorism financing in designated services. Where a FinTech company provides a designated financial service, such as lending or issuing or selling interests in managed investment schemes, they will become a reporting entity and have obligations under the Anti-money Laundering and Counter-terrorism Financing Act 2006 (Cth). These obligations include compliance reporting and conducting due diligence on customers prior to engaging in any financial services.

Licensing exemption for FinTech testing

ASIC has implemented a FinTech licensing exemption, to facilitate the testing of new FinTech services before requiring a business or start-up to obtain an AFSL or ACL. Based on the regulatory guide published by ASIC, allowing FinTech businesses to test their new products and services before they obtain a license can help alleviate the barriers to innovation (including access to capital and speed to market) by:

- allowing concepts to be validated and refined before businesses spend the time and money associated with obtaining a license; and
- providing increased opportunities for businesses to obtain investment that may assist with meeting the costs of complying with the law.

Three components are necessary in this regard:

- existing flexibility in the regulatory framework or exemptions provided by the law which means that a license is not required;
- tailored, individual licensing exemptions granted by the ASIC to a particular business to facilitate product or service testing (individual exemptions of this nature are similar to the regulatory sandbox frameworks established by financial services regulators in other jurisdictions); and
- ASIC's 'FinTech licensing exemption' – provided under ASIC Corporations (Concept Validation Licensing Exemption) Instrument 2016/1175 and ASIC Credit (Concept Validation Licensing Exemption) Instrument 2016/1176, which apply to certain products or

services (FinTech Exemption).

Under the FinTech exemption, a business may, without needing to hold an AFSL, give financial product advice in relation to (or deal in) the following products:

- listed or quoted Australian securities;
- debentures, stocks or bonds issued or proposed to be issued by the Australian Government;
- simple managed investment schemes;
- deposit products;
- some kinds of general insurance products; and
- payment products issued by Australian banks.

Initial Coin Offerings

The ASIC is due to release guidelines in relation to Initial Coin Offerings (ICOs) (which have not been released to date). It is expected that the ASIC will follow the lead of the US, Canada and Hong Kong regulators by including the fundraising method within the regulatory framework governing Initial Public Offerings. The ASIC is reportedly working with advocates in the startup community (including FinTech Australia), to develop guidelines although it is expected that the ASIC may take the view that many of the 'tokens' currently being issued through ICOs would fall within ASIC definitions of 'securities'.

Crowdfunding in Australia

Australia's previous regulatory requirements generally created a barrier to widespread use of crowdsourced equity funding. However changes are underway to make it easier and less expensive for businesses, including start-ups, to raise equity from the general public up to A$5 million in any 12-month period, while ensuring adequate investor protection. However, the Australian Parliament has enacted the Corporations Amendment (Crowd-sourced Funding) Act 2017 (Cth), which will allow eligible Australian businesses (including start-ups) to access crowdsourced equity investments through a licensed online portal.

For companies to access the benefits of the new crowdsourced funding regime, providers of crowdsourced funding services must hold an AFSL issued by ASIC. ASIC accepts applications from potential crowdsourced funding intermediaries for AFSL authorizations to provide crowdfunding services.

The following general restrictions apply:

- Individuals seeking to invest using a crowdsourced funding platform can contribute up to AUD10,000 per year, per company.
- Crowdsourced funding will also be available to Australian public companies with turnover/gross assets less than AUD25 million.
- Proprietary companies will be subject to additional governance and reporting requirements (including the provision of annual financial reports to shareholders).

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What type of funding arrangements and incentives are available to FinTech businesses?

Early stage

SEED INVESTMENT

Initial investment in FinTech businesses may be provided by family and friends of the founders and other high-net-worth individuals (often known as business angels) in return for an equity stake. Such seed investment is often used to fund the establishment and early growth of the business before larger investment is available. The investing individuals may also provide know-how and expertise to assist in the company's development. The seed investors would typically not require the same controls over the business as, for example, venture capital providers.

CROWDFUNDING

The crowdfunding sector is well established, and may be appropriate for a FinTech business in the early stages. It involves members of the public investing in a business by pooling their resources through an intermediary platform, such as Equitise and Pozible. Significant changes have recently been made in the Australian regulatory landscape to make crowdfunding more accessible. (For further information, please see FinTech products and uses – particular rules.)

There are two main types of crowdfunding: equity and reward-based.

- Equity crowdfunding involves company shares being given in exchange for investment in the business.
- Reward-based crowdfunding provides investors with a tangible benefit, such as early access to a platform or application that the business is developing.

Crowdfunding offers a large number of private investors an opportunity to make small-scale investments in early-stage businesses to which they may otherwise not have had access.

ACCELERATORS

There are various incubators or accelerators in the Australia market which offer support, facilities and funding for startups, often in return for an equity stake.

Venture capital and debt

Venture capital (VC) funding is a type of equity investment usually targeted at early-stage FinTech companies with an established business and some trading history. VC provides a viable alternative to traditional lending, given that the business is unlikely to have the tangible asset base or long track record needed to attract traditional debt funding from financial institutions. Australian VC funds include Blackbird Ventures, Carthona Capital, Our Innovation Fund and Squarepeg Capital.

Corporate venture capital (CVC) is a type of VC and involves an equity investment by a corporate fund, examples of which includes Reinventure, NAB Ventures and Telstra Ventures. The benefit of having a CVC as an investor for a FinTech start-up is that the fund is able to share its knowledge and expertise of the FinTech sector with the company and act as an advisor.

An additional funding option is venture debt, which is typically structured as a three-year term loan (or series of loans), which is secured against a company's assets and includes an equity element (i.e. a warrant) allowing the debt provider to purchase shares in the company. However, venture debt providers will usually only invest into companies that have already received investment through VC. At the time of writing, venture debt is increasingly a source of funding in the Australian market with about 5 regular providers of venture debt locally. However, the venture debt industry is still nascent as compared to the United States.

Warehouse and platform funding

Warehouse financing may be suitable for FinTech companies which own a portfolio of assets. Funding is often provided by way of a loan from a small number of lenders to an SPV. The loan is secured on the assets acquired by the SPV from the originator. The lenders will only fund a portion of the assets, with the remainder being financed by way of subordinated lending from the originator.

One recent example of warehouse financing involves Zip Money Limited, a listed Australian non-bank consumer financier, which involved a two-year asset-backed securitization warehouse in relation to its consumer receivables loan book.

Senior bank debt and capital markets funding

SENIOR BANK DEBT

Once a FinTech company is established and has a track record, bank debt becomes a more viable source of funding, either on a secured or unsecured basis depending on the creditworthiness and asset base of the business. In contrast to capital markets funding which is often covenant-lite, bank funding will generally involve the imposition of financial covenants and controls that will apply over the life of the facility. Bank finance may be particularly important for working capital, overdraft, accounts management and general liquidity purposes.

CAPITAL MARKETS FUNDING

Australia has both debt and equity capital markets which are accessible to businesses (usually of a certain size).

Raising finance by way of an Initial Public Offering (IPO) is a popular funding arrangement for FinTech companies that have grown to a certain size. An IPO is the initial sale of company shares on a public exchange, such as the Australian Securities Exchange.

CONVERTIBLE BONDS/LOAN NOTES

A popular funding tool for fast-growing FinTech businesses is to issue convertible bonds or loan notes which are essentially a hybrid between debt and equity. Convertible instruments begin as a loan accruing interest and are convertible into shares in the issuing company at prescribed prices in certain circumstances.

Initial Coin Offerings

An Initial Coin Offering (ICO) is an alternative to a share market IPO, crowdfunding or venture capital funding round for a startup with a blockchain-based platform or project. A startup looking to undertake an ICO will first produce a 'white paper' and then market itself to potential investors, much in the same way as a company undertaking an IPO.

ICOs are not common in Australia however there is a growing demand for this method of fundraising in Australia, particularly for startups with blockchain-based platforms that are looking to raise money fast.

In late 2017, Perth-based blockchain energy start-up Power Ledger become the first Australian company to undertake an ICO – raising AUD17 million in three days.

It is likely that, in most circumstances, Australian ICOs will involve the issue of securities and therefore fall under existing regulations for the offer of securities. This means ICOs will be subject to the same reporting obligations and regulations as an IPO.

Incentives and reliefs

INCENTIVES FOR EARLY STAGE INNOVATION START UPS

Incentives are available for startups (known as 'Early Stage Innovation Companies') which:

- are less than three years' old;
- have income less than AUD200,000 and expenses less than AUD1 million; and
- have businesses that are eligible (meaning that they have scalability, potential for growth and are undertaking research and development (R&D)).

Investments (less than 30% of the equity in an Early Stage Innovation Company) would generally qualify for a 20% non-refundable tax offset (capped at AUD200,000 per investor) and a ten-year exemption to capital gains tax.

ELIGIBLE VENTURE CAPITAL LIMITED PARTNERSHIPS

Investment funds investing into FinTech growth companies may be structured as venture capital limited partnerships (VCLPs) or early stage venture capital limited partnerships (ESVCLPs) to receive favorable tax treatment for the funds limited partners and with regard to carried interest payable to the funds general partner. For VCLPs, benefits include tax exemptions for foreign investors (eligible foreign limited partners) from capital gains tax on their share of any profits made by the partnership. For ESVCLPs, an income tax exemption applies to both resident and non-resident investors, plus a 10% non-refundable tax offset is available for new capital invested.

FINTECH INCENTIVES

The R&D Tax Incentive program is available for entities incurring eligible expenditure on R&D activities, including certain software R&D activities commonly conducted by FinTech/tech-growth companies. Claimants under the R&D Tax Incentive may be eligible for:

- **small businesses (< AUD20 million aggregated turnover)** – 43.5% refundable tax offset of the first AUD100 million of eligible R&D expenditure; and
- **other businesses** – a 38.5% non-refundable tax offset.

Generally, eligible R&D activities include experimental activities whose outcome cannot be known in advance and are undertaken for the purposes of acquiring new knowledge (known as 'core R&D activities'), and supporting activities directly related to core R&D activities (known as 'supporting R&D activities').

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Portfolio sales

Loan transfers and portfolio sales

What are common ways of buying and selling loans?

Buying and selling loans is very common in Australia.

A loan may be sold on an individual basis or packaged up with other loans and sold as a portfolio pursuant to overarching terms.

The most common ways of selling loans are novation, assignment and sub-participation, as described below.

NOVATION

A novation is a full legal transfer of the party's rights and obligations. It is a tripartite arrangement between the existing parties and the transferee. It results in a fresh contract being formed between the continuing party and the transferee, with the transferor being released from its obligations.

Assignment

An assignment is a transfer of rights only, not obligations. Subject to any contractual restrictions, an assignment may occur without the debtor's consent. An assignment may be effected as either an equitable assignment or legal assignment, depending on whether certain statutory requirements have been satisfied.

Sub-participation

A sub-participation is a transfer of the economic interest in a loan without the legal relationship between the existing parties changing. Sub-participations involve the buyer taking on double credit risk, on both the borrower and the seller.

TRANSFER MECHANICS

The facility agreement and the security trust deed will usually include transfer mechanics. These will specify the way in which the rights and obligations of an existing lender are novated or assigned to a transferee lender and any conditions that may apply, such as consents or restrictions on the nature of the transferee. The loan transfer itself is commonly based on the Loan Market Association recommended form documents made available by the Asia Pacific Loan Market Association. For more complex transactions, a more bespoke form of sale and purchase agreement will usually be used. The form and content of the transfer documentation will depend on the nature of the loan assets being sold.

Where security interests are transferred, registration may be required either on the Personal Property Securities Register or elsewhere (depending on the nature of the asset).

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What are the main considerations when transferring a loan and related security?

There are a number of issues to consider before transferring a loan or portfolio of loans. These issues are often considered in the due diligence undertaken by the seller's legal advisors. Some of the key issues are:

- **Confidentiality:** whether the seller of the loan is allowed to disclose information relating to the loan to a potential purchaser;
- **Data protection:** whether there is any personal data or other restricted information in the loan that should not be disclosed to a potential purchaser (in particular, the Privacy Act 1988 (Cth) and the National Credit Code should be considered);

- **Lender eligibility** – whether there are any restrictions considering the type of entity to which the loan may be transferred;
- **Undrawn commitments:** whether there are any continuing obligations for further funding or other material obligations of the lender that may bind the transferee or reduce claims made by the transferee;
- **Transfer mechanics:** whether there are any steps that need to be taken to transfer the loan in accordance with its terms;
- **Consent:** whether a transfer requires the consent of, or notification to, any other parties; and
- **Voidable transactions:** if the seller is insolvent, whether certain transactions may be declared voidable under the Corporations Act 2001 (Cth).

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Projects

Financing / investing in energy / infrastructure

To what extent are energy and infrastructure assets publicly or privately owned?

Generally

The ownership of energy and infrastructure assets in Australia varies according to the asset class. The main asset classes are usually considered to be:

- social infrastructure assets including:
  - health (hospitals and medical centers);
  - education (schools, childcare and universities);
  - social accommodation (social housing and retirement villages); and
  - community (court houses, fire stations and prisons); and
- economic infrastructure assets, including:
  - regulated utilities such as water companies;
  - transport assets such as roads and airports; and
  - telecommunication assets such as mobile phone towers.

Key sectors are considered below.

Energy

The gas and electricity industries in Australia are regulated by the states and territories.

ELECTRICITY

There is a mix of both government-owned and privately owned electricity distribution and retail businesses in Australia, with a trend towards privately owned utilities in all states and territories.

The majority of states and territories have combined to form an interconnected National Electricity Market (NEM), being Queensland (QLD), New South Wales (NSW), the Australian Capital Territory (ACT), Victoria (VIC), South Australia (SA) and Tasmania (TAS). The NEM is a wholesale electricity market for the supply and purchase of electricity across those interconnected states and territories and it is currently under construction with anticipated completion in 2021. Western Australia (WA) and the Northern Territory (NT) do not participate in the NEM and have their own major networks. The Australian Energy Market Operator (AEMO), an independent corporate body established by the Australian government, administers and operates the NEM.

There is only one major electricity transmission and distribution network in each of the ACT, SA and TAS. While there are multiple networks in QLD, NSW and VIC, each is a monopoly provider in a particular area. For example, Ausgrid, Endeavour Energy and Essential Energy operate monopolies in NSW. The distribution and transmission sectors are not generally integrated, although there is some common ownership in the distribution and retailing sectors in TAS and the ACT.

GAS

AEMO operates the wholesale and retail gas markets of eastern and southern Australia and oversees the gas transmission network in VIC.

In addition, AEMO is responsible for national transmission planning and the operation of the Short-Term Trading Market (STTM) for gas. The STTM is a market-based wholesale gas balancing mechanism that has been established at defined gas hubs in NSW, QLD and SA. The STTM facilitates the short-term trading of gas between pipeline owners/operators, shippers and gas producers. VIC does not participate in the STTM, and has established its own wholesale gas market which producers, transporters, retailers and end users all engage in.

Telecoms infrastructure

The telecommunications networks (fixed and mobile) in Australia are predominantly privately owned by a number of service providers.

Telstra, a wholly privatized company offering a full range of telecom services, is Australia's largest telecommunications provider and dominates ownership of the fixed-line network. Control of the wireless telecommunications sector is predominantly shared between three privately owned service providers, Telstra, Optus and Vodafone.

The Commonwealth Government is currently investing in fiber-optic, fixed wireless and satellite infrastructure to develop, construct and deliver Australia's first national wholesale only, open access broadband network (the National Broadband Network, or NBN) through a government-owned entity which is classed as a government business enterprise, NBN Co Limited. The new infrastructure will replace the existing broadband infrastructure, aiming to create quicker and more consistent broadband service and provide opportunities for development of improved asset management systems. The regulatory framework for the NBN provides that the Australian Government will retain full ownership of NBN Co until the national broadband network rollout is complete, which is anticipated to be in 2021.

Transport infrastructure

Public transport networks in Australia are predominantly government-owned and operated, across the three levels of government – federal, state and local, with certain exceptions where networks have been franchised, privatized or governments have entered into public-private partnerships.

RAIL

Typically, the infrastructure and assets for rail networks in Australia are owned by state governments or the federal government. The operation of trains in Australia is commonly franchised by the government and outsourced to the private sector. The passenger networks in each state and territory are typically owned by government entities. The railway infrastructure in QLD, TAS, VIC (for non-interstate lines), SA (for non-interstate lines) and the NT are integrated. The mainland interstate track is, for all states and territories except the NT and TAS, owned, leased, maintained and controlled by a federal government owned corporation (the Australian Rail Track Corporation), however, the interstate freight operations in Australia are wholly commercial, being privately owned and operated.

ROADS, BRIDGES AND TUNNELS

The operation, maintenance and improvement of roads in Australia is largely the responsibility of local governments, with the exception of the arterial road network and most local roads in unincorporated areas which are the responsibility of the state and territory governments. The federal government also shares responsibility with the states and territories for a defined national network of road transport corridors and rail-road inter-modal connections. The delivery, operation and maintenance of such infrastructure is often outsourced to the private sector. For example, management of toll-roads (including the design, build, financing, operation, maintenance and collection of tolls) is typically outsourced to the private sector on a full concession basis, with the states and territories holding the perpetual lease over toll road land.

AVIATION

Aviation infrastructure in Australia is typically government-owned. All federal airports are located on government-owned land and are under long-term leases to private entities. There are significant restrictions on ownership of airport-operating companies under the

Airports Act 1996 (Cth), including a 49% limit on foreign ownership, a 5% limit on airline ownership and a 15% limit on cross-ownership between paired airport operator companies. The majority of all other Australian airports are owned and operated by local government authorities, with a small number operated by the private sector on the government's behalf, or both owned and operated by the private sector for public use. The aviation regulator in Australia is the Civil Aviation Safety Authority (CASA). The government has influenced market structures to combat competition issues, for instance prohibiting the cross-ownership of airports.

MARITIME AND PORTS

The ports in Australia are typically owned by the state and territory governments, however, the operation of, and investment in ports is largely privatized, with port assets typically privatized on a long-term lease basis.

Infrastructure Australia, a government body, oversees rail, road, airports and other infrastructure at a national level.

Other infrastructure

WATER

State and local governments are typically responsible for the ownership of infrastructure and delivery of water services in Australia, generally through government-owned companies. The operation and management of water in SA has been privatized, and local utilities in VIC have been largely privatized. Water utilities are regulated across the states and territories by the relevant State authorities.

DEFENSE

Typically, defense assets are owned by the public sector.

EDUCATION

The education sector in Australia consists of both public and private institutions. Governance and management of education is split between the three levels of government. For instance, the majority of universities operate under State and territory laws and regulations, while early child education facilities operate under the guise of local governments. The Australian Government's Department of Education has the primary responsibility of distributing funding and developing policy in regards to childhood education, higher education, vocational education and training, international education and research.

WASTE

The waste management systems in Australia are the responsibility of state, territory and local governments. The sector is a mix of both public and private operations. The Australian Government is responsible for waste management policy. The private and public sector are involved in all forms of the waste management process.

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Are there special rules for investing in energy and infrastructure?

Generally

Energy and infrastructure markets in Australia, similar to other developed nations, operate in a heavily regulated environment. There is no specific regime governing or restricting investment in energy or infrastructure in Australia over and above existing regulation for investors and funders more generally. When making an investment, the legal and regulatory position relevant to the underlying project must be considered. For example, a project relating to a hospital will require various environmental and planning approvals, consents, building and operating permits, and work-health and safety accreditations.

AUSTRALIAN COMPETITION AND CONSUMER COMMISSION

The ACCC regulates a range of infrastructure services, such as energy, communications, water and smaller markets with limited competition. While the ACCC acts as an overarching regulator, investors, owners and operators must also comply with both State and industry-specific regulation. The ACCC facilitates the National Access Regime, which encourages third party access to nationally significant infrastructure services. The ACCC assesses access undertakings lodged by the owners or providers of infrastructure services.

FOREIGN INVESTMENT REVIEW BOARD

All foreign investment proposals in Australia above certain thresholds, determined on a case-by-case basis, are reviewed by the FIRB to ensure such investments are not contrary to the national interest. Notification and approval of foreign investment will differ depending on the type of transaction (i.e. telecommunications or energy transaction), or the type of investor (i.e. private sector or foreign government investor).

FIRB aims to provide a decision within 30 days of being notified. Once formally notified, the Treasurer has 30 days to make a decision and a further 10 days to notify the parties concerned of the outcome. If these timeframes are not met, the Australian Government loses the ability to block the proposal or impose conditions on it. The government may, however, extend the process by up to 90 days by issuing an interim order.

Key sector-specific issues are flagged in the sections below.

Energy

The energy markets in Australia have a complex system of arrangements between suppliers, generators, transmission and distribution which are moderately regulated. Regulation and market oversight of the energy sector is split between the Australian Energy Regulator (AER) (for all states other than WA) and the Australian Energy Market Commission (AEMC).

The National Energy Retail Laws and National Energy Retail Rules, establish a national energy customer framework for the regulation of the retail supply of energy (electricity and gas) to customers where the NEM applies. The laws aim to promote retail competition and empower customers to negotiate energy contracts. The NEM operates on a relatively competitive basis, with generation, transmission and retailing assets split in each state and territory. The market operates with streamlined regulations, limited barriers to access, and minimal direct government intervention. In WA and the NT, where the NEM does not apply, energy is regulated by the Economic Regulation Authority (ERA) and the Utilities Commission, respectively.

Under the NEM, an authorization issued by the AER is required prior to engaging in the retail sale of energy, unless an exemption applies. Under state-based authorities, transmission and distribution businesses are required to be issued with a license before providing transmission and distribution services. Applications must be lodged with the state based regulator and an associated fee will apply.

It is important to note certain infrastructure assets are subject to more stringent safeguards on pricing and staffing, in an effort to preserve community expectations. For example, in the recent sale of Ausgrid (in October 2016), the NSW government implemented legislation prescribing the minimum number of employees the buyer would have to maintain until 2020, and the categorization of employee.

Recently, increasing demand for 'clean' energy, alongside firm environmental regulation, has presented concern for external investors wishing to invest in Australia's energy sector. In 2015, the federal government increased Australia's Renewable Emission Target to 23.5% of Australia's electricity generation being sourced from renewable sources by 2020. Investors need to understand how environmental and technology changes may impact on the overarching regulatory framework and should consider whether the acquisition of any interests in the energy sector (at an entity or asset level) would cause any issues with license conditions or the granting of specific subsidies.

Telecoms infrastructure

The telecommunications sector in Australia operates in a competitive market, where the regulatory barriers to entry are limited. The telecommunications sector has two main regulators:

- The ACCC which operates under the Competition and Consumer Act 2010 (Cth) prohibits and prevents carriers engaging in anti-competitive conduct, breaching record-keeping rules or breaching access rules.
- The Australian Communication and Media Authority (ACMA) which operates under the Telecommunications Act 1997 (Cth) and has responsibility over technical matters (i.e. carrier licensing, service provider licensing and number portability). The cabling industry is regulated by the Telecommunications Cabling Provider Rules 2014 (Cth) (CPRs).

The ACCC's access regulation plays a key role in the increase of infrastructure and retail competition in the telecommunication sector. For example, the ACCC assisted opening access to Telstra's line services, increasing competition in retail and broadband networks. ACCC regulation is commonly higher in areas of insufficient competition, namely transmission routes in regional and outer metropolitan areas.

There are two different types of individuals or entities that may provide telecommunication services to the public – being carriers and carriage service providers (CSPs). Carriers are owners of telecommunications networks unit that supply carriage services to the public. The

ACMA requires carriers to obtain a carrier license and to comply with certain obligations under the license, unless an exemption applies or the authority allows for nominated authority declarations, whereby another party to takes on the responsibilities of a carrier for a network unit. The Minister for Communication also has the authority to impose license condition declarations, whereby further license conditions are imposed on certain classes of carriers. In contrast, a CSP, a person or entity that supplies a carriage service to the public using a network unit (i.e. internet service providers) is not required to hold a carrier license.

Under the CPRs, all cabling work is required to be performed by a registered cabler or under the express direction of a registered cabler. Cablers are required to register with an ACMA-accredited registrar.

Transport infrastructure

The National Transport Commission operates under the National Transport Commission Act 2003 (Cth) as an independent advisory body with the aim of enhancing safety, productivity and environmental performance of Australia's transport systems. The body provides impartial advice and reform proposals through the Transport and Infrastructure Council.

RAIL

The Office of the National Rail Safety Regulator (ONRSR) is responsible for the implementation of safe rail operations and controls a singular set of rail safety laws in Australia, with each state and territory (except QLD) passing enabling legislation to give effect to the Rail Safety National Law. Rail Transport Operators must obtain a license that certifies the competence and capacity of the operator to manage the risks associated with railway operations. The accreditation is required prior to commencing any railway operations.

ROADS

The state and territory governments each have government departments which administer the National Prequalification System for Civil (Road and Bridge) Construction Contracts (NPS). The NPS separately takes into consideration the financial and technical capacity of contractors and identifies prequalification categories for road construction, bridge construction and financial levels (referring to financial stability, solvency and capacity to manage cash flow), against which the NPS assesses the capacity of a contractor to undertake contracts of varying risk and complexity. Austroads is the key organization responsible conducting strategic research on transport developments, provides guidance on the design, construction, management and infrastructure of road networks.

Other infrastructure

For most infrastructure assets in the private sector, it is likely that there will be a 'change of control' provision requiring the regulator or controlling government to approve the new owner. On publicly-procured infrastructure, it is quite common for long-term projects to have a 'change in control' clause which restricts change in ownership structures of the private sector. For example, in most sectors there is a restriction on change in control during the construction period but this is often relaxed post construction provided any change in control is not to an 'Unsuitable Third Party'.

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What is the applicable procurement process?

In Australia, procurement of infrastructure projects is almost invariably carried out on a contestable tender basis. A contestable tender basis is deemed to be a fair, transparent and competitive way to obtain value for money. Such contestability may be publicly advertised or sought from a formal pre-qualified list of bidders or informally sought from a private list of contractors. Some states do, however, have unsolicited proposal regimes whereby the private sector may directly approach Government with a proposal for infrastructure development and then be awarded the rights on an uncontested basis, but there are strict criteria that apply.

Investing in energy and infrastructure

There is no body of public procurement law. Procurement by the state and federal governments is governed by a mixture of policies such as guidelines and codes of practice, statute, regulations and common law.

While private sector procurers of construction services are generally free to set their own 'rules' of procurement, they can still be exposed under statute (for example under the Australian Consumer Law) or at common law. Procurers will find themselves exposed to these laws if they either do not follow the process which has been specified in the tender documentation or if they make inaccurate representations

about the way in which the tender process will be managed or contracts awarded. Conversely, bidders may be exposed to common law process contract challenges if they withdraw during evaluation.

In addition to the infrastructure research and advisory bodies established by some states and the federal government, each government agency has at least one designated department or body which develops and implements policy applicable to procurement of infrastructure projects. In some cases specialized policies will apply to particular types of procurement such as defense, health infrastructure and the delivery of Public-Private Partnerships (PPP) and unsolicited proposals. In addition, government agencies which procure a large amount of infrastructure (for example statutory road management agencies) often have their own internal policies and procedures applicable to the procurement of that work.

For projects with a value in excess of AUD10 million, many government agencies have implemented a system of audits, checks and balances to seek to ensure that the tender and procurement processes are competitive, transparent and compliant with the relevant rules and policies. This means that many government agencies are required (or choose) to:

- appoint a probity (fairness and honesty) auditor to audit the tender process for the project;
- engage a probity advisor to provide ongoing advice to the agency in relation to management of the tender and tender queries; and
- participate in periodical reviews (sometimes known as 'Gateway' reviews) in order to benchmark, test and check the business case for the project.

STATUTORY REGULATION OF GOVERNMENT TENDERS

The Australian Consumer Law (and state based Fair Trading legislation) will prohibit certain kinds of behavior and conduct during the course of a procurement, for example, misleading and deceptive conduct. Bid rigging, cover pricing and certain other collusion between tenderers is prohibited under the Competition and Consumer Act 2010 (Cth).

To avoid the possibility of collusion or corruption, tenderers may be asked to provide a statutory declaration that there has been no collusion in the tender process with other tenderers.

To emphasize the transparent nature of government tendering, many government agencies are often now required by statute or policy to publish detailed information:

- identifying the successful tenderer;
- specifying the tender prices submitted by all tenderers; and
- detailing the nature and form of contract executed in respect of the works;

Additionally, government agencies may be required to disclose information under Freedom of Information legislation or through pre-trial discovery processes.

POLICIES, GUIDELINES AND CODES OF PRACTICE

There are numerous policies, guidelines and codes of practice which govern procurement of infrastructure by government agencies at all levels of government. Many government agencies also have specific policies directed at the delivery of projects by different forms of procurement such as a PPP or alliance contracting. In some cases, such as the Commonwealth Procurement Rules issued by the federal government, there are rules dealing specifically with when competition in a tender process may be limited, and additional requirements for procurements at or above a certain threshold.

The core objective of the Commonwealth Procurement Rules is to ensure that value for money is obtained in federal government procurement. The value for money principle requires consideration of all relevant financial and non-financial costs and benefits of each proposal including whole of life costs (such as any maintenance costs or costs in connection with a dispute). The Commonwealth Procurement Rules state that value for money is enhanced in government procurement by:

- encouraging competition and being non-discriminatory;
- promoting the use of resources;
- making decisions in an accountable and transparent manner;
- encouraging appropriate engagement with risk; and

- ensuring that the procurement process is commensurate with the scale and scope of the procurement.

Financing energy and infrastructure

There are three general ways that can be implemented to allow the private sector to assist deliver infrastructure:

- traditional procurement using government financing;
- corporate financing using private financing; and
- project financing using private financing.

PPPs are often perceived as a way to improve or create public infrastructure without hindering on government funds and budget constraints.

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What are the most common forms of funding / investing in energy and infrastructure?

The principal forms of private sector funding/investment in energy and infrastructure in Australia (including in relation to PPPs) are as follows.

Funding

Common forms of funding in energy and infrastructure include:

- debt finance, including:
  - loans made on a project finance basis;
  - loans made on a corporate finance basis (balance sheet debt); and
  - mezzanine debt;
- asset sales;
- federal grants;
- value capture;
- concessional loans;
- asset finance or hire-purchase arrangements; and
- subordinated shareholder loans.

PROJECT FINANCE

Generally, project sponsors prefer debt to be secured on a limited-recourse basis. Limited-recourse means that financiers only take security over the assets of the project itself and its outputs (including revenue) rather than any wider assets of the sponsor and its corporate group This preference is largely driven by the fact that it is only the project's assets and revenues which are 'at risk' of enforcement. This approach enables project sponsors to retain flexibility with respect to their other ventures.

A common structure for project finance involves incorporating a special purpose vehicle for the project (Project Co). The Project Co then enters into a range of documents for the delivery of the project including the *project documents* (relating to construction and operation of the project) and the *finance documents* (relating to the financing of the project).

In order to secure this funding, the project needs to stack up from a 'bankability' perspective. In essence, bankability is a term used to describe:

- the willingness of financiers to fund the project based on security of cash flows (in and out) of the project; and
- the minimization of any residual risk held by the Project Co receiving the funding.

CORPORATE FINANCE

Debt based on corporate finance facilities may be utilized where a project is not sufficiently bankable to receive limited recourse finance. Such facilities may be made on an aggregated basis so that a variety of smaller projects create a portfolio of assets. Recourse for the financier to security is limited to the security based on that portfolio of assets with all assets being cross-collateralised. Alternatively, such facilities can be full recourse, meaning financiers may have recourse against all assets of the relevant companies within the corporate group of the Project Co.

BONDS

While debt-based bond funding is available for project finance, the Australian bond market:

- currently lacks longer tenor instruments to provide the long-term certainty that is often desired in the infrastructure project finance market; and
- is often considered too small to support the funding needs of Australia’s mega projects.

It is now becoming increasingly common for those seeking bond debt to access the US and Asian bond markets instead.

Investing

Australia's superannuation funds have been predominate investors and experts in Australia's infrastructure sector over the past two decades. It is common to see large fund managers or infrastructure investment teams partner with Australian superannuation funds to participate in the infrastructure market. These specialists often compete with overseas investors and entities such as Chinese state owned enterprises.

Common forms of investing in energy and infrastructure include:

- equity investment in special purpose vehicles or entities that may have a portfolio of interests (i.e. share capital); and
- secondary market investment in operational projects.

Standard form documentation may be used when entering into an energy or infrastructure transaction in Australia. Standard forms include:

- Australian Standards (Standards Australia);
- PC-1 1998 (Property Council of Australia);
- Australia Building Industry Contract (Master Builders' Association and Royal Australian Institute of Architects);
- FIDIC (international Federation of Consulting Engineers); and
- NEC3 (Institution of Civil Engineers)

It is important to note that these contracts are heavily amended and bespoke contracts are often used for alliances, PPPs or hybrid models.

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Restructuring

Enforcement and sanctions

When can there be regulatory investigations?

ASIC is a key regulator of the financial services industry in Australia. ASIC has the power to conduct a formal investigation when it suspects that a breach of law is being committed or is likely to be committed by:

- a corporation;
- a financial services provider; or
- individuals.

In conducting such an investigation, ASIC has various compulsory powers including powers to require the production of documents and information, and for individuals to be formally questioned by ASIC.

ASIC also has the power to institute proceedings or seek other remedies for breaches.

Other regulators relevant to financial services businesses include APRA, ATO and ACCC, while Austrac operates as an intelligence gathering agency. Each of these bodies (except Austrac) has similar investigative powers to ASIC; Austrac has slightly more limited powers. All of them can also institute proceedings for contraventions of relevant legislation.

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What regulatory penalties may apply?

Where a breach of law has occurred, ASIC may take various steps, including obtaining an enforceable undertaking from, or issuing an infringement notice on, the offending party.

An enforceable undertaking may include providing compensation, or outlining a process for independent monitoring of an organization's continuing compliance with the law, while an infringement notice will impose financial penalties on an offending party.

If an infringement notice is not complied with or an enforceable undertaking is breached, ASIC can bring a civil penalty action against the recipient seeking payment of the fine and/or compliance with the terms of the enforceable undertaking. ASIC can also pursue civil penalties and other remedies (e.g. banning individuals from operating in the industry or serving as directors) even without first seeking enforceable undertakings or issuing infringement notices. For serious breaches which involve criminal conduct, it can (working with the Commonwealth Director of Public Prosecutions (CDPP)) pursue criminal charges.

ASIC will always assert the right to make an enforcement outcome public, unless the law requires otherwise.

The other regulators listed above (APRA, ATO, ACCC and Austrac) also have the ability to pursue various types of penalties for breaches of the legislation and rules that they respectively regulate.

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What criminal penalties may apply?

ASIC can and does pursue criminal charges (working with the CDPP) when it considers the conduct involved warrants it. ASIC will generally only consider criminal action for offences involving serious conduct that is dishonest, intentional or highly reckless, even if a civil remedy is available for the same breach. Such offences include:

- insider trading;
- a breach of statutory duty by a director; and
- market manipulation.

The same is also true for some of the other regulators listed, for example for cartel conduct (the ACCC), or failure to withhold withholding tax or committing a tax fraud or evasion (the ATO), or breaches of reporting requirements under Australia's AML/CTAF legislation (Austrac).

Current regulatory enforcement outlook

A major judicial inquiry into the Australian financial services sector held in 2018/2019 has resulted in Australian regulators switching to a 'why not litigate?' stance. This has resulted in regulators proceeding with court proceedings in circumstances where, in the past, they may have sought to reach a negotiated outcome on penalties to be imposed for breaches of non-criminal contraventions of legislation.

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Tax

Tax issues

Are stamp, registration, transfer or other similar taxes applicable?

Are there stamp, registration, transfer or other similar taxes payable on the advance, transfer or assignment of a loan?

There is no stamp duty, registration, transfer or similar tax payable on the advance of a loan in Australia.

Only one Australian state, Queensland, levies stamp duty (of up to 5.75%) on transfers or assignments of loans. In Queensland, the transfer or assignment may be dutiable where the borrower is located in Queensland or if the loan is secured by a mortgage or charge over property in Queensland.

Are there stamp, registration, transfer or other similar taxes payable on the taking, transfer or assignment of a mortgage, debenture or other security?

There is no stamp duty, registration, transfer or similar tax payable on the taking, or issue, of a mortgage, debenture or other security in Australia.

In certain Australian states and territories, the transfer or assignment of a mortgage can potentially trigger stamp duty. Certain exemptions or concessions are available, depending on the relevant jurisdiction. Also, there are potential structuring options (e.g. appointing a security trustee to hold mortgages and other securities) to minimize exposure to stamp duty in respect of an assignment of such securities.

Are there stamp, registration, transfer or other similar taxes payable on the issue, transfer or assignment of a debt security (e.g. a bond)?

There is no stamp duty, registration, transfer or similar tax payable on the issue of a debt security in Australia.

As noted above, Queensland is the only Australian state that levies stamp duty on transfers or assignments of loans and other debt instruments. However, the transfer or assignment of corporate bonds are generally exempt from stamp duty in Queensland. There are also exemptions in Queensland in respect of certain securitisation arrangements or debt factoring arrangements.

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Do tax authorities take priority on enforcement?

On the enforcement of security, do tax authorities take priority over secured lenders or secured debt security holders (e.g. secured bond holders)?

For federal taxes (e.g. income tax, Goods and Services Tax and Fringe Benefits Tax), the Australian Taxation Office (ATO) generally does not take priority over any secured lenders or debt security holders. However, in certain limited circumstances, the ATO may take priority over secured lenders, for example when:

- a garnishee notice is issued to allow the ATO to recoup from third parties amounts they owe, or may owe, a tax-owing taxpayer; or
- trustees (including administrators, receivers and liquidators) are obliged to retain sufficient monies from the trust fund to pay tax if the relevant assessment has been issued.

However, for certain state taxes (e.g. stamp duties and land tax), the relevant state revenue authority can take priority over secured lenders or debt security holders.

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Is withholding tax on interest payments applicable?

Is there withholding tax on interest payments under a loan?

Unless an exemption applies under domestic law or an applicable double tax treaty, where a payment of interest (as broadly defined) is paid (or is deemed to be paid) from Australia to offshore under a loan which is treated as debt for Australian tax purposes, the borrower is required to withhold and pay an amount equal to the applicable withholding tax rate to the ATO.

If so:
What is the rate of withholding?

The current rate of Australian interest withholding tax is 10%.

What are the key exemptions?

The more commonly relied on exemptions include:

- exemptions for a publicly offered syndicated loan facility or a publicly offered debenture issued by an Australian resident company or Australian unit trusts and by a company or unit trusts not resident in Australia but carrying on business at or through permanent establishments in Australia;
- exemptions for certain foreign tax exempt superannuation funds and foreign sovereign entities which do not have control or influence in certain Australian borrowers; and
- reliance on a double tax treaty (for example, an exemption is available for interest paid to government entities or independent financial institutions).

Would the same analysis apply to interest payments under a debt security (e.g. a bond)?

Yes, the analysis described above is generally applicable to both interest payments under a loan or other form of debt security.

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Are foreign lenders and debt security holders subject to tax on interest payments?

Will the lender be taxed on interest payments under a loan in the jurisdiction of the borrower (other than by way of the application of withholding taxes (if any)), assuming the lender is not otherwise resident in that jurisdiction for tax purposes (e.g. by virtue of incorporation, residence or local branch)?

Generally no.

Would the same analysis apply to interest payments under a debt security (e.g. a bond)?

Yes.

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