The regulatory regime governing the syndication of thoroughbred racehorses

The syndication of thoroughbred racehorses is subject to regulation under the Corporations Act and the Australian Rules of Racing

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Author: AB (Tony) Fleiter BEc., LLB – Principal, Macquarie Legal Practice
Postal Address: PO Box 299, NORTH SYDNEY, NSW, 2059. AUSTRALIA.
Telephone +61 2 9235 2500 Facsimile +61 2 9235 1511 Email tony.fleiter@maclegal.com.au
Website: www.maclegal.com

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This paper has evolved from a much shorter set of practice notes I compiled in 2002, and then a presentation paper when a principal speaker at seminars in Sydney and Melbourne during 2004. I first published it in a form akin to its present form in 2008 and have revised it numerous times since then. It remains a work in progress.

I have discussed my analysis and conclusions with numerous thoroughbred industry participants and lawyers with significant expertise in a variety of legal disciplines, including the law relating to managed investment schemes. I appreciate the input of those people.

If you would like to comment on any aspect of this paper, please do so.

This paper [with links to all judgements and other documents cited in it] is available at www.racehorseownership.com

INTRODUCTION

I have been acting for participants in the thoroughbred industry for 35 years and have heard the following words, or similar, many times, from aggrieved buyers of racehorses and shares in racehorses seeking advice as to their legal rights to rescind the bargain and claim restitution:

- "I contacted the guy after seeing an advertisement!"
- "I visited the stable and looked at the horse!"
- "He said he bought the horse at the sales on "spec" because he really liked it as a type, and it had a good pedigree!"
- "He said the horse had vetted 100% sound!"
- "He said he would aim the horse at the rich 2YO races!"
- "He said the horse is a well-bred and will maintain its value for breeding even if it doesn't win any races or prize money!"
- "He said he would look after everything and that I would receive a monthly invoice for my share of expenses!"
- "He said that he would consult me and that I would have a say in relation to important decisions relating to the horse, including what races it would run in – that didn't happen"! He never consulted me, and I had no say on anything!
- "We simply agreed it was a deal, shook hands and I paid him!"
- "There is nothing in writing. I do not even have a receipt for my payment!"
- "He seemed like a nice guy, and I trusted him!"
- "The monthly expenses are a lot more than he said they would be!"
- "The horse is a dud!"
- "The bastard has conned me and ripped me off!"
- "He has done the wrong thing!"
- "Can I get out of it without it costing me any more money?"
- "Can I get my money back?"

There are many industry partisans who advocate that the sale and purchase of racehorses, and shares in racehorses, should not be subject to regulation because investment in racehorses is highly speculative and nothing more than a game of chance. When doing so, they ignore, either through ignorance or for convenience, the fact that such transactions and ownership arrangements are subject to numerous laws (both federal and state) which can potentially impact the rights and obligations of the parties, including (without limitation) the following federal and state laws:

Commonwealth legislation:

- *Australian Securities and Investments Commission Act 2001;*
- *Competition and Consumer Act*;
- *Corporations Act 2001*;
- *Personal Property Securities Act 2009;*
- *Insurance Contracts Act 1984;* and

- Taxation legislation (GST, income tax and capital gains tax); and

State and territory legislation:

- *Sale of Goods Act;*
- *Partnership Act (Uniform partnership legislation);*
- *Conveyancing Act 1919 (NSW), Property Law Act 1958 (Vic), and similar legislation in other jurisdictions);*
- *Civil Liability Act 2002 (NSW*), *Wrongs Act 1958 (Vic), and similar legislation in other jurisdictions*;

some of which have consumer protection provisions embedded within them.

The sense of bravado and enthusiasm that often engulfs the parties and results in the bargain being consummated with a handshake after only a brief discussion (an effective sales pitch), instead of by a written agreement being signed by the parties after appropriate disclosure, due diligence and agreement as to terms, rapidly fades when problems arise causing one or other of the parties, usually the buyer, to review the bargain and consider his or her legal rights and remedies. Only then do they lament the fact that the transaction was not the subject of an appropriate disclosure document and written agreement.

This paper is about the sale of shares/interests in thoroughbred horses for racing purposes (known as "syndication") and the regulatory regime designed to promote and protect market integrity.

I estimate that during 2022 "ownership opportunities" in racehorses (yearlings and tried horses) with a total cumulative value of more than $50 million will be offered to investors by people who are, or should be, licensed.

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EXECUTIVE SUMMARY

This paper is intended to provide an in-depth analysis of the statutory provisions, regulations and rules that form the basis of the regulatory regime governing the sale of interests[1] in thoroughbred horses for racing purposes and the subsequent operation of those schemes[2].

People who engage in this activity (known as "syndication") as promoter or seller typically acquire horses, either at public auction or by private treaty, with the intention of reselling them by offering interests. They typically advertise on websites, various TV channels dedicated to racing, and in various newspapers and industry journals, asserting:

- the superior quality of the horses and their prospects of winning races (prize money);
- that the price of the interest(s) represents value for money;
- that the promoter has skill, expertise and a track record of selecting and syndicating horses that have progressed to winning races; and
- that the nominated trainer is a successful trainer of winners.

Some promoters have an exclusive arrangement with a trainer, while others place their horses with different trainers. A significant number of trainers also act as promoters.

WHY THE NEED FOR REGULATION?

Promoters predominantly target members of the public who have little, if any, prior ownership experience. Their lack of product knowledge and varying motivations to invest adds to investment risk and highlights the necessity for an appropriate disclosure regime. Market integrity is also important for promoting the depth of market necessary to attract investors.

WHY ASIC?

The regulatory regime governing this activity is founded upon the provisions of the *Corporations Act 2001* ("the Act")[3] relating to managed investment schemes and involves interaction between the *Australian Securities & Investments Commission* ("ASIC") and the Principal Racing Authorities of the various states and territories, as lead regulators.

WHAT IS A MANAGED INVESTMENT SCHEME?

Non-lawyers tend to associate the phrase "managed investment scheme" and its prefix "MIS" with investment schemes that are designed to invest in securities and other traditional investments. However, it is established law that the meaning given to that term by the Act is deliberately wide and designed to catch virtually all arrangements targeting collective investment and would, by itself, catch virtually all business models and structures.

The statutory provisions that govern the requirements of ASIC to carry out activities concerning managed investment schemes (and the restrictions on promoting them) have broad application and have been held to cover such diverse activities as film, agriculture, mortgage funds, property development, sports betting, thoroughbred horse breeding and racing, etc.

Under the Act, any person (promoter) who is "carrying on a financial services business" ["dealing is a financial product" (which includes the "issuing", "underwriting" and "disposing" of interests in any managed investment product), or "operating a registered scheme"], must hold an Australian Financial Services Licence (AFS Licence) or be an Authorised Representative of a licensee, and the scheme must be registered, subject to specific statutory exemption or ASIC Instrument relief granted administratively (e.g. ASIC Instrument).

[1] "interest" and "share" have the same meaning - in relation to the horse means an ownership or leasehold interest in the horse AND in relation to the scheme means a right to participate in the scheme. "interest" is used in the Corporations Act and the ASIC Instrument. "share" is used in the ARR and the Promoter Guides of the various lead regulators.

[2] "scheme" and "syndicate" are generic terms which have the same meaning – "scheme" is used in the Corporations Act. "syndicate" is used in the ASIC Instrument and the ARR. In the context of this paper, they can both be read as meaning "*the arrangements [typically co-ownership contract-based "common enterprise" arrangements] made between 2 or more people who own or lease a thoroughbred horse, or an interest in it, for the purpose of using it for racing.*

[3] each reference to a section is a reference to a specific section of the Corporations Act 2001, unless otherwise stated.

A distinction is made between "retail clients" and "wholesale clients." Generally, the consumer protection provisions will only apply to "retail clients", as it is recognized that "wholesale clients" (including professional and sophisticated investors) do not require the same level of protection, as they are better informed and better able to assess the risks involved in financial transactions. A financial product is provided to a person as a "retail client" if it is not provided to the person as a "wholesale client." To be treated as a "wholesale client", the investor must satisfy a wealth, occupation, or other threshold test.

The advertising or public promotion of "financial products" (that are managed investment products) is permitted only in relation to those offers of interests that require a Product Disclosure Statement ("PDS") and a PDS is (or is to be) made available, or where participation is available only to "wholesale clients."

WHO DOES THE REGULATORY REGIME APPLY TO?

The regulatory regime generally applies to any person who is (a promoter[4]) in the business of promoting horse racing schemes, as virtually all such arrangements [typically co-ownership, partnership, or unit trust arrangements] will, prima facie, satisfy the definition of a managed investment scheme.

WHAT OWNERSHIP ARRANGEMENTS ARE EXCLUDED FROM THE REGULATORY REGIME?

A one-off horse racing scheme established by a person who is not in the business of promoting managed investment schemes, generally will qualify as a "private" scheme, provided it has no more than 20 members. However, caution must be exercised as a person may be taken to be in the business of promoting managed investment schemes, as it could be considered to be the first of a series or in relation to that one scheme, it could be clear that the sponsor is 'carrying on a business' of promoting schemes.

WHAT IS ASIC'S APPROACH TO REGULATION?

While ASIC has responsibility for administering the Act, it has consistently exercised its discretionary administrative powers and granted conditional relief for small-scale schemes from the specific statutory provisions requiring scheme registration.

ASIC's approach to the regulation of horse breeding and horse racing schemes is set out in the following documents:

1. ASIC Corporations (Horse Schemes) Instrument 2016/790 issued by ASIC on 25/08/2016 (as amended on 16/12/2016 (ASIC Corporations Instrument 2016/1173) and under ASIC Corporations (Amendment and Repeal) Instrument 2021/799) (**ASIC Instrument**), which revoked and replaced
    - CO 02/319 [Horse racing] issued by ASIC on 15/02/2002 (as amended), which revoked and replaced
    - CO 98/65 [Horse racing] issued on 14/07/1998, which revoked and replaced
    - Policy Statement 20 – Horse racing schemes, issued on 04/05/1992 (as amended).
2. Explanatory Memorandum for ASIC Corporations (Horse Schemes) Instrument 2016/790 issued on 26/08/2016.
3. ASIC Regulatory Guides
    - RG 91 [2016] – Horse breeding schemes and horse racing syndicates, which superseded
        - RG 91 [2012], which superseded
        - RG 91 [2007].
    - RG 97 [2017] – Disclosing fees and costs in PDSs and periodic statements, which superseded
        - RG 97 [2011], which superseded
        - RG 97 [2007].

[4] the promoter test is in section 601ED(1)(b). See part 2.2 of this paper.

- RG 168 [2011] – Disclosure: Product Disclosure Statements (and other disclosure obligations), which superseded
    - RG 168 [2010], which superseded
    - RG 168 [2007].

The purpose of the ASIC Instrument (as was the case with the previous Class Order and Policy Statement) is to relieve those small-scale schemes which comply with the terms of the ASIC Instrument from otherwise having to comply with the statutory provisions requiring registration.

The scope of the relief is limited to the terms of the ASIC Instrument.

ASIC has reappointed the Principal Racing Authorities of the various states and territories as lead regulators to administer the terms of the ASIC Instrument within their respective jurisdictions.

If you have not already read these documents, it would be advantageous for you to do so before proceeding to read this paper.

WHAT ARE THE BASIC REQUIREMENTS OF THE CURRENT REGULATORY REGIME?

While the statutory provisions and regulations are complex, the basic requirements of the regulatory regime, and how it operates, is simply explained as follows:

1. THE RULES (SPECIFYING EXPECTED BEHAVIORS AND OUTCOMES)

Requirement for Schemes to be registered and the exceptions

Under the Act, any horse racing scheme established by a person who is (a promoter[5]) in the business of promoting such schemes must be registered as a managed investment scheme, unless it qualifies as an unregistered scheme that is:

(a) a personal offer scheme[6];

(b) a wholesale scheme[7]; or

(c) a lead regulator approved (ASIC Instrument[8] compliant) syndicate.

Investors who are "retail clients" are not permitted to participate in a wholesale scheme.

Requirement for promoters and managers to be licensed

Promoter

Under the Act, any horse racing scheme established by a promoter for promotion to retail clients will, prima facie, fall within the requirement for registration under section 601ED, so the promoter must hold an AFS Licence, when engaging in the activity.

The promoter of a wholesale scheme (in other words one that does not require registration) will also require an AFS Licence.

There is no statutory exemption or ASIC Instrument relief from this requirement for a "promoter" to be licensed, regardless of whether a specific scheme is relieved by statutory exemption or the terms of the ASIC Instrument from the requirement to be registered.

Manager

The manager of a horse racing scheme that is either a "registered" scheme, or an "unregistered" scheme where participation is available only by "personal offer", or to "wholesale clients", must also hold an AFS Licence.

[5] ibid.
[6] section 1012E.
[7] section 761G.
[8] ASIC Corporations (Horse Schemes) Instrument 2016/790.

The manager, if not the promoter, of a Horse racing syndicate that is the subject of a PDS approved by a lead regulator (Principal Racing Authority) may not require a licence, subject to the terms of the ASIC Instrument.

2. THE STANDARDS (USED AS BENCHMARKS FOR COMPLIANCE)

Disclosure of key information

The promoter of an "offer of interests" in a horse racing scheme that is either a registered managed investment scheme, or a lead regulator approved (ASIC Instrument compliant) syndicate, must disclose to prospective investors who are "retail clients" all key information required to enable them to make an informed decision whether or not to invest. The information is generally required to be set out in a PDS, which must be provided to prospective investors prior to sale.

The promoter must include with the key information the agreement which will govern the future ownership of the horse(s) the object of the scheme, including provisions dealing with the appointment of a manager and a trainer, and arrangements for the payment of operating expenses and distributions of income (prize money) earned, if any.

Handling of Application Moneys and transfer of ownership

The promoter must deposit all application money paid by investors into a designated application moneys trust account until the legal and beneficial ownership of the horse(s) is transferred to them, unencumbered. If an "offer of interests" is not fully subscribed, the promoter must refund to investors all application money received[9].

3. THE SANCTIONS (APPLIED FOR NON-COMPLIANCE WITH THE RULES)

There are serious consequences for promoters who engage in this activity in contravention of the Act and the ARR[10]. Enforcement action may include prosecution and the imposition of punitive penalties, or orders requiring the payment of compensation.

4. THE ADMINISTRATIVE PROCESS (TO ENFORCE THE RULES AND ADMINISTER SANCTIONS)

ASIC is responsible for administering the Act, including surveillance activities to promote compliance, investigating suspected non-compliance, and prosecuting breaches.

ASIC has appointed the Principal Racing Authorities of the various states and territories [as lead regulators] to administer the terms of the ASIC Instrument within their respective jurisdictions.

Each Principal Racing Authority (within its jurisdiction):

(a) is responsible for administering the ARR; and

(b) has the capacity to investigate and prosecute any person it suspects of breaching the ARR;

and as a lead regulator under the ASIC Instrument:

(c) is responsible for administering the syndication activities of promoters within the terms of the ASIC Instrument; and

(d) has the capacity to refer to ASIC for investigation and prosecution, any person it suspects of breaching the Act. In fact, it is probably fair to say that ASIC has an expectation that each Principal Racing Authority will undertake appropriate surveillance activities and refer suspected breaches of the Act to it for further investigation and prosecution.

GENERAL

While the current regulatory regime has been in place since 2002 (with very little change under the current ASIC Instrument) and is similar in effect to the old "prescribed interests" regime which operated from the early 1990's, there continues to be a significant level of conflicting opinion amongst industry

9 Section 1017E allows an issuer to retain interest earned on application money as long as this is disclosed to the investor (see regulation 7.9.08A)

10 the Australian Rules of Racing (as amended) (AR#), as determined by Racing Australia Limited (RA) and adopted and administered by the Principal Racing Authority of each state or territory, together with Local Rules (LR#).

participants (including various Principal Racing Authorities) in relation to its application. The writer hopes that the conclusions set out in this paper will provide clarification.

Various statutory provisions, regulations and rules of racing are quoted in full for the convenience of readers.

PART 1: DOES A HORSE RACING SCHEME SATISFY THE DEFINITION OF A MANAGED INVESTMENT SCHEME?

1.1 Part summary

This part deals with:

(a) the definition of a "managed investment scheme" in the Act, commonly referred to by its prefix "MIS;

(b) the unincorporated multi-party ownership arrangements of thoroughbred racehorses within the context of the regulatory regime; and

(c) the conditions of registration as the owners of a racehorse and the ARR that require the members of an unincorporated multi-party ownership arrangement to appoint:

(i) a manager; and

(ii) a licensed trainer;

to manage aspects of the arrangements on behalf of the group.

Conclusion

The managed investments scheme regulatory regime is imbedded within the Act.

It is a set of compliance rules for unincorporated arrangements (schemes) involving collective investment established by a person collecting contributions of money or money's worth from investors which are then applied and managed by the operator of the scheme on behalf of the group.

The purpose of the rules is to ensure minimum standards of investor protection in relation to the establishment and operation of such schemes.

The determining criteria of a managed investment scheme can only be the legislated definition of a managed investment scheme complemented by the principles established by the case law, objectively applied.

The analysis of a scheme to determine if it satisfies or falls outside the scope of the definition requires that consideration be given to:

(a) all its key elements, including:

(i) legal structure;

(ii) the nature of the members interests [contributions and rights to benefits]; and

(iii) modus operandi [the realities of how it is designed to operate in practice];

(b) the scheme as being the entire operation [all the activities carried out in relation to the scheme as comprising the scheme's operations]; and

(c) the necessary distinction between:

(i) the activities [and rights] of the individual members and those of the group; and

(ii) day-to-day "control in fact" and each of "the legal right to control" and "merely a right to participate in decision-making" [the existence of such rights in the members does not necessarily lead to the conclusion that the members have day-to-day "control in fact" over the operation of the scheme].

The fundamental distinction which underlies the whole of the definition is between:

(a) schemes where "all" the members have day-to-day control over the operation of the scheme by making "all" the decisions and implementing what is agreed; and

(b) schemes where any members' contributions [of money or money's worth] are to be:

(i) pooled; or

(ii) used in [made available, or paid or supplied, for the purpose of] a common enterprise;

with the day-to-day [routine, ordinary, everyday] activities of the scheme being managed or carried out by a person who is an operator of the scheme on behalf of the members collectively, (whether or not they have the right to be consulted or give directions).

The objective assessment in determining day-to-day control is necessarily prospective, viewed from the time when the arrangements are made.

The day-to-day control test in the context of the definition of a managed investment scheme is not about ownership or proprietorship, or the legal right to control of the scheme.

- *The purpose of the day-to-day control test is to make an important distinction about the nature of the investment each member of the scheme is making.*
- *If the substance is that all the members have day-to-day "control in fact" over the operation of the scheme by making all the decisions and implementing what is agreed [actually managing or carrying out the routine, ordinary, everyday activities that comprise the scheme's operations], then the scheme will not be a managed investment scheme.*
- *However, if the substance is that the members' contributions are to be pooled, or used in a common enterprise, to produce financial benefits, or benefits consisting of rights or interests in property, and the members appoint a person to operate the scheme [with the authority to actually manage or carry-out the routine, ordinary, everyday activities that comprise the scheme's operations] on behalf of the group, then the scheme will be a managed investment scheme (whether or not they have the right to be consulted or give directions).*
- *It is a negative test in the sense that for the arrangements to not be a managed investment scheme, they must be such that all the members will have day-to-day "control in fact" over the operation of the scheme, prospectively viewed from the time when the arrangements are made.*

The day-to-day control test includes consideration as to whether a person who provides management services in relation to the property is either:

(a) a mere "agent" who separately manages the property of each member or "investment professional" who simply provides advice to the members on enhancing the value of their own property without exercising control; or

(b) an "operator" of the scheme who manages "as a whole" the property of the group.

The management activities of a person who is the "promoter" or "operator" are not to be imputed to the members in determining whether the members have day-to-day control over the operation of the scheme.

Control over a number of significant decisions by members will not be sufficient for them to be taken to have "day-to-day control" [Spicer, para 28].

Where the rules of the scheme provide for the assumption of the manager of the assets of the scheme by another person, combined with a situation where the members do not know the identity of other owners so as to facilitate them acting collectively to exercise control, then the members will not be taken to have "day-to-day control" of the scheme [Spicer, para 29].

If the key elements of a scheme satisfy the definition, then generally its establishment and operation will be subject to regulation, except if it qualifies as a "private" scheme. To qualify as a "private" scheme it must not require registration under section 601ED. In other words, it must

not have more than 20 members and the person who established it must not be in the business of promoting managed investment schemes.

Horse racing schemes

Horse racing schemes generally [by practical necessity and to comply with the ARR] are sufficiently uniform in their key elements to justify the conclusion that any programme or plan of action formulated by a person for the purpose of 2 or more people acquiring a thoroughbred horse and using it for racing, [including the ancillary arrangements necessary for achieving that purpose] will, prima facie, satisfy the definition of a managed investment scheme.

The key elements that satisfy the definition are:

(a) one or some of the members contributions [of money or money's worth] are to be:

*(i) pooled [typical of **partnership** or **unit trust**-based "investment" arrangements]; or*

*(ii) used in a common enterprise [typical of **co-ownership** contract-based "common enterprise" arrangements];*

to produce financial benefits, or benefits consisting of rights or interests in property;

(b) the scheme is operated by a manager and a licensed trainer [with actual possession and control of the horse "as a whole"] on behalf of the members collectively; and

(c) the members do not have day-to-day control over the operation of the scheme (whether or not they have the right to be consulted or give directions).

***Co-ownership** is the most common legal form of racehorse ownership involving 2 or more people. A horse racing scheme based on co-ownership inevitably involves the joint participation by all the co-owners, as tenants-in-common, in a commercial enterprise for the common purpose of using the horse "as a whole" for racing with the objective of earning income (winning prize money), and hence is a **common enterprise**.*

*The realities of horse racing schemes formulated as **co-ownership** contract-based "common enterprise" arrangements, as they are generally designed to operate in practice, are:*

(1) People contribute money to acquire from the promoter/operator (or other holder of an ownership interest) proportionate ownership interests in a thoroughbred horse, as tenants-in-common, on the basis that they will:

(a) assume various obligations, including to contribute [make available, or pay or supply, at the direction of the promoter or operator]:

(i) the right to use their individual ownership interests in the horse in a common enterprise (scheme) so that the manager, as an operator of the scheme, can manage all their ownership interests in common [the horse "as a whole"] on behalf of the group; and

*(ii) money (on an ongoing basis) towards the scheme's operating expenses, in the same proportions as the ownership interests held [Clauses 3.3, 7.1 and 7.2 of the **TOR COA**];*

as consideration to acquire rights (interests) to benefits produced by the scheme; and

(b) acquire rights (interests) to benefits produced by the scheme, including to:

(i) participate as members of the scheme for the purpose of using the horse "as a whole" for racing with the objective of earning income for the benefit of the group [benefits derived as the holders of rights or interests in property]; and

*(ii) receive any income (net prize money) earned, in the same proportions as the ownership interests held [financial benefits produced by the scheme]. [Clause 3.2 of the **TOR COA**].*

(2) *The contributions by all tenants-in-common of the right to use their individual ownership interests comprising the horse "as a whole" in the scheme's operations, and the legally binding contractual promise to contribute money (on an ongoing basis) towards the scheme's operating expenses, in the same proportions as the ownership interests held, as consideration to acquire rights (interests) to benefits produced by the scheme, while not money, are of* ***money's worth****, and a "fair equivalent" of what is received.*

(3) *Each member's ownership interest in the property of the group [the horse "as a whole"] which is the subject of the scheme's operations, (not the scheme itself so far as that is different), from an operational perspective, is inseparable from the ownership interests of the other members and the horse "as a whole", and incapable of being separately managed.*

(4) *The right of the members to separately manage their individual ownership interests is:*

(a) *subordinated to the rights of the members collectively and the authority of the manager and the trainer [with actual possession and control of the horse "as a whole"] to operate the scheme on behalf of the group; and*

(b) *limited to voting on those matters specified in the relevant Owners Agreement or Training Agreement as requiring the members' approval (by the requisite majority).*

(5) *The manager and the trainer are both clearly "operators" of the scheme who:*

(a) *control aspects of the scheme's operations on behalf of all the members collectively;*

(b) *manage "as a whole" the property of the group [all the members' individual ownership interests in common - the horse "as a whole"]; and*

(c) *procure the services of other service providers such as veterinarians, farriers, jockeys, agisters and pre-trainers, etc.*

Neither of them is a mere "agent" who separately manages the property of each member or "investment professional" who simply provides advice to the members on enhancing the value of their own property without exercising control.

(6) *Accordingly, day-to-day "control in fact" over the operation of the scheme devolves to the manager and the trainer, being the people who, as operators of the scheme, actually perform "…* ***the acts which constitute the management of or the carrying out of the activities which constitute the scheme****." [Pegasus, para 55].*

(7) *Conversely, all the members do not have day-to-day "control in fact" over the operation of the scheme, prospectively viewed from the time when the arrangements are made. Practical necessity and the* ***ARR*** *(including the* ***TOR Rules****) require that the members:*

(a) *agree to:*

(i) *appoint a person (manager) to control aspects of the scheme's operations, including those relating to its legal structure and administration, dealings with racing officialdom, the trainer and other service providers, as required, on behalf of the group [in accordance with the* ***ARR*** *and the terms of the* ***TOR COA*** *or other agreement adopted by the members]; and*

(ii) *the manager on behalf of the group appointing a licensed trainer, [including agreeing to the terms of the Trainer's Training Agreement and Fees Notice], to take actual possession and control of the horse "as a whole" for the purpose of managing or carrying out those activities that collectively comprise the act of training a racehorse [in accordance with the* ***ARR*** *and the terms of the* ***TOR STA*** *or other agreement adopted by the parties]; and*

delegate to them the authority to operate the scheme on behalf of the group; and

(b) *surrender day-to-day control over their individual ownership interests to the manager and the trainer so that those people can manage all the members' ownership interests in common [the horse "as a whole"] for the benefit of the group, (whether or not they have the right to be consulted or give directions).*

(8) However, a scheme may not possess these characteristics alone. The fact that it may also possess other characteristics, including terms that provide for the members to:

(a) pay their ongoing contributions towards operating expenses directly to the relevant service providers [proportionate direct invoicing and payment of fees and expenses];*

(b) be paid their distributions of any income (net prize money) directly via the stakes payment system;*

*[*an alternative to the manager administering these arrangements via a designated scheme bank account] or*

(c) participate in selected decision-making in accordance with the procedure (and requisite majority) set out in the applicable Owners Agreement or Training Agreement;

does not take it outside the scope of the definition.

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The case law and the evidence clearly support the conclusion that the characteristics of a managed investment scheme are inherent in horse racing schemes as they are both designed to operate in practice and required to operate by the ARR. *Consequently, there is no apparent basis upon which any person, including a licensed trainer, who is (a "promoter") in the business of promoting horse racing schemes, could successfully argue in any legal forum that the resultant schemes are outside the scope of the definition of a managed investment scheme and not subject to regulation. Any such argument would likely be a misrepresentation of the arrangements to avoid the legislative intention of the statutory provisions.*

*The need for <u>all</u> the members to exercise day-to-day control over the operation of the scheme by making <u>all</u> the decisions and implementing what is agreed is impractical in the context of owning and managing a racehorse which is overcome by the members [as required by the **ARR**]:*

(a) appointing a manager and a licensed trainer [with actual possession and control of the horse "as a whole"]; and

(b) delegating to them the authority to operate aspects of the scheme on behalf of the members collectively.

1.2.1 What is a managed investment scheme?

The term "managed investment scheme" is defined in section 9 of the Act as:

"(a) a scheme that has the following features:

(i) people contribute money or money's worth as consideration to acquire rights ("interests") to benefits produced by the scheme (whether the rights are actual, prospective or contingent and whether they are enforceable or not);

(ii) any of the contributions are to be pooled, or used in a common enterprise, to produce financial benefits, or benefits consisting of rights or interests in property, for the people (the "members") who hold interests in the scheme (whether or not as contributors to the scheme or as people who have acquired interests from holders);

(iii) the members do not have day-to-day control over the operation of the scheme (whether or not they have the right to be consulted or give directions); …."

The definition is deliberately wide and all-embracing and designed to catch virtually all arrangements targeting collective investment. It would by itself catch virtually all business models and structures, including co-ownership [***Stewart v Spicer Thoroughbreds Pty Ltd***[11]], partnership [***ASIC v McNamara***[12]] and unit trust-based arrangements.

The following terms are also defined in the Act:

[11] n 27, at p 24.
[12] n 20, at p 16.

"*interest*" in a managed investment scheme means*:*

> *"a right to benefits produced by the scheme (whether the right is actual, prospective or contingent and whether it is enforceable or not)."*

"*investment*" in a registered scheme means:

> *"(a) an interest in the scheme: or*
>
> *(b) a legal or equitable interest in an interest in the scheme."*

"*member*" in relation to a managed investment scheme means:

> *"a person who holds an interest in the scheme."*

Some key words and phrases in the definition of a managed investment scheme are not defined in the Act, so must be given their ordinary meaning[13]:

"*benefit*" means:

> *"an advantage or profit gained from something: enjoy the benefits of being a member."*

"*common enterprise*" means:

> *"a project or undertaking by 2 or more people."*

"*contribute*" means:

> *"give (something, especially money) in order to help achieve or provide something."*

"*contribution*" means:

> *"a gift or payment to a common fund or collection … that part played by a person or thing in bringing about a result or helping something to advance*."

"*control*" means:

> *"the power to influence or direct people's behavior or the course of events: the whole operation is under the control of a production manager."*

"*day-to-day*" means:

> *"happening regularly everyday: the day-to-day management of the classroom."*

"*operation*" means:

> *"the activity in which a business is involved."*

"*to operate*" means:

> "*control the functioning of*."

"*scheme*" means:

> *"a project or undertaking."*

"*whether*" means:

> "*expressing a doubt or choice between alternatives*" and "*the statement applies whichever of the alternatives mentioned is the case*."

"*whether or not*" means:

[13] English Oxford Dictionary.

"*the statement applies whichever of the alternatives mentioned is the case*", and in the context of that statement "*…whichever…*" means "*used to emphasize a lack of restriction in selecting one of a defined set of alternatives – regardless of which*."

Modifier statements

Each limb of the definition contains a statement in brackets beginning *with ("whether…" or "whether or not…")* which is a modifier statement to the head statement. A modifier statement is intended to provide a default rule for resolving ambiguities in elements of the head statement.

In each case the modifier statement is a **nonrestrictive modifier** which provides additional [nonessential] information that <u>does not</u> [express an intention to] limit or restrict the legal meaning of an element of the head statement. Whereas a **restrictive modifier** is a statement that modifies an element of the head statement in a way that is essential to its meaning.

The three elements of paragraph (a) of the s.9 definition

First element

The head statement in the first element of the definition "*people contribute money or money's worth as consideration to acquire rights ("interests") to benefits produced by the scheme*" is subject to the **nonrestrictive modifier** "*(<u>whether</u> the rights are actual, prospective or contingent and <u>whether</u> they are enforceable or not)."*

Consequently, [giving the word "*whether*" its ordinary meaning] the head statement applies whichever [regardless of which] of the alternatives mentioned in the modifier statement is the case. In other words, the rights being actual, prospective, or contingent and whether they are enforceable or not <u>does not</u> limit or restrict the legal meaning of the head statement.

Second element

The head statement in the second element of the definition "*any of the contributions are to be pooled, or used in a common enterprise, to produce financial benefits, or benefits consisting of rights or interests in property, for the people (the "members") who hold interests in the scheme*" is subject to the **nonrestrictive modifier** "*(<u>whether or not</u> as contributors to the scheme or as people who have acquired interests from holders)*."

Consequently, [giving the phrase "*whether or not*" its ordinary meaning] the head statement applies whichever [regardless of which] of the alternatives mentioned in the modifier statement is the case. In other words, the members being either contributors to the scheme or people who have acquired interests from holders <u>does not</u> limit or restrict the legal meaning of the head statement.

Third element

The head statement in the third element of the definition "*the members do not have day-to-day control over the operation of the scheme*" is subject to the **nonrestrictive modifier** "*(<u>whether or not</u> they have the right to be consulted or give directions)*."

Consequently, [giving the phrase "*whether or not*" its ordinary meaning] the head statement applies whichever [regardless of which] of the alternatives mentioned in the modifier statement is the case. In other words, any right they (the members) may have to be consulted or give directions <u>does not</u> limit or restrict the legal meaning of the head statement.

General

A proper assessment of any arrangements between 2 or more people (members) owning or leasing a racehorse to determine whether the scheme satisfies the definition of a managed investment scheme will include an analysis of its legal structure, the nature of the members' interests, and its modus operandi. If it satisfies the definition and is not exempt, then its promotion and operation will be subject to regulation, regardless of what is intended by the person promoting or operating the scheme.

1.2.2 Relevant case law

Australian cases

"Scheme"

In ***Burton v Arcus***[14], *Buss JA* said:

> ***"The proper approach to construction of the statutory provisions"***
>
> *[51] "It is settled law that the broad words of the definition of "managed investment scheme" should not be read down."*
>
> ***"The concept of a "scheme" within the definition of "managed investment scheme"***
>
> *[52] "The three elements in par (a) of the definition of "managed investment scheme" are prefaced by the words "a scheme that has the following features."*

In ***Australian Softwood Forests Pty Ltd v A-G (NSW); Ex Rel Corporate Affairs Commission*** *(the "**Australian Softwood case**")*[15], *Mason J* said:

> *[11] "In attempting to apply the statutory definition of "interest" to the transaction already outlined, we must ask ourselves, first, whether there is a "financial or business undertaking or scheme" and, secondly, what are its elements. We begin with the circumstance that the words in question are of wide import. For example, all that the word "scheme" requires is that there should be some programme, or plan of action……the statutory definition is not concerned with identity of the person or persons who carry it on. It is not material that the person who offers the "interests" to the public does not himself carry on the undertaking or scheme. Nor does it matter that by subscribing for an interest a member of the public will constitute himself as one who is engaged in carrying on the enterprise."*
>
> *[12] "……There is nothing in the notion of an undertaking or scheme that requires or implies that there is joint participation in everything comprised in the plan or that there must be a share or pooling of profits or receipts. (at p129)."*
>
> *[15] "There are real difficulties in the suggestion that the court can read down the very comprehensive definition of "interest" by reference to the supposedly unintended consequences of a literal reading on everyday commercial transactions. The definition is so general and all-embracing that it is impossible to say that it necessarily excludes particular transactions which appear to be covered by the general words. The hazards of adopting such a course are not dispelled by the absence of a supporting context. It would be different if we could glean from the legislative provisions an overall purpose which, being limited in scope, justified a reading down of the definition. Unfortunately in this case the search for a legislative purpose takes us back to the very words of the definition for the intended scope of the operative provisions depends so heavily on the comprehensive language of that definition. As Young C.J. observed in **A Home Away Pty Ltd v Commissioner for Corporate Affairs (1981) VR 475, at p 478**, in discussing the meaning of "interest" as defined in s.76(1): "If it were said that we should give effect to the purpose Parliament wished to achieve, we must first ascertain the purpose."*
>
> *[25] "Although, in the light of the conclusion I have reached in connexion with par (a), it is unnecessary for me to examine this question, I do so because it was fully argued. The argument is that in order to constitute a "common enterprise" there must be a joint participation in all the elements and activities that constitute the enterprise. I do not agree. An enterprise may be described as common if it consists of two or more closely connected operations on the footing that one part is to be carried out by A and the other by B, each deriving a separate profit from what he does, even though there is no pooling or sharing of receipts or profits. It will be enough that the two operations constituting the enterprise contribute to the overall purpose that unites them. There is then an enterprise common to both participants and, accordingly, a common enterprise. (at p133)."*

In ***ASIC v Enterprise Solutions 2000 Pty Ltd***[16], the promoter of a betting scheme who collected funds from Australian punters and bet them on horse races in Australia and Hong Kong using a proprietary hardware program, was held to be operating a managed investment scheme.

[14] (Appeal Judgement) [2006] WASCA 0071. Also see (Original Decision) [2004] WASC 244.
[15] (1981) 148 CLR 121.
[16] (2000) 35 ACSR 620.

An argument that the punters did not acquire any "interest" in a scheme and were only provided with betting services was rejected. The court said that the scheme involved rights to the benefits produced even though there was no assurance that the money invested would result in winning bets.

In ***ASIC v Chase Capital Management Pty Ltd***[17], *Owen J* said:

> *[57] "…The term "scheme" is not defined in the Law. Some guidance can be obtained* ***from Australian Softwoods Forests Pty Ltd v Attorney-General for the State of New South Wales (1981) 148 CLR 121 at 129****, where Mason J said, in the context of the term "interest" in the former* Companies *legislation: "… all that the word 'scheme' requires is that there be 'some programme, or plan of action'"*; and
>
> *[63] "… the 'scheme' is the entire operation…."*

In ***ASIC v Takaran Pty Ltd***[18], *Barrett J* considered the concept of a "scheme" within the definition. His Honour said, at 395:

> *[15] "The essence of a "scheme" is a coherent and defined purpose, in the form of a "programme" or "plan of action", coupled with a series of steps or course of conduct to effectuate the purpose and pursue the programme or plan. In some cases, the scope of the scheme will readily be gathered from some constitutive document in the nature of a blueprint setting out all relevant matters. In others, there may be no writing or such as there is may tell only part of the story, leaving the remainder to be supplied by necessary implication from all the circumstances. Profit-making will almost invariably be a feature or objective of the kind of scheme with which s9 definition of "managed investment scheme" is concerned, given the definition's references in several places to "benefits." Whatever is incidental and necessary to the pursuit of the profit (or "benefits") will therefore be comprehended by the scheme, including, it seems to me, steps sensible to counter risk of loss (or detriment). Every cogent plan caters for – or, at least, recognizes and takes into account – contingencies of an adverse kind*."
>
> *[16] "It must also be emphasized that a scheme having the characteristics bringing it within the s9 definition of "managed investment scheme" will not necessarily possess those characteristics alone.* ***In Royal Bank of Canada v Inland Revenue Commissioners [1972] Ch665****, Megarry J observed, in relation to the concept of "ordinary banking business", that "a statement of the essentials of a business does not seem to me, without more, to be exhaustive of all that is ordinary in that business." A managed investment scheme, like a banking business, may involve elements beyond the core attributes that give it its essential character. Elements which lie beyond those attributes but contribute to the coherence and completeness which make a "programme" or "plan of action" must form part of that "scheme." Every programme or plan of action must be taken to include the logical incidents of and consequences of and sequels to its acknowledged components."*

In the case of ***Re Risqy Limited***[19] it was held that the prospective benefit of earning interest at a promised specified rate was a benefit of the scheme and that this requirement of the definition of "managed investment scheme" was therefore satisfied.

"Partnership"

In ***ASIC v McNamara***[20], *Mansfield J* said:

> *[17] "It follows, in my view, that the offer by AAIS and JJM of units in AFLP, and the acquisition of units by limited partners, was an offer and acquisition of interests in a managed investment scheme."*
>
> *[41] "I do not think there is any inconsistency between the Act [Corporations Act] and the Partnership Act 1892 (NSW). The Act does not purport to regulate partnerships of themselves, but to regulate managed investment schemes. A managed investment scheme can take on a number of forms, determined upon by the promoters of the scheme. It happens that in this particular case the scheme is in the form of a limited partnership, and to that extent in my view the Act is able to operate in relation to the scheme itself. It does*

[17] (2001) 36 ACSR 778.
[18] [2003] 1 Qd R 135 at 146.
[19] [2008] QSC 107.
[20] [2002] FCA 1005.

not involve the Act purporting to do something inconsistently with rights granted under the Partnership Act 1892 (NSW)…."

[44] "…S 109 of the Constitution provides that where there is an inconsistency between a law of the Commonwealth and a law of a State, the State law is invalid (or, in a practical sense), inoperable) to the extent of the inconsistency. Therefore, even if an inconsistency between the laws were apparent, the Act must operate to diminish the scope of the Partnership Act 1982 (NSW)."

"Co-ownership"

See ***Stewart v Spicer Thoroughbreds Pty Ltd***[21].

First element

In ***Burton v Arcus***, *Buss JA* said:

"The first element in par (a) of the definition of "managed investment scheme"

[55] "The first element of para (a) of the definition requires that:

a) "people contribute money or money's worth"; and

b) the money or money's worth be contributed "as consideration to acquire rights … to benefits produced by the scheme … "

[56] "This element was described in para 19.6 of the memorandum to the Managed Investments Bill 1997 as "incorporating a positive element in the definition". In other words, the money or money's worth must be contributed for the purpose of acquiring the relevant rights to benefits."

[57] "The word "contribute" means, in this context, to pay or supply. It is implicit in the first element in par (a) of the definition, in the context of the definition as a whole and the provisions of Ch 5C, that the people will pay or supply the money or money's worth to or as directed by the promoter or operator of the scheme."

In ***Crocombe v Pine Forests of Australia Pty Ltd***[22], *Young CJ* said:

[49] "I agree with Mr Foster that, generally speaking whilst it is clear that in interpreting the definition of managed investment scheme the Court is encouraged to take a broad view."

[50] "Doing this, it would seem to me that the mere fact that parties contribute their interest in land rather than cash means they still contribute in money's worth."

[51] "Mr McHugh further submitted that even if land did fall within the phrase, the Corporations Act required that people contribute money's worth. He put it that here the "investors" received land, they did not contribute anything. What was necessary for land to be "contributed" would be a transfer at law or in equity to someone."

[52] "Mr Foster put:

"The language of the Corporations Act 2001 does not warrant this conclusion. At the very least, at the outset, the initial members of the scheme were bound in contract to contribute their interests in the Land and their interests in the trees on the Land to the scheme. The fourth defendant, upon taking a transfer of some interest in the Land, continued to be bound by those contracts. The Fourth Defendant was well aware of the terms upon which the original owners had taken an interest in the Land and had repeatedly propounded the idea that the Land had to be dealt with upon the basis that it was to be pooled in the interests of all tenants in common and managed as a scheme. It must be taken to have become bound to the same contractual obligations by novation."

[21] n 27, at p 24.

[22] (2005) 219 ALR 692; [2005] NSWSC 151

"The Land and the interests of all tenants-in-common had to be pooled and made available for the purpose of the scheme: the requirement was contractual and bound all relevant parties. Alienation of the Land is not required."

[53] "In my view Mr Foster's submissions are sound."

[54] "It should be further noted that the Courts have taken a wide view of "contributions" in this area of the law: ***ASIC v Enterprise Solutions 2000 Pty Ltd*** *[2000] QCA 452; (2000) 35 ACSR."*

Also see ***Stewart v Spicer Thoroughbreds Pty Ltd***[23]*,* at *[24].*

Second element

In ***Burton v Arcus***, *Buss JA* said:

"The second element in par (a) of the definition of "managed investment scheme"

[58] "The second element in par (a) of the definition has three aspects:

(a) the contributions or some of them "are to be pooled, or used in a common enterprise";

(b) the purpose of the pooling, or use in a common enterprise, must be "to produce financial benefits, or benefits consisting of rights or interests in property"; and

(c) those benefits must be produced "for the people … who hold interests in the scheme (whether as contributors or as people who have acquired interests)."

[59] "The word "pooled" and the expression "to be pooled" in the second element in par (a) of the definition were considered by Douglas J in ***Australian Securities and Investments Commission v Enterprise Solutions 2000 Pty Ltd*** *(1999) 33 ACSR 403, and on appeal by the Court of Appeal of Queensland: [2003] 1Qd R 135."*

[60] "In Enterprise Solutions 2000 Pty Ltd, the activities which were held to be managed investment schemes comprised off-course punters giving money to either the second or the fifth appellant, pursuant to betting agency agreements, to bet on their behalf, on horses selected by the fourth appellant, with the assistance of a betting system. There were hundreds of participants in the scheme, and the money they contributed was deposited in two bank accounts. The moneys in the accounts were used to pay management fees payable under the betting-agency agreements, to place bets, to maintain credit balances with betting agencies, and to pay moneys due to the scheme investors. By the betting-agency agreements, the investors appointed one or other of the appellants to be their agent, and various duties were imposed in the agent, including a duty to pay moneys due to the investors. The procedure to the placing of bets was summarized in the judgement of the Court of Appeal at 142 [3]:

> *"Each bet is placed by and in the name of Mr Rebbeck [one of the appellants] and is placed on behalf of all of the investors covered by the relevant agreement, subject to the possibility that an investor may request exclusion from a day's betting or some other variation; such requests are usually accommodated, but can be disallowed. Subject to the possibility of the allowance of such a request, the investors have no control over either the amounts bet, or the selection of horses on which the bets are placed."*

[61] "The Court of Appeal noted, at 144 [9], that the words "pool" and "pooled" may be used with reference to "a fund made up of numerable payments from participants and used for a purpose they contemplate". The Court of Appeal also noted, at 144 [8], that pooling will occur where moneys paid or supplied by people are collected in a bank account."

[62] "The significance and application of the word "pooled", in the context of the second element in par (a) of the definition, was explained by the Court of Appeal at 144 [10] – [11]:

[23] n 27, at p 24.

> *"There is, according to the appellants' argument, no trust relationship between the holders of the bank account (in which monies are, the respondents, say, pooled), on the one hand, and the investors on the other. If that is right, then it would follow that, in the event of winding-up, of the account-holders, all the monies would go to the liquidators and the investors would have no right to a refund of any mommies paid in; that does not appear to be correct:* ***Barclays Bank Ltd v Quistclose Investments Ltd*** *[1970] AC 567. Apart from that, there is no reason to think that the use of the expression 'pooled' as to be confined to instances in which the contributors have a proprietary interest; so to hold might exclude from the definition schemes in which monies are in the ordinary sense 'pooled' for the purpose of investment, but the contributors expressly agree that they have no proprietary rights, but only rights in contract."*
>
> *"Another reason for rejecting, as we do, the submission that the contributions are not 'pooled' unless the result is to give the contributors property rights in the pool is that para (ii) quoted above contemplates that the contributions 'are to be pooled … to produce financial benefits ,* ***or*** *benefits consisting of rights or interests in property …'. The benefits, consisting of monies to come to the contributors out of the pool, need not be proprietary rights. And the 'rights' acquired need not even be enforceable, let alone proprietary."*

[63] "The Court of Appeal rejected, at 145 [13], an argument by the appellants that "a scheme for the collection and investment of funds cannot be a managed investment scheme (absent any 'common enterprise') unless it can be shown that the percentage return on investment in pooled money is expected to be higher than the return which would have been gained if the identical investment had been made by each individual contributor, using his or her own money". Their Honours said:

> *"The words 'to be pooled … to produce in para (ii) quoted above imply that the intention must be to pool the contributions and, by use of the pool, produce benefits; they do not imply that the benefits must be of such a kind as to be unobtainable without pooling."*

[64] "The Court of Appeal also rejected another argument by the appellants to the effect that the words "to be" in par (a)(ii) of the definition require that the scheme investors appreciate that their contributions are to be pooled. Their Honours said, at 145 [13]:

> *"That contributions would be dealt with in that way is obvious; <u>but in any event under the scheme pooling occurs and that is enough</u>." [emphasis added]*

[65] "In ***Australian Securities and Investments Commission v Young*** *(2003) 173 FLR 441 at 449 [43], Muir J expressed the following view, in relation to "pooling":*

> *"… the concept of 'pooling' for the purposes of s9(a)(ii), imports contributions to a discernible fund the moneys in which are to be used in an identifiable way to provide prescribed benefits to the contributors."*

Muir J then noted that his analysis "may be a little narrow", in the context of the observations of the Court of Appeal in ***Enterprise Solutions 2000 Pty Ltd*** *and of Barret J in Takaran, but it was sufficient for the purposes of the proceedings before his Honour. His Honour said, at 449-45- [44]-[46]:*

> *"Under the terms of the loan agreements … the moneys were agreed to be used for the benefit of a disparate group of persons and corporations with different interests. There was no expressed right on the part of the lenders to have the loan moneys used for the development in respect of the which they made the loan. The moneys could not therefore be regarded as pooled. For similar reasons, if regard is had only to the documentation, it is possible to conclude that the loan moneys are to be 'used in a common enterprise'. The moneys may be used in a variety of ways, assuming that it is possible to fulfill the obligation created by the clause under consideration, but there may be no commonality about the enterprise or enterprises in which the moneys are employed. Some club members and respondents may benefit more than others and at different times and in many different ways. Any benefit received by the lenders may bear no relationship to the loan moneys advanced and so on.*

> *Notwithstanding the wording of the loan agreements however, the respondents appropriate the money received from club members in respect of a particular development to that development and, where real property was acquired for the purpose of the development, used such moneys for its acquisition. It may be inferred that this was done pursuant to a pre-determined plan or course of action by the first and second respondents.*
>
> *In those circumstances the loan moneys were in fact pooled to produce financial benefits. … "*

[66] "In ***Australian Securities and Investments Commission v Drury Management Pty Ltd*** *[2004] QSC 068, Jones J held that there could be a "pooling" of contributions within par (a)(ii) of the definition, even though the scheme investors were unaware that the scheme promoter intended to pool their contributions, His Honour said, at [24]:*

> *"To suggest that for s9(a)(ii) to be satisfied, there needs to be a fund in the mind of a contributor, knowledge of an intention to pool the contribution, is, in my view, to impose an unwarranted restriction on the ordinary meaning of the words used in the definition, The cases to which I have been referred do not suggest otherwise. The point was authoritatively determined by the Court of Appeal in* ***ASIC v Enterprise Solutions 2000 Pty Ltd*** *…"*

"Jones J then referred to the observations of the Court of Appeal in ***Enterprise Solutions 2000 Pty Ltd****, at [13]. In particular, his Honour emphasized the statement by the Court of Appeal that "under the scheme pooling occurs and that is enough". Jones J concluded, at [25]:*

> *"The features that contributions 'are to be pooled' is in my view satisfied in this case by the fact that pooling occurred. …"*

[67] "In ***D.K.L.R. Holding Co (No 2) Pty Ltd v The Commissioner of Stamp Duties (New South Wales)*** *(1982) 149 CLR 431 at 439, Gibbs CJ explained that the words "to be", before a past participle, and used in relation to a noun, can express obligation, intention, possibility or simply futurity. The sense in which the words "to be" are used, in any case, depends on the context in which they appear."*

[68] "In my opinion where:

(a) people have paid money to or as directed by the promoter or operator of a scheme (as contemplated by the first element in par (a) of the definition);

(b) the promoter or operator intends to pool, or does in fact pool, the money; and

(c) the pooling occurs without the agreement, approval or knowledge of the people who paid the money,

the feature in the second element in par (a), that the moneys (or contributions) "are to be pooled", will be satisfied."

[69] "If the promoter or operator of a scheme in fact pools money contributed by people, and the pooling occurs without their agreement, approval or knowledge, the promoter or operator will have formed the intention prior to the pooling, that the pooling should occur or become a characteristic of the scheme. When this intention is formed, it may properly be said that the contributions of the people "are to be pooled" within the second element in par (a) of the definition."

[70] "In my opinion, the concepts and language in par (a) of the definition do not expressly or impliedly require that any pooling occur with the agreement, approval or knowledge of the people who have paid or supplied the money or money's worth. A scheme will not avoid characterization as a "managed investment scheme", within par (a) of the definition, where the promoter or operator intends to pool, or does in fact pool, money or money's worth, without the agreement, approval or knowledge of the people who have contributed it."

[71] "It is unnecessary for the purpose of this appeal, to consider the concept of a "common enterprise" in par (a)(ii) of the definition."

In ***WA Pines Pty Ltd v Hamilton***[24], *Jones J* said:

> *"… as to 'common enterprise', in my opinion that phrase is apt to cover not only an enterprise in common with other investors, but also an enterprise in common with the investor and the promoter*."

Also see ***Stewart v Spicer Thoroughbreds Pty Ltd****,* at *[24].*

Third element

In ***Burton v Arcus***, *Buss JA* said:

> ***"The third element in para (a) of the definition of "managed investment scheme"***
>
> *[72] "The third limb element of the definition requires that the members not have "day to day control over the operation of the scheme", whether or not they have the right to be consulted or give directions."*
>
> *[73] "The term "day-to-day" connotes routine, ordinary, everyday. See The Shorter Oxford Dictionary (1993), page 598; The Macquarie Dictionary (Third Edition), page 492."*
>
> *[74] "As the Privy Council observed in* ***Bermuda Cablevisions Ltd v Colica Trust Co Ltd [1998] AC 198 at 207****, expressions such as "control" take their colour from the context in which they appear: there is no general rule as to the meaning of the word "control". The expression "day-to-day control" is not a term of art. It must be given the meaning which the context requires. …."*
>
> *[75] "In* ***ASIC v IP Product Management Group Pty Ltd*** *(2002) 42 ACSR 343*, *Byrne J considered the third element, and observed, at 348 [22], in relation to the expression "day-to-day control":*
>
> > *"It will be recalled that under paragraph (iii) the existence of a right in a member to be consulted or to give directions as to the operation of the scheme does not necessarily lead to the conclusion that that member has day-to-day control over its operation. The law contemplates, therefore, some greater involvement."*
> >
> > *"After referring to the documents relating to the scheme the subject of the proceedings in IP Product Management Group, his Honour stated at, at 348 [22]:*
> >
> > *"As a matter of legal right, it is clear that the members have no legal right to day-to-day control over the operation of the scheme. The evidence shows, too, that they exercised no such control as a matter of fact. For the most part, the operation of the scheme was conducted in places distant from the residences of the investors and there is no evidence that, having paid their money, they took any interest in the detail of its operation."*
>
> *[76] "In* ***ASIC v Chase Capital Management Pty Ltd (2001) 36 ACSR 778,*** *Owen J considered whether scheme investors had day-to-day control of an investment scheme in circumstances where the investors delegated "management" of the scheme to a company related to the promoters. His Honour said, at 79 [67]:*
>
> > *"The question is whether the members have day-to-day control. It is not difficult to discern the distinction that the legislature was attempting to make. Very broadly, it is between the investment activities of an individual and that of a group. By the express terms of the applications, the investors have delegated "management" of the investment to CCML. There is no reservation of day-to-day or any other control or functions. I am not sure that the appointment of a committee of some of the investors to monitor the investments would make much difference. The question still remains: who has the day-to-day control."*
>
> *[77] "In* ***Australian Securities and Investments Commission v Pegasus Leveraged Options Group Pty Ltd*** *(2002) 41 ACSR 561, the first defendant, Pegasus Leveraged Options Group Pty Ltd, was established by the second defendant, Mr McKim, and attracted investors from numerous by offering exorbitant rates of return. Each of the investors was*

[24] [1980] SCWA

informed that his or her money would be used, together with the moneys of other investors, in a business transaction or transactions, which would create profits sufficient to enable Pegasus to pay the rate of interest which was promised. Davies J held that each investor had invested in a managed investment scheme. His Honour found, at 750 [32], that there was no doubt that the investor did not have day-to-day control over the operation of the scheme. Davies AJ also found that Mr McKim contravened the statute, by operating the managed investment scheme which was unregistered. His Honour also considered the meaning of "operate" in the context of s601ED, and said, that, at 574 [55] – [56]:

> *"The word "operate" is an ordinary word of the English language and, in the context, should be given its meaning in ordinary parlance. The term is not used to refer to ownership or proprietorship but rather to the acts which constitute the management of or the carrying out of the activities which constitute the managed investment scheme. The Oxford English Dictionary gives these relevant meanings:*
>
> *"5. To effect or produce by action or the exertion of force or influence; to bring about, accomplish, work.*
>
> *6. To cause or actuate the working of; to work (a machine, etc). Chiefly, US.*
>
> *7. To direct the working of; to manage, conduct, work (a railway, business etc); to carry out or through, direct to an end (a principle, an undertaking, etc). orig. US."*
> *"I have concluded that Mr McKim operated the managed investment scheme. He was the living person who formulated and directed the scheme and he was actively involved in its day to day operations. He supervised others in their performance.*
>
> *I have also concluded that Mr McKim is not exempted by s601ED(6). He did not "merely" act as the agent or employee of the Pegasus. He was the directing mind and will of Pegasus and of the scheme."*

[79] "In my opinion, the third element in para (a) of the definition is concerned with control in fact as distinct from the legal right to control. It is also concerned with control in fact by the members of a scheme as a whole. The members as a whole may not have control in fact even though the constructive document for the scheme may confer on them the legal right to control."

[80] "The members of a scheme will have "day-to-day control over the operation of the scheme" if:

(a) the members as a whole participate in making the routine, ordinary, everyday business decisions relating to its management; and

(b) the members as a whole are bound by the decisions which are made."

"Conversely, if the members as a whole do not participate in making the routine, ordinary, everyday business decisions relating to the management of the scheme or if the members as a whole are not bound by the decisions which are made, they will not have day-to-day control over its operation."

[81] "The concept of "day-to-day control over the operation of the scheme", within para (a) of the definition, does not, of course, require that there be activities in relation to the scheme on each and every day or even on most days during the term of the scheme."

[82] "In my opinion, the circumstance that the promoter or operator of a scheme manages the scheme (or certain aspects of it) on behalf of the members does not mean that the members by their agent, the promoter or operator, have day-to-day control in fact over the operation of the scheme. In other words, the management activities of the promoter or operator in relation to a scheme are not to be imputed to the members in determining whether the members have such day-to-day control."

[83] "My construction of the third element in para (a) of the definition gives effect to the evident legislative purpose or object embodied in the definition and Ch 5C. If:

(a) the third element in para (a) of the definition was concerned with the legal right to control and not control in fact; or

(b) the management activities of the promoter or operator in relation to the scheme were to be imputed to the members in evaluating whether the third element was satisfied or not, with the consequence that if the promoter or operator had "day-to-day control over the operation of the scheme" then the members, by their agent, the promoter or operator, would have day-to-day control;

the legislative framework for the regulation of managed investment schemes would be seriously, if not entirely, eroded."

In ***Burton v Arcus***, *McClure JA* said:

[2] "I have had the advantage of reading the judgement of Buss JA. I agree that the appeal should be upheld for the reasons he gives. I propose to make some additional observations on the third limb of the definition of managed investment scheme, namely whether the members had day-to-day control over the operation of the scheme. This limb of the definition links the prohibition in s601ED(5) and the relief (winding up) in s601EE of the Corporations Act 2001(Cth). Under s601ED(5) a person must not operate a managed investment scheme unless it is registered. If a person operates an unregistered managed investment scheme, that scheme can be wound up under s601EE. The word "operate" in the context of s601ED(5) and s601EE is to be given its ordinary meaning. The term is not used to refer to ownership or proprietorship but rather to acts that constitute the management of or the carrying out of the activities comprising the managed investment scheme: see ***Australian Securities and Investments Commission v Pegasus Leveraged Options Group Pty Ltd (2002) 41 ACSR 561 at 574****."*

[3] "The appellants contended that Global Finance Group Pty Ltd ("Global") operated the private contributory mortgage investment scheme to which the appellants and respondents were parties ("the Newrose scheme") and that it was a managed investment scheme as defined. If the investors collectively had the day-to-day control of the operation of the Newrose Scheme, it could not be said that Global operated the scheme (see s601ED(6) which provides that a person does not operate a scheme merely because he is acting as an agent or employee for another)."

[4] "A managed investment scheme must be registered prior to commencement of the operation of the scheme. The phrase "day-to-day" means routine, ordinary, everyday management or operational decisions. I am of the view that the term "control" in the definition means authority to decide and direct and not merely to participate in decision-making."

[5] "The respondents rely on two related submissions on the issue of day-to-day control. First, they contend the investors had control of all relevant matters which the identify as the nature, terms and conditions of the investment, whether to extend the term of the investment and matters relating to enforcement on default. Secondly, they contend that Global's role in the operation of the scheme was purely administrative and involved no decision-making in its implementation or operation. They identify Global's role in the operation of the scheme as confined to acting as a mere conduit for the payment of interest and the return of capital at the end of the term of the investment."

[7] "The appellants contended that Global's authority to administer the mortgage extended to enforcement upon breach. That would encompass decisions about whether and if so when to issue a notice of demand or default notice, whether to enter into possession of the mortgaged property or sell it or whether to commence proceedings. Without Global having such authority, the mortgagees could only take action under the mortgage if they all agreed to the proposed course of action."

[8] "The need for unanimity is a very significant practical impediment to acting in relation to, or under, the mortgage. I accept that is the commercial reason for the investors' express delegation to Global of authority to administer all matters relating to the mortgage. It would be impractical for all the investors to control the implementation of what had been agreed between each investor and Global and what was agreed in the mortgage…."

[9] "First it is necessary to identify the plan or scheme in question. Global carried on the business of promoting and arranging private contributory mortgage investments…."

[10] "That brings me to the issue of Global's role in the Newrose scheme. It is apparent from the affidavit evidence on which the appellants relied that the question whether Global

was in day-to-day control of the operation of the scheme was not understood to be a live issue. The evidence is scanty and incidental. Much depends on inference. What is clear is that Global initiated and promoted the Newrose scheme to a wide range of potential investors numbering more than 20. The promotion of the investment involved the provision of positive information and opinions as to the prudence of the investment. All contact relating to the Newrose scheme was between the individual investor(s) and Global. The investors did not know or deal with each other before the commencement of the operation of the scheme. During the term of the Newrose scheme, the identity of investors changed (by assignment of a share in the mortgage) without reference to the other investors. The change was organized and facilitated by Global."

[11] "Further, it can be inferred from the evidence that after acceptance of Global's offer and the payment of their investment contribution, the investors had no involvement in the management of the investment until after Global went into administration in February 1999. Thereafter it went into liquidation. It is the case that at some stage after Global went into administration the investors who were mortgagees at that time assumed day-to-day control over the Newrose scheme. However, that does not affect the position at the inception of the Newrose scheme until February 1999 or whether the mortgage is scheme property."

[12] "From the time of receipt of the investors' funds, Global acted in a variety of ways without reference to or direction from the investors…."

[16] "It is apparent from the above that the investors delegated significant management functions to Global. Although there were few discretionary decisions, other decisions involved evaluative judgements bearing a similarity to discretionary decisions. Still other decisions were supervisory in nature but fell short of being purely pro forma in nature. Indeed, the nature and extent of Global's day-to-day control in operating the Newrose scheme and other similar schemes resulted in widespread breaches of its express and implied duties to investors … I do not rely on Global's misconduct as establishing day-to-day control. Rather it demonstrates that its day-to-day control of management provided it with the opportunity to engage in systemic misconduct."

"… I am satisfied that Global had day-to-day control over the operation of the Newrose scheme."

In ***Enviro Systems Renewable Resources Pty Ltd v Australian Securities & Investments Commission***[25], *Martin J* said:

[36] "In my opinion, when the scheme documentation is analysed in its entirety, the intent of the scheme is that Enviro will control the day-to-day operations of the scheme from beginning to end. Enviro offers a total package which is presented in such a way that potential participants are encouraged to take up the entire package. Notwithstanding the assertions that participants will be running their own businesses. Enviro does not intend that the participants should take an active role in the day-to-day operations of any aspect of the scheme. The success or otherwise of the scheme is entirely dependent upon Enviro. In reality, although it is possible that some participants may choose to take an active role, the scheme is designed to attract passive investors."

[37] "The purpose or object of the legislation and the regulatory regime created pursuant to the legislation would be easily defeated if the court felt obliged to rely solely upon a strict view of the legal rights and duties created by the documentation and was required to ignore the realities of the scheme as it was designed to operate in practice."

In ***ASIC v Pegasus Leveraged Options Group Pty Ltd & Anor***[26], ASIC sought declarations that the defendants (Pegasus and its sole director Mr McKim) had breached numerous provisions of the Corporations Act including for operating an unregistered managed investment scheme. Mr McKim was caught by the prohibition against operating an unregistered managed investment scheme since he formulated, directed, and was actively involved in the day-to-day operation of the scheme.

In ***ASIC v Pegasus****, Justice Davies* also said:

[25] [2001] SASC 11.
[26] [2002] NSWSC 310.

[56] "… I have also concluded that Mr McKim is not exempted by s601ED(6). He did not "merely" act as the agent or employee of the Pegasus. He was the directing mind and will of Pegasus and of the scheme."

The only industry specific case law found by the writer which provide authoritative guidance as to whether or not horse racing schemes satisfy the definition of a managed investment scheme are:

(a) ***Stewart v Spicer Thoroughbreds Pty Ltd***[27]. In this case, *Justice Black* made various orders, including declarations to the effect that:

(i) the three (3) horse racing schemes the subject of the proceedings were managed investment schemes within the meaning of section 9 of the Corporations Act; and

(ii) the First Defendant (that is, Spicer Thoroughbreds) contravened section 601ED(5) of the Act by operating the schemes, which were required to be registered pursuant to section 601ED(1) of the Act, but were not so registered.

Justice Black said:

[24] "… I am satisfied that the first limb of the definition is satisfied, where co-owners contributed funds to the purchase of interests in the horse, and plainly did so to acquire prospective and contingent benefits by way of income from racing the horse and from other uses of the horse such as putting it to stud, and then applied their interests in the horses for that common purpose. I also accept that the second limb is satisfied where the relevant funds, and the interests in the horses acquired by them, were used in the common enterprise of the owners acquiring and racing the relevant horses, which was "an enterprise common to participants and, accordingly, a common enterprise": Brookfield Multiplex at [94]-[98]."

[29] "It seems to me that the Rules, and particularly AR57(2) (as at 12 January 2018 and 7 January 2019) and AR 63(2) (as at 1 February 2022), the prescribed Co-Owner Agreement and the practical arrangements by which the horses were placed under the management of trainers, were sufficient to deprive the owners collectively of day-to-day control of the horses. I therefore accept that Mr Stewart and the other owners did not have day-to-day control over the operation or management of the three horses, less by reason of the services which Spicer Thoroughbreds provided, than by reason of the Rules which provide for such control be exercised by a managing owner, a single person, who was Mr Spicer in the case of two schemes, and the trainer rather than by owners generally in specified matters. …."

[45] "… However, the parties seem to me to have conducted the case on a wider basis than Mr Stewart's pleaded case that Spicer Thoroughbreds "managed" the horses and addressed the question whether Spicer Thoroughbreds "operated" the Schemes by a review of the whole of its conduct, including its dealings with trainers and the co-owners. That approach is consistent with the scope of s 601ED(5) and I proceed on that wider basis. It seems to me that Spicer Thoroughbred's activities in respect of the Schemes, including at least the communications with co-owners and the trainer, amounted to carrying out the activities of the scheme and incidental activities sufficient to constitute "operating" the scheme for the purpose of s 601ED(5). Where I have held that the Schemes fell within the definition of "managed investment scheme" and an exception to the registration requirements has not been established, then it has been established that Spicer Thoroughbreds contravened s 601ED(5) of the Act in this respect."

(b) <u>The activities that constitute the act of "training" a racehorse and the person in "control" of those activities</u>

Racing NSW v Vasili[28] This case involved charges that were the subject of prior hearings against licensed trainer *Mr Con Karakatsanis* and registered owner *Mr Angelis Vasili*, it being determined that *Mr. Vasilis* was in fact the trainer of various horses owned by him when he was not the holder of a current trainer's licence and that he improperly held licensed trainer *Mr. Karakatsanis* out to be the trainer of those horses. In his judgement,

[27] [2022] NSWSC 310. Note: this case is currently subject to a Notice of Intention to Appeal by the First Defendant (Spicer Thoroughbreds) which must be filed by 20 August 2022.
[28] Racing Appeals Tribunal NSW 12 June 2019.

Mr. Armati referred to two Queensland decisions which were referenced in submissions in the following terms:

> *[78] "…The Appeal Panel referred to these cases in the following terms:*
>
> *"21 …Racing Appeal Authority Queensland … The appeal of Mrs Julie Nash, a decision handed down 8 January 2001, the Authority described training in the following way:*
>
> > *"There is no single action that provides and defines the concept of training a racehorse. Training encompasses a range of tasks that collectively make up the practice of training a thoroughbred. These include feeding, grooming, caring, stabling, treating, exercising, setting trackwork regimes, assessment of form, nominating, accepting and an increasing list of singular minor tasks. A trainer that participates in all the tasks can, when considered collectively, make up the practice of training."*
>
> *"22 …Racing Appeal Authority in the Appeal of Robert Heathcote, delivered on 18 June 2002:*
>
> > *"As has been commented on above, there are numerous tasks which make up the training of a racehorse. To these should be added that the essential matter which relates to who is the person training a racehorse, is who is the person in "control" of the horse. The meaning of "control" in this context is simply not the physical control of the horse but who has the dominance in those non-exhaustive activities referred to in the decision of Nash that make up the act of training."*

UK cases

Once regarded as the leading UK case in relation to precisely what constitutes "day-to-day control" is that of ***Andrew Brown (and others) v InnovatorOne PLC (and others)***[29].

The relevant aspects of this case centered on the meaning of "… *day-to-day control over the management of the property*" under *the Financial Services and Markets Act 2000 (UK), (FSMA),* which is the UK equivalent of the Australian legislation.

In ***Andrew Brown v InnovatorOne***, *Justice Hamblen* said:

> *[1166] "The crux of this issue was whether the Schemes met the negative "day-to-day control" requirement in s.235(2) – "The arrangements must be such that the persons who are to participate ("participants") do not have day to day control over the management of the property, whether or not they have the right to be consulted or give directions."*
>
> *[1167] "As already found, it was the understanding of the individual Defendants that the schemes were not CIS's because of the second advice of Mr Crystal and the amendments to the documentation made in consequence. In particular, it was believed that the investors had the requisite "day to day control over the management of the property" of the scheme."*
>
> *[1168] "There was and remains a lack of clarity as to what the "day-to-day control requirement means. This is illustrated by the July 2008 report of the Financial Markets Law Committee ("FMLC") entitled "Operating a Collective Investment Scheme: Legal assessment of problems associated with the definition of Collective Investment Scheme and related terms" written by a Working Group chaired by Mr Michael Brindle QC."*
>
> *[1169] "The role of the FMRC is to identify issues of legal uncertainty on the framework of the wholesale financial markets. Under the heading 'Legal uncertainties in the definition of CIS', the report states: "The notion of 'day-to-day control' is vague and FSMA does not give any further guidance on how it should be interpreted. Furthermore, the phrase "whether or not they have the right to be consulted or to give directions", which purports to clarify the "day-to-day control of the property" notion, is also obscure. There is no clear picture as to which level of control the "right to be consulted or to give directions" encompasses" (para 2.5). More specifically, the report comments as follows (para 3.9):*

[29] [2012] EWHC 1321.

> *"Day-to-day control over the management of …" is not a wholly easy concept. "Control over the management of…" is presumably intended to be distinguished from "management of …" i.e. arrangements will not qualify simply because the participants do not manage the property themselves. On the other hand "day-to-day control" must clearly mean more than "have the right" to be consulted or give directions." In Elliott, Laddie J referred in "colloquial terms" to "minding the shop." In practice it is not always easy to apply the test, though it appears as a minimum the participants should be in a position to tell the person who is actually managing the property what to do on a day-to-day basis."*

Justice Hamblen then confirmed that it is not the right to exercise control – but the actual exercise – that is important.

> *[1170] "In the present case the Claimants were in a position to tell Mr Carter, the person actually managing the property, what to do on a continuing day to day basis. They could have exercised that control at any time. However, I agree with the Claimants that more is required and that they must actually exercise that control sufficiently to be regarded as being in effective control. It is necessary to look beyond the documents which may provide for "day-to-day control" by investors and to consider how the scheme was designed to and did operate in practice. This is borne out by the Australian case of* ***Enviro (2001) 36 A.C.S.R. 762*** *in relation to the similar "day-to-day control" test under the Australian definition of the equivalent to a CIS. In his judgment Martin J stated as follows:*
>
> *[37] "…"*[30]*.*

Justice Hamblen found that the investors did not give directions or assert their rights to exercise day-to-day control sufficiently to be regarded as being in effective control over the management of the property and rejected an argument that this was the investors' choice, instead holding that:

> *[1171] "… the degree of control actually exercised was as envisaged by the [marketing documents] and the documentation. It was thought that the documentation would mean that that degree of control was sufficient, but I find that it was not."*

Justice Hamblen also found that:

(a) establishing such schemes was a regulated activity; and

(b) such schemes were collective investment schemes from the point in time when the investors paid their subscription money rather than from some later point in time when the members failed to exercise day-to-day control sufficiently to be regarded as being in effective control over the management of the property [see paragraphs *[1172]* to *[1179]* of judgement].

In relation to the observations of the FMRC referenced in paragraphs *[1168]* and *[1169]* of that judgement, those observations should be reviewed alongside the observations of the Financial Conduct Authority (FCA) subsequently published in its ***FCA Handbook (UK) [2014]***. See ***Perimeter Guidance – Chapter 11: Guidance on property investment clubs and land investment schemes – PERG 11.1. [Background] and PERG 11.2 [Guidance on property investment clubs]***, and particularly the answers to Q4, Q6, and Q12.

Chapter 11 is concerned with the rights of the members of some property investment clubs (sometimes known as buy-to-let schemes, buy-to-let syndicates, or property investment syndicates) in the UK, where the members have been considered to have control over the day-to-day management of the property:

> *"Q.4: What is a collective investment scheme and will my property investment scheme be one?*
> *Broadly speaking, a collective investment scheme is any arrangement:*
> • *the purpose or effect of which is to enable those taking part (either by owning the property, or part of it, or otherwise) to participate in or receive profits or income arising from the acquisition, holding, management or disposal of the property;*
> • *where persons taking part do not have day-to-day control over the management or disposal of the property;*

[30] ibid, n 25, at p 24.

- *where either the contributions and profits or income are pooled, or the property is managed as a whole by or on behalf of the operator of the scheme, or both.*

Whether your property investment club is a collective investment scheme or not will depend on its individual structure and the facts surrounding it. If your club meets each of the above conditions and is not exempt, then its operation and promotion should come under FCA regulation. This is regardless of whether that was intended by the person operating or promoting the club."

"Q.6: What is the purpose of the day-to-day control test and the nature of day-to-day control?
The purpose of the day-to-day control test is to try to draw an important distinction about the nature of the investment that each investor is making. If the substance is that each investor is investing in a property whose management will be under his control, the arrangements should not be regarded as a collective investment scheme. On the other hand, if the substance is that each investor is getting rights under a scheme that provides for someone else to manage the property, the arrangement would be regarded as a collective investment scheme.
Day-to-day control is not defined so must be given its ordinary meaning. In our view, this means, you have the power, from day-to-day, to decide how the property is managed. You can delegate actual management so long as you still have day-to-day control over it."

"Q.12: I run a scheme where each person owns individual properties or parts of properties in the property investment club either directly or indirectly (for example, through a limited liability company or a limited liability partnership of which he is the owner or through a limited liability partnership). … Is this scheme a collective investment scheme?
No, unless the properties belonging to each person, company or limited liability partnership are managed as a whole by or on behalf of the operator of the scheme. … This is provided the operator is managing each property on an individual basis.
... As an example, if a managing agent manages a block of flats on the basis that the only profit or income each individual flat owner obtains is what arises from the management of his property, there is no management as a whole. However, if the managing agent managed the flats in such a way that each individual flat owner received an income from total lettings, regardless of whether that person's flat was let or not, the properties are managed as a whole and the arrangements are likely to be a collective investment scheme."

Prior to the decision in ***Andrew Brown v InnovatorOne***, the leading case on the interpretation of the provisions of Section 75 of the Financial Services Act 1986, which Section 235 of the FSMA repeats virtually exactly, was that of ***The Russell-Cooke Trust Company v Elliott***[31].

In ***Russell-Cooke v Elliott*** it was held that to fall outside Section 235(2) [the definition of collective investment scheme] the arrangement must be such that all the participants have day-to-day control of the property. If even one of them did not, then it would be a collective investment for all of them since arrangements could not be a collective investment for some participants and not for others. If any of those involved in arrangements caught by Section 235(1) are passive investors, it would appear sub-section (2) will therefore be satisfied.

Both of those cases have now to some degree been superseded by the Supreme Court case ***Asset Land Investment PLC v FCA***[32]. In this case, the approach adopted by *Lord Sumption* in his judgement in relation to determining "*day-to-day control over the management of the property*" is more nuanced and makes it clear that the objective assessment is temporarily limited to the point in time when the arrangements were made.

Asset Land v FCA involved a land-banking arrangement pursuant to which the appellant company Asset Land Investments Plc (AL) acquired greenfield sites and sold them to investors in small parcels (plots). Despite various disclaimers in the documents, there was a clear understanding between AL and the investors that:

(a) AL would:

(i) move to have the whole property rezoned for housing development; and

[31] [2001] All ER (D) 300 (Mar). No 1, 26 March 2001, unreported and No 2, 16 July 2001, unreported.
[32] [2016] UKSC 17. On appeal from: [2014] EWCA Civ 435. Unlike Australia, the Supreme Court is the final court of appeal for civil cases in the UK and is a superior court to the High Court which heard both *Brown v InnovatorOne* and *Russell-Cooke v Elliott.*

(ii) [when that was done] would arrange for a developer to buy the whole property; and

(b) each investor would then receive a share of the profit from the sale of the property assuming it would be worth more than the prices they paid for their plots.

AL argued that the arrangement was not a collective investment scheme. However, the court held that AL was operating such a scheme.

In ***Asset Land v FCA***:

(a) the Supreme Court provides authoritative guidance in relation to the principles which should ultimately determine whether a given investment meets the statutory definition of a collective investment scheme. *Lords Carnwath* and *Sumption,* in their separate judgements*,* take the opportunity to consider the statutory definition of a collective investment scheme and proffer some significant guidance of general application of the definition going forward.

(b) *Lord Carnwath*, with whom *Lords Mance, Clarke, Sumption* and *Hodge* agreed, said:

- *"Arrangements"*

  [53] "…The word 'arrangements' has its ordinary meaning …."

  [54] "The content of the arrangements was a matter of fact for the judge … The judge was entitled to take the view that the understandings of the investors conformed to what was intended by the operator. Similarly he was not required to give special weight to contractual or other documents without regard to their context."

  [55] "The judge concluded that arrangements within the section were made when plots were marketed and investors paid their deposits, the object of the arrangements being that the company should achieve a sale of the site after seeking to enhance its value by improving the prospects for housing development, the price to be shared between the owners. That conclusion was amply supported by the evidence, and discloses no error of law."

- *"The property and its management"*

  [56] "Grounds 2 and 3 overlap and it is convenient to deal with them together. It is clear in my view that the relevant "property" for the purposes of section 235(1) was each of the company's sites taken as a whole, not the individual plots. That was the property whose sale was to lead to the profits which were the object of the exercise, and which brought about the scheme within the scope of the section."

  [58] "… The property for the purposes of the subsection (1) is the whole site. That definition remains the same in principle throughout the section. But management control of the property under subsections (2) and (3 may be achieved in different ways. It is necessary to consider the mechanisms by which the participants on the one hand or the operator on the other manage or have management control of the property. The mechanisms may not be the same in each case, and they need not be legal mechanisms. That follows from the acceptance that the term 'arrangements' is not limited to agreements binding in law. By the same token, the 'control' envisaged by those arrangements is not confined to legal control."

  [59] "Have … control in subsection (2) is not a technical term … it must be taken to refer to 'the reality' of how the arrangements are to be operated, which may or may not involve rights or powers enforceable in law … The FCA'S guidance (PERG 11.2) draws the correct contrast:

  > *"If the substance is that each investor is investing in a property whose management will be under his control, the arrangements should not be regarded as a collective investment scheme. On the other hand, if the substance is that each investor is getting rights under a scheme that provides for someone else to manage the property, the arrangements would be regarded as a collective investment scheme."*

[60] "The judge found that the facts of the present case brought it within the FCA's second category. He was entitled to do so … Their ability as individual owners to determine ultimately whether or not to participate in a sale cannot be equated with control of its management in the meantime. In any event as the judge found, it would make no sense for them in practice to opt out of the realization of the profit which was the only purpose for the arrangements."

[62] "Conversely, turning to subsection (3)(b), under the arrangements as found by the judge control of the management activities for the property as a whole lay with the company. It was acting as the operator of the scheme, not as mere managing agent for the individual owners. It is true that its control was not underpinned by any legal rights over the units making up the property. That did not affect the substance of the arrangements, even if it might have been an obstacle to their effective implementation…."

(c) *Lord Sumption*, with whom *Lords Mance, Clarke* and *Hodge* agreed, said:

- *"Section 235(1): arrangements"*

  [91] "'Arrangements' is a broad and untechnical word. It comprises not only contractual or other legally binding arrangements, but any understanding shared between the parties to the transaction about how the scheme would operate, whether legally binding or not. It also includes consequences which necessarily follow from that understanding, or from the commercial context in which it was made in these respects, the definition is concerned with substance and not with form. It is, however, important to emphasize that it is concerned with what the arrangements were and not with what was done thereafter…it must be possible to determine whether arrangements amount to collective investment schemes as soon as those arrangements have been made. Whether the scheme is a collective investment scheme depends on what was objectively intended at that time, and not on what later happened if different."

- *"Section 235(2): with respect to property"*

  [93] "…The reason is that the property referred to in subsection (1) is the property from whose acquisition, holding, management or disposal the profits or income were to be derived. On the judge's findings that was the whole site. It was the whole site that was to be rezoned and it was the whole site which was to be sold to a developer. The profit which each investor would derive from these transactions would be derived from an aliquot share of the entire sale price for the site."

- *"Section 235(2): day-to-day control"*

  [94] "'Control' of property means the ability to decide what is to happen to it … that does not only mean the legal ability to decide. It extends to a case where arrangements are such that the investor will in practice be able to do so. But the critical point is that the absence of day-to-day control in subsection (2) has to be a feature of the arrangements. This is necessarily prospective, viewed from the time when the arrangements are made. Either those arrangements confer or allow control on the part of the investors or they do not. The test cannot depend on what happens after the arrangements have been made. Nor would a test based on the actual exercise of control be realistic. Some kinds of property require little or nothing by way of management. Some situations do not require any exercise of management control. The question must necessarily be in whom would control be vested were control to be required…."

- *"Section 235(3)(b): management of the property as a whole"*

  [97] "Subsection (3)(b) provides that what has to be 'managed as a whole' is the property the subject of the scheme, not the scheme itself so far as that is different."

  [99] "The fundamental distinction which underlies the whole of section 235 is between (i) cases where the investor retains entire control of the property and simply employs the services of an investment professional (who may or may not be the person from whom he acquired it) to enhance value; and (ii) cases where he and the other investors surrender control over their property to the operator of the scheme

so that it can be either pooled or managed in common, in return for a share of the profits generated by the collective fund …."

[102] "On which side of the line does this case fall? In strictly legal terms, the three core representations did not call for any surrender of control over the plots to an investment intermediary. On the contrary, each investor remained the entire owner and sole controller of his plot and simply counted on Asset Land to enhance its value and find him a buyer. But the transaction cannot be viewed only in legal terms and the judge found that the practical consequences of the arrangement went wider that the express terms of the three core representations. He discounted the significance of the investors 'legal right to dispose of their plots as they pleased, because he considered that the arrangement embodied in the core representations could not work if the investors exercised the rights they theoretically possessed: see paras 162, 169 of his judgement. The dominion of the investors over their plots, although apparently complete, was in reality an illusion … On that ground … I agree that the schemes with which we are concerned are collective investment schemes."

The authoritative guidance provided by the ***FCA Handbook [2014]*** (quoted above) and cited with approval by *Lord Carnwath* in his judgement in ***Asset Land v FCA*** at *[59]* and *[60]* (quoted above), is in sharp contrast to the comments of the FMLC Working Group chair Mr Michael Brindle (in the July 2008 report of the FMLC) as to the vagueness of the "*day-to-day control*" test under the FSMA cited by *Justice Hamblen* in his judgement in ***Andrew Brown v InnovatorOne*** at *[1168]* and *[1169]* (quoted above).

Difference in wording between the UK and Australian definitions

There is a difference in wording and phrasing between the UK definition of a "collective investment scheme"[33]:

"… (2) The arrangement must be such that the persons who are to participate ("participants") do not have day-to-day control over <u>the management of the property</u>, whether or not they have the right to be consulted or to give directions …."

and the Australian definition of a "managed investment scheme"[34]:

"(iii) The members do not have day-to-day control over <u>the operation of the scheme</u> (whether or not they have the right to be consulted or give directions)";

which is also reflected in the dicta in the case law, although there is consistency in the judgements and reasons for decision. Regardless of this difference, since the decision in the UK case of ***Asset Land v FCA*** it is clear both definitions are now interpreted by the courts to have a similar meaning, particularly in relation to the application of the negative day-to-day control test. If anything, the Australian definition is more precise and less ambiguous than the UK definition.

While UK judicial decisions are not binding upon Australian Courts[35], the decisions cited above are nonetheless persuasive.

1.3 Questions relevant to a determination of whether a horse racing scheme is a managed investment scheme

As stated by *Buss JA in* ***Burton v Arcus****:*

"The three elements in par (a) of the definition of "managed investment scheme" are prefaced by the words "a scheme that has the following features."

So, the following questions must be asked:

First Question: Is there a scheme?

If the answer to that question is "No", then no further analysis is required. However, if the answer to that question is "Yes", then two more questions must me asked.

[33] Financial Services and Markets Act 2000 (UK).
[34] section 9.
[35] see paper titled: "Australian Bar Review – Precedent Law, Practice & Trends in Australia", by The Hon Justice Michael Kirby AC CMG.

Second Question: What is the scheme's legal structure and the realities of how it is designed to operate in practice? and

Third Question: Does the scheme have the characteristics of a managed investment scheme?

1.3.1 First Question: Is there a scheme?

Answer: "Yes". A horse racing scheme can reasonably be defined as:

> *"a programme or plan of action formulated by a person for the purpose of 2 or more people acquiring a thoroughbred horse and using it for racing, including the ancillary arrangements necessary to achieve that purpose."*

In ***Australian Softwood case***[36], *Mason J* said:

> *[11] "…all that the word 'scheme' requires is that there should be 'some programme, or plan of action'…."*

In ***ASIC v Chase Capital***[37]*, Owen J* said:

> *[63] "…the scheme is the entire operation…."*

In ***ASIC v Takaran***[38]*, Barrett J* said:

> *[15] "The essence of a "scheme" is a coherent and defined purpose, in the form of a "programme" or "plan of action", coupled with a series of steps or course of conduct to effectuate the purpose and pursue the programme or plan."*
>
> *[16] "It must also be emphasized that a scheme having the characteristics bringing it within the s9 definition of a managed investment scheme will not necessarily have those characteristics alone. …… Elements which lie beyond those attributes but contribute to the coherence and completeness which make a "programme" or "plan of action" must form part of that "scheme". Every programme or plan of action must be taken to include the logical incidents of and consequences of and sequels to its acknowledged components."*

1.3.2 Second Question: What is the scheme's legal structure and the realities of how it is designed to operate in practice?

Answer: Generally, when an offer of interests is made in a thoroughbred horse being syndicated for racing the following arrangements are predetermined by the offeror/promoter and understood by the investors:

(a) the nature of the legal relationship between the parties, as this determines both the nature of the investors' interests being acquired in the horse and the scheme, and to a significant extent the modus operandi of the scheme; and

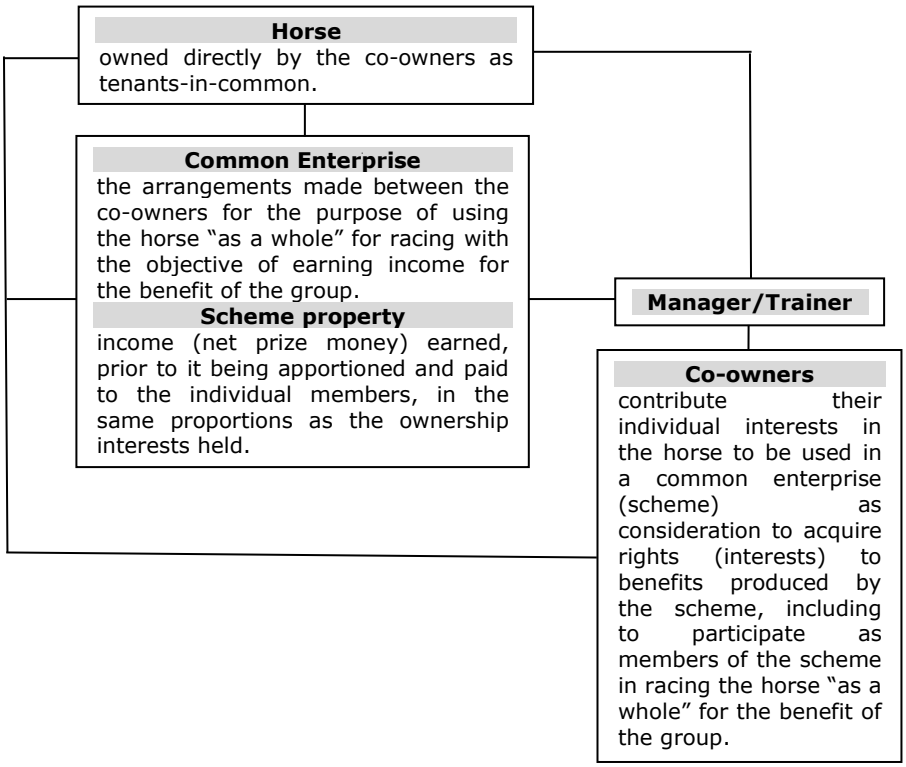
(b) the first appointees as manager and trainer.

The structure of the arrangements can be influenced by numerous factors, including risk exposure, taxation and other considerations. The most common is "**co-ownership**" [as distinct from "**partnership**" or "**unit trust**"], with such arrangements generally regarded as being more flexible and accommodating of the varying and often changing needs of the individual members.

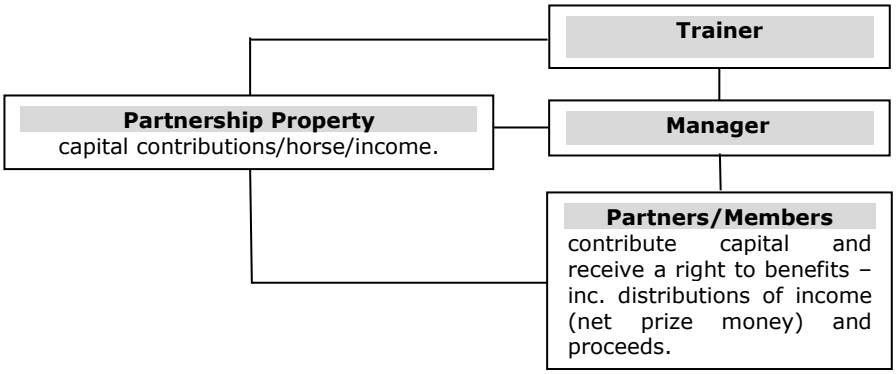
The realities of how a typical horse racing scheme based on "co-ownership" is designed to operate in practice are set out below, at parts 1.3.3 and 1.3.4.

[36] n 15, at 15.
[37] n 17, at p 15.
[38] n 18, at p 16.

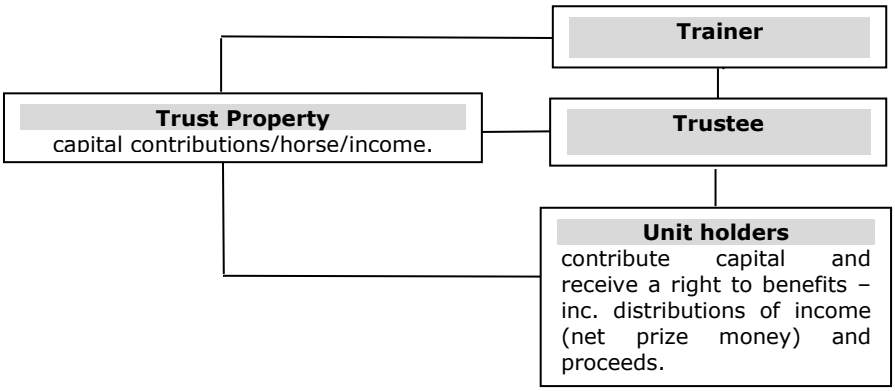
Co-ownership



Partnership



Unit Trust



1.3.3 Third Question: Does the scheme have the characteristics of a managed investment scheme?

Answer: Yes. This analysis concludes that horse racing schemes generally [by practical necessity and to comply with the ARR] are sufficiently uniform in their key elements to justify the conclusion that any programme or plan of action formulated by a person for the purpose of 2 or more people acquiring a thoroughbred horse and using it for racing, [including the ancillary arrangements necessary for achieving that purpose] will, prima facie, satisfy the definition of a managed investment scheme.

The first and second elements of paragraph (a) of the s.9 definition of a managed investment scheme may overlap and are best explained together.

A. The nature of the "contributions" by members

When considering where a horse racing scheme fits within the context of the managed investment scheme regulatory regime, it is important to distinguish between schemes that involve <u>any</u> members contributions of money or money's worth being either:

(a) pooled (typical of **partnership** and **unit trust**-based "investment" arrangements); or

(b) used in a common enterprise (typical of **co-ownership** contract-based "common enterprise" arrangements);

as this has significant implications for differentiating the property of the scheme from property owned directly by the individual members and used in the scheme's operations.

In the case of horse racing schemes formulated as:

(a) **partnership** or **unit trust**-based "investment" arrangements, the partners, or unitholders [members] contribute money or money's worth to the scheme to facilitate their pooled funds being used to:

(i) acquire the horse "as a whole", to be used as the property of the scheme and the benefit of the members collectively; and

(ii) pay ongoing operating expenses, including horse-related and racing expenses; and

(b) **co-ownership** contract-based "common enterprise" arrangements, people contribute money to acquire from the promoter/operator [or other holder of an ownership interest] their individual ownership interests in the horse, as tenants-in-common, on the basis that they will assume various obligations, including to contribute [make available, or pay or supply, at the direction of the promoter or operator]:

(i) the right to use their individual ownership interests in the horse in a common enterprise (scheme) so that the manager, as an operator of the scheme, can manage <u>all</u> their ownership interests in common [the horse "as a whole"] on behalf of the group; and

(ii) money (on an ongoing basis) towards the scheme's operating expenses, in the same proportions as the ownership interests held [clauses 3.3, 7.1 and 7.2 of the **TOR COA**];

as consideration to acquire rights (interests) to benefits produced by the scheme.

The contributions by <u>all</u> tenants-in-common of the right to use their individual ownership interests comprising the horse "as a whole" in the scheme's operations, and the legally binding contractual promise to contribute money (on an ongoing basis) towards the scheme's operating expenses, in the same proportions as the ownership interests held, as consideration to acquire rights (interests) to benefits produced by the scheme, while not money, are of **money's worth**, and a "fair equivalent" of what is received.

> The pooling of the contributions is not a necessary element of the scheme for it to satisfy the second element of paragraph (a) of the s.9 definition. It is enough that the co-owners contribute [make available, or pay or supply, at the direction of the promoter or operator] money or **money's worth** for the purpose of the common enterprise that is the scheme.

The concepts of "co-ownership" and "common enterprise" are inextricably linked

Co-ownership is the most common legal form of racehorse ownership involving 2 or more people. A horse racing scheme based on co-ownership inevitably involves the joint participation by all the co-owners, as tenants-in-common, in a commercial enterprise for the common purpose of using the horse "as a whole" for racing with the objective of earning income (winning prize money), and hence is a **common enterprise**. From an operational perspective, each co-owner's individual ownership interest in the horse is inseparable from the interests of the other co-owners and the horse "as a whole", and incapable of being separately managed.

There is no apparent basis upon which a promoter of horse racing schemes based on co-ownership could successfully argue, in any legal forum, that such arrangements do not involve the joint participation by all the co-owners, as tenants-in-common, in a commercial enterprise for the common purpose of using the horse "as a whole" for racing with the objective of earning income (winning prize money), hence a "**common enterprise**". Any such argument would likely be a misrepresentation of the arrangements to avoid the legislative intention of the statutory provisions.

Furthermore, there is nothing in the Corporations Act that prescribes express terms agreed by the co-owners as a pre-requisite to establishing the existence of a common enterprise for the purpose of paragraph (a) of the s.9 definition of a managed investment scheme. It is enough that a common enterprise be a characteristic of the scheme evidenced by the realities of how it is designed to operate in practice and reasonable terms can be implied to give business efficacy to the contract. In any event, the **ARR** and the **TOR COA** impose rules and express terms if the co-owners do not have their own terms which clearly require that the co-owners appoint a person to "operate" the scheme [manage the horse "as a whole"] on behalf of the group.

Contributions of "money or money's worth" to be used in a common enterprise (scheme)

In ***Stewart v Spicer*** *[para 24], Justice Black* concluded that the funds contributed by the Plaintiff and the other co-owners to acquire their individual ownership interests from the First Defendant, and the ownership interests themselves, satisfied the first and second elements of paragraph (a) of the section 9 definition. He clearly considered the concepts of co-ownership and common enterprise to be inextricably linked and the basis upon which the ownership interests were acquired.

Contributions by people of money to acquire their individual ownership interests

However, with respect to *Justice Black*, it is arguable that the initial funds contributed by the Plaintiff and the other co-owners towards the sale price were entitled to be appropriated by the First Defendant, as the seller of the interests, for its own use and benefit, and not used in the resultant common enterprise (scheme) for the benefit of the scheme's members.

Contributions by co-owners of their individual interests in the horse to be used in a common enterprise (scheme)

Not that this matters in the broader context of *Justice Black's* judgement, having also concluded that both the first and second elements of paragraph (a) of the s.9 definition were satisfied by the Plaintiff and the other co-owners acquiring their individual ownership interests from the First Defendant on the basis they would:

(a) contribute them to be used in a common enterprise (scheme); and

(b) jointly participate as members of the scheme for the common purpose of using the horse "as a whole" for racing with the objective of earning income, and possibly also for breeding, for the benefit of the group.

Justice Black's reasoning is consistent with that of *Young CJ* in ***Crocombie v Pine Forests of Australia Pty Ltd***[39] *[49]*, *[50], [51]* and *[52].* Also see ***ASIC v Young*** and ***ASIC v Enterprise Solutions***.

Contributions by co-owners of money (on an ongoing basis) towards the scheme's operating expenses

Having concluded that both the first and second elements of paragraph (a) of the s.9 definition were satisfied by the co-owners acquiring their individual ownership interests and contributing them to be used in a common enterprise (scheme), *Justice Black [para 25]* did not consider it necessary for him to determine whether or not expenses paid by the co-owners also satisfied those elements.

We do so here for completeness:

(1) Each of the subject schemes was a typical co-ownership contract-based "common enterprise" arrangement, and the Plaintiff and the other co-owners acquired their individual ownership interests in each of the horses on the basis that they would assume various obligations, including to also contribute [make available, or pay or supply at the direction of the First or Second Defendant, as the promoter or operator of the scheme], money (on an ongoing basis) towards the scheme's operating expenses, in the same proportions as the ownership interests held.

(2) Each co-owner's legally binding contractual promise to make such contributions, was, in itself, a contribution of "**money's worth**" as consideration to acquire rights (interests) to benefits produced by the scheme, and a "fair equivalent" of what was received, thus satisfying both the first and second elements of paragraph (a) of the s.9 definition.

(3) Practical necessity and clauses 3.3, 7.1 and 7.2 of the **TOR COA** required the co-owners to make such contributions to ensure the scheme's solvency and it being able to achieve its purpose for the benefit of <u>all</u> the co-owners as a group, and clauses 4.4 and 4.5 empowered the manager to sell the ownership interest of any co-owner who breached this obligation.

The members of a typical co-ownership arrangement will generally make such contributions either:

(a) to a designated bank account administered by the manager to facilitate payment of the scheme's operating expenses; or

(b) by each member being invoiced directly by and paying directly to the trainer and other third-party service providers their individual proportion of operating expenses.

The principal racing authorities generally invoice the trainer for 100% of entry fees, regardless of the invoicing and payment arrangements agreed between the manager and the co-owners.

The payment method used by members to make their ongoing monetary contributions does not change either the nature of their obligation to make the contributions [as the holders of rights or interests in property] or the fact that the obligation arises from their participation in a common enterprise (scheme) established for the purpose of using the horse "as a whole" for racing with the objective of earning income (winning prizemoney)]. See ***Burton v Arcus*** *[57]* and ***ASIC v Takaran*** *[16].*

Note:
(1) If the co-owners make their contributions of money (on an ongoing basis) towards operating expenses to the scheme's designated bank account administered by the manager, the correct accounting treatment for those contributions, in the normal course, is that they be credited to the co-owners individual owner's equity account(s) in the scheme accounts [and not pooled] until used to pay that co-owner's proportion of those expenses when due. This accounting treatment is necessary when co-owners (at least from an internal perspective) are "severally" liable for the scheme's operating expenses, and not "jointly and severally" liable for those expenses, as would be the case if the arrangements were a general partnership and the contributions were "pooled."

[39] [2005] 219 ALR 692; NSWSC 151

B. The nature of the "rights (interests) to benefits" produced by the scheme

The definition of a managed investment scheme recognizes that the benefits may be either financial benefits, or benefits consisting of rights or interests in property. It is not a prerequisite for a horse racing scheme to satisfy the definition of a managed investment scheme that the motivation of the individual members to participate in the scheme is to derive a financial benefit. In fact, there is no necessary relationship between the speculative nature of the scheme (and low probability of a financial return) and the ownership arrangement satisfying the definition. See ***ASIC v Enterprise Solutions 2000 Pty Ltd***[40].

ASIC states in RG91 [2016][41]:

> *[RG 91.32] "Regulation under the co-regulatory arrangements, subject to appropriate conditions about the content of the agreements, should promote informed and confident investment in the relevant horse racing syndicates, which are small in scale. We have also taken into account that participation in racing often occurs for the pleasure of following horse racing and having a stake in the performance of a racehorse, rather than primarily to produce financial benefits."*

The members rights (interests) to benefits produced by the scheme will generally include the rights to:

(a) participate as members of the scheme for the purpose of using the horse "a whole" for racing with the objective of earning income for the benefit of the group [benefits derived as the holders of rights or interests in property]; and

(b) receive any income (net prize money) earned, in the same proportions as the ownership interests held [financial benefits produced by the scheme] [Clause 3.2 of the **TOR COA**].

The members of a typical co-ownership arrangement will generally be paid their distributions of any income (net prizemoney), either:

(a) by the manager from the scheme's designated bank account administered by the manager (after the total amount of net prize money is paid into that account by the relevant principal racing authority); or

(b) by the relevant Principal Racing Authority directly to each member's nominated bank account.

The payment method used by members to receive their income distributions does not change either the nature of their entitlement to the distributions [as the holders of rights or interests in property], or the fact that the distributions are a financial benefit produced by a common enterprise (scheme) established for the purpose of using the horse "as a whole" for racing with the objective of earning income (winning prizemoney)]. *See* ***ASIC v Takaran*** *[16].*

Note:

(1) If any income is received into the scheme's designated bank account administered by the manager, the correct accounting treatment for the income, in the normal course, is that it be apportioned and credited to the co-owners individual owner's equity account(s) in the scheme accounts (and not held as pooled income), pending being either distributed to that co-owner or used to pay that co-owner's proportion of operating expenses.

C. The third element of the definition – the members do not have day-to-day control over the operation of the scheme

The fundamental distinction which underlies the whole of the definition of a managed investment scheme is between:

(a) schemes where <u>all</u> the members have day-to-day control over the operation of the scheme by making <u>all</u> the decisions and implementing what is agreed; and

(b) schemes where <u>any</u> members contributions of money or money's worth are to be:

[40] (2000) 35 ACSR 620
[41] Regulatory Guide 91 [2016] – Horse breeding schemes and horse racing syndicates.

(i) pooled; or

(ii) used in [made available, or paid or supplied, for the purpose of] a common enterprise;

with the day-to-day [routine, ordinary, everyday] activities of the scheme being managed or carried out by a person who is an operator of the scheme on behalf of the members collectively, (*whether or not they have the right to be consulted or give directions*).

The objective assessment in determining day-to-day control is necessarily prospective, viewed from the time when the arrangements are made.

The day-to-day control test in the context of the definition of a managed investment scheme is not about ownership or proprietorship, or the legal right to control of the scheme. See **Appendix C**[42].

- The purpose of the day-to-day control test is to make the important distinction about the nature of the investment each member of the scheme is making.

- If the substance is that all the members exercise day-to-day "control in fact" over the operation of the scheme by making all the decisions and implementing what is agreed [actually managing or carrying out the routine, ordinary, everyday activities that comprise the scheme's operations], then the scheme will not be a managed investment scheme.

- However, if the substance is that the members contributions are to be pooled, or used in a common enterprise, to produce financial benefits, or benefits consisting of rights or interests in property, and the members appoint a person to operate the scheme [with the authority to actually manage or carry-out the routine, ordinary, everyday activities that comprise the scheme's operations] on behalf of the group, then the scheme will be a managed investment scheme (*whether or not they have the right to be consulted or give directions*).

- It is a negative test in the sense that for the arrangements to be a managed investment scheme they must be such that the members do not have day-to-day "control in fact" over the operation of the scheme, prospectively viewed from the time when the arrangements are made.

The day-to-day control test includes consideration as to whether a person who provides management services in relation to the property is either:

(a) a mere "agent" who separately manages the property of each member or "investment professional" who simply provides advice to the members on enhancing the value of their own property without exercising control; or

(b) an "operator" of the scheme who manages "as a whole" the property of the group.

The management activities of a person who is the "promoter" or "operator" are not to be imputed to the members in determining whether the members have day-to-day control over the operation of the scheme.

See the separate judgements in ***Burton v Arcus***[43] of *McClure JA [2], [3]* & *[4]* and *Buss JA [82]* & *[83]*. Also see the separate judgements in ***Asset Land v FCA***[44] of *Lord Carnwath [59], [60]* & *[62]* and *Lord Sumption [91], [93], [94], [97], [99]* & *[102]*; and ***FCA Handbook (UK) [2014]***[45] – *PERG 11.2* at *Q.4, Q.6* and *Q.12.*

[42] Appendix C explains the different control tests and highlights the need keep in mind the different contexts in which the concept of "control in fact" is being applied when considering the principles established by the case law in the different jurisdictions and circumstances.
[43] ibid, at p 20 to 24 of this paper.
[44] ibid, at p 28 to 30 of this paper.
[45] FCA Handbook (UK), Perimeter Guidance – Chapter 11 Guidance on property investment clubs and land investment schemes – PERG 11.1 [Background] and PERG 11.2 [Guidance on property investment clubs], at Q4, Q6 and Q12, which are set out at p 27 and 28 of this paper.

Horse racing schemes

In the case of horse racing schemes that are typical co-ownership contract-based "common enterprise" arrangements:

(1) Each member's ownership interest in the property of the group [the horse "as a whole"] which is the subject of the scheme's operations, (not the scheme itself so far as that is different), from an operational perspective, is inseparable from the ownership interests of the other members and the horse "as a whole", and incapable of being separately managed.

(2) The right of the members to separately manage their individual ownership interests is:

(a) subordinated to the rights of the members collectively and the authority of the manager and the trainer [with actual possession and control of the horse "as a whole"] to operate the scheme on behalf of the group; and

(b) limited to voting on those matters specified in the relevant Owners Agreement or Training Agreement as requiring the members' approval (by the requisite majority).

(3) The manager and the trainer are both clearly "operators" of the scheme who:

(a) control aspects of the scheme's operations on behalf of the members collectively;

(b) manage "as a whole" the property of the group [the members' individual interests in common - the horse as a whole]; and

(c) procure the services of other service providers such as veterinarians, farriers, jockeys, agisters and pre-trainers, etc.

Neither of them is a mere "agent" who separately manages the property of each member or "investment professional" who simply provides advice to the members on enhancing the value of their own property without exercising control.

(4) Accordingly, day-to-day "control in fact" over the operation of the scheme devolves to the manager and the trainer, being the people who, as operators of the scheme, actually perform *"… **the acts which constitute the management of or the carrying out of the activities which constitute the scheme**"* [***ASIC v Pegasus***[46] *[55]*].

Also see ***Burton v Arcus***[47] *[2], [4], [79], [82],* and *[83]*, which cites with approval ***ASIC v Pegasus*** and provides additional authoritative guidance in relation to the application of the principle of "control in fact" when determining the meaning of day-to-day control within the context of the third element of paragraph (a) of the s.9 definition; ***Stewart v Spicer Thoroughbreds Pty Ltd***[48] *[29]* and *[45]; **Racing NSW v Vasili***[49]; and **Appendix C**].

(5) Conversely, <u>all</u> the members <u>do not</u> have day-to-day "control in fact" over the operation of the scheme, prospectively viewed from the time when the arrangements are made. Practical necessity and the **ARR** (including the **TOR Rules**) require that the members:

(a) agree to:

(i) appoint a person (manager[50]) to control aspects of the scheme's operations, including those relating to its legal structure and administration, dealings with racing officialdom, the trainer and other service providers, as required, on behalf of the group [in accordance

[46] ibid, at p 21 and 22 of this paper.
[47] ibid, at p 20 to 23 of this paper.
[48] ibid, at p 24 of this paper.
[49] ibid, at p 25 and 26 of this paper.
[50] AR.63.

with the **ARR** and the terms of the **TOR COA**[51] or other agreement adopted by the members]; and

(ii) the manager on behalf of the group appointing a licensed trainer[52], [including agreeing to the terms of the Trainer's Training Agreement and Fees Notice], to take actual possession and control of the horse "as a whole" for the purpose of managing or carrying out those activities that collectively comprise the act of training a racehorse [in accordance with the **ARR** and the terms of the **TOR STA**[53] or other agreement adopted by the parties]; and

delegate to them the authority to operate the scheme on behalf of the group; and

(b) surrender day-to-day control over their individual ownership interests to the manager and the trainer so that those people can manage the members' ownership interests in common [the horse "as a whole"] for the benefit of the group, (*whether or not they have the right to be consulted or give directions*) [see ***ASIC v IP Product***[54] *[22];* and ***Stewart v Spicer Thoroughbreds Pty Ltd***[55]].

(6) However, a scheme may not possess these characteristics alone. The fact that it may also possess other characteristics, including terms that provide for the members to:

(a) pay their ongoing contributions towards operating expenses directly* to the relevant service providers [proportionate direct invoicing and payment of fees and expenses];

(b) be paid their distributions of any income (net prize money) directly* via the stakes payment system; or

[*an alternative to the manager administering these arrangements via a designated scheme bank account]

(c) participate in decision-making in accordance with the procedure (and requisite majority) set out in the applicable Owners Agreement or Training Agreement;

does not take it outside the scope of the definition – applying the **nonrestrictive modifier** attaching to the third limb of the definition in relation to paragraph (c) and the principles established by the case law [see the judgements of *Owen J* in ***ASIC v Chase Capital***[56] *[57]* and *[63]*; and *Barrett J* in ***ASIC v Takaran Pty Ltd***[57] *[15]* and *[16].*

In ***Stewart v Spicer*** *[para 29 and 45], Justice Black* concluded that each of the subject schemes was operated by the First Defendant on behalf of the Plaintiff and the other co-owners [noting that the rules of racing, including the prescribed **TOR COA,** required the co-owners to appoint a person to act as the manager of the scheme on behalf of <u>all</u> the co-owners as a group, which was the Second Defendant in the case two of the horses], thus satisfying the third element of paragraph (a) of the s.9 definition.

Control over a number of significant decisions by members will not be sufficient for them to be taken to have day-to-day control [***Spicer****, para 28*].

Where the rules of the scheme provide for the assumption of the manager of the assets of the scheme by another person, combined with a situation where the

[51] the TOR Co-owners Agreement. Mandatory under the Trainer and Owner Reform Rules (TOR Rules), unless amended or excluded and replaced by another agreement. The TOR Rules are set out in Schedule 2 of the Australian Rules of Racing. See pages 39 to 41 of this paper.
[52] AR.61.
[53] the TOR Standard Training Agreement. Mandatory under the Trainer and Owner Reform Rules (TOR Rules), unless amended or excluded and replaced by another agreement. The TOR Rules are set out in Schedule 2 of the Australian Rules of Racing. See pages 43 to 44 of this paper.
[54] ibid, at p 21 of this paper.
[55] ibid, at p 24 of this paper.
[56] ibid, at p 16 of this paper.
[57] ibid, at p 24.

members do not know the identity of other owners so as to facilitate them acting collectively to exercise control, then the members will not be taken to have "day-to-day" control of the scheme [***Spicer**, para 29*].

Notes:

1. *Generally, when an offer of interests is made in a thoroughbred horse being syndicated for racing the following arrangements are predetermined by the promoter/operator and understood by the investors:*
   - *(a) the nature of the legal relationship between the parties, as this defines the nature of the investors' interests being acquired in the horse and the scheme, and to a significant extent the modus operandi of the scheme; and*
   - *(b) the first appointees as manager and trainer.*
2. *In the case of a scheme formulated as a **co-ownership** contract-based "common enterprise" arrangement:*
   - *(a) the establishment of the scheme is, in practice, inextricably linked to the transfer of the ownership interests in the horse from the promoter/operator to the investors;*
   - *(b) the members:*
     - *(i) liability to perform obligations, including to contribute the right to use their individual ownership interests in the horse in a common enterprise (scheme), so that the manager, as an operator of the scheme, can manage <u>all</u> their ownership interests in common [the horse "as a whole"] on behalf of the group; and money (on an ongoing basis) towards the scheme's operating expenses, in the same proportions as the ownership interests held; as consideration to acquire rights (interests) to benefits produced by the scheme; and*
     - *(ii) rights (interests) to benefits produced by the scheme, including to participate as members of the scheme for the purpose of using the horse "as a whole" for racing with the objective of earning income for the benefit of the group; and receive any income (net prize money) earned, in the same proportions as the ownership interests held;*

     are contractual and apply from the time when the ownership interests in the horse are transferred to the members; and
   - *(c) the members do not have day-to-day control over the operation of the scheme (whether or not they have the right to be consulted or give directions), prospectively viewed from the time when the arrangements are made.*
3. *Accordingly, the acquisition of interests by co-owners in a thoroughbred horse being syndicated for racing is an offer and acquisition of interests in a managed investment scheme [see **Stewart v Spicer Thoroughbreds Pty Ltd** [24], [29] ad [45]] in the same way as the acquisition of units by limited partners was found to be an offer and acquisition of interests in a managed investment scheme in **ASIC v McNamara**[58] [17] and [22].*
4. *It is not significant to this analysis:*
   - *(a) whether the manager and the trainer are the same person or different people;*
   - *(b) whether the members acquired their individual interests from either the manager or the trainer, or another person; or*
   - *(c) whether or not the members are required to pay a fee to the manager for performing the manager's duties.*
5. *The promoter or nominee will generally also be the manager [even if the promoter does not retain an interest in the horse].*
   - *In such cases, the first-named registered owner may be the manager in name only, with the promoter or nominee controlling and directing "in fact" those aspects of the scheme's operations that are the manager's responsibility under the relevant Owners Agreement and the ARR. This is often the case with schemes established by licensed trainers acting as promoters.*
   - *It is also possible for a person outside of the ownership group who is the manager to be recorded as the first-named registered owner with "nil" equity and the other registered owners as owning "100%" of the horse. This is often the case with schemes established by promoters who are unrelated to the trainer to give them an ongoing commercial profile with the horse during its racing career.*

Furthermore, while the Owners Agreement and Training Agreement [both now mandatory under the **TOR Rules**] generally set out various powers and duties of the manager and the trainer, and specify that certain decisions cannot be taken by the manager or the trainer without the approval of the members [by the requisite majority] [e.g. change of trainer, gelding, relocation of the horse to race in another jurisdiction, race entry fee above a specified amount, veterinary treatment above a specified amount, etc.], this <u>does not</u> equate to the members having control over the management of the scheme in the meantime [see judgement of *Lord Carnwath* in ***Asset Land v FCA***[59] *[60]*]. Generally, there are few, if any, other restrictions on the authority of either the manager or the trainer to operate the scheme.

The Owners Agreement or Training Agreement may also include terms that:

(a) empower the manager or the trainer to pursue remedies against a member who is in breach of a payment obligation; or

(b) restrict the members in dealing with their individual interests in the horse or empower the manager to sell or otherwise dispose of the horse "as a whole" if the members agree (by the requisite majority) that the horse be sold or transferred.

The case law and the evidence clearly support the conclusion that the characteristics of a managed investment scheme are inherent in horse racing

[58] ibid, at p 16.
[59] ibid, at p 28 to 30 of this paper.

schemes as they are both designed to operate in practice and required to operate by the ARR. Consequently, there is no apparent basis upon which any person, including a licensed trainer, who is (a "promoter") in the business of promoting horse racing schemes, could successfully argue in any legal forum that the resultant schemes are outside the scope of the definition of a managed investment scheme and not subject to regulation. Any such argument would likely be a misrepresentation of the arrangements to avoid the legislative intention of the statutory provisions.

The need for all the members to exercise day-to-day control over the operation of the scheme by making all the decisions and implementing what is agreed is impractical[60] in the context of owning and managing a racehorse which is overcome by the members [as required by the **ARR**]:

(a) appointing a manager and a licensed trainer [with actual possession and control of the horse "as a whole"]; and

(b) delegating to them the authority to operate aspects of the scheme on behalf of the members collectively.

The pooling of the contributions is not a necessary element of the scheme for it to satisfy the second element of the definition. It is enough that the co-owners contribute [make available, or pay or supply, at the direction of the promoter or operator] money or money's worth to be used in a common enterprise (scheme).

The role of the manager and the ARR requiring the appointment of a manager

The owners or lessees of a racehorse are required to submit themselves to the jurisdiction of the Principal Racing Authority in the state or territory where they propose to race the horse, and to comply with the **ARR** and any local rules.

Where an ownership or leasehold arrangement has 2 or more members, the **ARR** require that they appoint a manager[61]:

> "*manager*"[62] means:
>
> *"a person registered with Racing Australia as the manager of a horse owned or leased by a natural person, a group of natural persons, or a Syndicate. Unless established otherwise:*
>
> *(a) The first named person appearing in the Certificate of Registration or other official ownership or leasing record held by Racing Australia will be deemed to be the manager [subject to AR63(1)]; and*
>
> *(b) If a horse is owned or leased by more than one Syndicate, the first named person appearing in the Certificate of Registration or other official ownership or leasing record held by Racing Australia will be deemed to be the manager."*

AR.63 states:

> *"Removal of manager of a horse*
>
> *(1) Subject to the TOR Rules [and/or a term of the COA, if relevant], a manager of a horse may be removed or replaced from that position by written notice signed by the owners, lessees or Syndicate members representing more than 50% of the ownership of the horse.*
>
> *(2) A manager of a horse is of their own right [and without separate express authorization by the owners, lessees or Syndicate members] entitled to:*
>
> *(a) enter, nominate, accept or scratch a horse for any race;*
>
> *(b) engage a jockey to ride a horse in any race;*

[60] See Burton v Arcus, and specifically the judgement of McClure JA [2], [3], [4], [5], [7], and [8], at p 20 to 24 of this paper.
[61] AR.63.
[62] AR.2.

(c) receive any prize money or trophy won by a horse;

(d) act for and represent the owners, lessees or Syndicate members in relation to the horse for the purpose of these Australian Rules;

except that where a provision of the TOR Rules [and/or a term of the STA or the COA, if relevant] specifies a process, requirement, or course of action, that provision or term binds the manager in the event of any conflict or inconsistency with this subrule.

(3) The entry or nomination of a horse for any race must state the name of the manager.

(4) The trainer of a horse who enters, nominates, accepts or scratches a horse is, absent of proof an agreement between the trainer and owners to the contrary, deemed to have done so with the authority of the manager and all other nominees."

This rule is a practical way of overcoming what would otherwise be impractical and a significant impediment to the day-to-day operation of the scheme [a need for unanimity in decision-making by all the members and for all the members to exercise control over the implementation of what is agreed]. It ensures that the differing opinions and competing preferences of the individual members of the scheme are manageable, particularly in dealings with the trainer and racing officialdom.

On 1 August 2017, Racing Australia introduced the **Trainer and Owner Reform Rules – TOR Rules**. The **TOR Rules**[63] are currently set out in Schedule 2 of the **ARR**.

A requirement under the **TOR Rules** is that the members of a co-ownership arrangement must have an agreement setting out the terms which will govern their legal relationship. The terms of the **TOR Co-owners Agreement (TOR COA)**[64] are deemed to apply [except in the case of lead regulator approved syndicates established by licensed promoters, each of which must have its own approved agreement that complies with the requirements of the ASIC Instrument], unless the members elect to either add to or amend those terms, or to exclude and replace that agreement with another agreement.

The **TOR COA** includes the following terms which give the Co-owners the rights to any income earned, require the Co-owners to contribute towards the cost of operating the scheme, and give the manager the power and authority to manage and operate aspects of the scheme on behalf of the members as a group:

"3.2 Each Co-owner will share in the prizemoney, bonuses, rebates and other revenue earned by the Horse in proportion to their respective Owner's interest in the Horse.

3.3 Each Co-owner must contribute towards the cost of maintaining, training and racing the Horse, and to other expenses relating to the Horse, on a pro rata basis in proportion to that Co-owner's interest in the Horse.

3.4 The Managing Owner will manage the Horse Ownership Venture for the benefit of all Co-Owners. That will be on the basis of there being no cost to the Co-owners for the Managing Owner's services unless otherwise agreed by them by Unanimous Consent.

3.5 The Managing Owner must:

(a) use reasonable endeavours to properly manage the Horse Ownership Venture, including using reasonable endeavours to ensure that the Trainer complies with the Trainer's reporting obligations as set out in clauses 2.2(c) and 2.3 of the STA;

(b) make decisions in the best interests of the Co-owners as a whole;

[63] first published on 1 August 2017. Last amended 1 August 2021.
[64] first published on 1 August 2017, and subsequently amended on 1 August 2018 and 1 April 2020.

(c) comply with the Managing Owner's obligations under the TOR Rules; and

(d) ensure that no funds provided by the Co-owners in respect of the Horse Ownership Venture are applied other than for the purpose of the Horse Ownership Venture.

3.6 The Managing Owner can only make the following decisions, and carry out any reasonable actions to effect those decisions, on behalf of the Co-owners with Majority Consent:

(a) approve a scheduled treatment event for the Horse (including veterinary or surgical treatment) which in the reasonable opinion of the Managing Owner is expected to exceed $4000 (including GST);

(b) geld the Horse and/or to provide the consent to surgery for a gelding procedure;

(c) enter into, terminate and/or bring to an end the training agreement or arrangement between the Co-owners and the Trainer;

(d) accept or object to a Fees Notice provided by the Trainer (including a decision in respect of any proposed variations to a Fees Notice), provided that if Co-owners with 50% aggregate ownership of the Horse wish to accept, and Co-owners with 50% aggregate ownership of the Horse wish to object to, a Fees Notice (or any proposed variations), the Managing Owner must object on behalf of the Co-owners;

(e) engage a new Trainer;

(f) offer for sale, and/or sell, the whole of the Horse;

(g) pay nomination, acceptance or late acceptance fees in an amount in excess of $10,000 (including GST) for the Horse to contest a race;

(h) relocate the Horse to race in another State, Territory or Country;

(i) retire the Horse;

(j) pay or provide for a discretionary bonus or commission to a jockey or to the Trainer (other than if prescribed by the agreement for Training Services between the Trainer and the Co-owners);

(k) change the Managing Owner of the Horse; and

(l) if the Horse is used for breeding as part of the Horse Ownership Venture, then:

(i) if the Horse is an entire to be stood as a stallion, which stud the Horse should stand at and his service fee each year;

(ii) if the Horse is a filly or mare, whether she is to be bred in any given year and if so which stallion the Horse is to be bred to.

3.7 The Managing Owner can only make the following decisions, and carry out any reasonable actions to effect those decisions, on behalf of the Co-owners with Special Consent:

(a) if the Horse is a colt or entire, stand the Horse as a stallion, either alone as part of the Horse Ownership Venture or in joint venture or partnership with others;

(b) if the Horse is a filly or mare, use the Horse as a broodmare rather than sell or retire her;

(c) change any of the terms of this Agreement, except that a decision to make Co-owners jointly and severally liable in respect of obligations in connection with the Horse Ownership Venture can only be made with Unanimous Consent."

3.8 A decision to borrow funds for the purpose of the Horse Ownership Venture requires Unanimous Consent.

3.9 Other than as provided in clauses 3.6 to 3.8, and subject to the obligations of the Managing Owner in clauses 3.4 and 3.5, the Managing Owner can make all other decisions reasonably required for the purpose of managing the Horse Ownership Venture as the Managing Owner sees fit in his or her absolute discretion."

…….

*4.4 Subject to clause 4.5, the Managing Owner can sell the Owner's interest of any Co-owner (**the Defaulting Owner**) in any of the following circumstances:*

(a) if a Co-owner becomes ineligible to own a racehorse under the Rules of Racing) including on account of any valid decision taken pursuant to those rules);

(b) if a Co-owner is declared to be bankrupt or placed into administration or liquidation;

(c) if a Co-owner fails to make payments in respect of the Horse Ownership Venture as and when they fall due and that has the effect of stopping the Horse being properly maintained, trained, able to race, and/or able to be properly and commercially used for breeding; or

(d) serious or persistent breaches of tis Agreement which are reasonably considered to be unacceptable by the Managing Owner and to justify the sale.

…….

7.1 The Co-owners agree that liabilities incurred by the Managing Owner in respect of the Horse in good faith and in connection with the Horse Ownership Venture are to be borne by the Co-owners in accordance with their respective ownership interest in the Horse, and paid accordingly when due and payable.

7.2 The Co-owners agree all expenses and liabilities incurred in relation to the Horse Ownership Venture are to be borne by them in proportion to their respective Ownership interest in the Horse.

The role of the trainer and the ARR requiring the appointment of a trainer

The role of the trainer is a complex one. The trainer is:

(a) a contracted provider of training and ancillary services (including materials and products), with it being necessary for the trainer to take actual possession and control of the horse "as a whole" for the purpose of managing or carrying out those activities that collectively comprise the act of training a racehorse;

(b) the agent or authorised representative of the manager when procuring the services of other parties to provide services in relation to the horse "as a whole" while it is in the care and under the control of the trainer, including (without limitation) chiropractic care, dentistry, farriery and veterinary care, transportation, etc. [the trainer may also provide or procure agistment, breaking-in and pre-training];

(c) the authorised representative of the manager and all other nominees when nominating and accepting the horse for races and in most cases engaging the services of a jockey[65]; and

[65] AR.63(2)(b).

(d) the person directly responsible under the **ARR** for notifying the Principal Racing Authority of the location of the horse while it is in training and for presenting it at the races in a fit and proper condition to race (including being free of any prohibited substance or race day treatment).

The trainer is also a manager:

(a) responsible for supervising the trainer's own staff (including foreperson, stable hands, grooms, trackwork riders, racing manager, etc.) and all third-party service providers (including in most cases the jockey) in how they perform their duties and supply their services in relation to the horse "as a whole"; and

(b) in the sense that the trainer is the directing mind of the scheme, with day-to-day control over those aspects of the scheme's operations relating to the care, training, and racing of the horse to best advantage, with it being necessary for the trainer to exercise the trainer's own professional skills, judgment, and considerable discretion, when managing or carrying out those activities, including (without limitation) formulating and implementing during each preparation:

(i) a training program to bring it to racing fitness[66]; and

(ii) a racing program with the objective of racing it to best advantage;

notwithstanding any right of the manager or the members to be consulted or give directions.

It should also be noted here that track fees [training], race nomination, and entry fees, are generally charged to the trainer by the relevant principal racing authority, with it then being necessary for the trainer to on-charge those fees to the owner(s).

The significant role of the trainer as an operator of the scheme is further evidenced by the fact that most of the scheme's operating expenses will generally comprise invoices issued by the trainer [for services rendered, including materials and products supplied, race entry fees, etc.], and third-party service providers procured by the trainer to provide services and carry out activities in relation to the horse whilst in training and racing, pre-training or on agistment.

The **ARR** also require that the horse be trained by a licensed trainer[67]:

"*trainer*"[68] means:

> *"a person licensed or granted a permit by a PRA to train horses, and includes any persons licensed to train as a training partnership."*

"training services" means:

> *"all services provided by a trainer (or qualified and authorised employees or persons engaged or approved by a trainer) in relation to the care, training and/or racing of a horse including training, pre-training, rehabilitation, maintenance, stabling, feeding, exercising, freighting, agisting, rental of gear, and the provision of veterinary, chiropractic, acupuncture, dental, and farrier services and treatments."*

AR.61 states:

"Only horses trained by a licensed trainer to race, official trail or jump out

(1) To be able to be entered for or run in any race or official trial or jump-out, a horse must be trained by a person with a licence to train.

(2) Subrule (1) does not apply:

[66] AR.105(1)(a).
[67] AR.61.
[68] AR.2.

(a) to a horse entered for a race where the entries close more than 60 days before the advertised date for the running of a race; and

(b) to any other race excepted under the Rules."

AR.63(4) is also relevant here (see above).

AR.105 states:

"Matters that may affect the running of a horse in a race

(1) The trainer of a horse, or any person that is in control of a horse, that is nominated for a race must:

(a) ensure that the horse is fit and properly conditioned to race;

(b) by nominating time, report to the Stewards any occurrence, condition, surgery or treatment that may affect the horse's performance in the race where the occurrence takes place, condition is present, surgery is performed or treatment is administered before nomination time;

(c) as soon as is practicable after nomination time and before acceptance time, report to the Stewards any occurrence, condition, surgery, or treatment that may affect the horse's performance in the race where the occurrence takes place, condition is present, surgery is performed or treatment is administered after nomination time and before acceptance time;

(d) if the horse is accepted for the race – as soon as practicable, report to the Stewards any occurrence, condition, surgery or treatment that may affect the horse's performance in a race where the occurrence takes place, condition is present, surgery is performed or treatment is administered after acceptance time."

(2) The Owner and/or trainer of a horse must:

(a) as soon as practicable after a race, report to the Stewards anything which might have affected the running of their horse in a race; and

(b) immediately after a race, report to the Stewards:

(i) any loss or breaking of gear which occurred during the race; or

(ii) any unusual happening in connection with the race.

(3) Further to subrule (2), if a trainer becomes aware of any condition or injury which may have affected the horse's performance in the race, the trainer must report the condition or injury to the Stewards as soon as practicable and no later than acceptance time for its next race engagement.

It is also a requirement under the **TOR Rules** that the owner(s) or lessee(s) and the trainer must have an agreement setting out the terms upon which the trainer will provide training and ancillary services. The terms of the **TOR Standard Training Agreement (TOR STA)**[69] are deemed to apply unless the parties elect either to add to or amend those terms, or to exclude and replace that agreement with another agreement.

The **TOR STA** includes the following terms which give the trainer the power and authority to manage and operate aspects of the scheme on behalf of the members (as a group):

"THE RIGHTS AND OBLIGATIONS OF THE TRAINER

2.1 The Trainer agrees to care for, train, stable, feed, exercise and arrange appropriate treatment for the Horse in accordance with the Rules of Racing and

[69] first published on 1 August 2017, and subsequently amended on 1 August 2018 and 7 January 2019.

to the standard of a reasonable Trainer in the Australian thoroughbred racing industry.

2.2 The Trainer (or an authorised representative of the Trainer) must:

(a) care for and train the Horse in accordance with the Rules of Racing and to enable it to race to the best of its ability;

(b) train the Horse with due care, skill, and diligence with reference to industry practice in the thoroughbred racing industry in Australia; and

(c) periodically and in a timely manner report to the Owner about the welfare, progress, and performance of the Horse, at a minimum and without limitation:

(i) when the Horse enters the Trainer's stable for training;

(ii) when the Horse departs the Trainer's stable for agistment (including by identifying the place of agistment);

(iii) when the Horse transfers to another stable of the Trainer, or interstate, or to another Trainer, or to a selling agent;

(iv) when the Horse is nominated for or accepted for a trial or a race;

(v) when the Horse suffers a material injury or illness, requires veterinary treatment, or dies; and

(vi) by providing a post-trial or post-race report within a reasonable time of the completion of either.

2.3 A report in relation to any of the matters set out in clause 2.2(c) above may be provided in any comprehensible form including:

(a) verbally in person;

(b) by telephone (including by leaving a voicemail);

(c) in written form (including by post, email, text message or facsimile).

2.4 Subject to clause 2.5, the Trainer has the right to engage a qualified person considered by the Trainer to be appropriate and/or necessary to attend to the Horse, including a veterinarian, farrier, horse dentist, horse chiropractor, horse acupuncturist, or water walker therapist.

2.5 If the cost of any scheduled treatment event for the Horse (including veterinary or surgical treatment) is in the reasonable opinion of the Trainer expected to exceed $2000 (including GST), the Trainer must obtain the approval of the Managing Owner before arranging that treatment.

2.6 The Trainer has the right to nominate, enter, accept, scratch or withdraw the Horse from any race or trial as the Trainer thinks fit, except:

(a) if the Trainer comes to a separate agreement in relation to any of those matters to the contrary with the Managing Owner;

(b) if the amount of a fee associated with the nomination, entrance, acceptance, scratching or withdrawal of the Horse exceeds $2000 (including GST), the Trainer must seek approval from the Managing Owner in relation to its payment. If a Managing Owner does not respond within a reasonable time of that request for approval, the Trainer may proceed and will not be liable for doing so, including in relation to the payment of any fee referred to in this clause.

2.7 The Trainer is not required to nominate, enter or accept in relation to the Horse if, despite having made requests of the Managing Owner to be put into funds for the cost of the relevant nomination, acceptance or entry, that does not occur prior to the time for nomination, entry, or acceptance.

2.8 The Trainer will engage and instruct the race jockey unless prior agreement to the contrary is made between the Trainer and the Managing Owner.

2.9 The Trainer is entitled to accept the instructions of the Managing Owner as representing all Owners, except in relation to the proposed gelding, sale or retirement of the Horse, in which case the Trainer must inform all Owners and obtain confirmation of the consent of more than 50% of the ownership equity of the Horse."

1.4 Concepts not unique to this analysis of a managed investment scheme

The concepts of "scheme", "common enterprise", "contributions" and "benefits", and the distinction between "partnership", "unit trust" and "co-ownership" arrangements, are not unique to this analysis of a managed investment scheme. The same or similar concepts are fundamental to determining the nature of a person's rights and obligations when participating in any arrangement between 2 or more persons owning or leasing a racehorse and apply under various federal and state laws, including Australian tax law (income tax, depreciation, capital gains, GST, etc.).

The use by the courts of the concept of "control in fact" is also not unique to the law relating to managed investment schemes. The different control tests and contexts in which the concept of "control in fact" is applied are considered in **Appendix C**.

1.5 Further commentary that is relevant to this part is set out in the appendices:

PART 2: WHEN MUST A HORSE RACING SCHEME BE REGISTERED AS A MANAGED INVESTMENT SCHEME?

2.1 Part summary

This part deals with:

(a) the statutory provisions that require a managed investment scheme to be registered and the exceptions to this requirement; and

(b) the ARR that require an "offer of interests" in a horse racing scheme to be the subject of a PDS approved by a lead regulator.

Conclusion

A horse racing scheme established as a one-off "private" scheme generally will not require registration. To qualify as a "private" scheme it must not require registration under section 601ED. In other words, it must not have more than 20 members and the person who established it must not be "…in the business of promoting managed investment schemes."

A horse racing scheme that "… was promoted by a person, or an associate of a person, who was, when the scheme was promoted, in the business of promoting managed investment schemes", generally[70]:

(a) will fall within the requirement for registration under section 601ED, regardless of the number of members; and

(b) must be registered as a managed investment scheme, unless it is eligible for a specific statutory exemption or ASIC Instrument relief from the requirement to be registered because it qualifies as:

(i) a personal offer scheme[71];

(ii) a wholesale scheme[72]; or

(iii) a lead regulator approved (ASIC Instrument[73] compliant) syndicate.

An "offer of interests" in:

(a) a registered scheme must be the subject of a PDS that complies with the requirements of the Act; and

(b) an ASIC Instrument compliant syndicate must be the subject of a PDS that:

(i) complies with the requirements of the ASIC Instrument; and

(ii) is approved by a lead regulator.

Section 601ED(5) states:

"A person must not operate[74] in this jurisdiction a managed investment scheme that this Section required to be registered under Section 601ED unless the scheme is so registered"[75].

2.2 If a scheme satisfies the definition of a managed investment scheme and does not qualify as a "private" scheme, then generally registration will be required under section

[70] the promoter test is in section 601ED(1)(b)
[71] section 1012E. A scheme in which offers of interests are made only by "personal offer" and do not require a disclosure document.
[72] section 761G. A scheme in which offers of interests are made only to "wholesale clients" and do not require a disclosure document.
[73] ASIC Corporations (Horse Schemes) Instrument 2016/790.
[74] the meaning of the word "operate" within the context of section 601ED(5) has been judicially determined in *Burton v Arcus [2*]. Ibid n 26, at p19 to 22.
[75] section 601ED(5) is subject to section 601ED(6).

601ED unless the scheme is relieved by a specific statutory exemption or ASIC Instrument from the requirement to be registered.

Section 601ED(1) specifies a "three-pronged" criteria as to when a managed investment scheme is required to be registered. If the scheme is caught by any "one" of the criteria, then it is required to be registered, unless the scheme is the result of a promoter:

(a) dealing in interests that do not require disclosure because of the interests being made available only:

(i) by "personal offer" under the 20/12 Rule; or

(ii) to "wholesale clients"; or

(b) making an "offer of interests" that complies with the terms of the relief afforded by the ASIC Instrument, including that there be a PDS approved by a lead regulator.

Section 601ED states:

"When a managed investment scheme must be registered

(1) Subject to subsection (2) and (2A), a managed investment scheme must be registered under Section 601EB if:

(a) it has more than 20 members;

*(b) it was promoted by a person, or an associate of a person, who was, when the scheme was promoted**,** in the business of promoting managed investment schemes; or*

(c) a determination under subsection (3) is in force in relation to the scheme and the total number of members of all of the schemes to which the determination relates exceeds 20.

(2) A managed investment scheme does not have to be registered if all of the issues of interests in the scheme that have been made would not have required the giving of a Product Disclosure Statement under Division 2 of Part 7.9 if the scheme had been registered when the issues were made.

(3) ASIC may, in writing, determine that a number of managed investment schemes are closely related and that each of them has to be registered at any time when the total number of members of all of the schemes exceeds 20. ASIC must give written notice of the determination to the operator of each of the schemes.

(4) For the purpose of this Section, when working out how many members a scheme has:

(a) joint holders of an interest in the scheme count as a single member; and

(b) an interest in the scheme held on trust for a beneficiary is taken to be held by the beneficiary (rather than the trustee) if:

(i) the beneficiary is presently entitled to a share of the trust estate or of the income of the trust estate; or

(ii) the beneficiary is, independently or together with other beneficiaries, in a position to control the trustee.

(5) A person must not operate in this jurisdiction a managed investment scheme that this Section requires to be registered under Section 601EB unless the scheme is so registered.

Note: Failure comply with this subsection is an offence: see subsection 1311(1).

(6) For the purpose of subsection (5), a person is not operating a scheme merely because:

(a) they are acting as an agent or employee of another person; or

(b) they are taking steps to wind up the scheme or remedy a defect that led to the scheme being deregistered."

2.3 Promoter of interests in a horse racing scheme

The words "… *in the business of …*" in section 601ED(1)(b) import the notion of commercial activity that is "… *systematic, repetitious and continuous*." [See ***ASIC v McNamara***[76] *[17]*].

The word "promoting" in the context of marketing imports the notion of activities or communications carried out on behalf of a business with the objective of attracting consumers to its products or services and generating sales. Promotional activities may include direct marketing, personal selling, digital promotions (all forms of promotion found on the internet), public relations, sponsorships, general advertising, and publicity.

Whatever activities comprise "promoting" in the context of marketing, in the specific context of section 601ED(1)(b) it is only logical that they include the following activities in relation to formulating managed investment schemes:

(a) offering to sell or inviting people to buy; and

(b) dealing in, including issuing, etc;

interests in such schemes.

The term "*promoter*" is not defined in the Act or the ASIC Instrument, so must be given an ordinary meaning.

The term "*promoter*" is defined:

(a) in ASIC RG91[2016] and RG91[2012]

> *"a person who offers to sell, or invites people to buy, interests in a managed investment scheme."*

This definition replaces the definition set out in RG91 [2007]:

> "*the person who agrees to operate the managed investment scheme."*

(b) in AR.2[77] of the ARR

> *"any person or corporation who for valuable consideration offers or invites any other person or corporation to subscribe for shares or participate in any scheme with objects that include the breeding and/or racing of a horse."*

With respect to ASIC, the 2007 definition was a misstatement which it corrected in 2012.
The RG is not law, being a publication issued by ASIC to promote an understanding of the current law by industry participants. Save for this error in the first edition, the RG is an informative document.
The writer considers that this misstatement may have contributed to a misunderstanding of the current law by some industry participants who have subsequently argued, incorrectly, that if the terms of an offer of shares propose that:
(a) a person other than the promoter will manage the horse on behalf of the members; or
(b) the members will appoint the manager;
this will somehow constitute the members having "day-to-day" control over the operation of the scheme, and consequently the scheme will fall outside of the definition of a managed investment scheme and the promoter need not be licensed.

[76] ibid, n 20 at p 16.
[77] added 20/11/2002 following the issuing of the Class Order by ASIC on 15/02/2002.

2.4 Relevant case law

"promoted"

In ***ASIC v Young & Ors***[78], *Muir J* said:

> *[53] "Whatever the full scope of the meaning of "promoted" in the subject context, it plainly extends to activities in which a person formulates a scheme …. advertises it, solicits others to participate in it and embarks upon its implementation."*

2.5 Offers that do not require disclosure

An "offer of interests" in a managed investment scheme will normally require a PDS to ensure that prospective investors have all key information about the scheme to enable them to make an informed decision whether to invest. In certain circumstances, an issue of interests in a managed investment scheme can be made to investors without a PDS.

While the provisions of Chapter 6D [Fundraising] apply to securities generally, the provisions of Chapter 7 [Financial Services and markets] apply to financial products, or financial services generally, including interests in managed investment schemes.

Section 706 [Issue offers that need disclosure] provides that an offer of securities for issue needs disclosure under Chapter 6D unless section 708 [Offers that do not need disclosure], or 708AA [Rights issues that do not need disclosure], says otherwise.

Sections 708 and 708AA contain exemptions to the requirements to issue a PDS.

Sections 1012B and 1012C deal with obligations that require a regulated person to provide a PDS to any person who is a retail client when offering a "financial product" to the person; and section 1012D contains exemptions to the requirement to provide a PDS.

The relevant provisions of these sections are summarized below:

Section 1012B [Obligations to give Product Disclosure Statement – situations related to issue of financial products]:

(a) a regulated person must give a retail client a PDS for a financial product if:

  (i) they make an offer to issue, or arrange for the issue of, the financial product to the client;

  (ii) they issue the financial product to the client in circumstances where there it is reasonable to believe that that the client has not already received a PDS; or

  (iii) the client makes an offer to the regulated person to acquire the financial product by way of issue.

(b) The PDS must be prepared by the product issuer and given at or before the time when the regulated person either makes the offer, or issues the financial product to the client, or before the client becomes bound by a legal obligation to acquire the financial product pursuant to the offer[79].

Section 1012C [Obligations to give Product Disclosure Statement – offers related to sale of financial products]:

(a) a regulated person must give a retail client a PDS for a financial product that it has offered to sell to the client or that a retail client has offered to acquire by way of transfer, if the sale or transfer:

  (i) amounts to an indirect issue of financial products[80] and section 1012DA does not apply; or

[78] [2003] QSC 029.
[79] section 1013A(1).
[80] section 1012C(6).

(ii) is either an off-market sale by a controller[81], or amounts to an indirect off-market sale by a controller[82].

(b) The PDS must be prepared by the seller[83] and given to the client at, or before, the time the regulated person makes the offer to sell the product, or where the client makes the offer, before the client becomes bound by a legal obligation to acquire the financial product pursuant to the offer.

Section 1012D [Situations in which Product Disclosure Statement not required]:

(a) where the client has already received an up-to-date PDS, or the regulated person believes on reasonable grounds that this is the case[84];

(b) for offers of products that the client already holds, where the regulated person believes on reasonable grounds that the client has received, or has access to (and the client knows that he or she has access to), all the information that a PDS would be required to include through an earlier PDS and any ongoing disclosures, in relation to managed investment products, through continuous disclosure[85]; or

(c) for small-scale offerings of managed investment and other prescribed financial products, e.g. - personal offers that do not breach the 20/12 Rule etc.

"Personal Offers" under the 20/12 Rule

"Personal Offers" of interests in a managed investment scheme, where the promoter is compliant with the 20/12 Rule under section 1012E, do not require disclosure under Chapter 7. Similar provisions also appear in section 708(1) and apply to securities generally.

Section 1012E(2) provides that a "personal offer" of a "financial product" does not require disclosure, provided that the offer does not result in the number of purchasers to whom the products are "issued" exceeding 20, or the total amount raised from the "issuing" of the financial products in any 12 month period[86] exceeding $2 million.

Any "offer of interests" in an "unregistered" scheme, or schemes, to which the provisions of section 1012E apply, must be a "personal offer" within the meaning ascribed to that term by section 1012E(5).

Under the 20/12 Rule prescribed by section 1012E, an "unregistered" horse racing scheme, or schemes, must not result in more than $2 million of interests being "issued" to more than 20 persons (including joint owners) in a period of 12 months. Furthermore, if the number of persons (including joint owners) to whom the interests are "issued" by the "issuer" at any time becomes more than 20, each scheme must be registered as a managed investment scheme within 12 months of that happening.

An "offer of interests" by a promoter to an existing client who has previously either purchased interests or indicated an interest in doing so will likely satisfy the definition of a "personal offer"[87].

Section 1012E states:

> *"Small scale offerings of managed investment and other prescribed financial products (20 issues or sales in 12 months)*
>
> *(1) This Section applies only to financial products that are:*
>
> *(a) managed investment products; or*
>
> *(b) financial products of a kind prescribed by the regulations made for the purpose of this paragraph.*

[81] section 1012C(5).
[82] section 1012C(8).
[83] section 1013A(2).
[84] section 1012D(1).
[85] section 1012A(2).
[86] the 20/12 Rule.
[87] section 1012E(5).

(2) Personal Offers of financial products do not need a Product Disclosure Statement under this Part if:

(a) all of the financial products are issued by the same person (the issuer); and

(b) none of the offers results in a breach of the 20 purchasers ceiling (see subsections (6) and (7); and

(c) none of the offers results in a breach of the $2 million ceiling (see subsections (6) and (7);

(3) … to (4) …

(5) For the purposes of subsections (2) and (4), a personal offer is one that:

(a) may only be accepted by the person to whom it is made; and

(b) is made to a person who is likely to be interested in the offer, having regard to:

(i) previous contact between the person making the offer and that person; or

(ii) some professional or other connection between the person making the offer and that person; or

(iii) statements or actions by that person that indicates that they are interested in offers of that kind.

(6) An offer to issue, or arrange for the issue of, a financial product:

(a) results in a breach of the 20 purchasers ceiling if it results in the number of people to whom the issuer has issued financial products exceeding 20 in any 12 month period; and

(b) results in a breach of the $2 million ceiling if it results in the amount raised by the issuer from issuing financial products exceeding $2 million in any 12 month period.

(7) An offer by a person to sell a financial product:

(a) results in a breach of the 20 purchasers ceiling if it results in the number of people to whom the person sells financial products issued by the issuer of that financial product exceeding 20 in any 12 month period; and

(b) results in a breach of the $2 million ceiling if it results in the amount raised by the person from selling financial products issued by the issuer of that financial product exceeding $2 million in any 12 month period.

(8) In counting issues and sales of the financial products issued by the issuer, and the amount raised from issues and sales, for the purposes of subsection (2), disregard issues and sales that result from offers that:

(a) do not need a Product Disclosure Statement (otherwise that because of this section); and

(b) are made under a Product Disclosure Statement

Note: Also see provisions on restrictions on advertising (section 1018A) and the anti-hawking provisions in section 992A.

(9) In counting issues and sales of financial products issued by the issuer, and the amount raised from issues and sales, for the purposes of subsection (2), disregard any issues and sales made by a body if:

(a) the body was a managed investment scheme (but not a registered scheme) at the time that the offer of interests in the scheme that resulted in the issues or sales was made; and

(b) the body became a registered scheme within 12 months after that offer was made; and

(c) the offer would not have required a Product Disclosure Statement (otherwise than because of this section) if the managed investment scheme had been a registered scheme at the time that the offer was made.

(10) In working out the amount of money raised by the issuer from issuing financial products, include the following:

(a) the amount payable for the financial products at the time when they are issued;

(b) if the financial product is an option -- an amount payable in the exercise of the option;

(c) if the financial products carry a right to convert the financial product into other financial products -- any amount payable on the exercise of that right.

(11) If a person relies on subsection (2) to make offers of financial products without a Product Disclosure Statement under this Part, the person must not issue, arrange for the issue of, or transfer, financial products without a Product Disclosure Statement under this Part if the issue or transfer would result in a breach of the 20 purchasers ceiling or the $2million ceiling (see subsections (6), (7), (8), (9) and (10))

(12) For the purposes of this Section, an offer of a financial product is an offer to:

(a) issue the financial product; or

(b) arrange for the issue of the financial product; or

(c) sell the financial product."

Offer available only to "wholesale clients" (including "professional" and "sophisticated investors")

An "offer of interests" in an unregistered managed investment scheme, where participation is available only to "wholesale clients", does not require disclosure.

Chapter 7 contains tests in relation to specific products. A "wholesale client" is defined in section 761G(4) as a person who is not a "retail client." Insurance and superannuation products are treated differently, but investors in other financial products can be treated as "wholesale clients" if they satisfy a wealth, occupation, or other threshold test.

The "experienced investor" test in section 708(10) focuses on competence levels in securities generally, rather than specific products. It is the same as the "sophisticated investor" test in section 761GA which focuses on experience in relation to financial products or financial services generally. The class of "sophisticated investor" is intended to be a subset of "wholesale client."

The "sophisticated investor" test in section 708(8) is of similar effect to the "wholesale client" test in section 761G(7).

A "wholesale client" is a person who:

- invests $500,000 more; or
- can provide a certificate (given in the last 6 months) from a qualified accountant stating that the person:
    - has net assets of at least $2.5 million; or
    - has a gross income of $250,000 for each of the last 2 financial years; or

- is otherwise a wholesale client within the meaning of section 761G.

Who can participate?

(a) wholesale clients[88] - a person who has aggregated net assets of $2.5 million or has aggregated gross income for each of the last two financial years of at least $250,000 a year. A qualified accountant must certify the person satisfies the criteria and such certification must be no more than two years old.

(b) professional investors[89] - an investor who controls, or is the manager of, at least $10 million of investment in securities, or who has an AFS license[90].

(c) sophisticated investors[91] - where an offer to a person is made through an AFS licensee, and the licensee is satisfied, on reasonable grounds, that the person to whom the offer is made has previous experience in investing in securities that allows them to assess:

(i) the merits of the offer;

(ii) the value of the securities;

(iii) the risks involved in accepting the offer;

(iv) their own information needs; and

(v) the adequacy of the information given by the person making the offer.

Section 761G [Meaning of retail client and wholesale client] states:

"(1) For the purposes of this Chapter, a financial product or a financial service is provided to a person as a retail client unless subsection (5), (6), (6A) or (7), or Section 761GA, provides otherwise.

Note: …

(2) For the purposes of this Chapter, a person to whom a financial product or financial service is provided as a retail client is taken to acquire the product or service as a retail client.

(3) If a financial product is provided to a person as a retail client, any subsequent disposal of all or part of that product by the person is, for the purposes of this Chapter, a disposal by the person as a retail client.

Wholesale clients

(4) For the purposes of this Chapter, the financial product or a financial service is provided to or acquired by, a person as a wholesale client if it not provided to, or acquired by, the person as a retail client.

General insurance products

(1)… to (6) …

Other kinds of financial products

(7) For the purposes of this Chapter, if a financial product is not, or a financial service (other than a traditional trustee company service) provided to a person does not relate to, a general insurance product, a superannuation product or an RSA product, the product or service is provided to the person as a retail client unless one or more of the following paragraphs apply:

[88] section 761G.
[89] section 9.
[90] section 761G(7)(d).
[91] section 761GA.

(a) the price for the provision of the financial product, or the value of the financial product to which the financial service relates, equals or exceeds the amount specified in regulations made for the purpose of this paragraph as being applicable in the circumstances (but see also subsection (10); or

(b) the financial product, or the financial service, is provided for use in connection with a business that is not a small business (see subsection (12);

(c) the financial product, or the financial service, is not provided for use in connection with a business, and the person who acquires the product or service gives the provider of the product or service, before the provision of the product or service, a copy of a certificate given within the preceding 6 months by a qualified accountant (as defined in Section 9) that states that the person:

(i) has net assets of at least the amount specified in the regulation made for the purposes of this paragraph; or

(ii) has a gross income for each of the last 2 financial years of at least the amount specified in regulations made for the purposes of this subparagraph a year;

(d) the person is a professional investor.

Offence proceedings – defendant bears evidential burden in relation to matters referred to in paragraphs (7)(a) to (d).

(8) … to (11) …

Definition

(12) In this Section

"small business" means a business employing less than:

(a) if the business is or includes the manufacture of goods – 100 people; or

(b) otherwise – 20 people."

Section 761GA [Meaning of retail client – sophisticated investors] states:

"For the purposes of this Chapter, a financial product, or a financial service (other than a traditional trustee company service) in relation to a financial product, is not provided by one person to another person as a retail client if:

(a) the first person (the licensee) is a financial services licensee; and

(b) the financial product is not a general insurance product, a superannuation product, or an RSA product; and

(c) the financial product or service is not provided for use in connection with a business; and

(d) the licensee is satisfied on reasonable grounds that the other person (the client) has previous experience in using financial services and investing in financial products that allows the client to assess:

(i) the merits of the product or service; and

(ii) the value of the product or service;

(iii) the risks associated with holding the product;

(iv) the client's own information needs; and

(v) the adequacy of the information given by the licensee and the product issuer; and

(e) the licensee gives the client before, or at the time when, the product or advice is provided a written statement of the licensee's reasons for being satisfied as to those matters; and

(f) the client signs a written acknowledgement before, or at the time when, the product or service is provided that:

(i) the licensee has not given the client a Product Disclosure Statement; and

(ii) the licensee has not given the client any other document that would be required to be given to the client under this Chapter if the product or service were provided to the client as a retail client; and

(iii) the licensee does not have any other obligation to the client under this Chapter that the licensee would have if the product or service were provided to the client as a retail client."

2.6 The ASIC Instrument

ASIC's approach to regulating small-scale schemes is explained in RG 91 [2016][92]:

> *[RG 91.26] "A horse racing syndicate is an arrangement under which a group of people agree to contribute money in return for a share of prize money won by a racehorse. The syndicate members may contribute money to obtain a percentage ownership stake in the racehorse, or the owner of the racehorse may lease the racehorse to the operator of the syndicate. Sometimes, other benefits are available to members of a syndicate, such as an entitlement to attend social events."*
>
> *[RG 91.27] "Generally, a horse racing syndicate will be a managed investment scheme under s9 of the Corporations Act. ASIC Corporations (Horse Schemes) Instrument 2016/790 provides conditional relief to the promoter and manager of a small-scale horse racing syndicate from the requirement to register the syndicate under the managed investment provisions in Ch 5C of the Corporations Act."*

The ASIC Instrument is a grant by ASIC to the thoroughbred industry of conditional relief from specific provisions of the Act considered onerous if applied to small-scale schemes. The relief is in the form of industry co-regulation, with ASIC exercising its administrative power and appointing the Principal Racing Authorities of the various states and territories as lead regulators and delegating to them the responsibility for administering the terms of the ASIC Instrument within their respective jurisdictions.

The scope of the relief is limited to the terms of the ASIC Instrument.

(1) It applies only to small-scale schemes in which "there are no more than 50 participants" and "the total amount sought from the issue of scheme interests to participants does not exceed $500,000"; and operates to relieve the promoter and operator of such schemes from the obligation to comply with the provisions of section 601ED relating to scheme registration, which would otherwise require that they be established and operated as ASIC registered managed investment schemes.

(2) Only promoters and schemes that comply with the terms of the ASIC Instrument are eligible to be administered by the lead regulators. All other promoters and schemes must comply with the Act and remain subject to the direct regulatory power and authority ASIC.

The relief does not extend to the numerous other provisions of the Act relating to managed investment schemes, including Chapter 7 [Financial services and markets], that are also relevant to the promotion of schemes, and with which promoters must comply. Promoters are not relieved from having to comply with those provisions of Chapter 7 relating to licensing, conduct, and transfer of title, etc.

[92] ASIC Regulatory Guide – RG 91 [2016]: Horse breeding schemes and horse racing syndicates.

The terms of the relief require that:

(a) the "promoter":

(i) hold an appropriate AFS licence [or be an authorised representative of a licensee]; and

(ii) be approved and on the register of approved promoters [or approved authorised representatives] of a lead regulator; and

(b) the "offer of shares" be the subject of a disclosure statement and scheme agreement approved by a lead regulator prior to the offer being made.

The ASIC Instrument states in Part 2 – Exemptions:

"5 Horse racing syndicates

Exemption

(1) A person that is a promoter or a manager of a horse racing syndicate does not have to comply with subsection 601ED(5) of the Act in relation to the operation of the syndicate.

Where exemption applies

(2) The exemption in subsection (1) applies in relation to a horse racing syndicate where all of the following are satisfied:

(a) the promoter of the syndicate:

(i) holds an Australian financial services licence authorizing the promoter to provide financial services in relation to the syndicate; and

(ii) is registered by a lead regulator as the promoter of the syndicate;

(b) there are no more than 50 participants in the syndicate;

(c) the total amount raised from the issue of interests in the syndicate does not exceed $500,000;

(d) each Product Disclosure Statement given in relation to interests in the syndicate:

(i) contains the information and statements required by subsection (3); and

(ii) has been approved by the lead regulator;

Note: Because a reference to a Product Disclosure Statement is taken to:

(a) include the information and statements contained in any Supplementary Product Disclosure Statement (section 1014D of the Corporations Act); and

(b) be a reference to any Replacement Product Disclosure Statement for the syndicate must meet the requirements of paragraph (d).

(e) if:

(i) applications for the minimum number of interests in the syndicate are not received; or

(ii) the minimum amount for the syndicate has not been raised;

within 6 months after the date on which the Product Disclosure Statement in respect of the syndicate is approved by the lead regulator all money received from any person who applied to participate in the syndicate, together with interest (if any) which accrued in respect of that money, is repaid within 10 business days after the end of that 6 month period;

(f) from 45 days after:

(i) applications for the minimum number of interests in the syndicate are received; or

(ii) the minimum amount for the syndicate has been raised;

the syndicate is registered with the lead regulator;

(g) the syndicate agreement for the horse racing syndicate includes the terms referred to in subsection (4), unless these terms are excluded, modified or varied with the written agreement of all participants in the syndicate."

Product Disclosure Statement requirements

(3) For the purposes of subparagraph (2)(d)(i), the information and statements required in the Product Disclosure Statement are all of the following:

(a) the information required by Subdivision C of Division 2 of Part 7.9 of the Act;

(b) the name of the horse or horses to which the syndicate relates;

(c) the name of the promoter of the syndicate;

(d) the name of the manager of the syndicate;

(e) an undertaking by the promoter that the promoter will, within 45 days after:

(i) applications for the minimum number of interests in the syndicate are received; or

(ii) the minimum amount for the syndicate has been raised;

register the syndicate with the lead regulator;

(f) a statement that the manager will be required to manage the syndicate in accordance with the syndicate agreement and any rules, regulations or guidelines made by the lead regulator in relation to such manager or management;

(g) details of fees and costs in relation to the syndicate

Note: Fees and costs in relation to the syndicate would include fees paid by the promoter or manager to trainers or suppliers and costs related to the promoters' business such as administration and legal costs.

(h) details of any actual or perceived conflict of interest of the promoter or manager in relation to the syndicate;

(i) #;

(j) for each horse to which the syndicate relates, a statement as to whether the promoter was entitled to a free service to its sire;

(k) for each horse to which the syndicate relates, the purchase price and, where applicable, the passed-in price of the horse;

(l) for each horse to which the syndicate relates:

(i) if the participants in the syndicate are to have unencumbered title to the whole of the horse:

(A) a copy of the letter (vendor release statement) from the vendor or auction house confirming that the horse has been devolved to the syndicate or participants in the syndicate with unencumbered title, or confirmation by the promoter that the vendor release statement will be provided to the lead regulator before or on registration of the syndicate with the lead regulator; and

(B) a statutory declaration made by the promoter that:

(1) the promoter has a legally enforceable right to possession of the horse or that the promoter will, before or on registration of the horse racing syndicate with the lead regulator, have a legally enforceable right to possession of the horse; and

(2) the promoter will, before or on registration of the syndicate with the lead regulator, ensure that the participants in the syndicate will have unencumbered title to the horse; and

(C) confirmation that any personal property security interest registered against the title to the horse has been released or will be released and that the promoter will, before or on registration of the syndicate with the lead regulator, confirm to the lead regulator that the personal property security interest has been released; or

(ii) if the participants in the syndicate lease the whole of the horse under a finance lease agreement in a standard form:

(A) a copy of the standard form of finance lease agreement; and

(B) a statutory declaration made by the promoter that the promoter will, before or on registration of the syndicate with the lead regulator, ensure that participants in the horse racing syndicate lease the horse under a finance lease agreement in that standard form;

(m) a notice that a participant may elect to have a horse tested for a prohibited substance under the Australian Rules of Racing, with the cost of testing to be borne by all participants (whether or not they elected to have the horse tested).

The role of the manager

(4) For the purposes of paragraph (2)(g), the terms of the syndicate agreement are:

(a) the manager of the horse racing syndicate must manage the syndicate in accordance with the terms of the syndicate agreement throughout its duration unless that person:

(i) retires after being given written consent by the majority of the participants of the syndicate not associated with the retiring manager;

(ii) is removed in accordance with the terms of the agreement; or

(iii) otherwise retires or is removed after being given written consent by the lead regulator; and

(b) if the manager of the syndicate retires or is removed in accordance with paragraph (a), a new manager will be appointed and that manager will become subject to the terms of the syndicate agreement.

Conditions of the exemption

(5) A manager that relies on the exemption in subsection (1) in relation to a horse racing syndicate must:

(a) keep accounting records that correctly record and explain the transactions and financial position of the syndicate and that would enable financial statements to be prepared in respect of the syndicate from time to time; and

(b) in respect of each financial year, prepare financial statements in respect of the syndicate; and

(c) lodge the financial statements in respect of the horse racing syndicate with the lead regulator within 90 days after the end of each financial year; and

(d) if ASIC asks the manager in writing for a copy of the financial statements in respect of the syndicate, give the copy of those statements to ASIC within 14 days; and

(e) keep a separate account with an Australian bank in respect of the syndicate and use that account for the deposit and payment of all money relating to the operation of the syndicate.

(6) A promoter that relies on the exemption in subsection (1) in relation to a horse racing syndicate must comply with the conditions in subsection (7) to (14) in relation to the syndicate.

(7) The promoter must provide the lead regulator with a copy of all of the following in relation to the horse racing syndicate:

(a) the syndicate agreement and any changes to the syndicate agreement – promptly after the syndicate agreement is entered into or the changes are made;

(b) any finance lease agreement and any changes to the finance lease agreement – promptly after the finance lease agreement is entered into or the changes are made;

*(c) any other agreement (**relevant agreement**):*

(i) establishing or affecting the syndicate; or

(ii) that relates to the syndicate and to which a participant in the syndicate is a party;

and any changes to a relevant agreement – promptly after the relevant agreement is entered into or the changes have been made;

(d) each Product Disclosure Statement, before it is given to an offeree;

(e) any other information to be provided by the promoter or statement that is reasonably likely to induce people to acquire interests in the syndicate – before it is published.

(8) The promoter must not give an offeree a Product Disclosure Statement unless the promoter has received the approval of the Statement from the lead regulator.

(9) The promoter must not, without the approval of the lead regulator, advertise interests in the horse racing syndicate or publish any statement that is reasonably likely to induce people to acquire interests in the syndicate.

(10) The promoter must provide to the lead regulator any assistance or information reasonably required by the lead regulator in relation to the promoter or the horse racing syndicate.

(11) The promoter must not engage in acts or omissions in relation to the horse racing syndicate unless the promoter reasonably believes those acts or omissions are in compliance with any rules, regulations or guidelines made by the lead regulator that apply to the promoter in relation to the syndicate.

(12) The promoter must provide to ASIC any assistance or information reasonably required by ASIC in relation to the promoter or the horse racing syndicate.

(13) The promoter must, before or on registration of the horse racing syndicate with the lead regulator, ensure that either:

(a) The participants in the horse racing syndicate have unencumbered title to the whole of the horse racing syndicate horses; or

(b) The participants in the horse racing syndicate lease the whole of the horse racing syndicate horses under a finance lease agreement in standard form.

(14) The promoter must comply with section 1017D of the Act as if interests in the horse racing syndicate were a managed investment product."

"*manager*" is defined as:

"(a) in relation to a horse racing syndicate, means the person:

(ii) holding office as manager under the syndicate agreement; or

(iii) otherwise holding office as manager of the horse racing syndicate with the approval of the lead regulator; and …."

"*participant*" is defined as:

"a person who holds a beneficial interest in a horse racing syndicate or a private horse breeding scheme whether jointly or otherwise."

It should be noted here that this definition of "participant" treats persons who hold interests jointly differently to how they are treated under the Act.

Under the Act, the joint holders[93] of an interest in a scheme count as a single member.

[93] section 9.

PART 3: WHEN MUST THE PROMOTER OF INTERESTS IN A HORSE RACING SCHEME BE LICENSED?

3.1 Part summary

This part deals with:

(a) the statutory provisions that require any person who operates a financial services business to hold a financial services licence (AFS Licence) covering the provision of the financial services; and

(b) the ARR that require any person who wants to promote or make an offer of shares in a horse to be licensed, and to be an approved promoter with a lead regulator.

Conclusion

Under the Act:

(a) a horse racing scheme, other than a scheme which qualifies as a "private" scheme under section 601ED, generally will be subject to regulation as a managed investment scheme;

(b) an "interest" in a managed investment scheme is a "financial product";

(c) a person who operates a financial services business dealing in a financial product or providing a financial service must hold an AFS Licence covering the provision of the financial services[94] [or be an authorized representative of a licensee[95]];

(d) the promoter, manager (and responsible entity) of a horse racing scheme which is:

(i) a registered managed investment scheme;

(ii) a personal offer scheme; or

(iii) a wholesale scheme;

must hold an AFS Licence [or be an authorized representative of a licensee].

Under the ASIC Instrument, the promoter of a horse racing syndicate which is the subject of a lead regulator approved PDS must hold an AFS Licence[96] [or be an authorized representative of a licensee], but the members may, with the approval of the lead regulator, appoint a manager who is not licensed.

There is no statutory exemption or ASIC Instrument relief from the requirement for a "promoter" of such schemes to be licensed, regardless of whether or not a scheme is eligible for a specific statutory exemption or ASIC Instrument relief from the requirement to be registered.

Under the ARR, any person who wants to promote or make an offer of shares in a thoroughbred horse for the purpose of using it for racing must:

(a) hold an appropriate AFS Licence [or be an authorised representative of a licensee];

(b) be on the register of approved promoters [or authorised representatives] of a lead regulator; and

(c) obtain approval of a PDS for each offer of interests prior to making the offer.

3.3 Carrying on a financial services business

3.3.1 The requirement to be licensed

[94] Section 911A(1).
[95] Section 911A(2).
[96] SR 9 – Promoter Syndicates

Any person who is "*carrying on a financial services business",* which includes the kind of activity that constitutes "*dealing in a financial product*", or "*providing a financial service*", must hold an appropriate AFS Licence [or be an authorised representative of a licensee], unless an exemption under the Act applies, or administrative relief is afforded by an ASIC Instrument.

The limited asset classes that have been afforded administrative relief [ASIC Instrument or Class Order] can generally be characterized as "non-speculative" and for "personal use."

Section 911A states:

> ***"Need for an Australian financial services licence***
>
> *(1) Subject to this Section, a person who carries on a financial services business in this jurisdiction must hold an Australian financial services licence covering the provision of the financial services…*
>
> *(2) However, a person is exempt from the requirement to hold an Australian financial services licence for a financial service they provide in any of the following circumstances:*
>
> *(a) the person provides the service as a representative of a second person who carries on a financial services business and who:*
>
> *(i) holds an Australian financial services licence that covers the provision of the services; or*
>
> *(ii) is exempt under this subsection from the requirement to hold an Australian financial services licence that covers the provision of the services; …."*

Section 911D states:

> "***When a financial services business is taken to be carried on in this jurisdiction***
>
> *(1) For the purposes of this Chapter, a financial services business is taken to be carried on in this jurisdiction by a person if, in the course of the person carrying on the business, the person engages in conduct that is:*
>
> *(a) intended to induce people in this jurisdiction to use the financial services the person provides; or*
>
> *(b) is likely to have that effect;*
>
> *whether or not the conduct is intended, or likely, to have that effect in other places as well.*
>
> *(2) This section does not limit the circumstances in which a financial services business is carried on in this jurisdiction for the purposes of this Chapter."*

3.3.2 Financial product

A. Determining "what is" and 'what is not" a financial product

As to "what is" and "what is not" a financial product, see section 763A [Definitions], section 764A [specific things that are financial products (subject to Subdivision D)] and section 765A [specific things that are not financial products].

An "*interest*" in a managed investment scheme that falls within the requirements for registration under section 601ED(1) [i.e., it has more than 20 members or "*…was promoted by a person, or an associate of a person, who was, when the scheme was promoted, in the business of promoting managed investment schemes*"] is a "*financial product"* and subject to regulation.

Under section 765A(1)(s), an "*interest*" in a managed investment scheme that falls outside of the requirement for registration under section 601ED(1) [i.e. it does not have more than 20 members and was established by a person who was not when the scheme was

established "*…in the business of promoting managed investment schemes*"], is not a "*financial product*" and therefore falls outside Chapter 7 [Financial Services and markets] altogether, save for the provisions of section 1010B [*Part does not apply to financial products not issued in the course of a business*], which effectively deem all "*issues*" of interests in a managed investment product "*is taken to occur in the course of a business of issuing financial products*." The provisions of that section are relevant to section 1012E ["*Personal Offers*" under the 20/12 Rule]

Section 1010B states:

> ***"Part does not apply to financial products not issued in the course of a business***
>
> *(1) Apart from Division 5A, nothing in this Part applies in relation to a financial product that is not or was not issued, or that will not be issued, in the course of a business of issuing financial products.*
>
> *(2) For this purpose, the issue of:*
>
> *(a) any managed investment product; or*
>
> *(aa) any foreign passport fund product; or*
>
> *(b) any superannuation product;*
>
> *is taken to occur in the course of a business of issuing financial products."*

B. Determining what activity constitutes "dealing in a financial product"

The term "*dealing in a financial product*" includes "*issuing*", "*underwriting*", and "*disposing of*", the product.

The following conduct (whether engaged as principal or agent) constitutes "*dealing in a financial product*":

- "*applying for*" or "*acquiring*" a financial product;
- "*issuing*" a financial product;
- in relation to securities or managed investment interests – "*underwriting*" the securities or interests;
- "*varying*" a financial product; and
- "*disposing* of" a financial product.

Arranging for a person to engage in any conduct referred to above is also "*dealing*" unless the actions concerned amount to providing financial product advice.

Section 761E states:

> "***Meaning of issued, issuer, acquire and provide in relation to financial products***
>
> *General*
>
> *(1) This Section defines when a financial product is issued to a person. It also defines who the issuer of a financial product is. If a financial product is issued to a person:*
>
> *(a) the person acquires the product from the issuer; and*
>
> *(b) the issuer provides the product to the person.*
>
> *Note: Some financial products can also be acquired from, or provided by, someone other than the issuer (e.g. on secondary trading in financial products).*

Issuing a financial product

(2) Subject to this section, a financial product is issued to a person when it is first issued, granted or otherwise made available to a person."

Section 764A states [that an "interest" in a MIS is a "financial product"] as follows:

"Specific things that are financial products (subject to subdivision D)

(1) Subject to Subdivision D, the following are financial products for the purposes of this Chapter:

(a) a security:

(b) any of the following in relation to a registered scheme:

(i) an interest in the scheme;

(ii) a legal or equitable right or interest in any interest covered by subparagraph (i);

(iii) an option to acquire, by way of issue, an interest or right covered by subparagraph (i) or (ii);

(ba) any of the following in relation to a managed investment scheme that is not a registered scheme, other than a scheme (whether or not operated in this jurisdiction) in relation to which none of paragraphs 601ED(1)(a), (b) and (c) are satisfied:

(i) an interest in the scheme;

(ii) a legal or equitable right or interest in an interest covered by subparagraph (i);

(iii) an option to acquire, by way of issue, an interest or right covered by subparagraph (i) or (ii)."

3.4 Relevant case law

"carrying on a business"

"*Carrying on a business*", according to the case law, means a "*series of repetitious acts*" [see ***Smith v Anderson***[97]], and "*features of continuity and system*" [***Hyde v Sullivan***[98]].

In ***Hungier v Grace***[99], *Barwick J* said:

[15] The decision whether a person is one "whose business (whether or not he carries on any other business) is that of money-lending" can only be reached after a close examination of the facts in each particular case. It is not enough merely to show that a person has lent money to another. In ***Edgelow v MacElwee (1918) 1 KB 205, at p 206,*** *McCardie J* said:

"There must be more than occasional and disconnected loans. There must be a business of money-lending, and the word "business" imports the notion of system, repetition and continuity … The line of demarcation cannot be defined with closeness or indicated in any specific formula. Each case must depend on its own peculiar feature. It is ever a case of degree."

In ***Ballantyne v Raphael***[100] the Victorian Supreme Court held that a scheme involved a single transaction of purchasing a block of land, subdividing it, and selling the subdivided lots did not amount to carrying on a business. The operation of a single scheme of limited scope will generally

[97] 1874-80 All ER Rep 1121.
[98] (1956) 56 SR(NSW) 113.
[99] [1972] HCA 42; (1972) 127 CLR 210.
[100] (1889) 15 VLR 538.

not amount to carrying on a business. But in ***United Dominions Corp Ltd v Brian Pty Ltd***[101] where a single joint venture was held to be carrying on a business. The size and scope of the scheme was held to be relevant.

In ***ASIC v McNamara***[102] [see *[16], [17], [18], [19], [22], [23], [24], [41] and [42]*], a limited partnership was formed to provide finance to a joint venture entity. Two individuals, acting on behalf of the general partner, sought, and received subscriptions from 55 mostly retail investors for units in the limited partnership. The conduct in question spanned the transition date for the FSR reforms. The limited partnership was not registered as a managed investment scheme and neither the general partner nor the individuals acting on its behalf held a dealers' licence under the old law or an AFS Licence under the new law. The Federal Court held that the offering of units to 55 investors was sufficiently systematic, repetitious, and continuous that the general partner and the individuals concerned were all carrying on a securities business under the old law and a financial services business under the new law and had contravened the Corporations Act by not having the requisite licence.

> *[22] "In light of those provisions and the general findings which I have made, I further find that AFLP was the issuer of a financial product by providing units in the partnership to the limited partners. In doing so he was acting in a systematic, repetitious and continuous manner. Consequently, I am satisfied that AFLP required an Australian Financial Services licence (AFSL licence) to enable it to carry on the business of dealing in those products."*

"issuing"

In ***Australian Softwood Forests Pty Ltd v Attorney-General (NSW); Ex Rel. Corporate Affairs Commission***[103], *Mason J* said:

> *[30] "… It is clear that the word is sufficiently large in content to embrace the process by which the grower secures a binding contract. And I see no difficulty in saying that interests are issued to the public if, as will be seen to be the case, there are many instances in which an interest is allotted to an individual, the individual being selected or identified as the recipient of the interest by reference to his being a member of the public."*

3.5 The requirement under the ARR that a promoter be licensed and on the register of approved promoters of a lead regulator

"SR 9 – Promoter Syndicates

(1) Any person who wants to make an offer to promote shares in a horse/s must:

(a) hold an Australian Financial Services Licence ("AFSL") issued by ASIC;

(b) comply with any provision of the Corporations Act in relation to the promotion, offering, or issue of shares in horses; and

(c) comply with the provisions and requirements of any applicable ASIC Class Order or instrument [including ASIC Corporations (Horse Schemes) Instrument 2016/790, or any successor to it] in relation to the promotion, offering, or issue of shares in horses.

(2) Before an offer of shares in a horse/s is made, an AFSL holder must be recorded as a registered Promoter in the Register of Promoters held by a PRA.

(3) Promoters must obtain approval from a PRA for each Product Disclosure Statement prior to an offer of shares in a horse being made."

3.6 The Manager and responsible entity of a Horse racing scheme

3.6.1 The requirement to be licensed

The responsible entity of a horse racing scheme that is a registered managed investment scheme must be an AFS Licensee.

[101] (1985) 157 CLR 1 at 15.
[102] ibid, at p 16 of this paper.
[103] (1981) 148 CLR 121.

The responsible entity of a registered scheme must be a public company that holds an AFS Licence authorizing it to operate a managed investment scheme[104].

The responsible entity must operate the scheme and perform the functions conferred on it in accordance with the scheme's constitution and the Act. The responsible entity may appoint an agent, or otherwise engage a person, to do anything that it is authorized to do in connection with the scheme[105].

A person (such as a manager or promoter) who deals by arranging for subscriptions in the syndicate or promotes interests in:

(a) a personal offer scheme; or

(b) a wholesale scheme;

must also be an AFS Licensee, unless there is an available exemption from licensing.

3.6.2 The manager, if not the promoter, of a lead regulator approved (ASIC Instrument compliant) scheme need not be licensed

The ASIC Instrument includes terms that relieve the manager, if not the promoter, from the requirement to hold an AFS Licence, with the approval of the lead regulator.

3.7 AFS Licence conditions

The type of AFS Licence required to engage in the activity of offering interests in small-scale horse racing schemes which comply with the terms of the ASIC Instrument is a restricted licence for this activity only. The conditions of this type of licence are not as onerous on the licensee as the conditions of an unrestricted licence of the type required to enable the licensee to engage in the activity of offering shares in registered schemes.

A comparison of the different net tangible asset ("NTA") and surplus liquid funds ("SLF") requirements for a restricted and unrestricted AFS Licence best illustrates this point:

(a) the minimum NTA for a restricted licence is $50,000, compared to $150,000 for an unrestricted licence; and

(b) the minimum SLF for a restricted licence is $50,000, compared to $150,000 for an unrestricted licence.

Such conditions and requirements are imposed to ensure that a licensee, responsible for handling client money, has assets and funds of its own sufficient to maintain the financial viability of its business.

[104] section 601FA.
[105] section 601FB.

PART 4: WHAT INFORMATION MUST BE DISCLOSED TO PROSPECTIVE INVESTORS IN A PDS?

4.1 Part summary

This part deals with the statutory provisions and the terms of the ASIC Instrument that require the promoter of an "offer of interests" in a horse racing scheme to disclose to prospective investors who are "retail clients", all key information about the product on offer that is reasonably required by prospective investors to enable them to make an informed decision whether to invest.

Conclusion

Under the Act, both the nature of the key information about the product that must be disclosed to prospective investors who are "retail clients", and the format in which that information must be set out in a PDS is prescribed.

Under the ASIC Instrument, the nature of the key information about the product that must be disclosed to prospective investors in a PDS approved by a lead regulator is prescribed.

4.2 The nature of the information that must be disclosed

A PDS for an "offer of interests" in a registered managed investment scheme must include all key information about the product that prospective investors who are "retail clients" might reasonably require to be able to make an informed decision whether or not to acquire the product. Key information should, where practicable, be included in the PDS, and not be incorporated by reference.

The statutory provisions dealing with the content of a PDS are set out in Part 7.9 of the Corporations Act, specifically sections 1013C [PDS content requirements], 1013D [PDS – main requirements] and 1013E [General obligation to include other information that might influence a decision to acquire].

The provisions of section 1013D require that the following information appear in a PDS:

> *"(1) ……., a Product Disclosure Statement must include the following statements, and such of the following information as a person would reasonably require for the purpose of making a decision, as a retail client, whether to acquire the financial product;*
>
> *(a) a statement setting out the name and contact details of the issuer of the product;*
>
> *(b) information about any significant benefits to which a holder of the product will or may become entitled, the circumstances in which and times at which those benefits will or may be provided, and the way in which those benefits will or may be provided; and*
>
> *(c) information about any significant risks associated with holding the product; and*
>
> *(d) information about:*
>
> *(i) the cost of the product; and*
>
> *(ii) any amounts that will or may be payable by a holder of the product in respect of the product after its acquisition, and the times at which those amounts will or may be payable; and*
>
> *(iii) if the amounts paid in respect of the financial product and the amounts paid in respect of the other financial products are paid into a common fund – any amounts that will or may be deducted from the fund by way of fees, expenses or charges; and*

(e) if the product will or may generate a return to a holder of the product – information about any commission, or other similar payments, that will or may impact on the amount of such a return; and

(f) information about any other significant characteristics or features of the product or of the rights, terms, conditions and obligations attaching to the product; and

(g) information about the dispute resolution system that covers complaints by the holders of the product and about how that system may be accessed; and

(h) general information about any significant taxation implications of financial products of that kind; and

(i) information about any cooling-off regime that applies in respect of acquisitions of the product (whether the regime is provided for by a law or otherwise); and

(j) …

(k) any other statements or information required by the regulations; and

(l) if the product has an investment component – the extent to which labour standards or environmental, social or ethical considerations are taken into account in the selection, retention, or realization of the investment; and

(m) unless in accordance with the regulations, for information to be disclosed in accordance with paragraphs (b), (d) and (e), any amounts are to be stated in dollars.

(2) For the purposes of paragraph (1)(d), an amount will or may be payable in respect of a financial product by the holder of the financial product if:

(a) the holder will or may have to pay an amount in respect of the product; or

(b) an amount will or may be deducted from:

(i) a payment to be made by the holder; or

(ii) a payment to be made to the holder; or

(iii) an amount held on the holder's behalf under the financial product; or

(c) an account representing the holder's interest in the financial product will or may be debited with an amount.

It includes an amount that the holder will or may have to pay, or that will or may be debited, as a fee, expense or charge in relation to a particular transaction in relation to the financial product."

Section 1015C states:

"***How a Statement is to be given***

(1) A Statement:

(a) must be:

(i) given to a person, or the person's agent, personally; or

(ii) sent to the person, or the person's agent, at an address (including an electronic address) or fax number nominated by the person or the agent; and

(b) may be printed or be in electronic format.

(2) … to (4) …

(5) The regulations may specify requirements as to:

(a) the manner in which a Statement may be given to a person; and

(b) the presentation, structure and format for a Statement ……..”

REG 7.9.16N[106] states:

“Presentation, structure and format of fees and costs in Product Disclosure Statements

(1) For paragraph 1015C(5)(b) of the Act, the information required by paragraphs 1013(D) (1)(d) and (e) of the Act must be set out in a single Section of the product Disclosure Statement (fees Section) with the heading “Fees and other costs.”

(2) The fees Section of a Product Disclosure Statement must include:

(a) the Fees and Costs Template, comprising the template and the additional explanation of fees and costs set out in Part 2 of Schedule 10; and

(b) an example of annual fees and costs and associated notes as set out in Part 2 of Schedule 10; and

(c) the boxed Consumer Advisory Warning Statement set out in Part 2 of Schedule 10.”

The following ASIC Regulatory Guides are essential reading for any person involved in the preparation of a PDS:

(a) RG 97 [Disclosing fees and costs in PDS and periodic statements] issued in March 2017; and

(b) RG 168 [Disclosure: Product Disclosure Statements (and other disclosure obligations)] issued in October 2011.

The following parts of these RGs warrant highlighting here:

Complying with the worked example of annual fees and costs

RG 97.201

“PDSs for managed investment products must provide retail clients with a prescribed worked example of the application of fees and costs during a single year’s holding of the product: Div 5 of Pt 2 of Sch 10.”

RG 97.202

“If the nature of the product and its fees and costs arrangement supports disclosure in the prescribed format, that format must be used and prescribed information cannot be omitted. An example of such a product is an investment-type product.”

RG 97.203

“In other cases, we expect the issuer to adopt a format that provides retail clients with a clear example (or examples) of the application of the fees and costs arrangements of the product.”

RG 97.204

“Any adapted format for the example of annual fees and costs should bear in mind the objectives of the enhanced fee disclosure regulations and continue to reflect the central features of the prescribed format, including:

[106] Corporations Regulations 2001.

(i) the placement of the example of annual fees and costs in the fees Section of the PDS;

(ii) making the minimum necessary adaptations to the required preamble to the worked example;

(iii) that the fees reflected, as distinct from any indirect costs, should be the typical ongoing amounts that apply to the product, as required to be disclosed in the worked example;

(iv) for a PDS available in a particular financial year, calculating indirect costs that are included in management costs on the previous financial year (unless it is a new financial product);

(v) if contributions are clearly not relevant, the adapted disclosure need not refer to the contributions as would otherwise be required in the worked example;

(vi) that management costs are calculated in accordance with the definition in the enhanced fee disclosure regulation, as modified by [CO 14/1252];

(vii) that the adapted format note any establishment and withdrawal fees that may apply consistent with the prescribed content and format for the worked example."

RG 97.205

"We also expect that in adapting the disclosure product, issuers will provide a clear, concise and effective description of the annual fees and costs for the product and make such disclosures as necessary to ensure it is not misleading or deceptive …."

Disclosing start-up and initial one-off fees and costs

RG 97.214

"Generally, start-up and initial one-off fees and costs that will be paid should not be included in the fees and costs template. This is because management costs are intended to capture all relevant costs involved in managing the registered scheme and deriving an investment return."

RG 97.215

"For example, some agricultural schemes have a "start-up" cost that is often tax deductible for the member. Typically, this cost bundles some or all of the management costs for the scheme upfront."

RG 97.216

"Start-up and initial one-off fees or costs are not typical ongoing fees and therefore, if they are charged directly to members' accounts, do not have to be reflected in the example of annual fees and costs. However, to avoid the possibility that retail clients may misunderstand the cost structure of the product, responsible entities must explain these start-up and initial one-off fees and costs. It may be appropriate to provide an additional example that demonstrates the effect of these costs in the costs structure of the product."

Consumer advisory warning

RG 97.217

"The consumer advisory warning contains disclosures specific to managed investment products in order to provide retail clients with a relevant and accurate warning."

"Note: [CO 14/1252] modifies the consumer advisory warning for managed investment products by removing the reference to an "employer", because it is unlikely to be relevant, and by referring to an investment rather than an account, to avoid confusion where the PDS is used in connection with a custodial arrangement under which acquisition will not be made by the retail investor directly: cl 221(3)."

RG97.218

> *"The consumer advisory warning can be excluded for certain managed investment products when the structure of the product negates the relevance of having a consumer advisory warning, as there is no fund from which fees and costs are paid – for example, timesharing schemes: cls 221(2) and 222 of Sch 10."*

Disclosing fees, charges, and returns

RG 168.82

> *"We believe that the need for clear, concise and effective disclosure is most relevant for the disclosure of fees and charges and, in the case of investment-based products, the disclosure of returns. Information about fees, charges and investment returns is a key consideration for consumers when making decisions about financial products, and research show that it is often the most difficult information for consumers to understand."*

RG 168.84

> *"Division 4C of Pt 7.9 of the Corporations Regulations requires PDSs for superannuation products and PDSs for managed investment products to include a fees and costs template (although for superannuation products and simple managed investment products a simplified version of the template must be used in the PDS, with the full template incorporated by reference): Sch 10D item 8 and Sch 10E item 8. The regulations include standard descriptions and calculation methods for fees and costs. These measures are designed to assist with clear an, concise and effective disclosure of information about fees and costs and to allow for easier comparability of fees and costs information in PDSs for investment products. The enhance fee disclosure regulations also apply to periodic statements for superannuation products and for managed investment products."*

RG 168.85

> *"The types of product information that a consumer should be able to easily understand and compare include:*
>
> *(a) what the fees and charges are, the amount of fees (expressed as an amount in dollars where this is required), who the fees are paid to, what the fees are for, how and when the fees are paid, and how fees impact on returns;*
>
> *(b) whether fees are variable and, if so, how and when they vary, including through negotiation or the impact of rebates or discounts (e.g. group life rebates);*
>
> *(c) how returns are calculated and whether they are shown on a consistent basis. For example. Generally, if historical returns are disclosed for various investment strategies over different periods of time (e.g. 1, 3, 5 and 10 years), then, for each investment strategy, consumers should be able to understand whether or not the returns are shown on a consistent basis for each period. Generally, returns for financial products (including for different investment strategies of a financial product) covered by a PDS should be calculated on a consistent basis wherever possible: and*
>
> *(d) typical and material factors that may affect returns, including risk."*

RG 168.86

> *"If information about fees, charges and returns is not clear, concise and effective, comparability of products is harder to achieve."*

4.3 Additional information that should be included as attachments to a PDS for a typical horse racing scheme

Given the intricate nature of the contractual arrangements to which an investor will become a party by acquiring an interest in a typical horse racing scheme promoted by a person who is in the business of dealing in interests/shares, the PDS should include as attachments copies of:

(a) the Owners Deed or agreement governing the legal relationship between the co-owners, and between the co-owners and the manager;

(b) the trainer's Training Agreement and Fees Notice;

(c) the veterinary certificate upon which the promoter relies as evidencing the horse to be in good health and condition and suitable for syndication; and

(d) the Memorandum of Insurance, together with a statement to the effect that the full policy wording is available upon request.

4.4 The requirement for disclosure in relation to an "offer of shares" in a lead regulator approved (ASIC Instrument compliant) scheme

A PDS for a lead regulator approved (ASIC Instrument compliant) scheme must also comply with Part 7.9 of the Corporations Act and the additional requirements set out in the ASIC Instrument.

The lead regulators have published various *Product Disclosure Guidelines* to assist promoters when compiling a PDS for an "offer of shares" under the ASIC Instrument. Promoters should not interpret such guidelines as prescribing a lesser standard of disclosure for such offers than the statutory provisions prescribe for registered schemes.

RNSW has published the following documents, which appear on its website (in October 2018):

(a) Guidelines for Promoters re Product Disclosure Statements [Jan 2017];

(b) Pro forma Product Disclosure Statement (PDS);

(c) Information for Prospective Owners – Promoters may include Management Fees in PDSs; and

(d) Racing NSW – Guide to Ownership Costs.

All promoters, regardless of the state or territory in which they operate, should read these documents, together with any similar documents published by their own lead regulator, before proceeding to compile a PDS for the sale of interests. However, it should not be assumed that the Pro forma PDS referred to in paragraph (c) of the previous satisfies the requirements for a PDS.

4.5 General requirements for a PDS

The disclosure of key information, in the form of a disclosure statement, must be:

(a) delivered, or made available, for free, to an investor before the point of sale, to afford the investor the opportunity to consider the information and make an informed decision about whether to invest;

(b) delivered or made available in a manner that is appropriate for the target investor;

(c) in plain language and in a simple, accessible, and comparable format to facilitate a meaningful comparison of information disclosed for competing products; and

(d) clear, accurate and not misleading to the target investor.

4.6 Restrictions on advertising and promotion

The general requirement under the Act is that a person must not promote (including advertise) an "offer of interests" in a managed investment scheme where participation is available to "retail clients" unless:

(a) an appropriate PDS is available; and

(b) a Form SF88 [PDS in-use notice] has been lodged with ASIC.

If an "offer of interests" in a horse racing scheme is to be the subject of a PDS approved by a lead regulator under the terms of the ASIC Instrument, then the PDS must be approved prior to the commencement of any promotion. Similarly, any advertising must also be lodged with and approved by a lead regulator prior to publication.

The promoter of an "offer of interests" that requires a PDS must comply with the provisions of section 1018A [Advertising or other promotional material for product must refer to the PDS] when undertaking any advertising or public promotion. Such advertising or public promotion must specify:

(a) the issuer (or issuer and seller) of the shares and refer to the PDS;

(b) that a PDS is available; and

(c) that a prospective investor should consider the PDS when deciding whether to acquire the interest(s).

Failure to comply with the provisions of section 1018A (1) is an offence (section 1311 [General penalty provisions]).

There are no regulations applying to the advertising or public promotion of an "offer of interests" in a Horse racing scheme that is a "wholesale scheme", although any advertisement, or public promotion, should clearly specify both the nature of the scheme, and that participation is available only to "wholesale clients."

PART 5: WHAT ARE THE SANCTIONS FOR NON-COMPLIANCE?

5.1 Part summary

This part deals with the statutory provisions and the ARR that prescribe sanctions and penalties which may be imposed on persons who do not comply with the requirements of the regulatory regime.

Conclusion

ASIC has the power to pursue enforcement action and a range of remedies against persons who breach the provisions of the Act.

Each Principal Racing Authority, with its jurisdiction:

(a) is responsible for administering the ARR; and

(b) has the capacity to investigate and prosecute any person it suspects of breaching the ARR;

and as a Lead regulator under the ASIC Instrument:

(c) is responsible for administering the terms of the relief set out in the ASIC Instrument; and

(d) has the capacity to refer to ASIC for investigation and prosecution, any person it suspects of breaching the Act. In fact, it is probably fair to say that ASIC has an expectation that each Principal Racing Authority will undertake appropriate surveillance activities and refer suspected breaches of the Act for investigation and prosecution.

5.2 ASIC

ASIC has the power to investigate complaints, or suspected breaches of the Act, and to pursue a variety of enforcement remedies, depending upon the seriousness and consequences of the misconduct. Enforcement action may include prosecution and the imposition of punitive penalties, or orders requiring the payment of compensation.

If a person operates an unregistered managed investment scheme that is otherwise required to be registered, then there are adverse consequences that may apply, including:

(a) a maximum penalty for individuals of 200 penalty unit points ($22,000) or five years imprisonment, or both, and a maximum penalty for corporations of 1,000 penalty units ($110,000);

(b) upon application to the court by either ASIC, the person operating the scheme, or a member of the scheme, the court may order that the unregistered scheme be wound up[107];

(c) where a court finds that an investor has suffered, or is likely to suffer loss or damage because of the contravention, the court may make orders to compensate that investor for such loss or damage[108]; and

(d) a contract with an investor to subscribe for interests is voidable at the option of the investor[109].

5.3 Lead regulators (principal racing authorities)

Lead regulators also have the power to investigate complaints and suspected breaches of the Act and the ASIC Instrument, and to pursue a variety of enforcement remedies under the ARR.

[107] section 601EE.
[108] section 1325.
[109] section 601MB.

5.4 Compliance Check List

ASIC has overall responsibility for administering the regulatory regime, including the activities of the principal racing authorities as lead regulators for the purpose of administering the terms of the ASIC Instrument relief within their respective jurisdictions.

Set out in the following table is a compliance check list for both a registered managed investment scheme and a scheme that is the subject of a PDS approved by a Lead regulator.

ASIC registered managed investment scheme	**Scheme/Syndicate the subject of a lead regulator approved PDS**
Constitution	Agreement
Compliance Plan	
requirement to obtain compulsory managed investments PI insurance	
application to ASIC to register scheme	
PDS	PDS
	application to lead regulator to approve PDS
PDS in-use notice – ASIC Form FS88	PDS in-use notice – ASIC Form FS88
offer and sale of interests • provision of PDS to prospective investors prior to the point of sale • payment of application price by investors applying for shares • receipt of application money by promoter into designated trust account [which money must be refunded, together with any interest earned, if the offer is not fully subscribed and shares allotted] • Cooling-off • transfer of the legal and beneficial title in the horse to investors, unencumbered	offer and sale of interests • provision of PDS to prospective investors prior to the point of sale • payment of application price by investors applying for shares • receipt of application money by promoter into designated trust account [which money must be refunded, together with any interest earned, if the offer is not fully subscribed and shares allotted] • Cooling-off • transfer of the legal and beneficial title in the horse to investors, unencumbered
issuing and allotment of shares	issuing and allotment of shares
registration of scheme with the registrar of racehorses	registration of scheme with the registrar of racehorses
registration of the horse in the name of the scheme (or the members, if no more than 20)	registration of the horse in the name of the scheme (or the members, if no more than 20)
establishment of designated scheme bank account	establishment of designated scheme bank account (which obviously can be dispensed with if arrangements are put in place for proportionate direct billing of members for horse costs and proportionate direct payment to members of prize money)
accounting and annual financial reports	accounting and annual financial reports
annual syndicate and compliance plan audits – external auditors	
copies of audited annual financial report and compliance audit certificate to be lodged with ASIC and provided to members	copies of annual financial report to be lodged with lead regulator and provided to members
Compliance	compliance
Surveillance	surveillance
Breaches	breaches
Penalties	penalties

PART 6: WHAT TYPES OF HORSE RACING SCHEMES ARE PERMITTED UNDER THE ACT AND THE ARR?

6.1 Part summary

This part deals with the types of Horse racing schemes that are permitted under the Act and the ARR.

Conclusion

(1) A horse racing scheme established as a one-off "private" scheme may not be subject to regulation under the Act. To qualify as a "private" scheme, it must not require registration under section 601ED. In other words, the scheme must not have more than 20 members and the person who established it must not be "in the business of promoting managed investment schemes."

(2) A horse racing scheme that "…was promoted by a person, or an associate of a person, who was, when the scheme was promoted, in the business of promoting managed investments schemes":

(a) generally, will fall within the requirement for registration under section 601ED, regardless of the number of members; and

(b) must be registered as a managed investment scheme, unless it is eligible for a specific statutory exemption or ASIC Instrument relief from the requirement to be registered because it qualifies as:

(i) a personal offer scheme;

(ii) a wholesale scheme; or

(iii) a lead regulator approved (ASIC Instrument compliant) syndicate.

Investors who are "retail clients" are not permitted to participate in a wholesale scheme.

All such schemes must comply with the registration requirements under the ARR.

6.2 The nature of the legal relationship between joint owners or lessees

All ownership arrangements must comply with the Act.

Section 115 states:

*"**Restrictions on size of partnerships and associations***

(1) A person must not participate in the formation of a partnership or association that:

(a) has as an object gain for itself or for any of its members; and

(b) has more than 20 members;

unless the partnership or association is incorporated or formed under an Australian law. …… Note: An offence based on subsection (1) is an offence of strict liability. For strict liability, see Section 6.1 of the Criminal Code."

All ownership arrangements must also comply with the ARR.

The number of people who may register directly as the owners or lessees of a racehorse is limited to 20, except for schemes which are eligible for the relief afforded by the ASIC Instrument.

The number of people who may register a syndicate (with the Registrar of Racehorses) and own the horse in the name of the syndicate is limited to no more than 20[110].

The legal relationship between the members of any arrangement owning or leasing a racehorse will typically be:

(a) co-ownership;

(b) partnership; or

(c) unit trust.

6.3 Public horse racing scheme – promoter must be licensed

A horse racing scheme established by a person (promoter) who is "*in the business of promoting managed investment schemes*" will be either:

(a) a registered managed investment scheme – interests may be made available to prospective investors who are either "retail clients" or "wholesale clients." There are no statutory requirements (restrictions) relating to either the number of participants, or the total amount sought, from the "issuing" of scheme interests, for this type of scheme. Disclosure of key information in a PDS is required; or

(b) an unregistered scheme that is:

(i) a personal offer scheme – interests may only be made available by "personal offer" to prospective investors who are either "retail clients", or "wholesale clients." A scheme of this type is not required to be registered, provided it complies with the 20/12 Rule. There are no disclosure requirements prescribed by the Act;

(ii) a wholesale scheme – interests may only be made available to prospective investors who are "wholesale clients." A scheme of this type is not required to be registered. There are no statutory requirements (restrictions) relating to either the number of participants, or the total amount sought, from the "issuing" of scheme interests for this type of scheme. There are no disclosure requirements prescribed by the Act; or

(iii) a lead regulator approved (ASIC Instrument compliant) syndicate – interests may be made available to prospective investors who are either "retail clients", or "wholesale clients." A scheme of this type is relieved from the requirement to be registered, provided it complies with the terms of the ASIC Instrument. It must not have more than 50 members and the total amount sought from the issue of scheme interests must not exceed $500,000. Disclosure of key information in a PDS approved by a lead regulator is required.

6.4 Private horse racing scheme – promoter may not require a licence

Interests in this type of scheme may only be made available to potential participants by a person who is not "… *in the business of promoting managed investment schemes*." A scheme of this type must not have more than 20 members. There are no disclosure requirements prescribed by the Corporations Act.

Under the ARR, the members will be subject to the terms of the TOR Co-Owners Agreement[111] unless they exclude and replace it with their own agreement.

[110] see AR.69A.
[111] Schedule 2 – Trainer & Owner Reform Rules– The TOR Rules.

APPENDIX A

Definitions and rules set out in the ARR relating to arrangements between 2 or more persons owning or leasing a racehorse

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The ARR would appear to accommodate all forms of legal ownership of a racehorse. While an individual person can register an (ownership or leasehold) interest in that person's own name, a business or company is required to register a syndicate name and hold the interest in that name, while also nominating an individual person as the manager of that interest.

Each of the following words is attributed a meaning in AR.2 for the purposes of the ARR:

"*company*" means:

> *"(a) a company incorporated or registered under the Corporations Act or any statute or ordinance of any State and/or Territory of the Commonwealth of Australia; and*
>
> *(b) a 'foreign company' within the meaning of the Corporations Act."*

"*manager*" means:

> *"a person registered with Racing Australia as the manager of a horse owned or leased by a natural person, a group of natural persons, or a Syndicate. Unless established otherwise:*
>
> *(a) The first named person appearing in the Certificate of Registration or other official ownership or leasing record held by Racing Australia will be deemed to be the manager [subject to AR63(1)]; and*
>
> *(b) If a horse is owned or leased by more than one Syndicate, the first named person appearing in the Certificate of Registration or other official ownership or leasing record held by Racing Australia will be deemed to be the manager."*

"*member*" includes:

> *"any person who has an interest of any kind in a structure through which horses can be owned pursuant to these Australian Rules, including in any Syndicate."*

"*nominator*" means:

> *"a person authorized to nominate a horse for a race. It includes:*
>
> *(a) any owner;*
>
> *(b) if a horse is leased, any lessee by or on whose behalf the horse is entered;*
>
> *(c) any registered manager of a company;*
>
> *(d) any Syndicate Manager for a Syndicate; and*
>
> *(e) any person exercising the rights of a nominator under the Rules by reason of the death of a nominator, the sale of a horse with engagements, the termination of a lease, or otherwise."*

"*person*" includes:

> *"any Syndicate, company, combination of persons, or other organizational structure recognized by these Australian Rules which owns or races a horse/s."*

"*Stud"* means:

> *"a person, company or unincorporated organization which breeds horses for racing and which during the period of 12 months immediately prior to any relevant point of time, has returned to and had accepted 5 or more mares by the Australian Stud Book and/or the Australian Register of Non-Stud Book Mares."*

"Promoter" means:

> *"any person or company who for valuable consideration offers or invites any other person or company to subscribe for shares or to participate in any scheme with objects that include the breeding and/or racing of a horse/s."*

"Promoter Syndicate" means:

> *"a Syndicate where the co-owners own their interest in a horse as a result of acquiring shares in the horse offered by a Promoter approved by a PRA and licensed under the Corporations Act and/or offered pursuant to ASIC Corporations (Horse Schemes) Instrument 2016/790 or a successor or predecessor instrument to it."*

"*Syndicate*" refers:

> *"to any one of the following structures or entities by which a horse can be owned or leased which is accepted as a Syndicate for registration under these Australian Rules:*
>
> *(a) a combination of more than one but no more than 20 persons (or a combination of more than one but no more than 50 in the case of a Promoter Syndicate entitled to exemption under ASIC Corporations (Horse Schemes) Instrument 2016/790 (or any instrument, regulation or class order that replaces or supersedes that instrument);*
>
> *(b) a company;*
>
> *(c) an unincorporated organization (including a partnership or other form of unincorporated organization, such as an unincorporated sole trader with a business name or a Stud which has been registered as a Syndicate in the name of the Stud); or*
>
> *(d) a Promoter Syndicate."*

"*trainer*" means:

> *"a person licensed or granted a permit by a PRA to train horses, and includes any persons licensed to train as a training partnership."*

AR.61 states:

> *"Only horses trained by a licensed trainer to race, official trail or jump out*
>
> *(1) To be able to be entered for or run in any race or official trial or jump-out, a horse must be trained by a person with a licence to train.*
>
> *(2) Subrule (1) does not apply:*
>
> *(a) to a horse entered for a race where the entries close more than 60 days before the advertised date for the running of a race; and*
>
> *(b) to any other race excepted under the Rules."*

AR.63 states:

> "Removal of manager of a horse
>
> *(1) Subject to the TOR Rules [and/or a term of the COA, if relevant], a manager of a horse may be removed or replaced from that position by written notice signed by the owners, lessees or Syndicate members representing more than 50% of the ownership of the horse.*
>
> *(2) A manager of a horse is of their own right [and without separate express authorization by the owners, lessees or Syndicate members] entitled to:*
>
> *(a) enter, nominate, accept or scratch a horse for any race;*
>
> *(b) engage a jockey to ride a horse in any race;*

(c) receive any prize money or trophy won by a horse;

(d) act for and represent the owners, lessees or Syndicate members in relation to the horse for the purpose of these Australian Rules;

except that where a provision of the TOR Rules [and/or a term of the STA or the COA, if relevant] specifies a process, requirement, or course of action, that provision or term binds the manager in the event of any conflict or inconsistency with this subrule.

(3) The entry or nomination of a horse for any race must state the name of the manager.

(4) The trainer of a horse who enters, nominates, accepts or scratches a horse is, absent of proof an agreement between the trainer and owners to the contrary, deemed to have done so with the authority of the manager and all other nominees."

AR.105 states

"Matters that may affect the running of a horse in a race

(1) The trainer of a horse, or any person that is in control of a horse, that is nominated for a race must:

(a) ensure that the horse is fit and properly conditioned to race;

(b) by nominating time, report to the Stewards any occurrence, condition, surgery or treatment that may affect the horse's performance in the race where the occurrence takes place, condition is present, surgery is performed or treatment is administered before nomination time;

(c) as soon as is practicable after nomination time and before acceptance time, report to the Stewards any occurrence, condition, surgery, or treatment that may affect the horse's performance in the race where the occurrence takes place, condition is present, surgery is performed or treatment is administered after nomination time and before acceptance time;

(d) if the horse is accepted for the race – as soon as practicable, report to the Stewards any occurrence, condition, surgery or treatment that may affect the horse's performance in a race where the occurrence takes place, condition is present, surgery is performed or treatment is administered after acceptance time."

(2) The Owner and/or trainer of a horse must:

(a) as soon as practicable after a race, report to the Stewards anything which might have affected the running of their horse in a race; and

(b) immediately after a race, report to the Stewards:

(i) any loss or breaking of gear which occurred during the race; or

(ii) any unusual happening in connection with the race.

(3) Further to subrule (2), if a trainer becomes aware of any condition or injury which may have affected the horse's performance in the race, the trainer must report the condition or injury to the Stewards as soon as practicable and no later than acceptance time for its next race engagement."

Schedule 2 – Trainer & Owner Reform Rules – The TOR Rules

A requirement under the TOR Rules is that the members of any ownership or leasehold arrangement (scheme) between 2 or more persons (members) to maintain, train and race a horse for their mutual benefit must have an agreement setting out the terms that will govern the legal relationship between them.

The terms of the TOR Co-owners Agreement (TOR COA) are deemed to apply [except in the case of lead regulator approved syndicates established by licensed promoters, each of which will have its own

approved agreement which must comply with the requirements of the ASIC Instrument], unless the members elect either to add to or amend those terms, or to exclude and replace that agreement with another agreement.

The terms of the TOR COA provide for the appointment of a person to manage the common enterprise on behalf of the members.

It is also a requirement under the TOR Rules that the owner(s) or lessee(s) and the trainer enter into a training agreement setting out the terms upon which the trainer will provide training and ancillary services.

The terms of the TOR Training Agreement (TOR STA) are deemed to apply, unless the parties elect either to add to or amend those terms, or to exclude and replace that agreement with another agreement. The terms of the TOR STA provide for the appointment of a licensed trainer to take actual possession and control of the horse "as a whole" for the purpose of caring for, training and racing it to best advantage for the benefit of the owner(s) or lessee(s).

Schedule 3 – Syndicate Rules

There are 14 Syndicate Rules set out in this Schedule.

"SR 1 – Members of Syndicates"

> *"A person is deemed to be a member of a Syndicate if the person has an ownership or lease interest with no more than 20 persons in total (or not more than 50 in total in the case of a Promoter Syndicate) in any undertaking, common enterprise, arrangement or scheme relating to the racing of one or more horses."*

"SR 2 – Requirement of manager of a Syndicate"

> *"In order to enter or race a horse, a Syndicate must appoint a natural person as its Syndicate manager, with that person authorized to act for and on behalf of the Syndicate (to the extent permitted by the Rules and any agreement or instrument governing the Syndicate)."*

"SR 9 – Promoter Syndicates

> *(1) Any person who wants to make an offer to promote shares in a horse/s must:*
>
> *(a) hold an Australian Financial Services Licence ("AFSL") issued by ASIC;*
>
> *(b) comply with any provision of the Corporations Act in relation to the promotion, offering, or issue of shares in horses; and*
>
> *(c) comply with the provisions and requirements of any applicable ASIC Class Order or instrument [including ASIC Corporations (Horse Schemes) Instrument 2016/790, or any successor to it] in relation to the promotion, offering, or issue of shares in horses.*
>
> *(2) Before an offer of shares in a horse/s is made, an AFSL holder must be recorded as a registered Promoter in the Register of Promoters held by a PRA.*
>
> *(3) Promoters must obtain approval from a PRA for each Product Disclosure Statement prior to an offer of shares in a horse being made."*

Racing Australia – Horse registration

The following conditions of registration are stated on the front page of the Horse Registration form:

> *Appointment of Manager*
>
> *The manager of a horse is the first named person recorded on the Registration Application. If the first named owner is a registered syndicate, the syndicate manager is the manager of the horse.*
>
> *The manager acts for and represents the other joint owners as described in the Australian Rules of Racing. A copy of the rules can be found at [www.racingaustralia.horse]. As such, the manager may sign a sign a Transfer of Ownership and Change of Share % forms on behalf of all remaining*

owners (being those owners who are neither relinquishing nor acquiring a share in the horse), provided there is no change to the share percentage of each remaining owner. The manager must notify all remaining owners of the transfer of ownership or change of share percentage in advance. By signing this Horse Registration form, each owner consents to any future changes to the ownership composition and structure of the horse requested by the manager, provided there are no changes to the share percentage of each remaining owner.

By signing this Horse Registration form:

(a) each owner agrees that RISA, to the maximum extent permitted by law, is not liable to make any payment for any claim, loss or liability that may arise from the manager signing a Transfer of Ownership or Change of Share % form; and

(b) the manager indemnifies RISA against any claim, loss or liability that arises from the manager signing a Transfer of Ownership or Change of Share % form on behalf of another person.

Following registration, the manager can only be changed by the joint owners representing a majority interest in the horse signing and lodging with RISA a Change of Manager form (available for download at [www.racingaustralia.horse/RoR/Forms.aspx). If the manager plans to relinquish his or her interest or the new manager was not previously an owner (and there is no change to the share percentage of each remaining owner), the following procedure must be followed:

(a) the joint owners representing a majority interest in the horse must complete and sign a Change of Manager form;

(b) the new manager must notify all remaining members of the change to the ownership composition and structure;

(c) a Transfer of Ownership for must be completed and signed in accordance with the usual procedures; and

(d) the completed Change of Manager and Transfer of Ownership forms must be lodged, together with RISA or the relevant PRA.

Types of Ownership

A horse can be registered in the name of up to 20 owner entities. An entity can be a:

- *natural person*
- *registered syndicate*
- *company*
- *firm*
- *stud*

Fitness and Propriety of Applicants

All individuals, including registered syndicate members, who hold a share or interest in the ownership of a racehorse are required to notify the Registrar of Racehorses if they:

(a) have been convicted of or have a pending charge against them for any offence involving violence against a person or dishonest or criminal activity in the past 10 years; or

(b) have ever been convicted under the Australian Rules of Racing or the rules of any other Racing Authority.

Details of offence must be submitted in writing prior to an application being lodged. If an individual neglects or fails to truthfully respond to these questions, this application and any other application concerning the individual may be refused or cancelled or other penalties incurred.

Rules of Racing

As a condition of the horse's registration being accepted, all owners noted on the registration form must familiarize themselves with and agree to be bound by the Rules of Racing, both local and Australian as amended from time to time. The Australian Rules of Racing can be viewed at [www.racingaustralia.horse]. For Local Rules of Racing please contact the relevant PRA.

Prize Money

How is Prize money paid?
Payment of prize money and GST is administered by the PRA in whose jurisdiction the horse became eligible to receive prize money. Please note EFT payments can only be made to Australian bank accounts. See below for more information about stakes payment options in each state.

Please note EFT payment can only be made to Australian bank accounts.

See below for more information about stakes payment options in each state.

NSW, ACT & QLD

When ALL owners provide their bank account details on the form, prize money will be paid via EFT directly into each owner's bank account according to their entitlement. If an owner does not supply bank account details, all prize money will be forwarded to the Manager (Owner 1) except where an entity is GST registered for racing purposes. Where an entity is GST registered for racing purposes and supply a valid ABN and bank account, they will receive prize money together with the GST component directly into their account.

Please note a $16.50 processing fee (GST included) will be charged for all cheque payments made for NSW and ACT. QLD only pays via EFT – no payment is made by cheque.

Vic & SA

Individual entities who supply a valid bank account on the form will receive prize money directly into their account via EFT provided that the Manager (Owner 1) has also supplied their details on the form. If no bank account details are provided for any given entity, their prize money payment will be forwarded to the Manager. If the Manager has not supplied bank details, payment will be forwarded to them by cheque.

Tas

All prize money is forwarded to the Manager (Owner 1). Where bank details are provided on the form, payment will be made via EFT. If bank details are not provided, a cheque will be forwarded. Individual entities who have elected to have their percentage of prize money paid directly to them and who supply valid bank account details on the form, will receive prize money directly into their account via EFT.

WA & NT

All prize money is paid to the Manager (Owner 1) via EFT only. Where email addresses are not supplied, an administrative fee will be charged (WA only)."

Appendix B

Misinformation published by Principal Racing Authorities – RV and RWWA

Part 1 – Are the Racing Victoria questions and accompanying statements set out in the RV APP [Nov 2011] and RV APP [Jun 2014] helpful in determining whether the owners will have day-to-day control over the operation of the syndicate?

*Part 2 – Do the answers to the Racing Victoria questions change any determination [based on the questions set out in **Appendix C**] as to whether a typical horse racing syndicate satisfies the definiton of a managed investment scheme?*

Part 3 – Statements in relation to day-to-day control and advertising set out in RV PP [Jan 2017][112]*.*

Part 4 - RWWA and statements relating to "day-to-day control."

Part 1 – Are the Racing Victoria questions and accompanying statements set out in RV APP [Nov 2011] and RV APP [Jun 2014] helpful in determining whether the owners will have day-to-day control over the operation of the syndicate? The answer to this question is "No."

In November 2011, Racing Victoria published a document APP [Nov 2011][113] in which it set out (for the first time) a series of questions it obviously considered would assist in determining whether the owners will have day-to-day control over the operation of a specific horse racing syndicate.

The questions are as follows:

> *"Q.1. Does the promoter (or a person appointed by the promoter) manage the racing syndicate?*
>
> *Q.2. Do the syndicate members pay a management/administrative fee (whether initial or ongoing)?*
>
> *Q.3. Does the manager make decisions relating to the distribution of prize money such as how and when prize money is distributed (including the withholding of prize money in the instance of defaulting or late-paying members)?*
>
> *Q.4. Does the manager manage a bank account associated with the syndicate?*
>
> *Q.5. Do the members pay a set monthly fee?*
>
> *Q.6. Does the manager make decisions relating to the racing of the horse without consulting the Owners?"*

Racing Victoria then states:

> *"If the answers to the majority of these questions is "yes", **then the syndicate will most likely be a MIS**, but if the answer to the majority of the questions is "no", **then the syndicate will most likely not be a MIS**."*

Racing Victoria also published another document along with the RV APP [Nov 2011] titled *Regulation of Promoters of Shares in Horses and Horse Syndicates [undated 2011]*, in which the following statement appeared on page 2 of that document:

> *"When the syndicate is jointly managed by its members then the definition most likely does not apply in which case no approval of the share promotion is required."*

In 2014 Racing Victoria published a revised RV APP [Jun 2014][114] with a modified set of questions directed to the person who is considering selling shares in a thoroughbred horse for racing purposes, as follows:

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[112] RV Promoter Policy [Jan 2017].
[113] RV Approved Promoter Policy [Nov 2011].
[114] RV Approved Promoter Policy [Jun 2014].

"Q.1. Do you, or a person appointed by you, intend to set up or bring together the group of investors?

Q.2. Do you, or a person appointed by you, act as manager of the group of investors on an ongoing basis?

Q.3. Do the investors pay a management or administrative fee (whether initial or ongoing)?

Q.4. Does the manager of the investor group make decisions relating to the distribution of prize money such as how and when prize money is distributed (including the withholding of prize money in the instance of defaulting or late paying members of the group)?

Q.5. Does the manager of the investor group handle a bank account associated with the investors?

Q.6. Do the investors pay a monthly fee relating to the training and care of the horse directly to the manager of the investor group?

Q.7. Does the manager make decisions relating to the racing of the horse without consulting the investors?"

Racing Victoria then stated:

> *"If the answer is "yes" to the majority of the above questions,* ***then it would usually follow that the MIS definition is met****. When the syndicate is jointly managed by its members and the answer is "no" to the majority of the above questions,* ***then the definition may not apply****."*
>
> *"In any case, Racing Victoria will closely liaise with the promoter to determine whether the MIS definition is met. In most cases, provided the promoter is not promoting syndicates with system and repetition, any unique promotion will be permitted."*

Racing Victoria also published in 2014, a revised version of another document titled: *Regulation of Promoters of Horse Shares [2014 undated]*, in which the following statement appears on page 2*:*

> *"When a person buys a share in a horse and does not have day-to-day control over his or her investment, then it's possible that he or she has purchased a share in a MIS.* ***To determine whether the promoter is offering a share in a MIS, the following questions must be asked****: …."*

The Racing Victoria questions relate to the third element of paragraph (a) of the s.9 the definition of a managed investment scheme, being "day-to-day control over the operation of the scheme."

The questions, together with the accompanying statements as to what, if any, conclusion should be drawn from the answers to those questions suggest a unique proposition – that if the terms of an "offer of interests" propose that:

(a) a person or persons other than the promoter (presumably the members) will appoint the manager;

(b) the members are not required to pay a management or administration fee;

(c) the members will:

  (i) be invoiced directly by the trainer and other service providers for their proportions of operating expenses; and

  (ii) paid directly (via the stakes payment system) their proportions of prize money:

  [as opposed to the manager establishing a syndicate bank account for receiving/paying out members' contributions to operating expenses and income (prize money)]; and

(d) the manager and the trainer will consult with the members before making significant decisions in relation to the horse and the scheme;

then these characteristics may somehow constitute the members having "day-to-day control over the operation of the scheme" and place it outside the scope of the definition of a managed investment scheme.

Racing Victoria does not explain how "no" answers to the majority of its questions can necessarily lead to the conclusion that all the members will retain day-to-day control over the operation of the scheme by making all the decisions and implementing what is agreed, resulting in the scheme not being a managed investment scheme, when:

(a) the case law and the evidence support the conclusion that:

(i) horse racing schemes are neither designed to operate that way in practice nor permitted to operate that way by the **ARR**; and

(ii) **the key elements that satisfy the definition of a managed investment scheme are inherent in all such schemes as they are both designed to operate in practice and required to operate by the ARR**; and

(b) the determining criteria of a managed investment scheme can only be the legislated definition of a managed investment scheme, complimented by the principles established by the case law, objectively applied. See ***ASIC v Pegasus*** *[55]*; ***Burton v Arcus*** *[2], [3] and [4], and [73], [74], [79], [80], [82]* and *[83]*; ***and Stewart v Spicer Thoroughbreds Pty Ltd*** *[24, [29],* and *[45]*.

Racing Victoria itself appears to have been unsure as to the merits of its questions, evidenced by the change in wording used in 2014 from that used in 2011 as to what, if any, conclusion could be reached if the answer is "no" to the majority of the questions. It has changed from [in 2011] "*…then the syndicate will most likely not be a MIS"* to [in 2014] *"…then the definition may not apply."*

Furthermore, in RV APP [Jun 2014], the statement in the second paragraph immediately following the questions, implies that Racing Victoria was acting to ensure that "*…in most cases any unique promotion will be permitted*." This is contrary to the fact that there is a legislated definition of a managed investment scheme that needs to be objectively applied and satisfied. It confuses the policy role of exemption given by ASIC administratively.

Part 2 – Do the answers to the Racing Victoria questions change any conclusion based on the questions set out in Appendix C of this paper as to whether a typical horse racing scheme satisfies the definiton of a managed investment scheme? The answer to this question is "No."

Would it change any of the answers, or the conclusion, in **Appendix C**:

1. if the promoter, or a person appointed by the promoter, will act as the manager?

   Answer: No

2. if a person appointed by the members will act as the manager?
   Answer: No

3. whether or not the members pay a management or administrative fee?

   Answer: No

4. whether or not the manager makes decisions relating to the distribution of prize money, such as how and when it is distributed (including the withholding of prize money in the instance of defaulting or late paying members)?

   Answer: No

5. whether or not the manager handles a scheme bank account?

   Answer: No

6. whether or not the members pay a monthly fee relating to the training and care of the horse directly to the manager?

Answer: No

7. whether or not the manager makes decisions relating to the racing of the horse without consulting the members?

   Answer: No

Conclusion

With respect to Racing Victoria, the questions in both **RV APP [2011]** and **RV APP [2014]** are a wholly inappropriate criteria for determining if a specific scheme is a managed investment scheme. The determining criteria of a managed investment scheme can only be the legislated definition of a managed investment scheme complemented by the principles established by the case law, objectively applied.

While it is appropriate to consider those characteristics which are the focus of the Racing Victoria questions in their proper context as part of a broader analysis of the whole scheme, including its legal structure, the nature of the members' interests, and modus operandi to determine whether it satisfies or falls outside the scope of the definition of a managed investment scheme, it is inappropriate to consider only those characteristics in the context in which they appear in the Racing Victoria documents. This has the potential to create confusion in the minds of industry participants as to their significance which is avoided if they are included as part of a broader analysis.

It should be noted that neither ASIC in its **RG [2016]**, **RG [2012]** or **RG [2007]**, nor Racing NSW in its **Guidelines for Promoters [2017]** or **[2013]**, have included anything like the Racing Victoria questions.

It should also be noted that the Racing Victoria questions do not appear in its **RV PP [Jan 2017]**, although that document is also fundamentally flawed for an entirely different reason.

Part 3 – Statements relating to day-to-day control over the operation of the scheme and advertising set out in the RV PPG [2017]

"day-to-day control over the operation of the scheme"

The **RV PP [Jan 2017]** contains the following statement in part 1.3 [registration of a promoter with Racing Victoria]:

> *"What is an MIS?*
>
> *If an offer is to be made publicly, typically via a published advertisement or an online promotion accessible to the general public (including an email to clientele), then the threshold question is whether the offer constitutes an MIS.*
>
> *An MIS has the following features:*
>
> *(i) people contribute money or money's worth as consideration to acquire rights **~~("interests")~~** to benefits produced by the **horse racing** scheme **~~(whether the rights are actual, prospective or contingent and whether they are enforceable or not)~~**; and*
>
> *(ii) any **of the** contributions are to be pooled, or used in a common enterprise, to produce financial benefits, or benefits consisting of rights or interests in property, for the **horse racing scheme members** **~~people (the "members")~~** who hold interests in the **horse racing** scheme (whether or not as contributors to the **horse racing** scheme or as people who have acquired interests from holders); **and***
>
> *(iii) the members do not have day-to-day control over the operation of the **horse racing** scheme **~~(whether or not they have the right to be consulted or give directions).~~** **Another way to ask this question is whether or not the members have the right to be consulted or give directions about the day-to-day control over the operations**; …."*

The original wording is the legislated definition. Racing Victoria has deleted the highlighted lined through words and added the highlighted underlined words in an unconventional and questionable approach to

statutory interpretation. Text, context, and purpose are fundamental to statutory interpretation. It is inappropriate to change the text or context of a statutory provision before attributing a meaning.

Each element of paragraph (a) of the s.9 definition of a managed investment scheme contains a statement in brackets beginning *with ("whether…" or "whether or not…")* which is a modifier to the head statement. A modifier is intended to provide a default rule for resolving ambiguities in the head statement.

In each case the modifier is a **nonrestrictive modifier** which provides additional [nonessential] information that does not [express an intention to] limit or restrict the legal meaning of the head statement. Whereas a **restrictive modifier** is a statement that modifies the head statement in a way that is essential to its meaning.

First element

The head statement in the first element of the definition "*people contribute money or money's worth as consideration to acquire rights ("interests") to benefits produced by the scheme*" is subject to the **nonrestrictive modifier** "*(whether the rights are actual, prospective or contingent and whether they are enforceable or not)*."

Consequently, [giving the word "*whether*" its ordinary meaning] the head statement applies whichever [regardless of which] of the alternatives mentioned in the modifier statement is the case. In other words, the rights being actual, prospective, or contingent and whether they are enforceable or not does not limit or restrict the legal meaning of the head statement.

Second element

The head statement in the second element of the definition "*any of the contributions are to be pooled, or used in a common enterprise, to produce financial benefits, or benefits consisting of rights or interests in property, for the people (the "members") who hold interests in the Scheme*" is subject to the **nonrestrictive modifier** "*(whether or not as contributors to the scheme or as people who have acquired interests from holders)*."

Consequently, [giving the phrase "*whether or not*" its ordinary meaning] the head statement applies whichever [regardless of which] of the alternatives mentioned in the modifier statement is the case. In other words, the members being either contributors to the scheme or people who have acquired interests from holders does not limit or restrict the legal meaning of the head statement.

Third element

The head statement in the third element of the definition "*the members do not have day-to-day control over the operation of the scheme*" is subject to the **nonrestrictive modifier** "*(whether or not they have the right to be consulted or give directions)*."

Consequently, [giving the phrase "*whether or not*" its ordinary meaning] the head statement applies whichever [regardless of which] of the alternatives mentioned in the modifier statement is the case. In other words, any right the members may have to be consulted or give directions does not limit or restrict the legal meaning of the head statement.

With respect to Racing Victoria, its re-wording of the legislated definition is wholly inappropriate, and particularly its rewording of the **nonrestrictive modifier** attached to the third element of paragraph (a) of the definition. The revised words attempt to convert the **nonrestrictive modifier** to a **restrictive modifier** which is the opposite of what the legislature intended.

advertising

The **RV PP [Jan 2017]** also contains the following statements in part 1.6 [Licensed trainer requirements]:

> *"Licensed trainers, comparable to unapproved operators such as breeders and owners, cannot publicly sell shares in horses without the necessary approval from ASIC and Racing Victoria.*
>
> *However, the promotion of horse shares has traditionally been common practice. From an industry development perspective, Racing Victoria is committed to encouraging horse ownership through commercial syndications as well as through informal industry networks (such as friendship groups and close associates).*

Racing Victoria permits a licensed trainer to publicly advertise a whole horse for sale. In this instance, any advertisement for such must remain generic and cannot contain statements such as (or similar to) "shares on offer" or "seeking partners to race" or "limited opportunities available." Further, any advertisement should contain the whole costs of the horse (not specific to share value)."

The problem with these statements is that they:

(a) have the potential to be interpreted by licensed trainers as a "green light" for them to deal in shares so long as they do not refer to shares in the advertising; and

(b) are contrary to the fact that there is a legislated definition of a managed investment scheme that needs to be objectively applied and satisfied. They confuse the policy role of exemption given to ASIC administratively.

Regardless of Racing Victoria's statements, if a trainer or any other industry participant can reasonably be regarded as being in the business of promoting [including offering to sell or inviting people to buy, dealing in or issuing] interests in horse racing schemes, they will likely satisfy the "promoter" test under section 601ED(1)(b) of the Act and must comply with the statutory provisions relating to licensing, scheme registration and the promotion of such schemes.

NOTE: The RV Approved Promoter Policy issued [Nov 2011] & [Jun 2014] and Promoter Policy issued [Jan 2017] no longer appear on the Racing Victoria website.

It is concerning that these documents clearly evidence a conscious effort by Racing Victoria over many years to promote an alternative "restrictive" methodology for determining whether or not a horse racing scheme is a managed investment scheme, when the determining criteria can only be the "nonrestrictive" methodology of the legislated definition of a managed investment scheme complemented by the principles established by the case law, objectively applied. In other words, Racing Victoria's promoter policies have been the opposite of what the law requires.

The publication of these documents containing "incorrect" and potentially "misleading" information is a risk to industry participants who should be entitled to assume that all such documents published by the regulatory authority are in accordance with what the law requires.

Participants cannot avoid liability for breaches of the law by pleading that they have relied upon these documents or any other "wrong" advice from Racing Victoria when engaging in the business of promoting horse racing schemes without the requisite AFS Licence and disclosure documents. In such circumstances, any rules or policies made by Racing Victoria that conflict with the Act will simply be to no effect or invalid to the extent of the inconsistency.

Part 4 – RWWA and statements relating to "day-to-day control"

The following statement appeared in an Information Sheet published by *Racing and Wagering Western Australia* ("RWWA") in May 2012 titled *Public Promotion of Racehorse Ownership – Partnerships & Syndications*:

"Most horse syndicates would satisfy the first two features which means the question over day-to-day control is critical in determining whether in practice, a syndicate constitutes an MIS.

- *… When the syndicate is jointly managed by its members then the definition most likely does not apply in which case no approval of the share promotion is required. (This is often the case where the syndicate is formed from a "personal offer" where it is likely that the person interested in the offer of shares based on previous contact, connections or indications. A personal offer must not be advertised)."*

With respect to RWWA, these statements are incorrect.

Firstly, the determining criteria of a managed investment scheme can only be the legislated definition of a managed investment scheme, complimented by the principles established by the case law, objectively applied.

Secondly, the case law and the evidence clearly support the conclusion that the characteristics of a managed investment scheme are inherent in horse racing schemes as they are both designed to operate in practice and required to operate by the ARR.

Thirdly, the "personal offer" provisions set out in the Act only apply to the PDS requirements – not in relation to any determination as to whether or not a particular horse racing scheme satisfies the definition of a managed investment scheme.

RWWA may have confused the concept of a "personal offer" with the concept of a "private" scheme, although the concept of a "private" scheme also has nothing to do with the day-to-day control test under the third limb of the definition.

A horse racing scheme established as a one-off "private" scheme may not require registration. To qualify as a "private" scheme it must not require registration under section 601ED. In other words, it must not have more than 20 members and the person who established it must not be a "promoter" who is "*in the business of promoting managed investment schemes*."

A horse racing scheme established by a person (promoter) who is "*in the business of promoting managed investment schemes"*:

(a) will, prima facie, fall within the requirement for registration under section 601ED, regardless of the number of members; and

(b) must be registered as a managed investment scheme, unless it is an unregistered scheme that is:

  (i) a personal offer scheme;

  (ii) a wholesale scheme; or

  (iii) a lead regulator approved (ASIC Instrument compliant) syndicate.

A "promoter" must hold an AFS Licence or be an Authorised Representative of a licensee. There is no statutory exemption or ASIC Instrument relief from this requirement for a "promoter" to be licensed, regardless of whether or not a specific scheme may be relieved by statutory exemption or the terms of the ASIC Instrument from the requirement to be registered.

APPENDIX C

Control in fact

The concept of "control in fact" is sometimes referred to as "de-facto control." It is a concept applied by the courts to determine the realities of how certain arrangements are designed to operate in practice.

The different control tests and contexts in which the concept of "control in fact" is applied must also be considered when applying the principles established by the case law.

Day-to-day "control in fact" over the operation of a scheme

In Australia, the concept is relevant when determining whether an unincorporated association is a managed investment scheme for the purposes of the Corporations Act.

If the substance is that all the members have day-to-day "control in fact" over the operation of the scheme by making all the decisions and implementing what is agreed [actually managing or carrying out the routine, ordinary, everyday activities that comprise the scheme's operations], then the scheme will not be a managed investment scheme.

However, if the substance is that the members contributions are either pooled for use as the property of the scheme [typical of **partnership** and **unit trust**-based "investment" arrangements], or not pooled but used in a common enterprise that constitutes the scheme [typical of **co-ownership** contract-based "common enterprise" arrangements], to produce financial benefits, or benefits consisting of rights or interests in property, and the members collectively appoint a person to operate the scheme [with the authority to actually manage or carry-out the routine, ordinary, everyday activities that comprise the scheme's operations] on behalf of the group, then the scheme will be a managed investment scheme (whether or not they have the right to be consulted or give directions).

It is a negative test in the sense that for the arrangements to be a managed investment scheme they must be such that all the members do not have day-to-day "control in fact" over the operation of the scheme, prospectively viewed from the time when the arrangements are made.

Furthermore, the management activities of a person who is the "promoter" or "operator" are not to be imputed to the members in determining whether the members have day-to-day control over the operation of the scheme.

In ***ASIC v Chase Capital Management Pty Ltd***[115], *Owen J* said:

> *[67] "… The question is whether the members have day-to-day control. It is not difficult to discern the distinction that the legislature was attempting to make. Very broadly, it is between the investment activities of an individual and that of a group. By the express terms of the applications, the investors have delegated "management" of the investment to CCML. There is no reservation of day-to-day or any other control or functions. I am not sure that the appointment of a committee of some of the investors to monitor the investments would make much difference. The question still remains: who has the day-to-day control."*

In ***Enviro Systems Renewable Resources Pty Ltd v Australian Securities & Investments Commission***[116], *Martin J* said:

> *[36] "In my opinion, when the scheme documentation is analysed in its entirety, the intent of the scheme is that Enviro will control the day-to-day operations of the scheme from beginning to end. Enviro offers a total package which is presented in such a way that potential participants are encouraged to take up the entire package. Notwithstanding the assertions that participants will be running their own businesses. Enviro does not intend that the participants should take an active role in the day-to-day operations of any aspect of the scheme. The success or otherwise of the scheme is entirely dependent upon Enviro. In reality, although it is possible that some participants may choose to take an active role, the scheme is designed to attract passive investors."*
>
> *[37] "The purpose or object of the legislation and the regulatory regime created pursuant to the legislation would be easily defeated if the court felt obliged to rely solely upon a strict view of the*

[115] (2001) 36 ACSR 778.
[116] [2001] SASC 11.

legal rights and duties created by the documentation and was required to ignore the realities of the scheme as it was designed to operate in practice."

In ***ASIC v IP Product Management Group Pty Ltd***[117], *Byrne J* said:

[22] "It will be recalled that under paragraph (iii) the existence of a right in a member to be consulted or to give directions as to the operation of the scheme does not necessarily lead to the conclusion that that member has day-to-day control over its operation. The law contemplates, therefore, some greater involvement."

In ***ASIC v Pegasus***[118] *Davies AJ* said:

[55] "The word "operate" is an ordinary word of the English language and, in the context, should be given its meaning in ordinary parlance. The term is not used to refer to ownership or proprietorship but rather to the acts which constitute the management of or the carrying out of the activities which constitute the managed investment scheme."

In ***Burton v Arcus***[119] *McClure J* said:

[2] "… The word "operate" in the context of s601ED (5) and s601EE is to be given its ordinary meaning. The term is not used to refer to ownership or proprietorship but rather to acts that constitute the management of or the carrying out of the activities comprising the managed investment scheme: see ***Australian Securities and Investments Commission v Pegasus Leveraged Options Group Pty Ltd (2002) 41 ACSR 561 at 574****."*

[4] "… The phrase "day-to-day" means routine, ordinary, everyday management or operational decisions. I am of the view that the term "control" in the definition means authority to decide and direct and not merely to participate in decision-making."

In ***Burton v Arcus*** *Buss JA* said:

[73] "The term "day-to-day" connotes routine, ordinary, everyday. See The Shorter Oxford Dictionary (1993), page 598; The Macquarie Dictionary (Third Edition), page 492."

[74] "As the Privy Council observed in ***Bermuda Cablevisions Ltd v Colica Trust Co Ltd [1998] AC 198 at 207****, expressions such as "control" take their colour from the context in which they appear: there is no general rule as to the meaning of the word "control. The expression "day-to-day control" is not a term of art. It must be given the meaning which the context requires. …."*

[79] "In my opinion, the third element in para (a) of the definition is concerned with control in fact as distinct from the legal right to control. It is also concerned with control in fact by the members of a scheme as a whole. The members as a whole may not have control in fact even though the constructive document for the scheme may confer on them the legal right to control."

[80] "The members of a scheme will have "day-to-day control over the operation of the scheme" if:

(a) the members as a whole participate in making the routine, ordinary, everyday business decisions relating to its management; and

(b) the members as a whole are bound by the decisions which are made."

"Conversely, if the members as a whole do not participate in making the routine, ordinary, everyday business decisions relating to the management of the scheme or if the members as a whole are not bound by the decisions which are made, they will not have day-to-day control over its operation."

[82] "In my opinion, the circumstance that the promoter or operator of a scheme manages the scheme (or certain aspects of it) on behalf of the members does not mean that the members by their agent, the promoter or operator, have day-to-day control in fact over the operation of the scheme. In other words, the management activities of the promoter or operator in relation to a

[117] (2002) 42 ACSR 343.
[118] [2002] NSWSC 310.
[119] Appeal Judgement) [2006] WASCA 0071. Also see (Original Decision) [2004] WASC 244.

scheme are not to be imputed to the members in determining whether the members have such day-to-day control."

[83] "My construction of the third element in para (a) of the definition gives effect to the evident legislative purpose or object embodied in the definition and Ch 5C. If:

(a) the third element in para (a) of the definition was concerned with the legal right to control and not control in fact; or

(b) the management activities of the promoter or operator in relation to the scheme were to be imputed to the members in evaluating whether the third element was satisfied or not, with the consequence that if the promoter or operator had "day-to-day control over the operation of the scheme" then the members, by their agent, the promoter or operator, would have day-to-day control,

the legislative framework for the regulation of managed investment schemes would be seriously, if not entirely, eroded."

"Control in fact" of an entity

The following paragraph is quoted from an Advisory Note titled "***The Federal Court of Appeal clarifies the de facto control test***" issued by Canadian Law Firm *Gowling WLG* on 14 June 2016*:*

"In Canada, control is a concept that is relevant to a number of income tax rules. There are two types of control: de jure control and de facto control. Determining de jure control is straight forward, as it exists where a person (or group) has the power to elect a majority of the board of directors. De facto control is less concrete, requiring a determination of whether a person (or group) has direct or indirect influence that, if exercised, would result in factual control[120]." While the de facto control concept is relevant for a variety of the provisions in the ITA, it is particularly relevant for determining under various tax rules whether a corporation is a "Canadian-controlled private corporation" and whether corporations are "associated" for purposes of the ITA."

The seminal Canadian cases on de facto control are ***Silicon Graphics Limited v Canada***[121] and ***McGillivray Restaurant v Canada***[122].

The judgment in the ***Silicon Graphics*** case established that a person or group of persons would have de facto control if such a person or group has "*a clear right or ability to effect a change in the board of directors or the powers of the board of directors or to influence in a very direct way the shareholders who would otherwise have the ability to elect the board of directors*."

Subsequent cases expanded the test by introducing factors concerning operational control of the business, creating ambiguity and challenges in determining de facto control, until ***McGillivray*** in 2016, which clarified the de facto control test, reaffirming the test in ***Silicon Graphics***.

The facts in ***McGillivray*** concerned an attempt to split 3 restaurants into two corporations – to increase access to the small business deduction. That meant making sure the two corporations were not "associated", such as by the husband's "de facto control. The TCC judge (Boyle) had held that they corporations were associated, even though the husband might have no right to control appointment of the board of directors.

The FCA rejected that broad interpretation of ITAs. 256(5.1) control test:

[46] "I reject any assertion that the test for control in fact is based on "operational control." De facto control, like de jure control, is concerned with control over the board of directors and not with control of the day-to-day operations of the corporation or its business. Paragraph 256(1)(b) and subsection 256(5.1) specifically refer to control of a corporation and not to control of the corporation's business or operations …."

[48] "…, in my view, a factor that does not include a legally enforceable right and ability to effect a change to the board of directors or its powers, or to exercise influence over the shareholder or shareholders who have that right and ability, ought not to be considered as having the potential to establish de facto control."

[120] as defined in subsection 256(5.1) of the Income Tax Act (Canada) (the "ITA")
[121] [2002 FCA 260].
[122] [2016 FCA].

Although the FCA concluded that the TCC judge used the wrong control test, it came to the same conclusions as he. The FCA accepted that the husband and wife had an oral agreement that she would always appoint him as director. That was enough to ensure that the husband had de facto control thus rendering ineffective this tax avoidance scheme. [see e.g., paras 54, 55 and 57].

This case clearly establishes that, for the purposes of the control test in section 256(5.1), the difference between de facto control and de jure control is limited to the breadth of factors that can be considered in determining whether a person or group of persons has effective control, by means of an ability to elect the board of directors of a corporation. That said, it remains the case that the list of factors that may be considered when applying the ***Silicon Graphics*** test is open-ended. However, a factor that does not include a legally enforceable right and ability to effect a change of the board of directors or its powers, or to exercise influence over the shareholder or shareholders who have that right and ability, ought not to be considered as having the potential to establish de facto control.

Determining whether a person controls an entity is also relevant in circumstances throughout the federally regulated institution (FRFI) statutes, which are the *Bank Act*, the *Insurance Companies Act* and the *Trust and Loan Companies Act*. See Advisory Note titled "***Control in Fact***" issued by *Office of the Superintendent of Financial Institutions Canada,* January 2020.

APPENDIX D

The law of conversion

The law of conversion is also relevant to the syndication of thoroughbred racehorses, especially so because promoters, including trainers, typically utilize credit facilities provided by the auction sales companies to acquire horses with the intention of syndicating them during the term of the credit facility. They then apply the application money received from investors to paying for the horses and discharging the credit facility.

A conversion is the unauthorised exercise of control over the personal property of another in a manner that is inconsistent with the property rights of the owner.

Conversion is an intentional tort, although the intent required is not necessarily that of conscious wrongdoing. The focus of inquiry is whether a person has appropriated to their own use the property of another person without that person's permission and without legal right.

In circumstances where a promoter purchases a horse at auction utilizing the credit facility provided by the sales company, the promoter is usually given actual possession of the horse subject to terms that include:

(a) an acknowledgement by the promoter that legal title to the horse will not transfer from the sale company to the promoter until the horse has been fully paid for, and a grant by the promoter to the sales company of a security interest attaching to the horse as security for payment of the full amount of the sale price and interest;

(b) the right of the sales company to retake possession if the promoter does not pay for 100% of the horse within the terms of the credit facility; and

(c) an obligation on the part of the promoter not to encumber the horse in any way, or transfer, or otherwise dispose of it (or any interest in it), until the credit facility is fully discharged.

Wrongful conversion by the promoter of interests in the horse

If the promoter purports to sell and transfer to investors (applicants) unencumbered interests in the legal and equitable title to the horse during the term of the credit facility, such action by the promoter will likely be inconsistent with the property rights of the sales company in the horse.

Wrongful conversion by the promoter of application money

The application price for an interest in the horse may comprise:

(a) the sale price of the interest;

(b) the cost of insuring the interest;

(c) a proportion of the syndicate establishment expenses; and

(d) a proportion of the estimated syndicate operating expenses, including (without limitation), agistment, breaking-in and pre-training, training and ancillary expenses, for a specified period.

Payments by or on behalf of the promoter to reduce the promoter's credit facility in relation to a specific horse and payments by applicants for shares in the horse are distinguishable.

Application money should only be applied towards payment for the horse, or interests in the horse, in circumstances where there is a simultaneous passing of unencumbered ownership to those applicants whose application money is being applied. If ownership does not transfer simultaneously, this will likely be inconsistent with the property rights of the applicants in their application money.

The same principles apply to any proportion of the application money paid to the promoter on account of syndicate establishment and operating expenses. That proportion of such money should only be applied towards payment of those expenses upon the applicants becoming the owners of their respective interests in the horse.

Requirement for dedicated application money trust account

The current syndication regulations address these issues by requiring the promoter of an offer of shares to establish a dedicated application money trust account for receiving and holding all application money until the minimum overall subscription amount is met, thus enabling the promoter to then apply the application money towards payment for the horse and ensure that ownership is transferred simultaneously to the applicants.

Racing NSW has an additional reporting requirement to ensure strict compliance with this procedure by approved promoters operating in its jurisdiction. Before a promoter can apply application money to the purchase price of the horse they must complete and provide to Racing NSW a statement listing the names of all applicants for interests, their proportionate (%) interest applied for, and the amount of money they are each contributing to the purchase price of the horse and the establishment and operating costs of the syndicate. Racing NSW then issues an authorization to the promoter to apply the application money in paying for the horse. The promoter must then provide to Racing NSW the vendor release statement and the horse registration form (in the names of the applicants whose money has been applied), which Racing NSW then reviews and passes to Racing Australia for registration.

Actual cases that demonstrate how investors can lose their money when these procedures for the handling of application money are not followed are those involving Victorian-based unlicensed syndicators ***BC3***[123] and ***JSL Racing***[124]. *BC3* was a high-profile racehorse syndication company operated by former racing identity *Bill Vlahos* [who has since been convicted of operating an alleged "Ponzi" betting syndicate] and *JSL Racing* was a training partnership that included a high-profile Melbourne Cup winning trainer. In both cases, applicants thought they were acquiring interests in various horses in exchange for making the initial payments, but that proved not to be the case when things went wrong.

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   (7) ASIC V McNamara [2002] FCA 1005.
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   (9) ASIC v Takaran Pty Ltd [2003] 1Qd R 135 at 146 [17].
   (10) ASIC v Young & Others [2003] QSR 029
   (11) Ballantyne v Raphael (1889) 15 15 VLR 538.
   (12) Brookfield Multiplex Ltd and Another v International Litigation Funding Partners Pte Ltd and Others [2009] FCAFC 147.
   (13) Burton v Arcus (Appeal Judgement) [2006] WASCA 0071. Also see Brown v Arcus (Original Decision) [2004] WASC 244.
   (14) Butler v JSL Racing Pty Ltd (26/03/2013 VSC unreported).

(15) Crocombe v Pine Forests of Australia Pty Ltd (2005) 219 ALR 692; [2005] NSWSC 151.
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(24) The Russell-Cooke Trust Company v Elliott [2001] All ER (D) 300 (Mar). (No 1, 26 March 2001, unreported and No 2, 16 July 2001, unreported).
(25) Silicon Graphics Limited v Canada [2002] FCA 260].
(26) Smith v Anderson 1874-80 All ER Rep 1121.
(27) Stewart v Spicer Thoroughbreds Pty Ltd [2022] NSWSC 310.
(28) United Dominions Corp v Brian Pty Ltd (1985) 157 CLR 1 at 15.
(29) WA Pines Pty Ltd v Hamilton SCWA 1980.

6. Other
(1) Paper titled: "Australian Bar Review – Precedent Law, Practice & Trends in Australia", by the Hon Justice Michael Kirby AC CMG.
(2) FCA Handbook (UK), Perimeter Guidance – Chapter 11 Guidance on property investment clubs and land investment schemes – PERG 11.1 [Background] and PERG 11.2 [Guidance on property investment clubs].
(3) Advisory Note titled "The Federal Court of Appeal clarifies the de facto control test" issued by Gowling WLG on 14 June 2016.
(4) Advisory Note titled "Control in Fact" issued by Office of the Superintendent of Financial Institutions Canada on 3 January 2020.