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Managed funds investor protection still wanting

Despite the collective investment collapses of the last five years, managed fund investors are going into 2013 with little more regulatory protection than they had at the start of 2007, warns Harvey Kalman, head of corporate and fiduciary services at Equity Trustees Limited (EQT).

“Most financial services’ tightening of regulations have been focused on financial planners, although there have been some moves towards strengthening regulations for responsible entities (REs).

“The proposed reform look at tightening the financial requirements of REs but are likely to be cumbersome for compliance, inhibit investor choice, and prove inadequate when the next bubble bursts.

“There needs to be recognition that a ‘one size fits all’ RE regulatory approach will have some flaws.

“We also need to recognise that investment products, and financial instruments generally, are now much more complex than they were when REs were introduced in 2000.

“The investment landscape at the start of 2013 is a very different place to the one in 2009,” he said.

Mr Kalman said that he believes two or three levels of regulation are needed for REs, based on the size of the institution behind the fund, the independence of the RE, and the complexity of the assets that a fund is allowed to invest in.

“Such an approach does not have to make regulations more complicated; however it increases the likelihood that, in the event of a fund running into problems, there is someone left standing to return money to investors. It will also reduce the possibility of malpractice.

“Furthermore, it will mean new players in the funds management industry are not strangled at birth, which will ensure that a vibrant industry, offering wide investment opportunities and access to new managers, survives.

“Like today’s complex financial products, boutique managers didn’t play a significant part in the funds management industry when the untried concept of REs was developed and introduced.

“Boutiques have proved to be a boon to investors as well as the industry as a whole over the last decade, bringing in new investment approaches, generally good investment results, and a broader base to the industry.

“While the steps to strengthen REs currently being proposed are of some use in their present form, there is a danger they will inhibit start-up managers.

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"Today most funds, regardless of their size, are able to invest in structured financial investments. Those that do so should have a higher level of investor protection requirement than those that offer uncomplicated "vanilla" products.

"In my view, the regulators need to recognise there are different categories of funds management, and treat them differently.

"For instance, there are large institutions offering a range of collective investments but with strong financial backing; smaller funds offering complex products with increased investor risk; and small funds offering uncomplicated funds that do not use complex financial products.

"Each needs different regulatory consideration in a way that does not reduce investor options, but at the same time helps protect them.

"One simple option is mandated use of independent REs for small funds that use financial instruments. This is an approach that many boutique managers are moving towards anyway, because of the administrative and compliance benefits it brings.

"Introducing different regulatory 'tiers' depending on factors such as the fund manager size and type of investment, can be easily instituted under the existing licencing mechanism," Mr Kalman said.

About Equity Trustees:

Equity Trustees is a publicly listed company that provides a range of financial services to corporate and private clients. Its businesses include funds management, responsible entity appointments, private client wealth management and corporate and personal superannuation. The company has over \$4 billion in its funds management, private client and superannuation businesses and has more than \$19 billion under responsible entity administration. Equity Trustees employs over 180 people in its Melbourne, Sydney and Brisbane offices.

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