Disclosure Requirements and Investor Protection: the compatibility of Commonwealth, State and Territory laws in serviced strata schemes

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The law considers disclosure a key mechanism for the protection of consumers and/or investors. It is often regarded as an essential element in reducing the information asymmetry that accompanies the making of investment decisions. Where serviced strata schemes are concerned, the purchase of an investment unit combines the acquisition of real property with the acquisition of a financial product and financial services. Consequently, in this case, disclosure is obligatory under both the Corporations Act 2001 (Cth) and the various state and territory statutes dealing with vendor disclosure in conveyancing transactions. The purpose of this paper is to examine these disclosure mechanisms to determine the compatibility of state and territory laws with Commonwealth objectives. It is concluded that lack of consistency amongst state and territory laws is at variance with the unified approach advanced by the Corporations Act 2001 (Cth). Such variance potentially undermines the protection of investors. Therefore, the authors argue that the regulatory regime applying to serviced strata schemes should encompass Australia-wide standards, enabling state and territory disclosure provisions to work in synergy with Commonwealth aims and objectives.

Keywords: serviced strata schemes, disclosure, managed investment schemes, vendor disclosure, conveyancing transactions
1. INTRODUCTION

Over the last two to three decades, managed investment schemes have become an increasingly popular investment vehicle.¹ The variety of these schemes runs the gamut from cash management trusts, to investments in film production, commercial horse breeding schemes and the pooling of resources in real property ventures.² The latter, is itself a diverse category, encompassing property trusts and all manner of serviced strata schemes including hotels, resorts, and apartment blocks.

An investment in a serviced strata scheme is based on ownership of real property, yet it also combines the pooling of income or the fair allocation of tenants. Therefore, these investments are also regarded as financial products acquired in conjunction with the provision of financial services.³ Currently, the regulatory regime with respect to serviced strata schemes operates on two levels: the first at the Commonwealth level, where serviced strata schemes are regulated as managed investment schemes;⁴ the second at the state and territory level where serviced strata schemes are regulated as part of the greater corpus of law applying to real property and conveyancing transactions.⁵ The regime, therefore, may be described as a dual regulatory model. At both levels, disclosure is considered an important way of apprising investors.⁶

The purpose of this paper is to examine disclosure mechanisms to determine the compatibility of state and territory laws with Commonwealth objectives. The paper commences by examining how serviced strata schemes are classified as managed investment schemes before examining disclosure provisions under the Corporations Act 2001 (Cth) (referred to as the Corporations Act or the Act) and state and territory conveyancing laws. It is concluded that lack of consistency amongst state and territory laws is at variance with the unified approach advanced by the Corporations Act. Such variance potentially

⁴ See discussion in part 3 of this paper.
⁵ See discussion in part 4 of this paper.
undermines the protection of investors. Therefore, the authors argue that the regulatory regime applying to serviced strata schemes should encompass Australia-wide standards, enabling state and territory disclosure provisions to work in synergy with Commonwealth aims and objectives.

As a preliminary matter it should be noted that this paper refers to those who acquire an interest in a serviced strata scheme as ‘serviced strata scheme investor(s)’, shortened to ‘SSS investor(s)’ or in context, to ‘investor(s)’. While the question of whether those who acquire financial products and use financial services are consumers or investors is not settled, in this paper, the term ‘investor’ is used in its broadest sense. It includes the notion of an investor as a person who ‘consumes’ financial services and products. The terms ‘SSS investor(s)’ or ‘investor(s)’ have been chosen as expressions representative of an integration of the word ‘purchaser’ which is used in conveyancing legislation and the phrase ‘retail client’ which is used in the Corporations Act.

2. WHAT IS A SERVICED STRATA SCHEME?

A serviced strata unit is a furnished unit designed for short-term stays. In a practical sense, these units are likely to be classified as part of a managed investment scheme where they are located within a hotel, motel, resort or serviced apartment complex. Often these properties are located in popular holiday destinations – a feature which is regularly highlighted in the marketing of these schemes.

2.1 Section 9 of the Corporations Act

Section 9 of the corporations act defines a managed investment scheme as a scheme where people contribute money or money’s worth to acquire rights to benefits produced by the scheme. The contributions need to be pooled or used in a common enterprise in circumstances where the members of the scheme do not have day-to-day control over its operations. In the case of serviced strata units, the aim of pooling or combining resources is to enable the SSS investor to

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access gains resulting from increased performance of the pooled assets.\textsuperscript{11} The proprietor as an investor is not involved in the management of the pool of units. Consequently, in similarity with the ownership of shares in a company, the SSS investor will be placing his or her trust in the managerial skills of another person, in this case the operator of the scheme.\textsuperscript{12}

The expectation of an increased return resulting from another’s managerial skill are in fact part of the ‘rights’, which section 9 of the Act refers to. Arguably, such rights are ‘brought into existence by the scheme’ itself,\textsuperscript{13} rather than solely by ownership of the strata title unit.\textsuperscript{14} It is immaterial whether the pooling or operational arrangements are mandatory or voluntary. The fact that they are the ‘interest’ required by the legislation is said to justify regulation as a managed investment scheme.\textsuperscript{15} Certainly, this is how ASIC, the Australian Securities and Investment Commission, has interpreted section 9.\textsuperscript{16}

2.2 Regulatory Guide 140

ASIC is the body responsible for administering the Corporations Act and as such is also charged with the responsibility for determining the types of schemes considered to be managed investment schemes. In administering the Act, ASIC issues ‘regulatory guides’, which are official announcements on the way ASIC proposes to oversee the Corporations Act.\textsuperscript{17} In November 2000,

\begin{itemize}
  \item \textsuperscript{12} Robert P Austin and Ian M Ramsay, Ford’s Principles of Corporations, above n 6, paragraph 22.090.
  \item \textsuperscript{14} The investor will of course need to purchase the strata unit to participate in the scheme. However, the Corporations Act is concerned with the pooling arrangements, rather than the ownership of the strata unit.
  \item \textsuperscript{15} Chris Furnell, ‘Managed Investment Scheme Interests’, above n 13, 215-216; see also Maunder-Hartigan v Hamilton (1984) 2 ACLC 438; ASIC, ‘Regulatory Guide 140, Serviced Strata Schemes’ 13 November 2000, RG 140.21, 140.23.
  \item \textsuperscript{16} ASIC is the body responsible for administering the Corporations Act 2001 (Cth) and its administration of the Act is also important to the interpretation of the Act. See ASIC, ‘Regulatory Guide 140, Serviced Strata Schemes’ 13 November 2000, RG 140.22. For a discussion on the role of ASIC in interpreting the Corporations Act see generally, Dimity Kingsford Smith, ‘Interpreting the Corporations Law – Purpose, Practical Reasoning and the Public Interest’ (1999) 21 Sydney Law Review 161. For analysis of case law that has considered the definition of managed investment schemes see Enviro Systems Renewable Resources Pty Ltd v ASIC (2001) 36 ACSR 762; ASIC v Hutchings 36 ACSR 762; Macquarie Bank Limited v Australian Securities and Investments Commission [2001 AATA 868 and discussion in J Donnan, (2002) ‘Debentures, Derivatives and Managed Investment Schemes - the Characterisation and Regulation of Investment Instruments’, above n 11, 32-34.
  \item \textsuperscript{17} As of 5 July 2007, Regulatory Guides replace Policy Statements. Although these documents may be referred to either as a Policy Guide or a Regulatory Guide, in this paper they are referred to as a Regulatory Guide in keeping with the up-to-date terminology adopted by ASIC. See
\end{itemize}
ASIC issued ‘Regulatory Guide 140, Serviced Strata Schemes’ (Regulatory Guide 140).18 This regulatory guide is designed to provide direction on ‘the application of the Law to arrangements involving property under strata title’19 including providing guidance on the types of serviced strata arrangements that are considered by be managed investment schemes.20

ASIC considers that a serviced strata scheme should be classified as a managed investment scheme, where an investor’s right to a return depends totally or partially on the use of other investors’ strata units for that return.21 In reaching this classification, ASIC has placed importance on four criteria: interdependency between owners; dependency on the serviced strata arrangement; deferred pool or common enterprise; and, pre-packaged sale of interests.22

**Interdependency between Owners**

Interdependency between owners refers to the situation where an investor has a right (including by agreement or an understanding with the promoter) to a return, which depends, in whole or in part, on the use of other investors’ strata units (as opposed to common property). For example, the investor’s return might depend on an arrangement for pooling income, or for fairly allocating tenants.23

**Dependency on the Serviced Strata Arrangement**

Dependency on the serviced strata arrangement refers to those situations where an investor has a right (including by agreement or an understanding with the promoter) to a return, which depends, in whole or in part, on an investor’s strata unit being used as part of a serviced strata arrangement. For example, the investor may depend on the serviced strata arrangement to receive a return that might be proportionate, fixed or indexed. Where the return is proportionate, the investor receives a percentage share of the profits from the whole complex, proportional to his or her ownership. ASIC regards this type of arrangement as a common enterprise, because the return to each investor is likely to depend on the success or failure of the serviced strata arrangement as a whole. For similar

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19 Ibid, RG 140.1(A).
20 Ibid, RG 140.1(B).
21 Ibid, RG 140.22.
22 Ibid, RG 140.24-35.
23 Ibid, RG 140.24-7.
24 At least one commentator has criticised this approach, suggesting that the pooling or common enterprise does not produce ‘relevant benefits for investors as a group [unless the income] is pooled and divided amongst the owners.’ Rather, the pooling arrangements often benefit the operator of the scheme Chris Furnell, ‘Managed Investment Scheme Interests’ above n 13, 223.
reasons, a fixed or indexed return, where an investor receives a nominated amount, is also regarded by ASIC as a common enterprise.24

Deferred pool or common enterprise
In a deferred pool or common enterprise arrangement, the serviced strata scheme may not commence immediately. The promoter and investor, for example, may agree or come to an understanding that a common enterprise or pool will operate at some time after the strata unit is first made available to the operator. ASIC would generally consider that this type of arrangement functions as a serviced strata scheme; and, moreover, one that exists from the time when the investors first conclude an agreement or understanding that they have a prospective interest in the serviced strata scheme.25 This approach is consistent with the definition of “interest” in section 9 Corporations Act, which as already noted extends to “…a right to benefits produced by the scheme…”, and which has no regard to whether the right is actual, prospective, or contingent.

Pre-packaged Sale of interests
A serviced strata scheme may exist even where the interests in the scheme are sold as part of a pre-packaged re-sale of interests as would occur where an interest initially issued to a promoter is re-sold. This means that the concept of a serviced strata scheme as a managed investment scheme remains constant, whether the strata units are being issued, sold or re-sold.26

It is clear from this brief description of the types of schemes that are considered to be managed investment schemes that ASIC interprets the Corporations Act as applying to a broad range of serviced strata schemes. This approach conforms to ASIC’s objectives, as set out in Regulatory Guide 140, to regulate schemes involving strata units in accordance with the managed investment provisions of the Corporations Act, where strata schemes have the characteristics of a managed investment scheme.27 An important component of this regulatory regime is that of giving disclosure to SSS investors.

3. DISCLOSURE UNDER THE CORPORATIONS ACT

The Corporations Act provides for a system of regulation and disclosure as part of the law relating to managed investment schemes.28 In accordance with section 601ED, if a scheme has more than twenty members, or if the scheme is one promoted by people who are in the business of promoting managed investment schemes, then the scheme needs to be registered and administered in accordance with the Corporations Act. The scheme must be managed by a

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28 Corporations Act 2001 (Cth), section 601ED.
public company whose constitution regulates the rights of the participants of the scheme, – in the Corporations Act referred to as the ‘responsible entity’. The responsible entity also needs to hold an Australian Financial Services Licence, or AFS licence. A person is required to hold an AFS licence if they offer financial products or advice in relation to financial products. It is significant that the AFS licence represents a single licensing system, because it standardises professional conduct of the licence-holders. In some cases, even where a scheme is not required to be registered, or the operator is not required to be licensed, disclosure to investors would still need to be made.

3.1 Chapter 7 of the Corporations Act and Disclosure

In accordance with the Financial Services Reform Act 2001, the current disclosure provisions in the Corporations Act commenced on 11 March 2002. These amendments introduced a new Chapter 7 into the Act, including part 7.9 that establishes a product disclosure regime for the issue, sale and purchase of financial products and part 7.7 that establishes a regime for financial services disclosure. The disclosure regime set out in Chapter 7 does not apply to ‘securities’ such as shares and debentures, which are still regulated in accordance with the provisions of Chapter 6D that deals with prospectus and offer information statements.

Both product disclosure and financial services disclosure primarily apply to ‘retail’ as opposed to ‘wholesale’ clients, or ‘sophisticated’ investors. A person is presumed to be a retail client unless they meet the wholesale client criteria. In the latter case, the client needs to hold assets exceeding $2.5 million, or have an income of more than $250,000 per annum. A client is also not a retail client if the client has paid more than $500,000 to acquire, or be issued with, the financial product. A sophisticated investor is one who has had previous experience in the financial product and services sector, which allows

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29 Corporations Act 2001 (Cth) section 601FB.
30 Corporations Act 2001 (Cth) section 601FA.
33 ASIC, ‘Regulatory Guide 140, Serviced Strata Schemes’ 13 November 2000, RG 140.45 applying to management rights schemes. Management rights schemes refer to rights given to an on-site manager who has the right to let or grant a licence over the unit. See ASIC, ‘Regulatory Guide 140, Serviced Strata Schemes’ 13 November 2000, RG 140.41.
34 Corporations Act 2001 (Cth), sections 1012B, 1012C.
35 Corporations Act 2001(Cth), section 761G.
37 Corporations Act 2001(Cth), section 761G(7)(a); Corporations Regulations 2001 Reg 7.1.18.
the client to assess the value, merits and risk of the investment. Product disclosure is not required where the client already holds a financial product of the same kind, or where the client has already received another product disclosure statement that contains all of the information that would be expected to be found in the second disclosure statement.

The Corporations Act envisages two types of disclosure based on three disclosure documents. The first type of disclosure relates to product disclosure, and is based on a Product Disclosure Statement; while the second type of disclosure relates to services disclosure, and is based on the Financial Services Guide and the Statement of Advice.

Product disclosure is required in accordance with part 7.9 of the Corporations Act whenever a ‘regulated person’ supplies financial products. A regulated person includes a person who issues or sells a financial product, a person who is a financial services licensee, or their authorised representative, as well as a person who is required to hold an AFS licence, even where they have been exempted from holding such a licence.

Accordingly, a person who is exempt from holding an AFS licence may still be required to provide disclosure. The obligation to give a disclosure statement applies when the financial product is first issued, as well as where a person conducts secondary trading in the product. Consequently, in the case of serviced strata schemes, product disclosure applies to real estate agents engaged by a developer to sell strata title units off the plan, as well as to real estate agents who act for subsequent vendors. Moreover, where the sale of a strata unit in a serviced strata scheme involves a recommendation with respect to the purchase of the unit, section s1012A of the Corporations Act specifically sets out that a product disclosure statement must be provided to the purchaser.

The product disclosure statement needs to contain a wide range of information, including: the benefits that the holder of the financial product will or may become entitled to; the risks associated with holding the product; information about the cost of the product; amounts payable in respect of the

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38 Corporations Act 2001(Cth), section 761GA.
39 Corporations Act 2001(Cth), section 1012D(2)(a).
40 Corporations Act 2001(Cth), section 1012D(1)(a).
42 Corporations Act 2001(Cth), section 1010B where a person issues a financial product in the course of a business issuing financial products; section 1012B where a regulated person issues a financial product to a retail client; section 1012C where a regulated person offers a financial product to a retail client. For the purposes of section 1010B, section 1010B(2) specifies that the issue of any managed investment product is taken occur in the course of such a business.
43 Corporations Act 2001(Cth), section 1011B.
44 Corporations Act 2001(Cth), section 1011B, ‘regulated person’ (f).
45 Corporations Act 2001(Cth), section 1012C.
46 Corporations Act 2001(Cth) sections 1013C-1013L.
product after its acquisition; information with respect to fees, charges and expenses; as well as general information about significant taxation implications.\textsuperscript{47}

In accordance with part 7.7, division 2 of the Corporations Act, a similar regime of disclosure applies with respect to financial services in relation to managed investment schemes. The first disclosure document, the Financial Services Guide is a statement given to customers that sets out the types of financial products that the holder of an AFS licence is able to provide, the fees charged and details of dispute resolution mechanisms.\textsuperscript{48} The second disclosure document, the statement of advice, includes information on how the service provider takes into account the personal circumstances of the client and the basis of the advice given to a retail client.\textsuperscript{49}

As well as the content of disclosure, the timing is also considered significant. Section 1012A(3) for example, stipulates that product disclosure statements must be given ‘at or before the time when’ the advice with respect to the product is given. Sections 941D(1) and 946C(1) that respectively deal with the Financial Services Guide and the Statement of Advice specify that disclosure needs to be made ‘before the financial service is provided’. The combined effect of these sections is to establish a ‘point of sale disclosure’ system.\textsuperscript{50} It is therefore implicit in these obligations that effective disclosure needs to be made before the investor decides to acquire the financial product or service.

\subsection{3.2 Exemptions to Compliance with the Legislation}

While the registration, licensing and disclosure requirements provide a precise and comprehensive regime for the regulation of managed investment schemes, ASIC has mitigated these requirements in some circumstances. Relief is given either in the form of class orders,\textsuperscript{51} or on a case-by-case basis. For example, ASIC has given licensing exemptions to real estate firms who sell strata units that are part of a serviced strata scheme, unless the real estate agent is issuing the interests (that is the sale is not a secondary trade); is inducing buyers to become members of a scheme; or is giving financial advice with respect to the interests in the scheme.\textsuperscript{52}

\begin{footnotesize}
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\item \textsuperscript{47} Corporations Act 2001(Cth), section 1013D.
\item \textsuperscript{48} Corporations Act 2001(Cth), sections 942A-942E.
\item \textsuperscript{49} Corporations Act 2001(Cth), sections 947A-947E.
\item \textsuperscript{50} ASIC, ‘Regulatory Guide 140, Serviced Strata Schemes’ 13 November 2000, RG 140.114-118.
\item \textsuperscript{51} A class order is a pronouncement by ASIC of how it proposes to administer the Corporations Act with respect to a class of persons ‘who carry out a particular activity’, such as, for example, operators of time shares schemes. See ASIC fact sheet ‘Instruments and Class Orders’ available: [http://www.asic.gov.au/asic/ASIC.NSF/byHeadline/Instruments](http://www.asic.gov.au/asic/ASIC.NSF/byHeadline/Instruments) (visited November, 2008).
\item \textsuperscript{52} ASIC, ‘Regulatory Guide 140, Serviced Strata Schemes’ 13 November 2000, RG 140.114-118.
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However, while ASIC has given relief from strict compliance with respect to registration and licensing requirements, relief has not been extended to disclosure requirements. Indeed, in some instances, licensing exemptions, such as those applying to operators of managed rights schemes, are dependant upon the operators giving adequate disclosure to prospective investors prior to the investor joining the scheme.

3.3 Disclosure and Managed Investment Schemes

A number of conclusions may be drawn about the role of disclosure in the regulation of managed investment schemes. First, it is self-evident that disclosure is regarded as a significant component of investor protection. Not only does the Corporations Act provide for a comprehensive disclosure regime, but, as just noted, exemptions given by ASIC with respect to strict compliance with the Corporations Act have not largely been extended to product and service disclosure.

Second, the broad definitions of ‘financial product’ and ‘financial services’ signals a policy approach at the Commonwealth level to set comprehensive and uniform standards in the regulation of managed investments. This policy is underscored by the issuing of one licence, the AFS licence, for providers and operators of financial products and services.

Third, the nature and extent of disclosure are designed to meet minimum standards, both with regard to the content of disclosure and also with reference to the timing of disclosure. As one commentator has noted:

It is through commonality in the requirements of form, presentation to client, content and liability flowing from these documents that the single financial services disclosure regime is constituted

The commonality of information also assists retail clients in comparing the vast array of financial products available to them. Such an approach also accords

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54 A managed rights scheme refers to a scheme where an on-site manager manages the day to day running a serviced strata scheme with respect to caretaking and letting of the units. Government of Western Australia, Management Guidelines for Strata Titled Tourist Accommodation as Part of a Management Rights Scheme, Tourism Western Australia, (March 2008) 3.
with the explanatory memorandum that accompanied the introduction of
Chapter 7 which stated that disclosure is required ‘of any other material
information known to the product issuer …which might reasonably influence a
client’s decision to acquire the product…’.

Fourth, in the context of serviced strata schemes, an important feature of SSS
investor disclosure is that it builds on vendor disclosure applying in
conveyancing transactions at the state and territory level. ASIC itself has
conceded that disclosure not only emanates from the Corporations Act, but may
also ‘form part of, or accompany, any disclosure required under state or territory
legislation about the scheme or strata unit.’ Consequently, disclosure under
state and territory legislation is just as important to the regulatory regime as
disclosure under the Corporations Act.

4. DISCLOSURE UNDER STATE CONVEYANCING LEGISLATION

An interest in a serviced strata scheme is based on ownership of a strata title
unit which is a form of real property. Therefore, under state and territory
legislation, disclosure forms part of the wider body of law applying to real
property and conveyancing transactions. Often disclosure is effected by the
annexure of prescribed documents to the contract for sale of land and/or the
vendor providing a warranty or statement with respect to prescribed matters
relating to the property.

4.1 Disclosure Mechanisms at State and Territory Level

In New South Wales, the ACT and Tasmania prescribed documents must be
annexed to the contract for sale, or made available for inspection by prospective

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59 Parliament of the Commonwealth of Australia, House of Representatives, Financial Services
61 At common law, for example, see *Bernstein v Skyviews & General Ltd* [1978] QB 479, where
the court held that a person who owns the land, also owns as much air space above the surface
of the land that is necessary for his or her reasonable use and enjoyment of the land. Early Strata
titles legislation in Australia includes the Conveyancing (Strata) Act 1961(NSW), *Strata Titles
Act 1966* (WA), Strata Schemes (Freehold Development) Act 1973 (NSW). Legislation now
exists in every state in Australia permitting the creation of strata schemes for a variety of uses.
See generally K Everton-Moore, A Ardill, C Guilding and J Warnken, ‘The Law of Strata Title
These documents include copies of strata plans, by-laws, and folio identifiers for the common property. Additionally, the contract is subject to mandatory statutory warranties or vendor statements that deal with matters such as location and description of easements and other encumbrances and the amount of rates and taxes levied on the property.

In South Australia, the Land and Business (Sale and Conveyancing) Act 1994 (SA) provides that at least 10 days before settlement the vendor must serve on the purchaser a statement setting out any matter affecting title to or possession or enjoyment of the land and any charges and prescribed encumbrances affecting the land. In addition, where the property is held under strata title, further stipulations prescribe that the vendor must provide strata title and strata scheme information.

Queensland, Western Australia and the Northern Territory do not have a dedicated disclosure regime, although partial disclosure and warranties apply in some respects. In Queensland, for example, the standard contract provides for contractual warranties with respect to government notices and resumptions. In Western Australia, legislation imposes limited disclosure obligations on the sale of a strata lot. Purchasers must be given a copy of the strata plan, details of the unit entitlement and by-laws for the strata scheme. Where the vendor is the developer, the vendor is under additional disclosure obligations to provide details of service contracts over the lot and details of any pecuniary interest that the vendor has in those service contracts.

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62 Conveyancing (Sale of Land) Regulation 2005 (NSW), Schedule 1; Civil Law (Sale of Residential Property Act (ACT) 2003 sections 9 and 10; Property Agents and Land Transaction Act 2005 (Tas) section 190.
63 Civil Law (Sale of Residential Property) Act (ACT) 2003 section 9; Property Agents and Land Transaction Act 2005 (Tas) section 190.
64 Conveyancing Act 1919 (NSW) section 52A(2) and Schedule 3 of the Conveyancing (Sale of Land) Regulation 2005; Property Agents and Land Transaction Act 2005 (Tas) section 197.
65 Sale of Land Act 1962 (Vic), section 32.
66 Sale of Land Act 1962 (Vic), section 32.
69 Sharon A Christensen, William D Duncan and Amanda P Stickley ‘Evaluating Information Disclosure to Buyers of Real Estate – Useful or Merely Adding to the Confusion and Expense?’ (2007) 7 (2) Queensland University of Technology Law and Justice Journal 148, 163-4.
70 Strata Titles Act 1985 (WA) sections 68-70B.
71 Strata Titles Act 1985 (WA) sections 69A.
The Northern Territory has the lowest level of disclosure, with very few demands made upon vendors. In 2004, a proposal was made to amend the Law of Property Act (NT) by introducing the Law of Property Amendment Bill 2004. The amendments would have included a new division 5 to regulate sales of residential property with an enhanced disclosure regime. The motion to introduce the Bill was however ‘negatived’ on 5 October, 2004.

4.2 Lack of Uniformity

This brief exposition of vendor disclosure under state and territory jurisdictions demonstrates that disclosure requirements vary considerably amongst the states. New South Wales and the ACT have the most stringent level of disclosure, while Western Australia and the Northern Territory have the lowest. This variation also leads to a lack of uniformity – a position that may be contrasted with the standardized regulation applying under the Corporations Act.

The inconsistent approach evident at the state and territory level is primarily explainable by the fact that these regimes are based on property and conveyancing laws enacted on a state and territory basis. Consequently, each state and territory has enacted whatever laws its legislature considers appropriate. Yet from the point of view of the SSS investor, acquiring an interest in a serviced strata scheme is also the acquisition of a financial product within ‘a single market’, namely Australia. In this respect, a crucial issue is whether the lack of uniformity amongst the states and territories detrimentally impacts upon the protection of SSS investors. This is particularly significant, because as already noted, disclosure under the Corporations Act builds on disclosure at the state and territory level.

5. THE SIGNIFICANCE OF DISCLOSURE

Generally speaking, appropriate disclosure is said to accomplish a number of objectives including enabling investors to make informed decisions and

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73 Sharon A Christensen, William D Duncan and Amanda P Stickley ‘Evaluating Information Disclosure to Buyers of Real Estate – Useful or Merely Adding to the Confusion and Expense?’, above n 69, 163-4.
75 Sharon A Christensen, William D Duncan and Amanda P Stickley ‘Evaluating Information Disclosure to Buyers of Real Estate – Useful or Merely Adding to the Confusion and Expense?’ , above n 69, 175-176.
76 John Goldring, Laurence W Maher, Jill McKeough, Gail Pearson, Consumer Protection Law, above n 8, 15.
enhancing the integrity of property and financial markets. In this latter case, disclosure makes relevant information publicly available and improves both the transparency and operation of these markets.

The approach of ASIC, for example, is that disclosure apprises investors by reducing information asymmetry, especially where a person can avail themselves of many different types of investment opportunities. In the same way, disclosure in conveyancing transactions is seen as a way of reducing the information gap and achieving balance between the bargaining power of the parties. This allows purchasers to negotiate better and ultimately make a more informed decision with respect to the acquisition of the property. Indeed, legislative strengthening of vendor disclosure is often based on this premise.

Yet, studies in the United States of America that have analysed the way investors make decisions indicate that investors are influenced by a variety of reasons. Approximately one-quarter of the investors surveyed, scrutinise disclosure documents carefully and analyse risks and returns on investments before making a decision. Other investors however are influenced by different considerations, such as the reputation of the operator, previous experience with the manager or operator and whether or not the investment has been recommended by a friend or associate. For the majority of investors, these factors are likely to be just as, if not more significant than, information obtained under formal disclosure mechanisms. Indeed, criticisms with respect to disclosure of financial products include the fact that:

disclosure does not give investors sufficient protection; they often do not read disclosure documents and, even if they do, the material is too complicated for


Sharon A Christensen, William D Duncan and Amanda P Stickley, ‘Evaluating Information Disclosure to Buyers of Real Estate – Useful or Merely Adding to the Confusion and Expense?’, above n 69, 153-155.


Ibid.
most laymen and too voluminous for the rest...disclosure has been shown to work imperfectly.\textsuperscript{85}

Similarly, disclosure under conveyancing and land laws has also attracted criticism. In Australia, one report that examined disclosure in conveyancing transactions concludes:

Very little literature exists upon the question of whether the ‘sign now, search later’ process in Queensland provides any more effective buyer protection than the heavy seller disclosure and warranty regimes in other States and Territories although there appears to be a general national consensus, Queensland and Western Australia apart, that a seller should be responsible for providing a considerable amount of both title and quality of title information about the land prior to settlement.\textsuperscript{86}

Yet, regardless of these imperfections, statutory disclosure should at least provide a baseline of uniform and relevant information. This is an important consideration when it is kept in mind that the investor or purchaser makes the final decision on whether to acquire the interest in the serviced strata scheme and there is no ‘government guarantee’ against the investor suffering a loss.\textsuperscript{87} In addition, understanding financial markets may be more complex and difficult than understanding property markets;\textsuperscript{88} therefore, appropriate disclosure allows investors to make comparisons with respect to differing financial products and services.

6. RELATIONSHIP BETWEEN STATE/TERRITORY AND COMMONWEALTH LAWS

The hybrid nature of serviced strata schemes means that SSS investors depend equally on regulations at the state/territory level as they do on laws at the Commonwealth level. Accordingly, the relationship between these jurisdictions is an important linchpin in the regulatory regime.

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\item \textsuperscript{85} Hilary Huebsch Cohen ‘The Suitability Doctrine: Defining Stockbrokers’ Professional Responsibilities’ [1978] \textit{The Journal of Corporation Law} 533, 566.
\item \textsuperscript{86} Sharon A Christensen, William D Duncan and Amanda P Stickley ‘Evaluating Information Disclosure to Buyers of Real Estate – Useful or Merely Adding to the Confusion and Expense?’, above n 69, 148, 176.
\item \textsuperscript{87} Robert P Austin and Ian M Ramsay, \textit{Ford’s Principles of Corporations} Law, above n 6, paragraph 22.030.
\item \textsuperscript{88} Paul U Ali, ‘Australian Listed Property Trusts: Corporate Governance and Related Party Transactions in Stapled Securities’, above n 79, 43.
\end{itemize}
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6.1 A Fusion of Real Property, Financial Products and Financial Services

Those who purchase an interest in a serviced strata scheme make one decision that involves consideration of two matters: a decision to buy a strata unit, and a decision to become part of a managed investment scheme.89 The purchaser makes one decision because he or she will not be able to decide whether to join the scheme independently from the decision to acquire the unit.

One reason why people invest in serviced strata schemes is similar to the reason people invest in other types of managed investment schemes – to enjoy the benefits that flow from professional management of pooled resources. Theoretically, such management should enhance returns so that SSS investors receive greater profits than would otherwise be available if the scheme assets were managed individually by the investor.90 Another reason is more aesthetic. Often developers target ‘mums and dads’ investors who probably think:

they are buying a residential product or a very sexy, fantastic part of the tourism industry [that will make them] a lot of money. But, the reality is that the unit they purchased is a risk they are taking on.91

This type of persuasive marketing may be exacerbated in those cases where the SSS investor retains the right to use the unit for several weeks a year – a feature that potentially provides an additional incentive to acquire the unit, while glossing over the financial risks involved.

First and foremost, vendor disclosure under state and territory laws is designed to assist the purchaser to negotiate better and evaluate the acquisition as an item of real property. On the other hand, disclosure under the Corporations Act deals with the acquisition of a financial product. Consequently, disclosure under conveyancing legislation provides purchasers with information concerning the title and use of the property; while disclosure under the Corporations Act provides information sufficient for the investor to evaluate the cost of the product, the fees and charges payable, and the risks involved with investing in the product.92 In this last respect, disclosure should particularly point to whether the risk associated with the investment is ‘greater than [the] investor can bear.’93

Accordingly, while each level of disclosure deals with a different aspect of the transaction each level is nevertheless related to or even dependant on the other. This means that where regulatory objectives encompass the protection of SSI investors, state and territory laws relating to vendor disclosure need to act in synergy with Commonwealth laws that protect ‘retail clients’. However, given that the states and territories do not have uniform vendor disclosure laws, a crucial issue is how these differences impact upon goals and objectives advanced at the Commonwealth level. It is argued that the differences are important in at least three respects: the content of disclosure, the timing of disclosure, and the type of investor that is protected.

6.2 Commonwealth Objectives v State and Territory Laws

With respect to the content of disclosure, the lack of uniformity amongst the states and territories means that the extent and quality of disclosure is highly dependant on the location and ultimately the jurisdiction of the unit. Therefore, depending on the location of the unit, purchasers will either receive a great deal of information, or very little information concerning their prospective purchase. This uneven approach is at odds with the high degree of uniformity created by the Corporations Act. As already noted, that legislation establishes one disclosure regime applying throughout the whole of Australia and across a range of financial products and services. It allows investors to compare products and services, assisting them to pinpoint the most suitable investments.94

Uniformity is also especially important where an investment comprises an amalgam of products and services95 as occurs with serviced strata schemes. Where disclosure is uniform with respect to only one part of the investment, it may be difficult for investors to compare products and services, making it less likely that they will reach informed decisions.96 Such an outcome, of course, militates against the goals and objectives advanced by the Corporations Act to protect investors by promoting informed decision making. On a more pragmatic level, SSS investors may purchase units in serviced strata schemes located in different states or territories from the one where they reside. The differing disclosure regimes potentially create confusion, thus further impeding effective decision-making.

The second issue relates to the timing of disclosure. Under the Corporations Act, disclosure needs to be made at the time or prior to the investor acquiring a financial product or service.97 Yet, under state and territory regulations,

95 Ibid.
97 See, for example, Corporations Act, sections 941D(1), 946C(1) and 1012A(3), discussed in part 3.1 above.
purchasers in a conveyancing transaction acquire different degrees of information at different times.

In those states and territories, such as New South Wales and the ACT, where documents must be annexed to the contract for sale, disclosure is available at an early stage in the transaction and closely mimics disclosure under the Corporations Act. However, in other cases, such as occurs with Victorian legislation, disclosure is made by way of a vendor warranty. Although breach of a vendor warranty gives the purchaser the right to rescind or claim damages, practical disclosure occurs when the purchaser obtains his or her searches and associated documentation. More often than not, this will occur after the decision to acquire the unit.

Yet, as Griggs has pointed out, disclosure at an earlier point in time, notably when the decision to purchase is being made, is more effective than disclosure after the contract has become binding. 98 Certainly, if the aim is to balance the information asymmetry between vendor and purchaser and enhance investor decision-making, the timing of disclosure needs to be harmonised – both with respect to the acquisition of the strata unit and with respect to the acquisition of the interest in the managed investment scheme. Moreover, harmonisation should tend towards early disclosure in accordance with the Corporations Act, rather than later disclosure, as occurs in some state jurisdictions.

Third, an anomaly potentially exists with the type of purchaser or investor that each regime protects. While both regimes contemplate that certain purchasers or investors require greater protection than others, there is merely partial agreement as to who these investors should be. At the state and territory level, the ACT mandates disclosure only with respect to ‘residential properties’, while other states that specify disclosure, such as New South Wales and Victoria, adopt vendor disclosure for all types of properties. The approach of the ACT is inconsistent with the objectives of the Corporations Act, which specifies that disclosure be given to ‘retail’ investors’, irrespective of whether the property is residential or commercial.

Finally, using one benchmark for real property located Australia-wide may create unintended consequences. Although this paper is advocating harmonisation of state/territory regimes with the Commonwealth regime, the regulatory approach should still be flexible enough to take into account necessary differences amongst the states and territories.

For example, in setting the benchmark for disclosure at $500,000, the Corporations Act may not adequately take into account whether a fixed benchmark is appropriate for the acquisition of an interest in real property. To start with, unlike securities that have a consistent value throughout Australia,

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the median prices of real property, including units, varies considerably in different geographical areas. This variation is magnified when prices in less populated geographical areas are compared with prices in heavily populated areas, such as capital cities and holiday towns. Yet, this important point does not seem to have been taken into account in the formulation of the monetary yardstick. Additionally, investors may perceive an investment in real property to be more stable than an investment in shares and may thus be more inclined to spend $500,000 on real property, compared with shares.

In reality, more research is needed to determine whether the $500,000 cut-off is too high as a criterion for interests in serviced strata schemes. This issue will increase in significance as the acquisition of units in serviced strata schemes continues to grow in popularity. Since the 1990s, for example, ‘investors seeking independence for their retirement, have [increasingly] poured billions of dollars into the supply side of unit accommodation.’

Indeed, it is a matter of some irony that while this paper has highlighted a number of disadvantages stemming from lack of uniformity, a comparable disadvantage can stem from lack of acknowledgement that differences amongst the states may sometimes also need to be taken into consideration.

7. CONCLUSION

Although disclosure is an imperfect mechanism, it is still regarded as an appropriate way to apprise investors. Hence having a regulatory regime that provides for uniform laws with respect to vendor disclosure in conveyancing transactions would provide for a more standardised form of disclosure with respect to all aspects of serviced strata schemes. For this reason, the authors have argued that disclosure at the state/territory level should act in synergy with disclosure at the Commonwealth level. This is particularly important as Commonwealth regulation builds upon vendor disclosure in state and territory conveyancing transactions. Essentially, vendor disclosure should not only be adequate for conveyancing purposes, but should also provide a sound base for objectives advanced by the Corporations Act. Unfortunately, the inconsistent level of disclosure amongst the states and territories does not currently present such a case.

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101 Ibid.

102 John Goldring, Laurence W Maher, Jill McKeough, Gail Pearson, Consumer Protection Law, above n 8, 15 setting out similar arguments with respect to protection of consumers.
One point worth mentioning is that this paper does not advocate the adoption of a particular level of disclosure. Rather, the authors propose that whatever level is adopted, it should represent a unified response and one that is appropriate to the best interests of purchasers, vendors and SSS investors.