

**From:** [Paul Cartmill](#)  
**To:** [Advice Review](#)  
**Cc:** [Steven Everett](#)  
**Subject:** Quality of Advice Submission  
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**Attachments:** [image002.png](#)

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This submission to the Review of the Quality of Financial Advice ('the Review') is on behalf of Thesan Asset Management (ACN 634 179 945, AFSL 528 351)

Thesan Asset Management ('Thesan') is an asset manager acting on behalf of wholesale clients only. This submission is made with reference to 3.2 in the Draft Terms of Reference document dated December 2021.

Thesan is aware that the Review will receive many submissions from licensees who service both retail and wholesale licences. The majority of these submissions will be supportive of a change to the definition of wholesale clients which seeks to either, (a) abolish the class of wholesale clients entirely or (b) raise the threshold for what constitutes a wholesale client.

Thesan is not supportive of substantive changes to the wholesale client definition but is supportive of more clearly defining wholesale client in the Corporations Act 2000 (*Cth*) ('*Corps Act*'). Our arguments and reasons are stated below.

1. Argument for Change: ***The thresholds for what defines a wholesale client have not changed in a long time.***

Rebuttal:

While it is true that thresholds have not changed for a substantial period of time, this does not provide a sufficient reason for change. Thesan submits that the thresholds (a) were too high when they were initially created and are only now consistent with current US thresholds, and (b) those thresholds provide income and net asset tests well above current median Australian income and average net assets statistics.

*Consistent with US Standards*

The US maintains a Sophisticated Investors test and an Accredited Investors test. The Accredited Investor test is similar to Australia's wholesale client test provided by s761(G)(7) as it relates to the objective tests requiring wealth/income thresholds. The Accredited Investor test is clearer however, as it specifically identifies trustees, individuals and married couples whereas Australia's definition refers to a 'person'. Briefly, an investor qualifies under the SEC's Accredited Investor test if the investor is:

- An individual with more than \$200,000 in annual income for at least two years, or
- A married couple with more than \$300,000 in annual income, or
- A household with more than \$1 million in assets, or
- A bank, savings and loan association or other similar financial institution, or
- An investment firm or trust with more than \$5 million in assets

The US Sophisticated Investor test regulated by the SEC is more subjective and mirrors that of Australia's s761(GA) *Corps Act* in that the SEC defines a sophisticated investor as an

individual/institution that “must have sufficient knowledge and experience in financial and business matters to make them capable of evaluating the merits and risks of the prospective investment.”

A country by country comparison is beyond the scope of this submission, but Thesan submits to the Review that the US is home to the world’s deepest capital markets and is the world’s richest economy. By this measure Australia would do well to compare itself against such a successful economy with regard to how we define our investors.

We submit that such a comparison should lead the Review to conclude that, similar to the Accredited Investor test outlined above, while objective tests could be better defined in the *Corporations Act* as it relates to individuals, couples and company trustees, the objective tests outlined in s761(G)(A) do not contain significantly different threshold tests than those defined in the US as Accredited Investors.

*Thresholds are well above Australian Income/Wealth levels.*

Thesan submits that the median Australian income for all workers is ~\$62,000 p.a. This is substantially lower than \$250,000 p.a. income threshold as defined by s761(G)(7) *Corps Act*.

Thesan submits that the average Australian individual is estimated to have net wealth of around \$525,000. This is substantially lower than the net asset threshold of \$2,500,000 as defined by s761(G)(7) *Corps Act*.

With reference to the above statistics, the vast majority of Australians will not meet the provisions of s761(G)(7)(c) *Corps Act* to be considered Wholesale clients. Thesan further submits that Australians falling below such Wholesale Client thresholds would be highly unlikely to have the wealth to invest \$500,000 capital to commit to one product pursuant to s761(G)(7)(a) *Corps Act*, and would therefore fail the Wholesale Client test on this front as well.

### Conclusion and Recommendation

Thesan concludes that the wholesale client definitions in the *Corps Act* should not change because:

- Although thresholds have not been updated for some time, the thresholds provided by s761(G)(7)(c) are not vastly different from US Accredited Investor definitions,
- Australian wealth data suggests that Australians would not have the \$500,000 capital available to be classified as wholesale pursuant to s761(G)(7)(c).

Thesan recommends that:

- Similar to the US Accredited Investor definitions, Australian wholesale client definitions could be better defined in statute for investor types (i.e. Individual vs Joint Account vs Individual Trustee vs Corporate Trustee vs Company) rather than simply a ‘person’ as it is currently defined. Edelman J in his *Storm Financial Case* judgment may provide the regulators with some guidance in this regard.

### 2. Argument for Change: ***The definition of a wholesale client focuses on client wealth rather than client knowledge***

## Rebuttal:

This is wrong at law. S761(GA) of the *Corps Act* provides for a knowledge test to be applied to clients to ascertain their financial knowledge and risk tolerances.

### *Operational & Legal Risk*

Thesan believes that the Review will find it difficult to observe the practical execution of this test in Australia because most financial advisers and managers will not employ this test due to operational and legal risk. Thesan has spoken to a number of financial services lawyers who have confessed that they have no clients currently employing this test due to litigation risk. In summary, it is much easier for financial advisers and wealth managers to defend vexatious legal claims from clients defined as wholesale clients under the **objective** test provided by s 761(G)(7) than the **subjective** test provided by s761(GA). The level of fear with regard to legal risk has reached such heights in Australia that Thesan submits to the Review that it is not unusual to speak to wealth managers and financial advisers who mandate that clients satisfy **both** s761(G)(7) and s761(GA) in order to be considered a Wholesale client. Furthermore, Thesan can submit to the Review that is also not unheard of that some wealth managers/advisers will demand both s761(G)(7)(a) and (c) to be satisfied to be classified as a Wholesale client.

## Conclusion and Recommendation

Thesan concludes that:

- S761(GA) *Corps Act* already provides a subjective test for clients to be defined as Wholesale clients.
- A subjective test alone would put prohibitively high legal risk upon all businesses which currently advise/service only Wholesale clients.

Thesan recommends that no change be made to the *Corps Act* with regard to subjective knowledge tests for clients.

### 3. The Risks of Change

Thesan is aware that the Review will receive myriad submissions pushing for a change to the definition of wholesale client provided by the *Corps Act*. Thesan questions (a) the motives of those participants requesting change, and (b) questions such changes within the context of financial risks currently carried by most Australians.

#### Motives for Change

The initial costs that are invested by equity holders into a financial business in Australia is simply massive. Our financial sector is more heavily regulated than most other industries and therefore the compliance costs are greater still. There will be higher costs associated with servicing retail clients than solely wholesale clients because of regulations. Established companies who service both retail and wholesale clients have spent substantial sums of money, and it is in their competitive interest to raise the cost of doing business for smaller financial firms. With fewer wealth managers/advisers in the market, a greater market share can be achieved by those established firms.

Thesan is a small asset manager that seeks to be more cost effective, achieve better risk adjusted returns for clients and be more client focused than the larger established firms. We submit that competition is a threat to established firms that realise larger economies of scale that can afford heavier regulatory burdens. It is in the interests of established large financial wealth managers/advisers, but not the national interest, to restrict competition. The easiest way to restrict competition is to raise the fixed costs associated with regulations for smaller 'wholesale client' only wealth managers/advisers.

Thesan urges the Review to ignore such requests from large wealth advisers/managers aimed at destroying Australia's competitive environment.

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Yours truly,

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