



ASIC

Australian Securities & Investments Commission

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“Avoiding Share Scams in Cyberspace”

ADDRESS BY

Tim Phillipps

Director, Electronic Enforcement

Australian Securities & Investments Commission

Email: tim.phillipps@asic.gov.au

Web site: <http://www.asic.gov.au>

Infoline: 1300 300 630



Internet Scams and the financial services sector

I'm inclined to say at the outset: "*History repeats itself - repeatedly*" - though I'm sure that someone of considerable importance has already claimed this.

Internet scams, perhaps more appropriately described for today's purposes as fraudulent activity relating to or making use of the Internet, are largely nothing new.

History has repeatedly seen a range of fraudulent criminal activity develop around new technologies. Without going too far back into history, (and to mention but a few), we saw it with the introduction of photocopiers, fax machines, credit cards, mobile phones, automatic teller machines, Eftpos terminals, personal computers and now, not surprisingly, the Internet.

Internet scams, in my view, is simply a well-established tradition of criminality finding a temporary home in new technology.

The Challenge for law enforcement agencies and regulators alike in the fighting financial scams is understanding and leveraging new technologies without inhibiting the creativity and innovation of the financial services sector.

That the Cyberworld has made dramatic changes to the way the financial services sector operates is without doubt. Market innovation and services development in response to escalating rates of human technology adoption pose new challenges for ASIC and continue to influence regulatory strategy and enforcement approaches. This paper will look at these developments essentially from an enforcement perspective.



ASIC and Cyberspace

ASIC maintains a keen interest in the Internet and electronic commerce. As the Australian regulator of the securities and futures markets and consumer protection in the financial services sector including life insurance, general insurance, superannuation and deposit taking activities, ASIC must ensure consumer confidence, commercial certainty, efficiency and market integrity irrespective of the medium employed.

ASIC's approach to the Internet and electronic commerce is driven by a desire to maintain a consistency of regulation within these new channels, and to look to the future as a real-time Cyber regulator. ASIC believes that electronic commerce has the potential to provide benefits to business and consumers alike in terms of efficiency, costs and choice. It also has the potential to generate innovative new problems which must be managed if business and consumers are to have confidence in electronic commerce systems.

ASIC's general approach to the Internet and electronic commerce, and an essential part of the philosophical basis for developing its approach to enforcement issues, is:

- The same types of regulatory mischief that occur in the electronic environment, occur in the traditional markets;
- Technology is a positive development - a tool for changing and improving the current market structures;
- ASIC is concerned with achieving regulatory objectives rather than developing technological solutions;
- ASIC will aim to be technology neutral in its policies;
- To the extent that it is consistent with good policy, ASIC will seek to ensure that regulatory requirements applying to electronic commerce are no more onerous than those applying to more traditional ways of doing business;
- ASIC will seek to ensure that consumers using electronic commerce have at least the same levels of protection as are provided by the laws and practices that apply to existing forms of commerce; and
- ASIC will pro-actively assess the impact of technological developments on efficiency, safety and equity of the financial system and will seek input from industry as appropriate.



Cybertrading: The Australian Experience

■ The rise of online broking

“In just a few years the clubby world of stockbroking has been left far behind as discounters and Internet operators signal a new era”¹

The dramatic rise of online or Internet broking is following closely behind the lead of the U.S.² and providing Australian Investors with substantial opportunities. Paralleled to these opportunities are the inherent risks associated with innovative product and advanced technologies.

Globally, investors are becoming increasingly comfortable (and demanding) with Internet transactions and the almost overwhelming level of information access and transaction facilities which were previously jealously guarded by what was considered a closed shop, more akin to a club, than a financial services industry. Closely held information and company research in the hands of traditional “full service” brokers was the redoubtable foundation of the industry and to a lesser extent still remains so today.

Growing numbers of investors, particularly Australians (who are known as technology adopters following their uptake of mobile phones) do not want the formality and selectivity of advice from a full service stockbroker, electing instead to conduct their own research from within the myriad of online facilities available.

Steven Wallman, former commissioner with the US securities and exchange Commission just over two years ago commented;

“...Internet companies can disseminate information about stock offerings more efficiently, easily cheaply, quickly and with greater interactivity than ever before.... Technology can lower the cost of transactions and increase the liquidity of thinly traded stocks. It can provide greater transparency in pricing and reduce error rates”³

¹ *Brokings Brave New World* by Maureen Murrill - Business Review Weekly 15 February, 1999

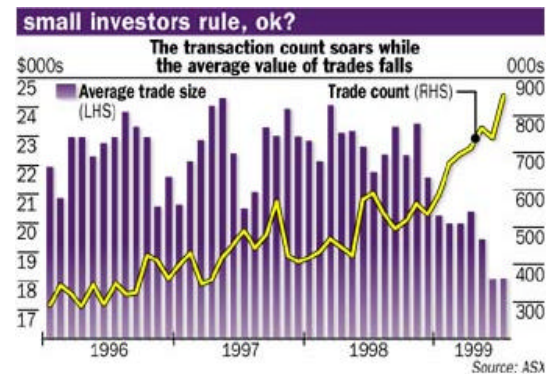
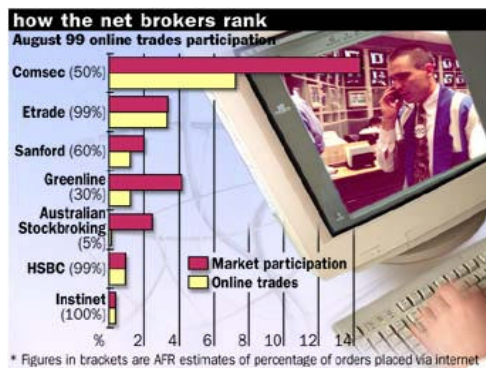
² Australian Securities markets are widely considered to be no more than 2 years behind the U.S. in a technological development context.

³ Steven Wallman, Former Commissioner with the U.S. Securities and Exchange Commission. IEEE Spectrum Magazine, February, 1997



■ Characteristics of Australian Internet Brokers

- 13 Internet brokers operating in Australia (one listed on the stock exchange);⁴
- E*Trade and Quick Broker presently the only fully automated Internet brokers;⁵
- Registered online users estimated to exceed 500,000 ⁶;
- Internet order processing is increasing exponentially;
- ASX estimate \$value of Internet trading to have grown from 0.05% in June 1998 to approximately 1% by June 1999; and
- Approximately 10% of all ASX trading now done online (20% of all retail transactions).



Source: Australian Financial Review 11-12 September, 1999

The above tables suggest an immature but rapidly expanding industry. The low \$value of the transaction (as a proportion of the \$value of all trading in listed entities) coupled with a high percentage of trading done online supports the view that the early adopters of Internet broking services in Australia has predominantly been relatively unsophisticated investors trading regularly, but investing very moderate sums - the familiar "mums & dads" of Australian investment.

⁴ E*Trade - though two other brokers (not online) are also listed (Hartley Poynton Limited & Barton Capital Holdings)

⁵ Both use the ASX's Open Interface system allowing access to ASX SEATS trading system via an electronic messaging interface.

⁶ Comsec alone has 370,000 clients (though many may not be active)



■ **Impact of Internet trading in Australia - the pros & cons**

- Internet Investors have a vastly more expansive range of online information sources upon which to base investment decisions;
- Internet Investors are often influenced by the unreliable information from unproven sources in the form of e-mails, e-newsletters, bulletin boards & chat rooms
- Internet trading has the capacity to improve the liquidity of thinly traded stocks - particularly those launching new technology product;
- Internet trading has the potential to artificially inflate the price of thinly traded, illiquid stocks by “creating” interest;
- Internet Investors get direct control over the entered price but are more inclined to enter a price at BID/ASK spread which tends to drive to price up - no human intervention to “finesse” the market;
- Automated order entry can streamline the process for Internet Investors and effectively give them direct access, through the Online broker, to the market.
- The limited number of Internet Brokers with automated order entry, and delays experienced in order placement for heavily traded stocks can result in some Internet investors placing a bid at a quoted price only to find that by the time the trades are executed the price has changed;
- Accessibility to Online brokers is generally available from any average home PC with an Internet connection;
- Some Internet investors have been frustrated by poor response times with their Internet service provider or the computer facilities of their broking house - particularly on heavy trading days.



Misconduct in Securities Trading

ASIC has received an increasing number of reports of misconduct, ranging from illegal offerings of securities; prospectuses and associated marketing material being placed on the Internet without relevant approval; "hot tips" about particular securities; and investment advice offered by unlicensed persons. A significant increase in the number of reports has been observed following the media coverage of ASIC's April fools day Millennium Bug Insurance cyberscam.

Much of the more recent activity has been emanating from within Australia and overseas, (USA, Canada and South Pacific Island nations) and for the most part is governed by the Corporations Law. Broadly the activity can be divided into the following categories:

- **electronic markets:** the approval and subsequent regulation of electronic equities and futures markets, in particular the introduction of direct to market (usually USA) electronic trading systems;
- **initial public offerings:** ensuring that IPO's by electronic means comply with the law on prospectuses and provide prospective investors with at least the same protections as the physical world;
- **illegal investment:** illegal investment schemes promoted via web sites, bulletin boards and broadcast emails. Often inventors of web based product who need funding support and turn to the web;
- **investment advice:** advice given by persons without an appropriate licence or with no consideration of the needs of investors receiving the advice - often self proclaimed Internet "financial gurus".
- **computer software advice:** escalating numbers of trading analysis software systems that generate buy and sell signals or provide interpretive information recommending or promoting the trading of securities (no securities dealers license). Often accompanied by expensive (\$10,000 or more) training seminars;
- **disclosure of interests:** non-disclosure of commissions and potential conflicts of interest by persons providing advice about securities;
- **free stock offers and share hawking:** a growing trend towards web site promotion through the offer of "free stock" in companies yet to be formed. Promoted as a means of encouraging web users to register with the site - also introduces consumer breaches such as "referral selling" with more "free stock" offered if friends and acquaintances are referred;



- **false statements:** the dissemination of false and misleading information about securities on the Internet or company announcements for the purpose of market manipulation, e-extortion or competitor attack;
- **market manipulation:** the potential for creation of false markets, manipulation of prices or volumes, and insider trading as a result of information disseminated about securities through Bulletin Boards, Chat rooms and promotional web sites;
- **high yield trading schemes:** aggressive scheme promotion characterised by the offer of high returns in offshore investments - Promoted by word of mouth emails and web sites with information delivered to potential investors at “confidential” seminars; and
- **promotion of “exotic” scams:** the transition of exotic investment, pyramid and ponzi type schemes from the physical environment to the Internet.



Internet Challenges for ASIC?

The Challenges for ASIC and law enforcement generally, are substantial.

History has shown that criminals and other market wrongdoers are early adopters of technology with law enforcement following behind. There are many reasons for this, not the least of which involves, funding and resource issues.

Nevertheless, as new technologies are created and gain acceptance legislatures and law enforcement must adapt and apply new legislation and techniques to solve the challenges involved. The problems associated with the Internet are not necessarily all that different to the challenges encountered by Law enforcement with the introduction and adoption of the motor car earlier this century.

The motor car was affordable, introduced speed, the ability to travel long distances in a short period of time and resulted in the growth of crimes like, Bank robberies, smuggling and the transport of illicit goods and the theft of the car itself. Law enforcement then were forced to adopt the technology themselves to counter the challenge and developed countermeasures such as vehicle registration to assist with identity, and police motor cycle and wireless motor car patrols.⁷

In respect of the Internet, the technology is substantially more advanced but the challenges introduced with the adoption equally apply. Specifically the Internet poses challenges such as:

- borderless, global nature;
- the affordability and accessibility of system access;
- the anonymous nature of the technology;
- the use of cryptography;
- the immediacy with which transactions can be conducted; and
- the lack of collateral information (eg fingerprints or eye witness ID)

⁷ From a report prepared by Electronic trading Concepts P/L and the CSIRO



Online broking - a consumer driven challenge

■ The changing trading profile

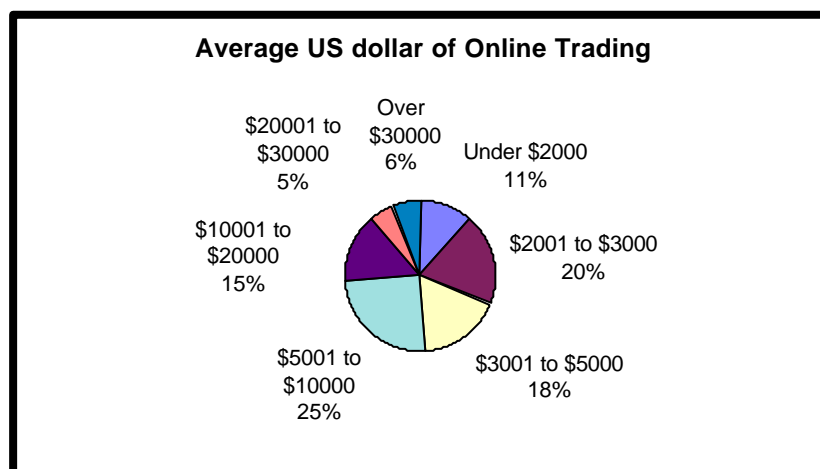
The development of discount broking and in particular, Internet broking, in Australia is changing the trading landscape. The traditional full service environment is by reputation, characterised by semi professional, sophisticated investors who generally trade less often but with higher values. They tend to act on the advice of their well respected (often well heeled) advisers taking significant and decisive plunges into stocks for the medium or long term.

Mums, Dads, cyber youth, and grandparents (the so-called “silver surfers”) are now taking advantage of the accessibility, low cost and relative ease of entry provided by Online broking.

Though too often influenced by speculative media content, the hype associated with new public offerings, and the unreliable chat and gossip which tends to proliferate online, this new generation of investors are conducting their own research and taking their relatively small investment pools and dabbling in the market.

While it is clear that there is a fair proportion of serious online investors operating with Australia, there is also abundant evidence to suggest that majority of online clients tend to invest relatively small sums (often less than \$10,000) and are more likely than not to trade their holdings on a regular basis. This is the developing paradigm of online broking within Australia.

Research by Jupiter Communications in 1998⁸, examining the US online broking sector revealed that of all the online orders processed in the US market only 26% exceeded US\$10,000 with further 49% less than US\$5000.



⁸ “Online Investing Report - navigating the discount brokerage revolution” - Jupiter Communications, New York, 1998 - www.jup.com



A similar pattern is being observed within the Australian market - put in context, this is not necessarily a bad thing. It is providing substantial opportunities to ordinary Australians and has the potential of developing a great sense of pride and “ownership” in business Australia resulting in the continued creation of wealth and a solid base of support for growth. Paradoxically, it also brings with it challenges which cannot be said to be the sole responsibility of either the regulator or the market itself.

Online investors in today’s market, it can be argued, tend to be more average consumers of financial services rather than sophisticated investors. They are influenced by, and respond to, all manner of information sources, making decisions often equally based on emotion and hype as much as good investment practice.

Enter the regulator and the online broking business. Today’s entry level consumers will be the sophisticated investors of the future. In the interest of growth and credibility of the market it is vital they are educated, encouraged and protected.

■ **ASIC - Consumer protection and technical regulation**

In the context of online broking, ASIC has responsibility for providing a regulatory framework which supports the development of innovative product and industry level creativity while ensuring that consumers of financial product have at least the same protection online as they would expect in the physical world. Information needs to be reliable

ASIC, in my view is not the gate keeper of technological standards. We are not in the business, nor best placed, to determine, for example, the size of the communications pipes that an online broker ought establish to carry customer and data communications, or the type of back office software that ought be applied to process order entry.

In my recent visit to the two leading online brokers in North America it was quite evident that they perceive the regulators role as an observer and commentator - that standards associated with technological innovation are the purview of industry - predominantly controlled by customer satisfaction and competition.

I do not accept the view that the regulator should do little more than observe and commentate. I am, however, inclined to a “partnership” approach with the online broking sector. In this way ASIC’s knowledge and understanding of the environment will be expanded, improving the capacity to respond to the consumer implications of the technology development and the challenges facing the broking industry themselves.



■ Online broking - the expectation gap

From a regulatory perspective, one of the most significant challenges facing Online brokers is finding the balance between advertising and marketing that demonstrates the ease and flexibility of the service, while managing the expectations of consumers as to delivery on the promise. This is particularly evident in the area of order entry response times and the concept of “straight through processing”.

Over recent months ASIC has been contacted by increasing numbers of online investors expressing concern over delays or irregularities in order execution. These concerns have included broking firms who offer “straight through processing”.

This “expectation gap” is a product of the technology itself.

In the past when a client placed an order with their broker adviser many understood that the SEATS operator, who would actually enter the trade to market, may be located elsewhere in the building and by the time the broker wrote out the order slip and passed it on, some seconds or even minutes might pass before it made it to the market.

Investors generously took into account a range of very human reasons why the passing of the order slip might delay the entry.

However, phrases like *“hit enter and go direct to market”* have built an expectation (perhaps unrealistic) that pressing the enter button will on **all** occasions see the trade immediately entered into SEATS.

But then that is the technology - before the computer we were happy to wait a week to get a letter - then with faxes we were happy to wait a day. Now with computers if the email doesn't load up the second we hit the “read mail” button on our browser we are straight on the phone to abuse the nearest IT support person

Clearly for those customers using an online broker who has adopted the ASX's straight through processing a quick entry should ordinarily be these case. In addition to the impact of heavy trading periods on particular stocks, computer based “filters” may slow down the process when checking that:

- the client exists,
- sufficient cleared funds or credit exist to cover the purchase,
- stock has been lodged to cover the sale or an electronic market number exists,
- the proposed trade does not exceed any margin lending arrangements; and



- the bid/ask spread is not outside reasonable parameters

The “expectations gap” in Australia is not a unique phenomena.

The US experience reflects a similar level of occurrence. My own observations of two of the US largest online brokers with “straight through processing” suggests a high occurrence of “filter” related rejections (sometimes as high as 2 in 5 trades), with the most common rejections related to either user entry errors or payment issues. Both brokers have a large human “back office” instantly receiving rejected trades and immediately contacting clients to rectify - though in most circumstances delays to market may exceed 2 minutes.

Both also spoke of their concern about “expectations”. One of the brokers has recently instituted a substantial (broker funded) joint education venture with the US Securities and Exchange Commission in an effort to manage expectations and maintain good client relationships.

The technical capacity of the client’s Internet Service Provider (ISP) is an issue which is often overlooked in the response time debate. Keen investors watching their costs will often select local ISP’s for access without giving adequate consideration to bandwidth and carrier capacity - a very slow connection with an ISP is often overlooked by users who interpret slow response times as an online broker issue.

■ Online brokers or financial services aggregators

The web is made for financial services - financial services are made for the web.

Australia is already seeing the development of online financial service aggregators who either establish themselves initially as online broking providers and then, leveraging their existing client base, expand to insurance and a range of other financial services.

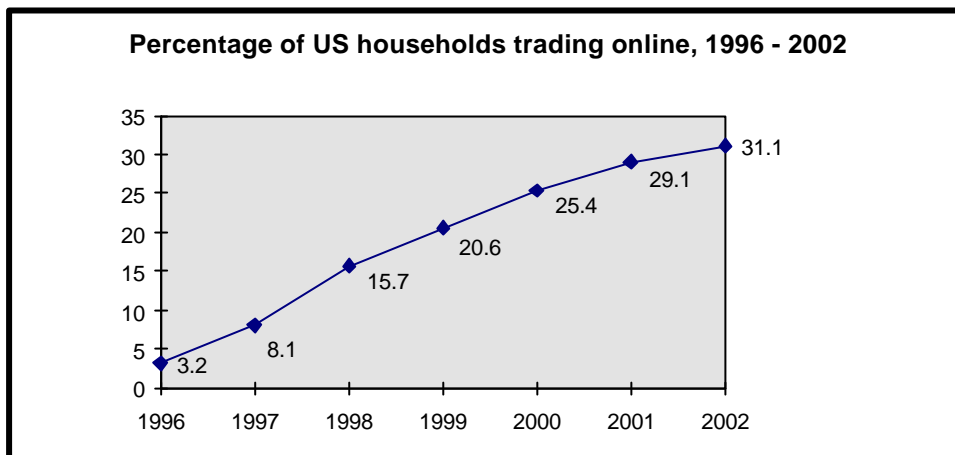
The reverse also applies. In very recent times we have seen examples of online bankers expanding into online broking, either directly or through strategic partnerships. Similarly, we have seen financial software providers in Australia launch online broking operations.

My observation of the strategic direction of organisations like Charles Schwab & Co. in the US reflects a significant shift in the industry. Utilising financial aggregation as a tool to make the transition from discount broker to discount financial and investment centre, Schwab in 1998 had 4.6 million active trading accounts and total client assets of US\$326 billion (including US\$ 73.4 billion online only)⁹. They have recently commenced their own banking operation to assist their clients and facilitate further trading.

⁹ “Online Investing Report - navigating the discount brokerage revolution” - Jupiter Communications, New York, 1998 - www.jup.com



Given that the number of households expected to trade online in the US by 2002 is estimated¹⁰ to exceed 31%, it is no wonder that financial aggregators are planning to take advantage the benefits delivered to consumers by conveniently wrapping up broking, banking, insurance, lending and a range of other financial services.



¹⁰ "Online Investing Report - navigating the discount brokerage revolution" - Jupiter Communications, New York, 1998 - www.jup.com



Alternative Dispute Resolution

Online broking in Australia is characterised by high volume, low value transactions which introduce regulatory and consumer protection challenges not previously encountered in the full service industry. In my view the introduction of a sector based complaint resolution scheme would resolve more simply and effectively the complaints of online broker clients and would establish credibility for fledgling industry.

As a consequence of the demands of these consumer based issues, including questions of “expectation gap” management, ASIC is considering the application of Alternative Dispute Resolution (ADR) schemes which are already proposed across other parts of the Australian financial services sector and reflect the consumer solution approach of industry, government and the regulator.

The Financial Services Complaints Resolution Scheme (Financial planning industry) and the Financial Industry Scheme (Life Insurance advisers) are both close to formal introduction as the first industry based ADR’s in the financial services sector. Both have a claim of jurisdiction over ASX participants but only in the context of the provision of financial advice.

In any event, online broking is a transaction based activity rather than a financial advising activity. Consequently, online brokers, who provide no advising services, are not captured by the existing schemes.

Without access to a low cost, transparent and timely complaint resolution mechanism disputes may go unresolved and the reputation of the industry will suffer.

Computer transaction based activity is well suited to ADR as many of the issues can be adequately resolved by reference to computer transaction logs and a settlement quickly mediated. Closely analogous to the experience of the Australian Banking Ombudsmen in the settlement of disputes surrounding electronic funds transfers

Industry must accept that that ADR is becoming a significant component of the financial services regulatory landscape in Australia. It may surprise some that the experience of others already participating in ADR’s schemes has led to the identification of emerging systematic problems.

Clearly is it far better for industry themselves to identify these and rectify them, than have the regulator impose a solution upon them.



Regulation & Enforcement

■ Countermeasures

ASIC and Law enforcement alike have are considering a range of countermeasures which may assist with dealing with the challenges of the Internet. These include;

- **Adoption of technology** – Financial sector regulators and enforcement agencies must harness the available technology themselves for use in detecting and prosecuting offenders.

By way of example, ASIC has piloted an in-house web automation tool which enables all “.au” domains to be surveilled on a routine basis against a pre-determined risk criteria. Those sites at greatest risk of breaching the Corporations Law then subject of further analysis.

ASIC has also made significant use of web based technologies including, web site and evidence capture tools, messaging and web analysis and web information design strategies such as aggressive (targeted) meta tagging.

- **Forensic Computing** – Regulators and Law enforcement must invest into the development of expertise in the area of forensic examination of computer and Internet security systems.

It is unacceptable in today's technological environment to have regulators, investigators and litigators hamstrung by a lack of forensic expertise in the computing, web and messaging security environment. Those agencies who have attempted to develop a capacity in-house have generally had their staff “poached” once their level of expertise has reached a “commercial” standard.

The research group into law enforcement implications of e-commerce, which is chaired by Elizabeth Montano, Director of AUSTRAC, has recently produced a number of reports on the overall issue.¹¹ The groups consists of representatives from all Commonwealth law enforcement and revenue agencies in Australia.

One of the recommendations contained within the report suggests that there is a need to develop a national computer forensic capacity within Australia to “conduct quick online investigations”

¹¹ see <http://www.austrac.gov.au/publications/RGEC/2/html/>- “RGEC report - Contributions to electronic commerce: what can law enforcement and revenue agencies do.”



While this would be a good start I'm not convinced that it provides a sufficiently broad base to meet the technology needs of law enforcement for the next decade.

In my view, government should consider the immediate establishment of a Law Enforcement Technology Centre to act a centre of learning and expertise for all State and Commonwealth law enforcement, regulatory and revenue agencies.

Potentially capable of being entirely outsourced, the centre would provide a consolidated knowledge base and operational support for;

- forensic computer seizure, evidence analysis and expert evidence;
- web based tracing and investigation methodologies;
- communications security advice and investigations;
- encryption technology advice and investigations;
- continued research and laboratory based technological tools development; and
- skill and expertise development to international standards.

Additionally, the centre could provide a clearing house, assessment and intelligence gathering function for all web based complaints in Australia, along the lines of the FBI Internet fraud clearing house which is presently being developed in the United States.

- **Techno governance** – The development of partnerships with technology developers and users of automated Internet technologies (such as online brokers) to assist with filters that detect misconduct and provide intelligence about application trends
- **Consumer Education** – ASIC has taken a fairly aggressive position on education to drive home the message; Don't get ripped by your own stupidity.

Many of you will have seen the ASIC April fool's day Millennium Bug Insurance cyber-scam which was designed by ASIC to educate consumers about the risks of investing on the Internet. On 1 April 1999, ASIC set up a scam website offering a fake investment scheme in an effort to highlight the willingness of people to invest in companies that they know nothing about.

Exposed in May, ASIC's April Fools Day Joke had succeeded in convincing more than 1400 people to seek out further investment information and 233 people to pledge over \$4 million to the scheme.

To tie in with the Internet investor campaign, in May 1999, ASIC launched the



'Gull Awards' located on the ASIC website (www.asic.gov.au). The Gull Awards feature precautionary, but eye-catching, tales of money and deceit and continue the alert to consumers of investment scams and how to avoid them.

ASIC is drafting a series of 'Consumer Alerts' which will be placed on the ASIC website. The Consumer Alerts will relate to the risks associated with on-line trading, spam-scams and warnings in respect of investment advice from bulletin boards, chat rooms and on-line investment newsletters.

Also, the ASIC website now includes 'Internet Safety Checks' that highlight basic checks that can be made by consumers before investing in Internet based schemes. For example, checks to ascertain whether a company exists and whether or not it has issued a prospectus.

■ Is this enough in the online broking context ?

Charles E Schumer, United States Senator (New York) has recently introduced a bill to congress to "Protect online investors from Fraud and Limit risks" - As a key part of his strategy he has proposed the following legislative changes;

- Require online brokers to disclose any delays in transactions due to service outages, and any investor loses that resulted - posted on the broker's web and to the US Securities & Exchange Commission (SEC);
- Require online brokerages and investment advisers to provide direct Internet links to investor education and fraud prevention sites; and
- Increase the ability of the SEC to combat fraud by increasing the SEC budget by US\$350 over five years and doubling the monetary penalties for any fraud offence involving the Internet.

ASIC has already commenced discussions with a number of financial services providers who are voluntarily seeking to establish direct links to consumer information releases within ASIC's website.



Jurisdiction¹²

ASIC has recently released Policy statement 141 which makes clear that ASIC does not intend to regulate offers, invitations and advertisements of securities that are accessible in Australia on the Internet if:

- the offer, invitation or advertisement is not targeted at persons in Australia;
- the offer or invitation contains a meaningful jurisdictional disclaimer;
- the offer, invitation or advertisement has little or no impact on Australian investors; and
- there is no misconduct.

ASIC wants to improve certainty for people who use the Internet for commercial transactions (in respect of the Corporations Law) and does not generally seek to regulate offers, invitations and advertisements that have no significant effect on consumers or markets in Australia. If every regulator sought to regulate all offers, invitations and advertisements for financial products that were accessible on the Internet in their jurisdiction, the use of the Internet for transactions in financial products would be severely hampered.

A prospectus is required when an offer¹³ or invitation is made or received in Australia. This means that the Law may apply to an offer or invitation of securities on an Internet site accessible from Australia irrespective of where the offeror is located¹⁴

Experience to date suggests that sites operated outside Australia do not often target Australians and generally have limited impact on Australian investors or our investment markets. In any case, they frequently lie beyond the reach of Australian law and so Australians who rely on such sites are not provided the protections of the Corporations Law in their dealings with overseas promoters. ASIC will, however attempt to assist in cases of serious fraud through our relationships with overseas authorities.

¹² see ASIC policy statement 141

¹³ includes the distribution of material that would encourage a member of the public to enter into a course of negotiations calculated to result in the issue or sale of securities

¹⁴ see ASIC Policy Statement 56, *Prospectuses*, ASIC Policy Statement 107, *Electronic prospectuses*.



What is ASIC doing ?

■ Electronic Enforcement Unit

In acknowledgment of the growing need for focus on electronic enforcement, ASIC established its Electronic Enforcement Unit (EEU), in mid 1999. EEU aims to increase ASIC's ability to take swift and effective action against unlawful behaviour on the Internet and focus on building expertise in the electronic environment.

EEU is also establishing a nationally consistent approach to electronic enforcement and a framework that confirms consumer and investor protections.

EEU is assisting regions in the identification of appropriate Internet based activities, coordinating ASIC's case selection, enforcement and litigation activity and providing expert consulting support in web based technologies.

Current focus areas for EEU include

- the pilot use of a 'virtual toolkit' to provide automated Internet surveillance
- the development of an electronically published enforcement resource ("the Enforcement toolkit") containing legal precedents, relevant legislation, electronic guidelines, model affidavits, expert statements, protocols, contacts and various other litigation support tools to assist in case preparation;
- the establishment of an "enforce.net" network of trained ASIC enforcement staff capable of undertaking entry level Internet based investigations and litigation; and
- the establishment of a Global enforce.net Internet based discussion forum for international members of the securities regulation community.

Recent enforcement actions include:

- ASIC's Internet service provider surveillance program in November 1998. The purpose of the surveillance program was to ensure that Internet service providers understand and comply with the Corporations Law (see ASIC media release 98/346);



- The Chimes case. In February 1999, ASIC obtained injunctive relief against Stephen Matthews, the publisher of an Internet site called *The Chimes Index*, to prevent investment advice being provided in breach of the Corporations Law (see ASIC media release 99/37). In July 1999 the Supreme Court of NSW affirmed the Federal Court orders which had been made and were later struck down by a High Court decision;
- Enforceable undertaking from Paritech Pty Ltd not to market, advertise, distribute or sell the computer software package Omnitrader until Paritech obtained an investment advisers licence (see ASIC media release 99/268);
- Enforceable undertaking from Martin Leigh Davies-Roundhill to cease promoting an investment offer which he had posted to 25,000 newsgroup sites through his home computer (see ASIC media release 99/249);
- Federal Court orders obtained against Investors International Pty Ltd and its Director Stuart Arthur to prevent illegal fundraising on the Web;
- Injunction against Netlink Ltd to restrain website promotion of investment opportunity in an Internet based product (see ASIC media release 99/274);
- Enforceable undertaking against a NSW resident who was giving futures/investment advice on the Internet;
- Undertaking from a multinational company, On Line Investor Advantage to cease providing unlicensed investment advice in Australia and promoting without proper authority buy and sell signal software on their website; and
- August 1999, ASIC joined the Securities and Exchange Commission campaign to stop Internet based free share offers (see ASIC media release 99/299).



■ Additional ASIC strategies

- **EFT Code** - With its new consumer role in financial services, ASIC has taken responsibility for monitoring the Electronic Funds Transfer Code of Conduct. ASIC will work with industry and government to review and broaden the EFT Code to cover all financial electronic transactions
- **ASIC's Public Information Program** - ASIC has progressively increased its electronic commerce capabilities and embraced the Internet with new products benefiting Australian business and consumers. These including electronic lodgement of returns (EDGE), free Internet company index and register searches (Netsearch), electronic company registration (ECR) pioneering the application smart cards in Government, E- registers, providing the ability for clients to make changes to incorporation details online and finally facilitating the examination of disclosure documents through the FUNDEX project.
- **Policy Development** - Since September 1996 ASIC has been actively releasing policy designed to facilitate electronic commerce. Policy to date includes:
 - Electronic Prospectuses (Policy Statement 107);
 - Investment Advisory Services - Media, Computer Software & Internet Advice (Policy Statement 118);
 - Offers of securities on the Internet (Policy statement 141); and
 - The release of a policy proposal paper on electronic applications for securities in September 1999.

ASIC will continue to review the need for further policy. Projects are presently underway on fundraising and disclosure document lodgement, electronic application forms for disclosure documents and electronic corporate communications.



- **Industry partnerships** – The ISP industry over the past few years has grown from approximately 60 in August 1995 to over 715 in 1998. Recent research by ASIC¹⁶ revealed the business and corporate inexperience of the fledgling industry. ASIC has commenced working on partnerships arrangements the Internet Industry Association to assist the industry body to improve standards of corporate governance and conduct and ultimately assist in protecting consumers.
- **Regulatory & International Relationships** - ASIC recognises that from an enforcement perspective, greater coordination and cooperation of regulatory efforts is essential - both domestically and internationally. ASIC has had, and continues to have, formal and informal discussions about electronic commerce with various domestic regulators and agencies to identify and work together on areas of mutual interest.

¹⁵ Source: www.consult

¹⁶ “Internet Service Providers New South Wales Assessment” – ASIC National Intelligence & Analytical Service September, 1998 – Kirsten Beyer, Analyst



Where to from here?

In the last ten years over 100,000 Australians have lost their savings in failed or fraudulent investments, and ASIC is committed to reducing this casualty rate.

Investors and consumers need information and advice about investments and financial products that is honest and fair. Otherwise they lose confidence in investing. They also need people to advise them efficiently, honestly and fairly. We license only those people who demonstrate basic standards of competence and good character.

More consumers are using the Internet to find information they can rely on to make financial decisions. At the same time cheats and frauds have been using the Internet to set up financial scams. Australian law gives investors and consumers the right to accurate information about investments and financial services, whether that is published in hard copy or on the Internet. Advice on the Internet does influence investors' decisions, and they are entitled to expect Australian operators and other users to obey Australian law.

As consumers, users, providers and regulators we have to be adaptive and vigilant.

The opportunities for the Internet seem endless and the soaring popularity for Cyber investing also appear boundless.

Unfortunately the opportunities for con artists and the ethically challenged also grow in proportion.

