

# PARLIAMENTARY JOINT COMMITTEE ON CORPORATIONS AND FINANCIAL SERVICES

## ASIC OVERSIGHT HEARING

Tuesday 13 June 2006.

ASIC witnesses:

Jeffrey Lucy; Chairman. Australian Securities and Investments Commission

Jeremy Cooper; Deputy Chairman. Australian Securities and Investments Commission

Discussions regarding the Westpoint group

This Hansard is an extract from proceedings transcribed by the Hansard office of the Australian Parliament.

**Ms BURKE**—Do you think that in some roles you need to be a bit more proactive in your litigation work? Westpoint is a case in point where there has been a bit of criticism that you did not act as quickly or as efficiently as could have been the case.

**Mr Lucy**—There are two points to your question: firstly, do I think that we could be more aggressive with our litigation? No, I do not. There is litigation in two categories, civil and criminal. Our dialogue with the DPP is effective. There is the right level of attention as to whether or not matters should be taken on criminally, so I think that is appropriately dealt with. Similarly, with the civil side of things, we have a success rate in the courts of some 97 per cent. We are very energetic with our investigations to make sure that if there are opportunities for prosecutions we will follow them through.

It is interesting that you refer to Westpoint in the manner that you suggested, where there is an implication of criticism. To some extent that was one of the major thrusts of our last meeting a fortnight ago in the Senate estimates. We really spent a fair bit of time providing some background to show that certainly that is not ASIC's view. Indeed, all the action that has been taken to date has been taken by ASIC. If you hark back to the responsibilities of the directors, the office bearers of the company, the third parties such as legal firms, auditors and so on, all the way along the line it has been ASIC that has been taking the action. We continue to have a matter before the court where we are waiting on a decision. Notwithstanding that situation, we took action in about October 2005 to have these companies wound up. In the press last week the auditors said that they advised us in December 2005 they felt there was an insolvency issue. We had acted by that time. We think that our action in respect of Westpoint is more than defensible; we think it has been appropriate.

**Ms BURKE**—I have to be honest: I did not read all the transcript from Senate estimates.

**CHAIRMAN**—We do not want duplication!

**Ms BURKE**—We do not want duplication, so I am not actually going there. My question was more in essence about the media reportage of it and how action is taken, whether it is something you instigate or it is brought to you by the liquidator or by somebody making a complaint. Using Westpoint as an example, given there are now so many mum and dad investors, as we keep referring to them, out there bleeding, at what point does someone act? Is that your responsibility? Is it the liquidator's responsibility? Is it the director's responsibility? As I am interpreting it, the media criticism seemed to be that ASIC waited too long to take action.

**Mr Lucy**—You suggested that we should not be preoccupied with Westpoint. In relation to something like that, unfortunately a lot of the media choose not to really get into the facts and do the full investigation. The point that you raise is a very important point. We do receive

complaints. Some of the complaints are beyond our jurisdiction and, therefore, we would respond accordingly. Many of the complaints really do provide invaluable intelligence to us as to the sorts of mischief that can be going on, and we accumulate them and deal with them intelligently. If a name crops up more than once, then it starts to add weight as to the fact that there is something going on that perhaps needs to be more closely addressed.

We have also taken a number of administrative decisions within ASIC as to our structure. About a year ago we commenced a directorate called compliance, and that is now undertaking surveillance work right across our entire agency, from liquidators and auditors to holders of financial service licenses—the full gamut. There is a very close correlation between complaints coming in and the sorts of issues that have been raised and the surveillance activities. We have also taken the decision to give more enforcement teeth to our complaints area. Matters that are more straightforward but not necessarily routine can be dealt with within the complaints area without necessarily having to be referred to the enforcement area. I think your point is very well made. Again, we are not acting from a position of being defensive but we do think there are opportunities for doing things better and that is what we are working to do.

**Ms BURKE**—Regarding Westpoint again—I have read all of the stuff on it today—there is an issue of how we actually advise investors. I keep saying to people, ‘If I could legislate commonsense, I would be a happy woman but you cannot do it.’ You put out press releases and you have done some shadow shopping but a lot of your press ends up in the *Financial Review*. That is not a criticism—it is just the area that picks it up. Not every investor—not even every financial planner—reads the *Financial Review*. How are we getting the message out there? As we are getting more and more people on stream with their super funds at their own disposal through super choice, how are we actually educating people not to blow their money in these investments? In this case it sounded reasonable and was sold as reasonable. How do we educate the public?

**Mr Lucy**—It is a very pertinent question and I think there are several layers to it. The first is the area of financial literacy. The government have undertaken a process where they are trying to specifically improve financial literacy in the community. That project is something for which ASIC and the ANZ Bank really were the germinators, and we are delighted that it has legs and is being carried forward. We have also looked very hard at the media communications. You are quite right: historically it has been in either the *Financial Review* or, if not, the financial press of something like the *Australian*. The mums and dads do not always read those sections of the newspaper. We have broadened that quite considerably into the *Telegraph*, some other sorts of media and also magazines. We now are doing a lot more by way of talkback radio, radio interviews per se and television to an extent. The balance is that we cannot oversell ASIC. We do not want ASIC to get to the point where people say, ‘Goodness me, it’s ASIC again in the press,’ which reaches a point where it is a turn-off. We need to continue our currency and for people to continue to want to listen to our messages. Our FIDO website, which is an excellent website, really provides incredibly important and useful information. The numbers of hits to that go up exponentially each year, so that is working. I think it is really just a matter of doing it better. We are looking at the possibility of doing some war stories. For example, it is one thing for me to say, ‘Well, this is what you should avoid,’ but we think that there is a real benefit in having an investor who has been caught out saying, ‘This is where I was caught out. This is the lesson for me.’ We think that would be a very powerful message, so we are looking to do that in addition to the spokesperson saying things as well. It is something which is right in front of us all the time. We are looking at our media unit, not just for the sake of historical media announcements but again to try at every opportunity to put the extra flavour to it to say, ‘Yes, we’ve jailed somebody’ or ‘Yes, we’ve sought to ban somebody,’ but then the next side of the story is the consumer message about that. We really are looking at all dimensions.

**Ms BURKE**—Insofar as just monitoring where you are getting hits and feedback, have you got somebody tracking that to say, ‘This has worked; this hasn’t worked’?

**Mr Lucy**—Yes, I think that we do that quite intelligently. As a budget funded organisation spending taxpayers' money, we are very careful that we do not waste any money. We are also very careful that we apply the right amount of money in the right area. I think that we do give that the attention which it deserves. Having said that, it is a never-ending story to get the message out.

**Ms BURKE**—Besides the financial literacy task force—which I have some doubts about, but that is just me personally—are there other organisations you are working with outside that to actually spread the message?

**Mr Lucy**—Yes. We have a group that has been in existence as far as I can remember—we could give you the exact date that it commenced if you wish—called the Consumer Advisory Panel. Apart from our Executive Director of Consumer Protection, everybody is external. They come from the full spectrum of people that you would reasonably assume present consumer positions, and they give us invaluable feedback. We fund them to do research. That is very effective for us.

...

**Mr BAKER**—Was there an initial lack of diligence on the part of the auditor KPMG in respect of Westpoint? Can you give us an update?

**Mr Lucy**—Perhaps you would be kind enough to rephrase the question because I was not quite sure of the context.

**Mr BAKER**—Where does KPMG sit in this issue? Can you confirm or deny that there was a total, a small amount or an initial lack of diligence on their part?

**Mr Lucy**—We are in a position where we have a very active investigation on foot in relation to Westpoint. We met your parliamentary colleagues 10 days ago and spoke in some detail about the history of Westpoint. As far as where we go in going forward, we indicated that we are investigating all circumstances dealing with Westpoint, including the role of directors, officers and third parties, including auditors. That is a matter that we are working on. We have it in front of us, but it is not appropriate to go into any particular detail.

**Mr BAKER**—Is there anything you can say about how we can move forward and prevent this type of thing happening in the future? What have we learnt at this stage from the situation?

**Mr Lucy**—It really is too early to tell what particular offences may or may not have been committed. Certainly we are communicating with the investors as openly as we possibly can be. We have a specific website set aside for Westpoint investors. There is due to be a second meeting in Sydney of a core of representative investors, about 70 of them. My recollection is that is scheduled for 22 June. We will provide them a further update on where we are with our investigations, as appropriate. You will have read in the press that we have been extremely energetic in all sorts of areas, including bringing people back from the United States and other activities to try and protect the investors. It is an investigation that is receiving the due priority, the commission is engaged, and I am very comfortable that we are doing whatever we prudently can.

**Mr BAKER**—From a consumer's perspective or from a regulator's perspective, if you take the two approaches, and also obviously from the government's perspective, how can we identify that there are not other Westpoints out there?

**Mr Lucy**—I think there are couple of things, and again these are messages that we have been putting out as loudly as we possibly can. Firstly, people should be encouraged to deal with licensed advisers. There is a distinct advantage, in our view, in people dealing with

licensed advisers; they have very clear responsibilities. Also, we are stressing to people that they need to take responsibility for their decisions. They need to have regard to risk and what they can afford to lose. They need to have regard to their own financial circumstances. They need to understand that it is a bit like the bull's eye in the centre. One can deposit money with an APRA regulated bank and the risk is absolutely minimal. The further you move out, the greater the level of risk. There is nothing wrong with undertaking risk as long as it is properly balanced with what you can afford and what your circumstances are as to whether or not you are employed or retired. It is a matter of balancing. In the case of financial advisers, those are exactly the responsibilities that they have—to know their client and to know their products. There needs to be the right legislative mix. It is a matter of making sure that those guys that are out there that are licensed are heeding their responsibilities.

**Mr BAKER**—Have you identified the number or the breakdown of licensed and unlicensed planners involved in this?

**Mr Lucy**—We are in the process of doing that. We have sought communications from essentially all of the investors. I cannot give you the number, but I can give you a statistic. Investors who total \$300 million in aggregate of investment out of about \$350 million to \$400 million have responded. We have a very high participation rate and we are in the process of collating that intelligence.

**Mr BAKER**—How do these clients get involved in unlicensed planners? Where do they seek these—

**Mr Lucy**—In the first instance it might be a friendship, Much of it is through ethnic groups where a particular circle, be it a religious circle or an ethnic circle, encourage their colleagues and friends to participate in this investment in which they have participated. It is human nature. When you come across your friends, they all say, 'I've come across this greatest lawyer or greatest accountant or greatest financial planner, you should all share in what I've found out.' It is just how the community seems to work.

**Mr BAKER**—From a regulatory perspective, that group is very difficult to regulate. The major concern would be the licensed planners who have gone against the recommended list and knew that what they were doing was purely for financial gain.

**Mr Lucy**—That is why we have made it very clear that the advisers are part of our investigation and we will follow that through with a great deal of detail.

**Senator MURRAY**—Have you checked with the tax office whereby any of these planners or advisers were also listed by the tax office under the mass marketed tax effective schemes investment? You might recall the settlement negotiated with the Senate and then carried through by the tax office that distinguished between sophisticated and unsophisticated investors and then identified the planners, accountants, lawyers and so on who had been involved in these things. It would be worth knowing if there were people who had been involved in both sets of activities,.

**Mr Lucy**—That did come up at the estimates, where we were asked whether or not there were any tax agents—

**Senator MURRAY**—By me.

**Mr Lucy**—That is a work in progress for us now.

**Senator MURRAY**—Good.

**Ms BURKE**—Is anything happening against the licensed planners who have given advice in this regard?

**Mr Lucy**—It really depends upon the outcome of our investigation. At the low level it would be a ban and at the high level it could be criminal prosecution.

**Ms BURKE**—Will that be investigated? Are you going to follow that path down to see if—

**Mr Lucy**—All of those areas will be investigated fully.

**Ms BURKE**—Regarding the commissions area and the fairly high commission that these planners were getting, both licensed and unlicensed, do you see a need to change that law or to beef up how commissions are described? I thought that magical 10 per cent to which you were getting was pretty huge anyway; most commissions are in the area of 1.5 per cent to three per cent on average.

**Mr Lucy**—There are a couple of ways of dealing with this, but firstly we need to recognise that like oils aren't oils, commissions aren't commissions. Quite appropriately there should be a higher level of commission for some products compared to simply getting something over the phone. I think that there is an argument to say to the industry that they should identify what they regard as a benchmark commission rather than us, a regulator, announce it. Then, in the disclosure statements, they should nominate to the extent that they move outside that band. For example, let us say the band is two per cent and your reference is 10 per cent, I would not say that is eight per cent; I would say that is five times higher.

**Senator SHERRY**—I have one aspect of Westpoint that I wanted to touch on briefly. Was the appointment of KordaMentha Receivers of Keypoint Developments Pty Ltd as liquidators an ASIC decision?

**Mr Lucy**—It is ultimately the court's decision but—

**Senator SHERRY**—You would be involved in the process?

**Mr Lucy**—Yes.

**Senator SHERRY**—An issue that I have had raised with me by a victim is whether KordaMentha also act for some of the financial institutions, the banks, that are owed money? Is that your understanding?

**Mr Lucy**—It would be my expectations, if not my understanding. There is a very small community of insolvency practitioners. You have a number of players that are already involved because of their other relationships with Westpoint, so they are obviously eliminated. Within that small community you have to deal with who is left.

**Senator SHERRY**—What about the potential conflict though where KordaMentha are acting for a bank who would be first mortgagees in most cases, I assume?

**Mr Lucy**—Probably a receiver, which would mean a floating charge. It may also mean that they have a specific charge but they would be in there as a receiver because of a floating charge.

**Senator SHERRY**—Whatever moneys flow or are left over, it is first mortgagee first, usually a bank, and then whatever is left—if there is anything left—goes to the consumer. Do you see any conflict with KordaMentha working in respect to the bank and also being the general receiver?

**Mr Lucy**—I will take that on notice because, for example, let us say company A and company B are both under the Westpoint family. I could imagine company A having a firm of receivers appointed and company B having that firm as liquidator, but I could not envisage company A having both the same firm acting as receiver and liquidator.

**Senator SHERRY**—What about where a liquidator is not able to obtain any assets; how do they get paid in those circumstances?

**Mr Lucy**—You then come back to the underlying basis for the assetless administration process. Where a liquidator is faced with essentially insufficient assets or, as you describe, no assets, then under the new regime they can come to us and we will fund them to do the reports.

**Senator SHERRY**—Could that happen in this case?

**Mr Lucy**—Yes.

**Mr BAKER**—That will follow what you do in the legal process. The major concern that I have is what other mezzanine type property developments are out there that have the potential to cause just as much damage? How can we use this as an example of identifying what is happening out there?

**Mr Lucy**—One of the difficulties which we all face is that we have an open-ended appeal decision with the Western Australian Court of Appeal. Once that decision is finalised, then we can recommend to the government that they need to look at amendments; or, if the decision goes in our favour, then we do not need to worry about that. We are all up in the air over that particular issue.

**Mr BAKER**—Have you got ideas or interests in other plans that are currently out there?

**Mr Lucy**—Other entities? Yes, we have. We have several that we are engaging with very closely.

**Mr BAKER**—Very good; that is reassuring.

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**Senator SHERRY**—I return to a question on notice relating to Westpoint applying for a licence. I refer to E43, question AT36. I asked whether they had applied for one and you said:

*No, Westpoint Finance Pty Ltd held an Investment Adviser's licence ... from 27 June 1996 to 21 January 1999.*

*ASIC has no record of Westpoint Finance Pty Ltd ever making an application for an AFSL, however it was an Authorised Representative ... for CGU Insurance Ltd ... during the period 4 February 2004 to 14 July 2004.*

As Westpoint was an authorised representative of CGU, could or did ASIC take any action against Westpoint at that time as an authorised representative of CGU?

**Mr Lucy**—Was that a question on notice 10 days ago or at some earlier time?

**Senator SHERRY**—This relates to the additional estimates of 16 February 2006. We got the answer in that batch last week and I have those in front of me.

**Mr Lucy**—I will have to take that question on notice. I am not aware of whether or not we looked at the CGU issue.

**Senator SHERRY**—According to ASIC's answer on notice, Westpoint Finance Pty Ltd were an authorised representative of CGU for a period of time. In those cases, can ASIC take action against the authorised representative because it was licensed through CGU?

**Mr Cooper**—In relation to what? We will have to take this on notice. It could well be that that licence was in order to advise about and sell CGU insurance to people who invested in real estate.

**Senator SHERRY**—Take that on notice. It does not make that clear.

**Mr Cooper**—It does not.

**Senator SHERRY**—Is this a possible loophole for an unlicensed adviser effectively to become licensed?

**Mr Cooper**—Again, taking it as a hypothetical question, no. The licensee takes full responsibility for what the authorised representative does, so we do not—

**Senator SHERRY**—Take a hypothetical: couldn't an entity that has been given an authorised representative's licence mislead a consumer by quoting the licence number but it is in fact very much restricted in the activity in which it can engage?

**Mr Cooper**—That is possible but you would not find too many licensees tolerating that.

**Senator SHERRY**—Anyway, have a look at those issues I have raised. There is another issue relating to Westpoint. I put some questions on notice back in February and you provided me with a copy of a letter from Ian Campbell, the then parliamentary secretary, which he sent to the WA minister for consumer affairs, Mr Kobelke, on 3 February 2002 in respect of Westpoint. The letter from Senator Campbell to the minister in WA said:

*Thank you for your letter of 21 August 2002 to the Treasurer concerning the use of mezzanine financing to raise funds for property development. I am responding on the Treasurer's behalf. You would be aware that the Australian Securities and Investments Commission, ASIC, especially through its Perth office, has been in regular contact with your department concerning this issue over a number of months. Further, upon receiving your letter, the Commonwealth Treasury also raised your concerns with ASIC. ASIC advised the Treasury that it is carefully examining this issue and has been obtaining comprehensive legal advice on the regulatory status of these property financing schemes to which your letter referred.*

It is still not entirely clear to me, from the answers provided, exactly what ASIC was doing at that time. What were you examining back in late 2002 and early 2003 to which the parliamentary secretary is referring?

**Mr Lucy**—My notes indicate that you are quite right: there was dialogue between the former Parliamentary Secretary to the Treasurer and the Hon. John Kobelke in Western Australia in early 2002 and also in about August-September 2002. We obtained senior counsel advice around that time as to what our jurisdictional options were, which led us to commence action in the Supreme Court of Western Australia in 2004.

**Senator SHERRY**—Wasn't an alternative to recommend to the government to change the law to make it clear at that time? You had received warnings in 2002; you received legal advice in early 2003—

**Mr Lucy**—At that stage both the minister in Western Australia and ASIC separately undertook consumer warnings as to the issues regarding promissory notes greater than \$50,000. Bearing in mind that the decision to deliberately carve out promissory notes greater than \$50,000 was a deliberate decision taken by parliament. That position existed. At that stage, as we have said in earlier forums, the complaints which we received were to do with

the jurisdictional issues; they were not to do with business plan issue or business model issues. People were not suffering financial hardship at that time through their investments.

**Senator SHERRY**—That you knew of.

**Mr Lucy**—That we knew of.

**Senator SHERRY**—The letter from Senator Campbell says, 'If required, the government will consider any recommendations ASIC makes to improve consumer protection in this area.' Did ASIC seek at that time to change the law to take clear jurisdictional control of promissory notes?

**Mr Lucy**—No. We took the matter to court. At that stage you do not know whether or not the law needs changing until you test it in the court.

**Senator SHERRY**—You do; you can get legal advice.

**Mr Lucy**—We did. The legal advice was that we would be successful, and we were not fully successful.

**Senator MURRAY**—If you were successful then you would not need to change the law; that is your point?

**Mr Lucy**—Correct. Indeed, the whole Westpoint saga would have played out quite differently.

**Senator SHERRY**—Wouldn't it have been quicker to have sought to change the federal law back in early 2003? That would have been quicker in terms of a process to cover this, wouldn't it?

**Mr Lucy**—In hindsight. But again, typically, the way that parliament and the government of the day work is that it is an issue identified that is before the courts, so we wait for the courts to make it clear.

**Senator SHERRY**—But it was not before the courts at that moment. You apparently received advice that you did have jurisdiction—

**Mr Lucy**—As explained at Senate estimates, it was not clear-cut advice. It was advice that was quite complicated, it was really almost self-serving to get us to a point. Ultimately, that was not successful.

**Senator SHERRY**—I do not understand with respect to the activity that was occurring. If you had said to government, 'Look, we want this matter made very clear very quickly,' it seems to me reasonable and quite conceivable that such a change in the law would have got through the parliament by the end of 2003—it would not have been significant—and some people would have been saved a lot of grief.

**Mr Lucy**—Legislation cannot guarantee that there will not be failures. Parliament specifically, for whatever reason, chose to carve out the promissory notes of greater than \$50,000.

**Senator SHERRY**—After that there were warnings coming from the WA minister, the responsible minister, and the department, a number of warnings to the Treasurer, then referred to Senator Campbell, to ASIC direct nationally and to your local office, that there was a practical problem on the ground in WA.

**Mr Lucy**—Yes.



**Senator SHERRY**—The government was considering it. The parliamentary secretary's letter says: 'We have received advice from you, we have received advice from Treasury, and I expect to shortly receive advice from ASIC after they have fully considered the issue.' You were obviously considering it. The letter goes on to say:

If required, the government will consider any recommendation ASIC makes to improve consumer protection in this area.

Your preferred action was to take court action?

**Mr Lucy**—Correct.