



COMMONWEALTH OF AUSTRALIA

Official Committee Hansard

SENATE

SELECT COMMITTEE ON SUPERANNUATION AND
FINANCIAL SERVICES

**Reference: Prudential supervision, global financial services and superannuation
guarantee charge**

FRIDAY, 16 JUNE 2000

BRISBANE

BY AUTHORITY OF THE SENATE

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SENATE
SELECT COMMITTEE ON SUPERANNUATION AND FINANCIAL SERVICES

Friday, 16 June 2000

Members: Senator Watson (*Chair*), Senator Sherry (*Deputy Chair*), Senators Allison, Chapman, Conroy, Hogg and Lightfoot

Senators in attendance: Senators Allison, Hogg, Lightfoot, Sherry and Watson

Terms of reference for the inquiry:

For inquiry into and report on:

- (a) prudential supervision and consumer protection for superannuation, banking and financial services;
- (b) the opportunities and constraints for Australia to become a centre for the provision of global financial services; and
- (c) enforcement of the Superannuation Guarantee Charge.

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Committee met at 8.32 a.m.

BAKER, Mr Bruce, Director, Puzzle Financial Advice

LANHAM, Mr Gary (Private capacity)

WHIMP, Mr Mervyn (Private capacity)

CHAIR—I call the committee to order. This is the fifth public hearing which the committee is holding for its main terms of reference. They are: the prudential supervision and consumer protection for superannuation backing and financial services; the opportunities and constraints for Australia to become a centre for the provision of global financial services; and the enforcement of a superannuation guarantee charge. The aim of today's hearing is to take further evidence on the issues associated with the term of reference dealing with the prudential supervision and consumer protection. All of the witnesses who appear before the committee are protected by parliamentary privilege with respect to the evidence that shall be given before the committee. This means that witnesses are protected from action arising from what is said and the Senate has power to protect any one from an action that would disadvantage them on account of evidence given before the committee. The committee does prefer to conduct its hearings in public; however, if there are matters which it is wished to be discussed with the committee in private the committee will consider such a request. I would like to welcome this morning Mr Gary Lanham, Mr Merv Whimp and Mr Bruce Baker. You have an opening statement. Would you like to speak to that statement?

Mr Baker—Thank you. A key role that a financial planner plays is to help clients and their families achieve greater financial security and certainty. This is what caused me to uncover the problem with binding superannuation nominations. Merv Whimp, a client of mine, sought assistance to help ensure certainty to his family on his death, and unfortunately, as my submission shows, existing legislation has not made this as easy as it should be. The original intent of binding superannuation death benefit nominations is right, the implementation seems to be poor.

CHAIR—What are the aspects that make it poor that you are worried about?

Mr Baker—Let me go back to the original submission. Consider the scenario where you have a 70-year-old member of a superannuation fund who makes a binding death benefit nomination. If, in the following year, he becomes mentally incompetent—which is frequently a problem for the elderly, of course—in a further two years that binding death benefit nomination will lapse and later the superannuation member might die and then there is a range of situations in which the member's wishes may not be carried out. We feel that if someone's will survives their mental incapacity, then so should their binding death benefit nomination.

CHAIR—Mr Lanham, what is the solution from a legal point of view?

Mr Lanham—The solution is either to take out the sunset clause on the binding death benefit nomination or to enable that nomination to be altered, revoked or confirmed by a person who

has authority during the period of mental incapacity. That means extending the power of change to an enduring attorney.

CHAIR—Are there any differences, legally, between a power of attorney and a binding death benefit?

Mr Lanham—Oh, yes. A binding death benefit nomination is something that only exists in the superannuation realm; an enduring power of attorney is a document of wide application to all commercial and business transactions.

CHAIR—Is there likely to be a conflict if a person gives somebody power of attorney and at the same time has a binding death benefit?

Mr Lanham—Yes, there can be a conflict, but the constituent legislation which creates the notion of enduring powers of attorney deals with that in that it requires attorneys not to enter into conflict situations. One example that might be present in the senator's mind is that the same person who is appointed the enduring attorney could well be a person who has an expectation of being mentioned in the superannuation nomination. If a person was making an enduring power of attorney and knew that that situation was in contemplation, then it would be wise for that person to mention it in the enduring power of attorney so that everybody who read the document could be aware that the maker contemplated that and excused it.

CHAIR—Good point, thank you.

Mr Baker—For the same reason that a person holding an enduring power of attorney could not change or create a new will for a person, I would expect a person holding an enduring power of attorney should not be able to change someone's binding superannuation death benefit nomination, because we are talking about a similar type of instrument, something that relates to distribution of assets on death. If it were felt logical that someone holding an enduring power of attorney should be able to change someone's binding superannuation death benefit nomination, then that same person should be able to change the will. So we really have a major change of philosophy of law if people feel that someone holding an enduring power of attorney should be able to change a binding death benefit nomination.

CHAIR—Mr Lanham has covered that.

Mr Lanham—To take out the use-by or sunset clause would be the alternative that I think Mr Baker would prefer. He would prefer not to have it in the hands of another decision maker, such as the enduring attorney.

CHAIR—Why do you think they put the time limit on it? Is it being paternalistic?

Mr Baker—Yes.

CHAIR—Apart from that?

Mr Lanham—I think it was an endeavour to make sure that they were kept up to date.

CHAIR—It puts a big responsibility on trustees. This is not particularly popular with trustees.

Mr Lanham—The trustees will probably respond by giving annual reminders, rather than wait for the three years. If you give a reminder after the first year, the recipient of the notice has two years in which they might overlook the notice before they respond and say, ‘Oh, I’ve got to do something.’ That is probably what the trustees will do. It is going to add to the compliance costs, I guess.

Senator SHERRY—Thank you for your submission and for drawing our attention to this particular issue. I thought I had heard of every problem in superannuation until I read your submission, so thanks for that. I think your suggestions are important and we should take them up.

Mr Baker, I go to your letter of 14 June that I got yesterday. You made some comments on choice of funds. That chart you prepared on the last 20 years is as good as it gets. Thank you for that; it is fascinating to look at. You make some comments about consumer knowledge. When we talk about choice, we are talking about two concepts: choice of investment and choice of membership of a particular fund. Often the two concepts are muddled together. I have a question in respect of choice of investment. I am sceptical as to whether a significant number of the eight million people in Australia who are in superannuation would be able to make what I would refer to as an informed choice no matter how much education you embark on. What sort of model do you see in terms of investment choice? Do you believe everyone should be required to exercise investment choice or should it be an option within a fund that a member may exercise if they wish to exercise it?

Mr Baker—The simple answer is it should be an option, not a compulsory requirement to make a choice. I do not think there is any question about that. I think you are right in that, firstly, the vast bulk of people are not in a good position to make good choices with regard to investment selection. In addition, it is also very clear that, until a member of a super fund has sufficient funds in superannuation, they are simply not interested in the problem, and therefore not motivated to consider learning what they need to learn to make wise decisions. It is only once people have accumulated significant funds that they suddenly become interested because they can see that it has a significant bearing on their future financial security. Those people should have the right to choose their own fund and their own investment selection.

Senator SHERRY—Let us assume it is optional, and my understanding is a lot of funds are now offering this as an option. They are offering menus of choices for investment. Would you agree that, where a person does not get actively involved in investment choice, the obligation then falls back on the trustees to have carried out the investment across the fund on behalf of those members?

Mr Baker—There is no alternative but for that to occur, as I can see. This is not an area I have given great thought to but who else is there who can make that decision? There is no obvious person.

Senator SHERRY—I am sceptical that you can educate all eight million Australians.

Mr Baker—I agree.

Senator SHERRY—For example, 15 per cent of the population is functionally illiterate. I suspect that a lot more people, regardless of the size of the moneys in their account, would find it difficult. It might have got lost in the translation, but do you agree with that?

Mr Baker—I agree entirely with where you are coming from. In fact, I find that, when a new client comes on board, it takes about two or three years before they have got the level of knowledge that I would like them to have to make the sorts of decisions I want them to be making. Clearly, the vast bulk of the community is not prepared to put that investment of time in.

Senator SHERRY—Why do you think that is? Why aren't people prepared to put that sort of time in?

Mr Baker—There is a range of different reasons. Some people are simply not interested in financial matters, even if they have a lot of assets themselves. Some people want these sorts of decisions made for them. It is a worry for someone like me to take on a client who wants financial planning done for them. This imposes enormous risks on an adviser. There is one group of people like that. There is also a group of people who have assets who want to be educated. Those people are the right type of people for people like me. Clearly, when people do not have a lot of assets, there is no reason why they should spend a lot of time trying to make a small amount of assets work very well for them.

Senator SHERRY—You would only see the tip of the iceberg.

Mr Baker—Sure.

Senator SHERRY—The people who would come to you would be those who are more likely to be interested in these types of issues.

Mr Baker—Of course.

Senator SHERRY—In terms of the costs involved, and I am not having a go at you and what you would charge, what are the sorts of charges and costs associated with the provision of advice in this area? Can you just give me an indication or a range of what is typical?

Mr Baker—There is no such thing as typical. If you ask 10 financial planners what they do, you will get 10 different answers. The sort of thing I do is provide long-term financial planning advice aimed at helping a client and his family achieve long-term financial security. Then you talk about quite a few thousand dollars of up-front charges because the most effort is at first. Then there are still a couple of thousand dollars a year typically after that.

Senator SHERRY—A couple of thousand dollars a year would be a good indication of what the costs are.

Mr Baker—That would be for a medium sized client.

Senator SHERRY—What do you define as a medium sized client?

Mr Baker—Someone with investment assets of half a million dollars.

Senator SHERRY—So realistically the average amount in a superannuation account at the moment is only about \$24,000 or \$25,000.

Mr Baker—That is a different league.

Senator SHERRY—That is average. For the average person to be going off to seek advice from people like yourself is not a realistic option.

Mr Baker—The thing you are putting your finger on here is quite a crucial issue. It is that the people who really need advice the most cannot afford it. That is for two reasons. One is that the time someone like me would have to spend with them would be a cost they would not be prepared to afford as part of it. Part of the reason for that is my legal obligations to that client. This is actually an issue that is discussed amongst my profession a fair bit. The increasing hurdles which are being built up makes that advice increasingly inaccessible to the people who need it. That means that people with only a small amount of assets are increasingly subject to the sharks.

Senator SHERRY—You mention hurdles. As legislators we have a considerable obligation on us, given that superannuation is now compulsory for employees and is for retirement.

Mr Baker—I agree.

Senator SHERRY—We have to be very responsible in the legislative and regulatory framework. You will never get rid of all abuse, but we must at least minimise the potential of abuse, given the very special nature of superannuation.

Mr Baker—We have to keep in mind that superannuation is special in one sense in that it is under one special part of law. We must be very careful not to lose sight of the fact that this is part of the person's investment assets and both super and non-super together will help them to achieve their financial security in their retirement. We have to be very careful not to create too much of a different set of rules under super from what we see from the non-super regulations as well. If we lose sight of that then we go back to the old system. You might remember we had the ISC regulated and ASC regulated investments. We are finally, after Wallis and hopefully after CLERP 6, getting back to one regulator with one set of regulations. Those things will help people like me to keep costs at a lower level because they will help make the compliance simpler. If we then suddenly revert into two sets of regulations again, we are going to create more problems.

Senator SHERRY—I appreciate that. If I were in your shoes I could understand it. Just perhaps from our point of view, there is not unanimity on all of these issues obviously, but there are the difficulties of a major scandal such as have occurred in some other countries involving mis-selling or wrong advice or poor advice or deliberate fraud. The dangers in a retirement income system of political backlash are enormous. You may be aware of problems in the UK.

From the point of view of legislators, whilst philosophically we might disagree on some of the details, everyone at this table is fairly concerned about that issue.

Mr Baker—I think it is a serious concern, and I think the challenge before you as a committee and the other legislators—and this is not something I have given enormous thought to—is to somehow try to create an environment where there is adequate and appropriate level of advice to this most vulnerable tier in the community: the people who generally cannot access people like me. I think it is a very serious challenge. There is no good available solution out there now. Some creative thought needs to be given to how to make available affordable, competent, ethical advice so that those people are not subject to sharks.

Senator SHERRY—Thank you for your submission and your interest, and thank you for some of the details you have just given us.

Senator ALLISON—Could I just pursue the question of binding death benefits. In your experience, Mr Baker, are there big differences between the way people allocate their benefits and superannuation and the way they allocate the rest of their assets?

Mr Baker—It is all part of the whole. There are different problems in how they have to deal with the distribution of it, because we are dealing with different bodies of law. As you would be aware, only part of your assets are distributed via your estate, and there is a whole range of other things which are distributed by different means, whether they be joint assets, life insurance investments, superannuation or assets in trusts. So it just part of ensuring that the result the client is looking for is achieved. It may be that the assets from super might go to one person and the assets via the estate could go to another person, for some reason.

Senator ALLISON—The CPA told us yesterday that few people were taking up the binding death benefits option because of the complexity and because of the need to review after three years. Is that your experience too, or do your clients do it in spite of the complexity?

Mr Baker—The issue is that there are very few funds which offer that option. I am sure there are many members who would like it to be available, but there are very few super funds which will offer it to you, and a lot of those super funds have held back from doing it because of the onerous nature of the legislation.

Senator ALLISON—Mr Whimp, would you like to tell the committee about your own experience in terms of binding death benefits?

Mr Whimp—It is something I have not got a complete knowledge of, I have to admit that. But in the few inquiries I have made of Bruce, it is obvious that there are some problems, for me at least. I have a second marriage, a happy marriage. Most of my superannuation was contributed over a period of about 40 years during my first marriage. I lost my wife about 10 years ago, and four years after that I remarried. I now have stepchildren as well as my own children. The question in my mind concerns one point about binding death benefit nomination. At present, the trustee of the fund has to ensure every three years whether their client wants to change that.

Within three years, I have had the experience of my stepbrother contracting Alzheimer's, and it seems to me that if he had made a binding death nomination and contracted Alzheimer's within that three years, there is no reason why it should be changed at all. It is binding. He had full mental faculties and he made his wishes within that nomination. There does not seem to me to be any reason why that should be changed. It seems to me that a better procedure on the part of the trustees of the funds would be for the person to nominate a change, if they wish, when they are fully mentally competent. This other procedure does not seem to be correct to me.

The other thing is the enduring power of attorney over the binding death benefit nomination. To bring up a pseudo case or a possible case, if my second wife and I are driving and we are both killed in an accident, or we are both rendered mentally incompetent in an accident, she may have given a power of attorney to one of her children. I may have given it to mine or I may not have, but that raises the issue for me as to whether my wishes within my binding death benefit nomination can be changed by my stepchildren. I have a very happy marriage and I get on with my stepchildren, but things can happen. So that is the question I have: should I make one or shouldn't I? I do not think it should be so complex to have to make that decision. Something should be clear to people like myself, who are probably not thinking this far down the track. I am into my seventies now and I do not know how much time I have left. We are both ageing. We could easily have an accident in the car together. Briefly, that is what I am thinking about.

Senator ALLISON—Thank you. Mr Baker, I was interested in one aspect of your submission which talks about the mining industry. You say that we need to review the role of the mining industry in the Australian economy to ensure that it plays a more valuable role in increasing the standard of living of Australians. You provide us with a number of useful charts that show that mining shares are not performing as well as the rest. What are the implications for superannuation? Does this mean that the diversification of shareholdings in superannuation funds should not now include mining interests? Is there a move away from them? What are the implications of your saying what you have said here for superannuation?

Mr Baker—I do not think it has a huge implication with regard to superannuation, because mining stocks represent only about 15 per cent of the market capitalisation of the Australian share market now. While mining shares might therefore be part of the portfolios, it is generally likely to be only a small part of the portfolios now. From a superannuation accumulation point of view it is not a major issue. It is more an issue about the other issues. It is more to do with broader issues for Australia.

Senator ALLISON—Issues of the economy. As one witness said—and it may not have been to this committee—Australia has a Third World export profile, and a First World standard of living. I guess that is part of that argument.

Mr Baker—Maybe it is Second World standard of living these days, because we are so far behind the Japanese and Americans. I was looking at some information the other day that said that our average standard of living, average per capita income, is now about two-thirds of the Americans, about half of the Japanese and about two-thirds of the Singaporeans and that quite a number of our northern Asian neighbours have got higher standards of living in per capita terms than we have.

Senator ALLISON—And they do not do as much mining. Is that what you are saying?

Mr Baker—On mining, from a strategic point of view, I think we need to do a little strategic thinking as a nation—my impression is that we are turning assets in the ground into cashflow but there is no profit. That would be a pretty dumb way to run a small business. Whereas if you look at it from a Boston business consulting perspective, where you can have a star business or a dog or a cash cow or something you are not sure of, you would have to say that the mining industry was a dog so you should be doing something about it. The only thing we are getting out of the mining industry in this country is maybe some taxes from a few employees and a few excises and royalties and those sorts of things that we are charging these companies. But I think we have to get smarter as a country to make this part of the economy provide a positive contribution to the future standard of living in this country. I think it is actually contributing to our sliding comparative standard of living rather than, say, contributing to it.

Senator LIGHTFOOT—Mr Baker, would you be kind enough to tell the committee the process that applies with respect to money coming in, in the form of superannuation, and what you do with it in a generic sense. I do not want to know what you do with it physically, but what do you do with it in an investment sense. Do you allocate that to someone else or do you just give advice to that? What happens? I am not quite sure what your organisation does.

Mr Baker—I think you are asking what our role is as a financial planner. A typical case would be like this: a client would come to me and often their objective boils down to achieving financial security for themselves and their families for the rest of their lives.

Senator LIGHTFOOT—When you say ‘a client’, you mean a superannuant would come to you and you would give him or her advice, or is this another organisation that would come to you?

Mr Baker—An individual. Superannuation is just part of the investment assets that they have to invest. Investing is just part of what goes to achieving financial security in your life. It is, if you like, part of a much bigger pie and cannot be seen in isolation. The investment decisions you are making in terms of investment selection within superannuation cannot be seen in isolation for other investment decisions they are making in other parts of their portfolio. It just happens that superannuation has a slightly different tax structure from the other ways that they are investing.

Senator LIGHTFOOT—So the superannuant agrees that you are the man he wants and he writes you out a cheque. Is that the way it goes?

Mr Baker—No, not at all. Are you assuming that he is delegating the job of investing to me?

Senator LIGHTFOOT—Yes.

Mr Baker—I would be loath to accept a client who wanted to do that. I believe it is very important that the client work together with me as a team and, at the end of the day, the client has to be comfortable with the sort of decisions we are making. He has to understand the decisions we are making and why. We need to be sure that the decisions are consistent with their

goals. So, first of all, I have to understand what their circumstances are. We have to work out where they want to go; look at the means of getting from here to there and work out how best to do that; and also look at the risks that may exist along the way and how we can minimise those risks.

Senator LIGHTFOOT—I guess they do not want to hear about the risks. They want to hear about the safety and security of their investment.

Mr Baker—If a client wants only safety and security, he should be investing in cash or a capital guaranteed investment. If a client is not prepared to consider risk, he probably should not deal with a financial planner. Either that, or I will have to do a lot of educating of that client before we go any further with him or her. But it is very important for me that clients understand about risk if they want me to give them the best possible solution to their requirements.

Senator LIGHTFOOT—Yes. So when they do that, what is the next step with that? I still have not worked out where you direct them and, if you direct them, how does that brush off on to you or your organisation?

Mr Baker—Firstly, let me make it clear that financial planning advice is not something you do to a person once. It is a long term partnership you have with a client. The advice process does not happen at one point. It is an evolutionary process and the most intensive part happens over about the first three years. During that three-year period, generally, I find that the knowledge level of the client rises quite dramatically and, therefore, probably in about three years' time, if legislation has not caused us to make changes, then we can probably get that person close to the sort of trajectory that that we want them to be on. Of course, we have to watch out for the changes in life; odd things that happen in markets, or odd things that happen in legislation, and other things that might come up.

It is quite a long process. It is something that, if it is going to work well, needs to have the client and the adviser working on the same side and the client is going to have to want to receive advice. If you have a sales situation where someone is selling a product, I do not think that is really consistent to a long term financial planning advisory relationship. That is why I work on a fee basis.

Senator LIGHTFOOT—So you say to your client you have reviewed his investment portfolio and you say, 'Look, you are light on major mining shares. Mt Isa Mines—for the sake of a name—are looking pretty good. They paid a dividend last year of 9 per cent. Their price earning ratio is excellent. I recommend that you put five per cent or 10 per cent of your investment into Mt Isa Mines shares.' Do you get down to that stage of doing it?

Mr Baker—No. The father of security analysis would say that that is a very flawed approach anyway. Benjamin and Graham would say that this is a probabilistic thing and adequate diversification is very important. That would include a wide diversification if you are looking at shares—both Australian and internationally—and having five or 10 per cent in one stock in Australia fails the diversification test.

Senator LIGHTFOOT—Okay. So apart from the percentage investment, would you do that? Would you guide someone into a share as open and as specific as a nominated mining company?

Mr Baker—No. In fact, generally I suggest my clients avoid the mining sector.

Senator LIGHTFOOT—Okay, but what about other commodities?

Senator HOGG—Western Australian is losing out!

Senator LIGHTFOOT—Western Australia is doing pretty good without Mr Baker recommending clients.

Mr Baker—The runs are not on the board for the mining industry, I am afraid.

Senator LIGHTFOOT—I am trying to build up a picture of where your particular company fits into the myriad of financial advisers. You take a much broader approach to that, do you? Would you invest in some other organisation such as BT or some Deutsche Bank run investment arm or something?

Mr Baker—As you are probably gathering because I have to get involved in superannuation and the estate planning side of things as well as the tax planning, investment planning and a whole host of different areas of expertise that a professional planner has to cover, we are generalist by trade.

Senator LIGHTFOOT—I have so far found that out this morning.

Mr Baker—This is something that varies quite dramatically from adviser to adviser, but I am a very strong believer in finding proven and competent fund managers who are pursuing at this point the philosophies which I am comfortable with, and delegating the individual investment selection to those managers.

CHAIR—Is that a reflection on the industry? You are saying you are having trouble?

Mr Baker—No, I did not say I was having trouble.

CHAIR—I am sorry, I must have misheard you.

Mr Baker—I seek to find investment fund managers who are proven and competent and who are pursuing philosophies which I am comfortable with at this time and delegating both the investment selection to them and also, because the management of shares in particular areas is a very dynamic thing, the ongoing day-to-day management of a portfolio which I believe can be done far more competently by a proven competent manager.

Senator LIGHTFOOT—So you do invest in shares, but in the industrial sector or the banking sector?

Mr Baker—Much more broadly, but generally I try to avoid mining.

Senator LIGHTFOOT—So you look at the stock market but you dismiss the mining sector and you concentrate on—it is becoming something of a puzzle to me, at the risk of a pun, Mr Baker. Where do you invest? Where do you direct your clients? What do you do? Is it right across the whole section of Australian investments, less the mining sector?

Mr Baker—Australian and international.

Senator LIGHTFOOT—If you do invest internationally, do you do that as your particular investment adviser to an international source of the investment? Do you go through third parties or fourth parties, or do you invest directly or advise your client to invest directly?

Mr Baker—Using the same philosophy I have already indicated about Australian shares, I believe it is important to find proven competent fund managers—and we are talking about Australian based fund managers—to invest offshore.

Senator LIGHTFOOT—Okay. When you are notified of the demise of a client who has cash invested through your organisation, what is the procedure then? Have you already had, under normal circumstances, a will that directs you where you should distribute those assets or do you have a power of attorney by necessity that allows that signatory to then take it over completely without you having to bother legally—I am not talking about the moral issue there—to find out whether that is being distributed in accordance with a will? Can you give the committee some idea of how that happens?

Mr Baker—Sure. Let us go through the issues. Firstly, when someone dies, the responsibility for investment decisions with regard to the assets which fall into their estate rests in the hands of the executor. The executor has to decide whether they wish to seek my advice, and that is the executor's decision. If they do not like me, then they do not need to seek my advice—that is purely up to them.

Then there is the issue of superannuation, for example, which often will not travel via the estate. What will happen if you have a fund manager running a super fund—and we will look at self-managed funds as well, if you wish—is that the fund manager typically will write to the nominated beneficiary, if there is one, and they will also seek a copy of the will, and probate and all that sort of thing, to help them make their decision.

Senator LIGHTFOOT—That is nothing to do with you, is it, the probate?

Mr Baker—I get involved in it in the sense that the family who I am advising typically want me to be part of it and make it all happen easier. Typically, for that family, I have been the interface to those various institutions. So, yes, I am typically called on for advice to help make it easy for that family going through that difficult time.

Senator LIGHTFOOT—Let me get down to the nitty-gritty. You pass on all that money in investment, but have you reduced it to cash or do you keep it, by necessity, in its present form of investment and pass over the shares, certificates, bonds, or what have you, in that form?

Mr Baker—Firstly, let me come back to a turn of phrase you are using which I am not comfortable with. Money does not travel through my organisation. I am an adviser and, yes, I will recommend that a client invest with a certain organisation or a certain investment. Money never passes through my organisation. I do not make the decisions for my clients; my clients make the decisions. It is a team effort and I help them come to their decisions by giving them information, but it is their decision.

CHAIR—Can we please keep the questions relevant to the terms of reference.

Senator HOGG—Yes, mine are following on from what Senator Lightfoot was asking about. How often are the binding death benefit nominees one and the same as those that might be in the will of any of your clients? Do you know that?

Mr Baker—I am trying to think how many have put it in place yet. The trouble is that very few funds have done it yet because of the legal complexity. In fact, one of the things that I discovered in exploring this issue is that there is a very wide level of ignorance in every sector about this legislation at this point in time. Fund managers in general have a problem with it and so the vast bulk of fund managers have not been prepared to implement these sorts of flexibilities in their trust deeds. There are only two fund managers I use who have implemented binding death benefit nominations.

Senator HOGG—My second question is: how many of your clients do you know have a will which nominates the distribution of their assets upon death?

Mr Baker—Absolutely all of them.

Senator HOGG—When you first are engaged by a client, is that one of the issues you pursue with them?

Mr Baker—Absolutely.

Senator HOGG—Seeing that you are dealing with those people who have assets and are aware of their assets and the distribution of their assets, do you find that they are more likely to have a will than those who are at the lower end of the asset area?

Mr Baker—They tell me that Holmes a'Court died without a will. I suspect that people who have assets are probably more likely to have a will. I have not seen data on it but I do believe a big proportion of the community do not have a will. Yes, there is a problem in this area.

Senator HOGG—Do you believe this binding death benefit nomination was put in place to try to overcome those areas where people do not have wills?

Mr Baker—No, it is a totally unrelated event. What happens on death to superannuation often is quite unrelated to what happens to the rest of their estate, so it is an unrelated question.

CHAIR—Is it the wish of the committee that the documents as tabled by the witness be accepted? There being no objection, it is so ordered.

Mr Baker—Could I make one point on those documents you are holding now?

CHAIR—Yes.

Mr Baker—What I have tried to emphasise in the extension to my submission that I faxed on Wednesday is that, as you can hear from what Mr Whimp said when he was trying to make his decisions in this area, the law is still very complex if a member of a super fund is trying to come to grips with the issues and decisions they have to make. If the Attorneys-General and the federal government adopt an approach along the style of philosophy that the Queensland government have with their new enduring powers of attorney, both in terms of descriptive documents and in terms of perhaps forms and processes that can be followed, I think this area of the law can be made much more accessible and understandable by the general public.

CHAIR—Thank you, gentlemen.

[9.15 a.m.]

BELL, Mrs Yvonne Aileen, Consultant to fund, Hairdressers Association Superannuation Fund

OSBORNE, Mr Jeffrey Douglas, Director (Trustee Company), Hairdressers Association Superannuation Fund

CHAIR—Welcome. Thank you for appearing. The purpose of the inquiry here in Queensland is to look at the number of cases where problems have arisen and to check the adequacy of the legislation and the discharge of responsibilities by the regulators and trustees, et cetera. We invite you to make a brief statement to the committee, after which we will ask you questions.

Mr Osborne—I have been involved now since March 1999. I am a qualified hairdresser and have been in the hairdressing industry for some 35 years. I believe that my involvement with the superannuation company is giving something back to the industry.

CHAIR—Would you like to speak briefly to the submission and outline the structure of the Hairdressers Superannuation Fund?

Mrs Bell—Yes, certainly. The Hairdressers Superannuation Fund now has a trustee company in place with four directors with equal representation applying. All those directors are current hairdressers. This structure was put in place at the insistence of the then ISC in 1994 after it began investigating the fund late in 1993 for irregularities of a different nature, and they found matters had progressed worse than they had hoped. Going from a position of wanting merely a different administrator appointed they progressed to appointing a whole new trustee and management structure for the fund.

CHAIR—Who was your previous administrator?

Mrs Bell—The original administrator was a private company two of the directors of which were also trustees of the fund.

CHAIR—The administrators and trustees were basically the same people?

Mrs Bell—They were.

CHAIR—That was one of the weaknesses you perceived?

Mrs Bell—Yes, that is correct. That is highlighted in the table I have presented, which identifies the shortcomings pre 1994-95 and the current changes in structure that have remedied those.

CHAIR—Can we incorporate the table you are talking about so that people reading the *Hansard* understand your presentation. Is it the wish of the committee that the document be incorporated in the transcript of evidence? There being no objection, it is so ordered.

The table read as follows—

Mrs Bell—I have here a brief that I would prefer to read from, seeing as the fund's solicitor said not to ad lib too much.

Senator SHERRY—We are pressed for time so I hope it is not too long.

Mrs Bell—No, it is not. Basically, no amount of legislation will ever prevent premeditated fraud. The superannuation industry is already heavily regulated and absolutely oozing with compliance requirements. The industry has been, and still is, subject to an enormous raft of legislative changes. Consumer confidence in the product as a retirement vehicle is under enormous pressure. This will only be restored if the regulators are seen to be competent, supportive and in control. The present image is one of incompetence and revenue raising. Trustees need to be allowed to perform their fiduciary roles within a workable framework of legislative requirements. Members do not need to be burdened with administrative and compliance costs that add no value to their savings.

This fund was asked to make a presentation in view of its chequered history. The table presented clearly shows how in the last four years the fund has completely turned itself around. It is now a very credible superannuation fund, not only in investment performance, which is highlighted with those statistics, but also the funds under management have gone from just over \$2 million to over \$11 million in the last four years.

The investment problems brought about in the 1993-94 year by the original trustees consisted of an investment made in November of \$300,000 in a venture in a private company and of another million dollars in June 1994 in another private company. Both companies had related parties and the apparent dominant trustee was a shareholder in one of the companies. The debenture was contracted to pay 17½ per cent interest and this was only paid until September 1994 when it defaulted. The fund size at that time was \$3.1 million; therefore 41.95 per cent of the total fund was invested in related private companies. The \$300,000 went to the first company under the debenture. It exactly matched the timing of that company's purchase in a shareholding in the second company, eventually placing the entire \$1.3 million in the same company.

The fund took a negative return of 38.4 per cent in 1994-95. As these two investments were written off, both companies were liquidated with no likelihood of distribution. These write-offs have since given rise to capital gains tax losses. The fund also had a direct property investment. In 1991 it purchased six units for \$1.04 million. One of these units was also occupied by one of the trustees. Rents were collected irregularly and no leases were in place. These units were sold in October 1999 for \$800,000, eventually giving rise to a further capital loss of \$208,000.

The management agreement with the company, as I have already mentioned, involved two of the trustees and then the same trustees sought to self-insure the members. The fund deducted fees from the members' accounts for life insurance and TPD cover. The insurance policy was originally taken out. However, eventually the funds were withheld from the insurer and kept within the fund. During 1994 the fund took out a new policy under the guidance of the new administrator with the life office and began remitting premiums collected to the insurer. During 1996, when the fund looked like surviving, the original insurer mounted an action against the trustees to recover several years' premiums. During 1998 the fund lost in court and was forced

to pay premiums plus interest and some cost to the insurer. The cost to the fund members above what had been set aside during the years of apparent self-insurance was an additional \$150,000.

CHAIR—What was the basis of the fund losing its money in the court action? What was the reason for the judgment?

Mrs Bell—The judgment was that the policy had not lapsed. Our argument was that there was a clause in the policy that said that if payment were not made within 30 days of the due date the policy lapsed. The original trustee took the view that the policy had lapsed and therefore there was no debt owing to the original insurer. The insurer maintained that that was not the case and he won. A QC's opinion was sought on the prospects of appealing a judgment in that matter and the opinion was that the appeal was unlikely to succeed.

CHAIR—So the fund members actually ended up paying for the wanton action of a trustee?

Mrs Bell—Yes. And they actually finished up paying just over a year's worth of premiums twice because the period for which the court ordered the premiums be remitted to the original company included some of the period when there was a new policy in place and that policy was being complied with.

CHAIR—Aside from that particular transaction, why didn't the members sue the trustees?

Mrs Bell—That is my next point—legal action against the original trustee.

Senator LIGHTFOOT—Could you say which court that was? Was it the District Court, the Federal Court or the Supreme Court?

Mrs Bell—It was in Brisbane here.

Senator HOGG—I would suspect it was the Supreme Court.

Mrs Bell—I think it was the Supreme Court.

Senator LIGHTFOOT—You might care to take that on notice.

Mrs Bell—Okay. The new trustee accepted legal opinion that to mount a case on behalf of the members against the old trustees for breach of trustee duties would not be recoverable, as the only trustee with any assets was one with a home jointly owned with her husband. Two trustees had recently divested themselves of all real and business assets and the remaining trustee was found to be of no substance and legal action would only further erode the members' funds. The poor investments were taken out under OSSA. The then ISC could take no action under that act. The situation under the SIS Act offers far more protection for the members.

CHAIR—Why couldn't SIS take action against the trustees?

Mrs Bell—Because they said there was not a legal framework for them under OSSA. All these things were done before 30 June 1994. They came down with the opinion that they could take no action under that act, other than what they did do with the fund under surveillance request: first of all a manager being placed in there and then eventually the trustee being replaced. They also asked the new trustee to put a voluntary freeze on withdrawals from the fund until a realistic valuation could be made of the funds asset. This freeze lasted from September 1994 until February 1995. During the intervening months, asset write-offs and write-downs were done to align stated members' balances with the market value of the fund. The ISC was concerned that, if members were paid out during that period, they would be paid out effectively from funny money.

Senator SHERRY—Can I have the names of the original trustees?

Mrs Bell—Yes, certainly. They are Brian Cox and Nancy Gower. I am sorry, the other two names escape me but I will take that on notice.

Senator SHERRY—Thank you. There seems to be a particular problem in Queensland with a number of funds. I am interested in exploring this process. Is this a fund that is based on an award or industrial agreement that requires contributions to be paid into the fund from the hairdressing industry?

Mrs Bell—This is a standard employer-sponsored fund that requires normal SG contributions to be paid in from employer members for their staff.

Senator SHERRY—But is that based on an industrial provision in an award?

Mrs Bell—Yes. In Queensland we have our own awards, of course, and it is the same as the standard rates, et cetera. The only difference with the award is that, under the award, they should be contributing monthly. Under SG provisions, you have this anomaly where they are only required to pay annually, so administrators are constantly—

Senator SHERRY—I understand that. That is another issue. Were the original trustees office holders of the hairdressers association at the time?

Mrs Bell—They are still the office holders, as far as I am aware, of the Hairdressers Federation of Queensland.

Senator SHERRY—So they were office holders of the—

Mrs Bell—The federation was actually the initial sponsor of the fund.

Senator SHERRY—Do you know if they were the ones who had the fund inserted in the particular award or industrial provision?

Mrs Bell—No. Metway Bank did that when they took over the administration of the fund.

Senator SHERRY—Which was when?

Mrs Bell—September 1994.

Senator SHERRY—And what about the employee representatives? The fund has to have a requirement for equal employer/employee representatives. Is that the case at the moment?

Mrs Bell—Yes.

Senator SHERRY—How are they selected?

Mrs Bell—When the ISC insisted on new trustees, a company, HAS Pty Ltd—Hairdressers Association Superannuation Pty Ltd—was set up, which has four directors. Those directors are elected from within the industry as equal representative directors.

Senator SHERRY—Are there employee representatives?

Mrs Bell—Yes, there are two employee and two employer representatives.

Senator SHERRY—When the fund was originally set up you mentioned that it was based in the hairdressing industry and that it became an industrial provision in 1994, I think you said.

Mrs Bell—It was inserted in the Queensland awards in 1994 as a suitable fund.

Senator SHERRY—How were they ensuring that the hairdresser employers were contributing money up to that date on behalf of their employees?

Mrs Bell—There was no check of that under the old administrator. Under the new administrator that was done by the normal accounting systems.

Senator SHERRY—But how were they getting hairdressers to pay money into the fund if there was no award provision?

Mrs Bell—Previously they would have had to pay into Sunsuper. Sunsuper was always there. That was the default fund until 1994 when this fund was entered as an additional fund for hairdressers.

Senator SHERRY—So they were in Sunsuper originally and then came into this particular fund?

Mrs Bell—They can still be in Sunsuper if they prefer. Of course, Queensland has its own rules on that anyway.

Senator SHERRY—I beg your pardon?

Mrs Bell—In Queensland, you are not forced to comply with those sorts of rules any more.

Senator SHERRY—What sorts of rules?

Mrs Bell—The employer can choose. It is not compulsory to be in Sunsuper or the hairdressers fund, or Stefan has his own fund. As it is now in Queensland, the employer can actually pick any fund.

Senator SHERRY—I understand in Queensland there was some legislation by the former National Party government which attempted to prohibit national industry funds from applying in this state and therefore there were a significant number of locally based funds that were formed and established in the late 1980s and early 1990s. Are you aware of that?

Mrs Bell—I am certainly aware of the results of that. As you say, Queensland seems to have a more chequered history than some of the other states.

Senator SHERRY—There is a proliferation in this state of locally based funds, some good, some apparently bad. Mr Osborne, I think Mrs Bell said the original trustees are still officials of the hairdressers association?

Mr Osborne—I believe so.

Mrs Bell—It is the Hairdressers Federation, not the association.

Senator SHERRY—Have they been questioned, disciplined or queried through the federation about their lack of performance?

Mr Osborne—Not to my knowledge, no.

Senator SHERRY—You might take that on notice. It just seems incredible to me that they have not been held to account for what is obviously a very sad and sorry story, particularly for the members of the fund.

Mrs Bell—It was. It is fine now and has been for some years.

Senator SHERRY—I am not being critical of you or Mr Osborne. I understand you have had to clean up the mess, but it is important to try to find out why this occurred so we can recommend policies that make sure it does not happen again in other areas.

Mrs Bell—These people will never be brought to task by that federation because they run the federation.

Senator SHERRY—What do you mean by that?

Mrs Bell—They effectively are the federation. It is a Queensland based organisation of which they are the most senior officials.

Senator SHERRY—I understand that, but they must be elected, surely, Mr Osborne.

Mr Osborne—Maybe I could bring some light onto the hairdressing industry. We are a very fractured industry. We have something 4,500 salons in Queensland in which employers employ probably four people. It is a very fractured industry, so they do not have any binding commitment to any one person or persons.

Senator SHERRY—I can appreciate that, but what you have is a number of officials of the hairdressers who were able, using their office, to effectively draw a significant number of employers and employees into a very dodgy superannuation fund.

Mr Osborne—Yes, that is the crux of it.

Senator SHERRY—I am puzzled as to why the association has not tried to hold them to some account.

Mr Osborne—I believe that anybody can form an association here in the hairdressing industry. We have IHS, for example. As I said, it is a very fractured industry.

Senator HOGG—How many associations are there?

Mr Osborne—I believe there are about three.

Senator HOGG—So you have this association, the hairdressers—

Mr Osborne—Not a superannuation association; this is the only one that I am aware of in Queensland.

Senator HOGG—I am talking about associations with employers. How many of those would exist?

Mr Osborne—I know of three and two of those are art based; they are not industry based. They are more on the artistic side of the hairdressing industry, whereas the federation is more on the business side, if you like, for which we have to pay a nominal fee each year.

Senator SHERRY—So there are no misunderstandings, I congratulate you on the job you have done in getting the thing back on its feet. It is just that it is important to me to understand how this happened and what the structures, rules and regulations were that let it happen.

Senator ALLISON—In 1994-95 why was the money not rolled into Sunsuper? Why was it decided to press on with this fund rather than just fold that money into the bigger one?

Mrs Bell—Because the four new directors that came into the company were very keen to keep this fund alive as a fund for the industry. Sunsuper is a general award fund and these people had a lot of pride within their industry. They wanted to go in there, fix it up, save it and show the industry that it could run its own fund. Therefore it became really quite a goal and a dream to get this thing back on its feet for the Queensland hairdressers.

Senator ALLISON—Was that an attitude developed by the four directors or did that have widespread support and, if so, how do you know it did?

Mrs Bell—I believe it did by the very fact that those directors did a lot of work within the industry to convince the employers—and some of the employers were larger group employers—not to take their staff out of the fund and to trust them. There was a lot of work done within the industry and by the new directors liaising with the employers to convince them. They said, ‘Talk to us. We will talk to you a lot over the next six months. We will let you know where we are, where we are going and what is being done.’ Of course the biggest disappointment to all within the industry was that no action was taken against the previous trustees.

Senator ALLISON—I see the funds under management have grown enormously since 1992. Does that mean that the fund now has a higher proportion of the industry in its membership than it had previously?

Mrs Bell—No. In fact its members are fewer now than they were back then simply because when the fund was put into the new administration most of the accounts were found to be fairly inactive. Several were, in fact, found to be negative. In other words, the administrators’ fees were coming out of those accounts which had no money in them so the existing members were effectively supporting that. After tidying up the database the support for the fund has built up. It has about 4,500 members now, which is possibly where it was back in its original heyday, but I do not believe that reflects loss of market share. I think you will find that hairdressing is, if anything, a slightly declining industry as far as employment numbers go.

Senator ALLISON—But as a percentage of the total you would not know whether the fund is now increasing?

Mrs Bell—No, we do not know that.

Mr Osborne—Our industry is a very transient industry. The lifespan in our industry is probably from the age of 15 to 30. The majority are women, and at 30 they are usually married with babies. They do not come back into the industry and, if they do, they come back on a part-time basis. Our concern has been that 15-year-old to 30-year-old group. That is where we are picking them up now and we are picking up a lot of new people.

Mrs Bell—A lot of the salons are owner operated and, as such, the owners cannot be members of this fund.

CHAIR—Did any financial planners put clients into your fund?

Mrs Bell—No, they are not permitted to. Only the employer can put the clients in.

Senator LIGHTFOOT—Mrs Bell, what did the insurance that the association took out cover? What was the insurance specifically for?

Mrs Bell—There was a range in scale up to \$35,000 age based for death and a similar payout for total or permanent disability.

Senator LIGHTFOOT—This was like another form of compensation?

Mrs Bell—That is right. If the member died then the estate, or whoever, would receive the proceeds of that policy as with a normal death policy.

Senator LIGHTFOOT—Was it workers compensation with respect to employees?

Mrs Bell—It was life cover.

Senator LIGHTFOOT—What about malpractice insurance?

Mrs Bell—The original trustees had no insurance whatsoever on themselves.

Senator LIGHTFOOT—Is there insurance now?

Mrs Bell—Absolutely.

Senator LIGHTFOOT—What is the pay-out on that? How much is it covered for?

Mrs Bell—The fiduciary insurance that the trustees now have is in excess of \$10 million per claim.

Senator LIGHTFOOT—That's interesting. The insurance premiums which the court deemed were payable, with interest, were not fiduciary, they were—

Mrs Bell—No, they were life insurance for the members.

Senator LIGHTFOOT—So you had two of those running at the one stage?

Mrs Bell—We did for several months.

Senator LIGHTFOOT—That is illegal, but the court did not find it that way?

Mrs Bell—We were of the opinion, on legal advice, that the original policy had lapsed. The current fund's legal adviser did agree with the original trustee's opinion that that policy had lapsed.

Senator LIGHTFOOT—But it had not, in fact. The court found that it had not.

Mrs Bell—The court found it had not.

Senator LIGHTFOOT—Did you take any action against the advice that you had received, or did the organisation?

Mrs Bell—No.

Senator LIGHTFOOT—Is the industry still regulated in Queensland?

Mr Osborne—I believe not, no.

Senator LIGHTFOOT—It is totally deregulated?

Mr Osborne—Yes.

Senator LIGHTFOOT—What about a 15-year-old who comes into the organisation? At what stage do they pay into the superannuation fund?

Mr Osborne—From day one.

Senator LIGHTFOOT—What happens then to someone who comes in, does not like the industry and then leaves? What happens to those particular funds? They are not big.

Mrs Bell—If they are compulsorily preserved, over the minimum, the member is notified and they may choose to either leave them in the fund or roll them into another fund.

Senator LIGHTFOOT—What happens with a lot of those people who cannot be traced? They may have left their workplace because they have shifted interstate.

Mrs Bell—Yes, there are always a certain amount of funds each year transferred over to the Australian Eligible Rollover Fund for lost—

Senator LIGHTFOOT—How long do they stay in the fund?

Mrs Bell—They stay in the hairdressers fund for up to 12 months. If the member still cannot be located they are transferred to the Australian Eligible Rollover Fund. They will stay there until they become officially lost members after age 65.

Senator LIGHTFOOT—Until?

Mrs Bell—Until they are declared lost members.

Senator LIGHTFOOT—And at what stage is that?

Mrs Bell—When they reach pension age.

Senator SHERRY—The Queensland government gets the money then.

Senator LIGHTFOOT—You have done a remarkable renaissance since the devastating years of 1993-94 and 1994-95, in particular. It would be too nice to expect that exponential growth, would it not, in subsequent years?

Mrs Bell—Yes. I believe the fund is now performing to industry standards.

Senator LIGHTFOOT—What do you call industry standards? Is there a cut-off point? Is it 10 per cent? Does that sound something like—

Mrs Bell—It is not an absolute figure every year; it is what industries achieve in that year in the general. This year that fund should achieve in excess of 10 per cent. I believe when we do see the industry tables that will be quite a competitive return.

Senator LIGHTFOOT—That is a compounded figure you are giving there, is it not?

Mrs Bell—It is compound for the year after all costs.

Senator LIGHTFOOT—What sort of hands-on control of the direction of the investment do you have, Mrs Bell or Mr Osborne? What are your respective roles?

Mr Osborne—We take advice from our consultant, plus also from our administrators. As you can see here, we have advisers from Zurich and ANZ, so it is fairly broad based advice we take.

Senator LIGHTFOOT—Mrs Bell, what is your hands-on role?

Mrs Bell—My hands-on role with the investment of the fund is just not on, it is not part of my brief.

Senator LIGHTFOOT—What about the minutes of that advice? Do you take minutes of that advice?

Mrs Bell—Yes, the administrator, who is now Suncorp-Metway, keeps full minutes of every meeting.

Senator LIGHTFOOT—Do you ensure that the advice that you are given is always in a written form of some kind, or do you accept advice over the telephone?

Mr Osborne—No.

Senator LIGHTFOOT—So you do not do that as a matter of course. Thank you for your answers.

CHAIR—Thank you very much for appearing before the committee today, it has been most helpful.

[9.45 a.m.]

READING, Mrs Carmel Margaret (Private capacity)

CHAIR—Welcome, Mrs Reading. Thank you for your submission and for being prepared to appear before the committee today. Can you tell us in what capacity you appear?

Mrs Reading—I am a member of the Law Employees Superannuation Fund.

CHAIR—Would you like to highlight some issues arising from your submission?

Mrs Reading—The issues raised in my letter that I sent to the fund?

CHAIR—Yes.

Mrs Reading—The issues of concern are the delay in the receipt of benefit statements and the annual report; the poor performance of the fund and the dismissive tone of the statement under item 1 on page 4 of the report—namely, that investment results for all fund managers were significantly less than the year before, and the lack of detail relating to the poor performance. With all due respect to the trustee, how other fund managers perform is irrelevant. The other point is the decision of the trustee not to reveal any information about the borrower of the defaulting loan other than to state that it is a commercial loan secured by mortgage and the release of specific information may prejudice the party concerned.

CHAIR—You said ‘late receipt of member statements’. How long after the end of the year did you receive your member statement?

Mrs Reading—We received that at the end of January.

CHAIR—So it was seven months after the end of the year.

Mrs Reading—Yes, seven months after the end of the financial year.

CHAIR—Did it contain all the information required under law?

Mrs Reading—Yes, as far as I am aware for the benefit statement itself.

CHAIR—You mentioned the low crediting rates. Have we got a record of the crediting rate of the fund for the record?

Mrs Reading—That is in the annual report of the fund.

CHAIR—We have not got that. The document I am referring to is the ‘Law Employees Superannuation Fund (LESF)’ of 30 June 1999.

Mrs Reading—On page 5.

CHAIR—So it is a company that has some reserving policy from time to time?

Mrs Reading—Yes.

CHAIR—Basically, you had a good year in 1998 and a disastrous year in 1999?

Mrs Reading—Yes.

CHAIR—I might ask the committee members if we could table this report for the purpose of the record. Thank you very much. You are unhappy about the communications with the administrator?

Mrs Reading—Yes, at the lack of detail in the communication—namely, the report.

CHAIR—Can you expand on that for the record?

Mrs Reading—With respect to the loan, we were given no information as to the borrower, the amount of the loan, or whether it was first mortgage. I asked who the borrower was. In excess of five per cent of the fund was lent on that one transaction. We are not told exactly how much, only in excess of five. I asked whether more than one loan to that borrower was included in that or whether there was just the one. I asked for the date on which the trustee evaluated the loan and determined it was in default and for how long prior to that was the loan actually in default? Was it a first registered bill of mortgage? Was there any other collateral security, such as a charge on company assets? Was it secured over vacant land? When was it made? If the borrower was a private company were personal guarantees obtained from the directors? Who introduced the borrower to the fund? Was there a mortgage broker? Did any director, past or present, or any previous secretary of the fund or any members of their families have any relationship with or interest in the borrower? What commercial procedures were observed before granting the loan? Was an independent valuation obtained and were any inquiries made into the credit history of the borrower? What was the ratio of debt to equity in the loan? Who approved it? Who was the receiver appointed? What was the state of the receivership as at the date of the annual report?

CHAIR—Was that activity referred to in the annual report? Did the auditors qualify the report? They do not seem to have qualified the report, do they?

Mrs Reading—I do not know whether they qualified it or not.

CHAIR—They do appear to have a spread of investments, but one of those investments is a direct loan which could have been as high as 15 per cent in 1998. That is obviously the problem area. Is it?

Mrs Reading—As far as we are aware, yes. As we have no information we cannot answer.

Senator ALLISON—Do you have a response to the letter of 9 May?

Mrs Reading—We have an acknowledgment.

Senator ALLISON—An acknowledgment, but not an answer to your questions?

Mrs Reading—No. The date of the acknowledgment was 6 June.

Senator ALLISON—Acknowledging the receipt of the letter.

Mrs Reading—There is a new fund administrator at the moment—a division of AMP. The letter thanks us for our letter and apologises for the delay in responding to our concerns. It then says:

With Australian administration services taking over the administration of the fund from 1 May 2000 and given the detail of your questions I need to liaise with the fund secretary in order to obtain the information required. As soon as I have sufficient information on the issues you have raised I will forward this to you.

Senator SHERRY—Mrs Reading, thank you for coming along. It is not easy coming before a Senate committee. Congratulations for the interest you have taken. How long have you been in the fund?

Mrs Reading—Since its inception.

Senator SHERRY—Which was when?

Mrs Reading—I think it was 1989. When the legislation was first introduced we were in a fund, but National Mutual was in charge of it, or was the administrator at that stage.

Senator SHERRY—Was this just a fund with your employer?

Mrs Reading—Yes.

Senator SHERRY—Was it encompassing a number of employers, do you know?

Mrs Reading—I do not know.

Senator SHERRY—What happened in 1989?

Mrs Reading—The fund that we were initially in was administered by National Mutual. Subsequent to that, at a date of which I am not sure, the Law Employees Superannuation Fund came into existence and we were put into that.

Senator SHERRY—You say ‘you’ were put into it—your colleagues at your workplace and other legal firms in Queensland, presumably?

Mrs Reading—Yes. I believe there are about 6,800 members at the present time.

Senator SHERRY—Yes, there is some detail of it here, so presumably it is Queensland wide.

Mrs Reading—It is Queensland based, yes, but I believe that not all law firms' employees are in it. I believe that some are still in Sunsuper.

Senator SHERRY—You do not know the legal basis on which your firm and the employees became members of the fund?

Mrs Reading—No.

Senator SHERRY—Was any of this explained at the time, in 1989?

Mrs Reading—I cannot really recall.

Senator SHERRY—Did you participate in the ballot for the member directors?

Mrs Reading—Yes.

Senator SHERRY—Do you know the current member directors?

Mrs Reading—Yes. Mercedes Barrie and Brendan Frankcombe.

CHAIR—On the doubtful debt expense, perhaps we might ask the next witnesses some of the technical details, because just reading the report, until you get to that, it looks all right in that there is no highlighting that there is a problem about the poor rate of return or what caused a poor rate of return. I think members are entitled to know that. Thank you so much for highlighting this. We appreciate that you are not in a position to answer technical questions. Your important role has been to draw it to our attention. Did you also draw it to the attention of the regulators?

Mrs Reading—No.

CHAIR—You have not?

Mrs Reading—No. We took the first step of approaching the fund.

CHAIR—Maybe we should be doing that ourselves because they have much more detailed resources than we have.

Senator SHERRY—I would like to ask a bit about the group that signed this letter. One of our considerations is the ability of employees and members of funds to identify problems. Clearly in the legal sector you would expect there to be a fairly high level of understanding of financial matters, compared with, say, the hairdressing association.

Mrs Reading—Not necessarily so.

Senator SHERRY—Not necessarily?

Mrs Reading—No.

Senator ALLISON—Can you tell us who amongst your number had the wit to look carefully at this document and to investigate further? Can you give a bit of the history about how this group of people came to do this?

Mrs Reading—When we first got our benefit statements, one of the members brought it to our attention and said, ‘Have you carefully examined this to see how low the return is?’ I must confess that a fair few of us said no, so we went back to it and had a look at it and then started asking some questions of our member director who was also an employee of our firm, Mr Brendan Frankcombe. At that point we were told to wait for the annual return, so we then waited until about 8 April for the annual return to turn up.

Senator ALLISON—Are you aware of whether or not the fund has an investment strategy? Was there at any stage any suggestion that members might be involved in oversighting or developing that strategy?

Mrs Reading—I am not aware of any and I am not aware of any suggestion that members participate in that.

Senator ALLISON—Do you think there should be a strategy which is an open document you can scrutinise if you wish?

Mrs Reading—Yes. One of my points is that there should be an annual meeting of members called where trustees can be called to account, answer questions et cetera, and also inform members of the investment strategies.

Senator ALLISON—Have you any other suggestions?

Mrs Reading—Yes, I have a few. In regard to that document, as it is, quite a few of us decided that a letter had to be written. So I sat down one weekend and went through page by page and just raised all the points and then took them into work and we all sat down with it and went through it.

CHAIR—Thank you very much for being such a diligent member. I think superannuation in Australia would certainly be a lot healthier if there were a lot more people like you who really drew attention to the deficiencies and inadequacies of trustees and regulators. We do appreciate your coming before us. I think we should receive that as a submission. You and your colleagues certainly deserve better answers, I think. Thank you very much.

[10.02 a.m.]

RINAUDO, Mr Ray, Director, Law Employees Superannuation Fund

SHORT, Mr Peter John, Chairman, Law Employees Superannuation Fund

CHAIR—Welcome to the committee. Would you like to make a presentation to us?

Mr Short—I have reduced some of the facts to two pages, which I have got 10 copies of. That might lead you somewhere, and then you can ask questions.

CHAIR—Is it the wish of the committee that the document be incorporated in the transcript of evidence? There being no objection, it is so ordered.

The document read as follows—

CHAIR—Would you like to speak to this document, Mr Short?

Mr Short—If you wish, I can give you a moment to read it. It is not long, but it answers some of the questions which you have just touched upon.

CHAIR—Would you like to speak to the paper, Mr Short?

Mr Short—There is nothing particularly that I wish to add to it, Senator.

CHAIR—So you have just come in at a relatively late stage?

Mr Short—I have been there a bit over a year and Mr Rinaudo has been there a bit less than a year.

CHAIR—Who is responsible for preparing the annual report?

Mr Short—Which one are you referring to?

CHAIR—The one dated 30 June 1999.

Mr Short—I would have been on the board then.

Mr Rinaudo—I was on it for about a month or two before that report.

CHAIR—There does not appear to be an adequate explanation as to the dramatic drop in earnings in the annual report. Why not?

Mr Short—I am not an economist, and I would not presume to comment on the economy. The fund is managed by Bankers Trust, Zurich and Macquarie. If there are any specific questions you would want to ask them about the economy or why their funds were not as good in that year as they were in other years, I could direct them to them.

CHAIR—But you would be aware, as chairman, of a doubtful debt expense of \$520,000—half a million dollars—surely.

Mr Short—Yes, I refer to that in the second page of this report.

Senator SHERRY—That is the private mortgages?

Mr Short—Yes. When I came onto the board I was told that the fund had previously made four private mortgage loans. I made it known immediately that I thought that was not appropriate for a fund of this size—not necessarily because they were risky but because if one of them fell over, it was a bigger percentage of the fund. As it turned out, three of them were good and one of them was to a child-care centre. Child-care centres in the last couple of years, as senators would know, have been subject to a change in their basic funding. This child-care centre fell into arrears, we appointed a receiver, and the receiver is in there trading.

It is too early to say what the loss will be, but in that report we made a provision for what we thought was the difference between the loan value and our best guess on advice of recovery. In the next year there will be another provision made. The plan is for the receiver to sell the child-care centre in about September or October of this year when he says he gets occupation rates up to an appropriate level. It is likely, from where we sit now, that there will be some loss on the loan, but not a significant loss in terms of the overall fund.

CHAIR—Don't you think it is misleading on page 26 where you have a report, which is in relation to 30 June 1999, in which you actually give a fairly rosy position by virtue of excluding results up to June 1999 and giving the generic investments up to 31 January 1998? Why do you have 1998? Obviously, that paints a far better picture than if you had taken the accounts as at 30 June 1999. Why aren't you consistent in terms of the preparation of information to shareholders or beneficiaries?

Mr Short—I cannot answer that; I was not involved in the drafting of it. At that stage, as the new chairman of the directors, the point you make certainly missed me. I do not think it is intended to be misleading, is it?

CHAIR—It is misleading, because you are giving people information at different points of time. If people are looking and assessing a fund, they assume the information should be as at a point of time. The people who prepared this document have given information as to likely returns—five-year rates, et cetera—to 31 January 1998. I ask you: why did you choose January 1998? I submit that it would appear, given the disastrous result for 30 June, that that may have influenced the decision. Or am I wrong?

Mr Short—I think you are wrong, Senator.

CHAIR—Why do directors nowadays provide this sort of information to shareholders, not on a consistent basis? There is some information as at January 1998, yet you prepare the accounts for June 1999 on the balance sheets.

Mr Short—No, all the information is there. I take your point that if you can have end-to-end years exactly the same, it is much more useful. There was no intention for it to be misleading. Hindsight is a marvellous thing. I do not think it necessarily is misleading.

CHAIR—I am just reading your report.

Mr Rinaudo—This is the first time we have heard it expressed that way. Certainly, as Mr Short said, we take your point on the issue, but to give you an answer immediately off the cuff is not possible. All we can say at this time is that there was never any intention for the material to be in any way misleading and, of course, the accounts are there to 30 June. Why it is expressed that way we cannot say immediately, but we are happy to take it on notice and report back to the committee.

CHAIR—Thank you.

Mr Short—They do conform to the accounting standards. I take your point that they are more useful if they are like on like on like, but they are in conformity with the accounting standards.

CHAIR—In terms of presenting the statistical information, did the auditor look at this document before its publication?

Mr Short—My word, yes.

CHAIR—And he approved the report prior to publication with this information, as at that date? You might like to refer to him.

Mr Short—Without trying to duck the question, when you look back a couple of years and isolate sentences and paragraphs, it is easy to say that perhaps I would not have done it that way had I been involved in the drafting of it. I will take your point and it will not be done that way in future. As a new director of the board at the time, I can assure you it was not done with any intention of obfuscation or to confuse.

CHAIR—You were a director at the time this report was issued?

Mr Short—Yes.

CHAIR—And you were chairman of the board, so you have a responsibility to—

Mr Short—I am not sure I was chairman at that time, but it was about then.

CHAIR—ensure the report is consistent and—

Mr Short—Not only in accordance with the law but meaningfully informative.

CHAIR—Thank you.

Senator SHERRY—Mr Short, who did you replace?

Mr Short—Mr Parker.

Senator SHERRY—And who did you replace, Mr Rinaudo?

Mr Rinaudo—I replaced Dr Tony Tarr.

Senator SHERRY—How long was Mr Parker a trustee?

Mr Short—I think it was since it was revamped in about 1992.

Senator SHERRY—He was one of the original trustees?

Mr Short—No, the fund was originally formed about 1989. It was managed by National Mutual. I do not know who the original trustees were.

Senator SHERRY—He came on board in 1992, and when did Dr Tarr become a trustee?

Mr Short—The same time—as did the two employee directors. In early 1992 there was a clean sweep.

Senator SHERRY—You say there was a clean sweep; it sounds as though there was a ballot, a bit of a contest, in the Queensland Law Society.

Mr Short—No, could I correct that. It is not the Queensland Law Society. When these employee funds came on the social agenda in the late 1980s, the Queensland Law Society sponsored this one.

Senator SHERRY—I understand that.

Mr Short—They have no financial or other interest in it.

Senator SHERRY—Who nominates you?

Mr Short—Under the trust deed, myself and Mr Rinaudo are nominated by the law society representing the employers.

Senator SHERRY—Yes, that is what I am getting at. So the law society nominates you. What is that group? The managing directors of the lawyers' employer organisation?

Mr Short—It is the professional body that represents lawyers— the solicitors' branch of the legal profession.

Senator SHERRY—Why weren't Mr Parker and Dr Tarr renominated by the society?

Mr Short—I have no idea, but they had been there for seven or eight years, and one would logically say there is a time for being on these sorts of institutions and seven or eight years might be just about it.

Senator SHERRY—Do you know, Mr Rinaudo?

Mr Rinaudo—I do not have any idea why they were replaced.

Mr Short—Dr Tarr had moved to the university then, so there was a change in his career.

CHAIR—Mr Parker was, through Just Consulting Pty Ltd, the fund's secretary, who managed the fund overall, including interaction, coordination, management and advice to the trustee. Was Mr Parker a trustee as well?

Mr Short—He was the trustee that I replaced, but he remained as secretary.

CHAIR—And he also happened to be the company secretary?

Mr Short—That is right. He remained as secretary, but I replaced him as a director of the trustee company.

Senator SHERRY—But it was during Mr Parker's time that they developed or invested in private mortgages?

Mr Short—That is right.

Senator SHERRY—Do you know if they sought any independent advice about investing in private mortgages?

Mr Short—I do not think they sought any economic advice. The point that I made when I became a director was that it was my view—the other directors did not necessarily share that view—that you should not put all your eggs in one basket or a big percentage of your eggs in one basket because if it falls over—

Senator SHERRY—I agree with you. I understand that. I am still a bit mystified about how you ended up as a director. What happened? Did someone come along to you, too, and say, 'In your case, Mr Short, Mr Parker is not going to renominate.' Was it a special appointment? You did not come on the board at the same time as Mr Rinaudo?

Mr Short—Someone from the Law Society rang me and said, 'If we nominated you as a director of the superannuation fund, would you accept?' I said, 'Tell me more about it.' They did and I said yes.

Senator SHERRY—Who was the someone who rang you?

Mr Short—I think it was the president at the time, Dr Geoff Mann.

Senator SHERRY—Did Mr Parker resign?

Mr Short—He just said that the Law Society, under the trust deed, had the right to nominate two directors. It was time to put some new people on.

CHAIR—Is he still the secretary?

Mr Short—Who are you referring to?

CHAIR—Mr Parker?

Mr Rinaudo—No.

Mr Short—One of the things I did when I got there was to lay out all the administrative arrangements. I suggested to the board, and they agreed, that the administration of the fund be put out for competitive tender. We did that and, as of May this year, the AMP have taken over as administrators. Mr Parker is no longer involved.

CHAIR—Including the role of fund secretary?

Mr Short—Yes.

CHAIR—I do not want to be critical of your new role in any way, but we want to learn where funds run into trouble, where there are deficiencies in the law and questions in terms of the regulator.

Senator SHERRY—Is the requirement for employees of legal firms to be members in some sort of industrial award, provision or agreement?

Mr Short—I am told that, when this fund was started in 1989, it was started in case occupational superannuation became compulsory or fashionable. The fund did not do very much between 1989 and 1992. It was there. In 1992, under the stewardship of Dr Tarr, it improved its act and it performed quite well. There is no compulsion for anyone to join it. In fact the members of the legal profession, generally speaking, are in the old Suncorp fund, which I think is bigger.

Senator SHERRY—I am sure not all of them are active but there are some 6,000-odd members looking at the—

Mr Short—A lot of them are inactive.

Senator SHERRY—But it just cannot be coincidence that people voluntarily ended up on the fund. If there is no formal prescription, what is the informal prescription?

Mr Short—People are joiners and, if you are employed in the Senate, you join the Senate fund, if there is one called that.

Senator SHERRY—Or if there is a legal prescription.

Mr Short—There is no legal prescription for this, but people, I suppose—

Senator SHERRY—If there is not a legal prescription, you must know why people join the fund. Are they told to by their employer or are they advised? What happens? There has got to be a process.

Mr Short—There is no marketing of the fund that I am aware of.

Senator SHERRY—Does Mr Rinaudo know what goes on?

Mr Rinaudo—I can only say why my staff are in the fund. It is because it is a fund that was set up by the Law Society for the industry. They have got to be put somewhere. It seemed as good a place as any. I have had staff in the fund since its inception. I have been a director for less than a year. It has got nothing to do with my own view about the running of the fund or anything. My own perception at the time was that I had to put them somewhere and this seemed to be an appropriate industry fund. That would generally be the same for most law practices across the state.

Senator SHERRY—There would be a Law Society policy that this is good to encourage?

Mr Rinaudo—I am sure the Law Society would encourage it. I do not know if it is as formal as a policy but, certainly, the Law Society has set it up for that purpose, for the benefit of staff of member practitioners. Certainly they would encourage member practitioners to put their staff into them.

Senator SHERRY—So, if you have a new staff member, you or someone with your authority says, ‘Look, we want you in this particular fund’?

Mr Rinaudo—Yes. I would ask them if they had any preference, but if there is no preference—and there normally is not because, at my level, staff are coming in at a quite young age and starting out—I arrange for them to be put into the fund.

Senator SHERRY—In terms of the way your company operates as an employer, do you see that as a convenient way for superannuation payments to be made? If you were paying moneys into 20 different funds—I do not know how many employees you have got—would you see that as being more difficult administratively?

Mr Rinaudo—Yes. I have got six staff, but it is much easier to send one cheque once a month.

Senator SHERRY—And they are all in this fund?

Mr Rinaudo—Yes.

Senator SHERRY—Thank you.

Senator ALLISON—I want to ask firstly about the letter from a number of members which was signed and sent to you on 9 May. When can we expect this letter to be answered in detail?

Mr Short—I said to the previous witness, just after she gave evidence, that I have never seen the letter. But I said I will make it my business to find it and answer it.

Senator ALLISON—Mr Rinaudo, have you seen the letter?

Mr Rinaudo—I have not seen the letter, no. I have not seen the letter and it has not been referred to me. The first I heard about the letter was in the lead-up to these hearings, in the last couple of days, and I understood then that there was a concern.

Senator ALLISON—How do you explain not having seen the letter?

Mr Short—I do not know. I was told it was sent to the wrong address or something—it is not the address of the fund—and then it eventually found its—

Senator ALLISON—Mrs Reading has a letter of confirmation of receipt, acknowledgment.

Mr Short—Yes, and it eventually found its way to the AMP. They have not referred it on to us yet.

Mr Rinaudo—The reply was dated 6 June, I understand.

Senator ALLISON—Yes, that is correct. It is now a week and a half later and still the AMP has not referred this to your attention?

Mr Rinaudo—No. We have not seen it.

Mr Short—Now that we know it is there, I will answer it. There are no secrets about it, and there is no information there that cannot be given readily and openly.

Senator ALLISON—Since this is central to our inquiries, perhaps we can move through that letter and ask you some of those questions. There is the question of the delay and why it took over six months.

CHAIR—Perhaps you might like to have a copy in front of you?

Mr Short—Senator, I will listen rather than try to do two things at once.

Senator ALLISON—Why does it take over six months and nine months respectively for the fund to distribute benefit statements and annual reports to members?

CHAIR—In terms of fairness to the witness, as you have not seen it, would you prefer to take the questions on notice?

Mr Short—If it is all right by you, Senator, I will answer as best I can, because there is no secret.

CHAIR—We would not want it to be an inquisition in any way at all.

Mr Short—Senator Allison, when I came onto the board the history of the fund was that it was originally administered by National Mutual. National Mutual sold the administration company, which I think was called Nexus, to Suncorp. A lot of the data apparently was not accurately transcribed. The fund has had a history of changing administrators and, every time they change, it is a bit like when the software goes down on your computer—it is no-one's fault; it just happens. The person transferring the data says, 'I transferred it properly.' The recipient says, 'This is missing and this is missing.' For example, in one of those funds the auditors were

anguishing over, I think, \$12,000. To a fund of this size, in the end we had to say, 'Look, \$12,000 is \$12,000. So long as there is not any systemic problem, if it is just timing differences, for goodness sake get the accounts out.' Some of the meetings with the auditors and with the administrators were terse.

Senator ALLISON—So that is the reason for the delay?

Mr Short—Yes. For our sins, having changed again from the existing company to AMP, I have a feeling in my bones that we are going to go through the whole process again.

Mr Rinaudo—At least this year.

Mr Short—Yes, at least this year. The benefits of changing administrators outweighed the anguish of getting it right.

CHAIR—Do the auditors audit the transfers? In and out?

Mr Short—Yes. I do not want to be disrespectful to KPMG, but dealing with KPMG and AMP is a bit—

Senator ALLISON—There are a number of other questions in that delay category which I will leave for you to answer. Perhaps the last one is: why did it take over 10 months for the members of the fund to receive information known to some solicitors who raised it at the Queensland Law Society annual general meeting in 1999? Were you aware that these issues were raised at that meeting?

Mr Short—No, I do not know if the writer of the letter is confusing this fund with the Law Society's internal staff fund or not. There are two funds.

Senator ALLISON—Perhaps you can have a look at the progression of questions.

Mr Short—Also, there were four private mortgage loans. Three of them turned out to be, with hindsight, terrific investments because they were a rack rate of interest and it was all repaid. The fourth one, as you alluded to earlier, is the one to a child-care centre and the borrower fell into arrears and we appointed a receiver. One of those first three loans was a matter of some public debate, not for prudential reasons but because the borrowers were notorious.

Senator ALLISON—Did Mr Parker have a relationship with that child-care centre?

Mr Short—Yes, he did.

Senator ALLISON—What was the nature of that relationship?

Mr Short—He was a financial adviser, as I understand it, to the borrower in another capacity. He is a financial adviser by occupation.

CHAIR—Wasn't that a conflict of interest?

Mr Short—Yes. I raised that and, in his defence, he pointed out that he had declared the nature of the interest at the meeting at which the loan was considered and the directors at the time had approved it nevertheless. The rules of the fund and the company require you to declare your interest and not vote on it, and the minutes record that he did conform with that.

Senator ALLISON—Did he have an interest in any of the other three loans?

Mr Short—I have not asked, Senator, because by the time I got there they had been repaid, and at high interest rates. There is a limit to how far you can go back into these things.

Senator ALLISON—A question which seems to me to be very reasonably asked is why all three investment options performed equally badly.

Mr Short—I cannot answer that economically, except to say that they are managed by, respectively, Bankers Trust, Zurich and Macquarie. I guess if you asked them, without being glib, they would probably say the Asian crisis, or interest rates are down, that sort of thing. When people produce charts of industry funds, this fund seems to be in the middle to top quarter. Not that it is a defence for performance, but they seem to be performing as well as the average.

Senator ALLISON—Even the last witnesses we had suggested there was an increase in the previous year's performance. I do not know that we have all noticed a downturn in that particular year.

Mr Short—It may be misleading to guess, but I will anyway. I think those three mortgage loans were at a very high rate of interest and they might have in that year pushed it up to an abnormally good performance. When you take risks you get rewards, but there is a point beyond which a superannuation fund should not go, in my view.

Senator ALLISON—Is there a problem with identifying the details of that direct loan?

Mr Short—Not at all as far as I am concerned. One would expect as a borrower that some of your financial affairs are kept confidential, but there is no reason, so far as I am concerned, to do so. I will tell the writer of the question who it was and everything about it.

Senator ALLISON—What sorts of details should be withheld from members if they ask?

Mr Short—If you were borrowing from the Commonwealth Bank and for some reason your loan fell into arrears, you would not like some of your personal affairs to find their way into the Commonwealth Bank's annual return. In terms of relativity, this is much more important than you dealing with the Commonwealth Bank. But I do not think in the annual return you would normally include as much detail as that.

Senator ALLISON—It was not so much in the annual return as, in the event of a particular investment failing so dramatically as this one, what are members entitled to know about it?

Mr Rinaudo—I think there is a matter of timing, too. We are looking at the annual return from the end of June 1999. At that time the receivers had not been appointed and there was a possibility for the debt to go bad. I think it would be inappropriate at that time for us to be speculating or making statements about what is likely to be a return which might have an effect in the marketplace—for instance, if we did have to sell at auction or if the borrower himself was trying to sell with a view to repaying the debt. These are some of the issues I think that at that time the fund was probably best advised to be coy about. They are commercial issues that needed to be considered in terms of protecting the fund at that time. Now it has probably gone a lot further than that. Receivers have been appointed and that knowledge may not have the same commercial expediency that it did at the time.

CHAIR—Just to put some figures into perspective, approximately over 40 per cent of your total expenses were incurred under the heading ‘doubtful debts expense’. In terms of your total income that represents just under six per cent.

Mr Short—Forty per cent of the expenses.

CHAIR—Under expenditure on doubtful debts.

Mr Short—That would include non-payments by—

CHAIR—Which would be a write-off as well.

Mr Short—members who have not paid. I can answer it in this way, Senator, the only doubtful debt is this child-care centre one. It is not a bad debt. It is a loan that will in large amount be recovered from the sale under the mortgage. We have made provision according to the best guess that we can of its book value and resale value. It is in the hundreds of thousands. I think \$140,000 was the provision we made. So \$140,000 does not sound like 40 per cent, does it?

CHAIR—I have got a doubtful debt expense of \$520,000.

Mr Rinaudo—Yes. That is the same debt. It was about \$500,000-odd.

CHAIR—And the previous year was \$119,000?

Mr Short—Rather than guess, could I come back to you in a week in writing on that?

CHAIR—Yes. That is why your results were down. The investment performance from the Zurich and these sort of people could have been quite good, but these sorts of costs, which included the doubtful debts expense as a result of the bad investment decisions, have cost the members dearly.

Mr Short—I remember it was cents for the one year, not dollars. Figures would not lie, Senator.

CHAIR—You will have to take it on notice.

Senator ALLISON—Could I just clarify the position of the property debt that was written off? That affected all three options: the equities investment option, the composite investment option and the incoming investment option. Is that correct?

Mr Short—I am just trying to get the year right, Senator. Member choice was introduced at the end of 1997. In that year it would have affected two of the three funds.

Senator ALLISON—Which two of the three would it have affected?

Mr Short—Not the Zurich, not the pure equities.

Senator ALLISON—It did not affect the equities investment option?

Mr Short—No.

Senator ALLISON—And yet that went from 22 per cent earnings rate to 3.73 per cent.

Mr Short—It was under the management of Zurich.

Senator ALLISON—Is that explained in the annual report?

Mr Short—Not in economic terms of why it happened. It is a worldwide fund.

Senator ALLISON—We did not see that sort of movement worldwide in too many funds.

Mr Short—All I can say it is a worldwide fund; it is invested in the management of Zurich.

Senator SHERRY—Take that on notice.

Mr Short—Yes.

CHAIR—It is certainly doing quite well this year, I can assure you.

Senator SHERRY—Have you got your money in it this year though?

CHAIR—Yes.

Senator LIGHTFOOT—Mr Short, since your appointment to the board on 23 December 1999—

Mr Short—It would have been 1998, Senator.

Senator LIGHTFOOT—What fundamental changes have you undertaken to ensure that the process of lending is much more prudent? Where was the weak link in the chain? Was it through the valuation and then, indeed, is it a matter of statutory obligation for you to obtain a valuation, and a proper valuation at that, not a market appraisal? Was it at the process of not

checking out the recipients of a loan so that you were assured that the personal guarantees that they gave were effective—in other words, they were not people of straw? Or was it because of economic factors outside the control of the directors when making that loan? The last one in that bracket of questions is: do you make it a practice of physically going and checking out collateral or other assets that borrowers put up as collateral?

Mr Short—Taking those one by one, at the very first board meeting I attended I asked questions about these issues and said, as I have said in the statement, that I would oppose any further private lending because I thought that, for a fund of this size, it was not wise to put such a percentage of assets in one basket with the best systems in the world just because mortgages do fall over for one reason or another. I said then that I would not myself vote in favour of it and would argue strenuously against it if it were raised in the future. I know Mr Rinaudo, since coming on the board, shares my view. There is no present board policy about it, but if anyone comes with a similar loan in the future, they will certainly have to get it past me and I will vote against it. I do not think a fund of this size should lend on private mortgage. The second question is to procedures. As to these particular four loans, I have not looked at the first three very carefully because they have been repaid. All four of them seem to have been done perfectly normally. Valuations—

Senator LIGHTFOOT—Are they proper valuations or are they market appraisals?

Mr Short—No, they are not kerbside valuations. They are Herron Todd or someone similar. They are formal valuations.

Senator LIGHTFOOT—For which normal fees were paid to the valuer?

Mr Short—Yes, to the valuer.

Senator LIGHTFOOT—The proper fees, whatever they are—half a per cent or one per cent?

Mr Short—I have not drilled down as deeply as that. I assume, because they are reputable valuers, that they would have had a normal arms-length deal. Of the four loans that were made, three of which I have not looked at carefully, they all appear to be normal prudential sorts of loans on first mortgage. Three of them in fact were repaid. With the fourth one, the securities have been enforced, so they are good. I have quite a long background as a banking lawyer. There is nothing in the fourth loan that stands out and says, ‘This is abnormal.’ It is perfectly normal as far as I can see.

Senator LIGHTFOOT—So why didn’t the collateral itself on which the money was borrowed stand up? If the valuation was so good and so proper, why wasn’t it a simple case of recovery then?

Mr Short—I can answer that in two parts. The game is not over yet. The receiver is in there and he is hopeful of selling it at a pretty good rate, so most of the money will come back. We have made a conservative provisioning, as we should as trustees.

Senator LIGHTFOOT—So where was the design flaw?

Mr Short—I think, with hindsight—and it is a marvellous thing to have—the loan was made to a child-care centre, which is a business as opposed to something that itself has a value. The child-care industry has taken a downturn because of an alteration in its funding. This child-care centre had an occupancy rate that dropped from 95 to 75, or some figure like that, which had an impact on its cashflow, which meant it could not maintain the interest payments.

Senator LIGHTFOOT—So it was not a land valuation; it was a business valuation?

Mr Short—Land and business. The property is a child-care centre with a swimming pool next to it at the Gold Coast. The receiver and the manager of the fund say it is a first-class centre and will sell easily when they get the occupation rates up to a certain rate. The advice we have is that we should wait until the occupation rates get up to a certain level because child-care centres sell on a return.

Senator LIGHTFOOT—Have you implemented any fundamental changes to the process of loans since December 1998?

Mr Short—So far as I am concerned, I have made it plain that I am opposed to it. Private loans for a fund this size—

Senator LIGHTFOOT—That is one of the changes that you have implemented.

Mr Short—Yes.

Senator LIGHTFOOT—Is that now an obligation under the board?

Mr Short—No, because, as I say in the statement, the situation has not come up again. When it comes up again, if it ever comes up again—I would be surprised if it ever does—if somebody brings one of these loans to the board for approval, I certainly will say no.

Senator LIGHTFOOT—What about interfund loans? Do you agree with interfund loans and do they occur? Does it happen with your particular funds?

Mr Short—There are certainly no interfund loans. Do you mean from one superannuation fund to another?

Senator LIGHTFOOT—Yes.

Mr Short—I would not imagine that would be lawful, because it is not an investment, is it?

Senator LIGHTFOOT—So it does not happen?

Mr Short—Certainly not; no. So far as I am concerned, the trustees' obligation is to invest the funds, which means two things. They have got to be secure and they have got to have a good return.

Senator LIGHTFOOT—Would you be surprised if it did happen?

Mr Short—Never say 'never' until you know the facts, I guess. As you say it now, I am surprised. But I expect there might be some situations where anything could happen. So long as it meets the criteria of being a sound, secure place to put the money and it produces a return, it might be possible.

Senator LIGHTFOOT—I have one last question. You took over the chairmanship from Professor Tarr? Is that right?

Mr Short—Yes. Professor Tarr was appointed dean of the law faculty.

Senator LIGHTFOOT—It is a pretty formidable organisation, given the legal background. Professor Tarr is professor of the law faculty at Queensland University and there are your eminent personages here this morning. To fall into some of these problems—what show have we got with other superannuation funds?

Mr Short—I am not quite sure what you are getting at Senator?

Senator HOGG—We are.

Mr Short—If you let us into the joke, we might be able to laugh with you.

Senator LIGHTFOOT—If you look at the CV of the directors, and particularly the chairman of the fund, it is a pretty formidable line-up. One would have thought that it would be impregnable.

Mr Short—Professor Tarr, you mean?

Senator LIGHTFOOT—Yes, and so on. I just make the comment. Was it an AGM in December 1998?

Mr Short—Under the trust deed, the Law Society has the right to nominate two of the four. The other two go for election, and there had not been an election, ever, so it was one of the other changes introduced. They did have an election and the two employee representatives were re-elected.

Senator LIGHTFOOT—What date was that election?

Mr Short—1999.

Senator SHERRY—It was July 1999, according to the document.

Mr Short—Yes, I think that is right. It was about 12 months ago.

Senator LIGHTFOOT—That is all I have. Thank you very much.

Mr Short—Thank you.

Senator ALLISON—Mr Short, you said earlier that you had no knowledge of the letter from Mrs Reading until today. The secretariat reminds me that you were in fact sent a summary of the content of that letter and that you were informed that a letter had been sent to you and had not been responded to.

Mr Rinaudo—It would have been nice, actually, because we did ask. We told them that it was going to be asked today, in the normal way of these sorts of inquiries.

Senator ALLISON—What were you sent?

Mr Short—I was sent a couple of press clippings, two green folders, and submissions 32 through 36 or something. I would not like to tell you what your procedures are, but it is not appropriate for you to give submissions to other people until they have been submitted to you, is it?

CHAIR—That is right, and they are published.

Senator ALLISON—The committee does make submissions publicly available.

Mr Short—I think there are some restrictions on your actually doing what you said you might have done.

Senator ALLISON—There are not, actually. Once the committee agrees that submissions can be made public, they are available to anyone who chooses to ask for them.

Mr Short—But to get to the bottom line, now that I have the letter, I give you an assurance that it will be answered within a week, and it will be answered fulsomely.

Senator HOGG—I wanted to pursue with Mr Rinaudo the issue of the options presented to employees to join funds. You mentioned that the majority or all of your employees join the Law Employees Superannuation Fund. What are the other options that are available to them, and do you know the other options that are made available by other solicitors and lawyers throughout the industry?

Mr Rinaudo—They could join any fund that was available to them. I am not exactly sure to what extent those funds are available as employees—

Senator HOGG—There is no trick in the question.

Mr Rinaudo—No, I am just trying to think it through.

Senator HOGG—I just want to know what the funds are. Let us say I am a new employee at your business. You say to me, ‘This is the fund, the LESF fund, and that is the one we all go into.’ Realistically, are there other options that they could choose? Do you know what those options are?

Mr Rinaudo—There probably are not too many other options, when you think about it.

Mr Short—There must be some. I cannot answer the specific question.

Senator HOGG—Could you take that on notice? I would be interested to know what range of funds is made available to people. I would imagine Sunsuper would be one fund and I would also expect CARE would be another. I would be interested in how many options are made available to people when they join. If you take that on notice and get back to me that would be good. The other question is specifically with respect to the trustees. How often do the trustees meet?

Mr Rinaudo—Historically we have met once a month, and more if necessary. In fact, last year when we were in the process of our tender, we were meeting every second week or even more than that, but as a general rule we meet once a month to consider fund business.

Senator HOGG—What assistance or training is given to the employee trustees to bring them up to speed, so to speak, to be able to participate in a reasonable way in those meetings?

Mr Short—In the case of this fund, they have been to seminars in the industry—about two or three of them, I think. Almost every year, one or other of them goes to a trustees seminar.

Senator HOGG—So there is some trustee training for these people?

Mr Short—Yes.

Senator HOGG—So they are aware in a deeper sense than the average person who is a member of the superannuation fund?

Mr Short—Yes.

Mr Rinaudo—The reason I was hesitant is that both of them have been there a lot longer than I have. I am not quite sure what they have done in the years previous to when I came onto the fund, but both of them seem to be up to speed and certainly do contribute to the discussions at meetings.

Senator HOGG—Given the specialised nature of superannuation, is there any training that you people as the employer trustees undertake?

Mr Short—There is nothing in terms of superannuation that is so unique. It might be a mistake to think that superannuation is absolutely unique. You are talking about investing, on one hand, and administering, on the other. You can administer a superannuation fund if you have administration skills—there is nothing unique about a superannuation type business as

opposed to other sorts of business. On the investment side, investing funds that are held in trust for other people is a fairly common occurrence. Therefore, it might be a mistake to think that superannuation is absolutely unique and there is special training for it. There are special problems which come from superannuation, but you can be a bit isolated.

Senator HOGG—The training of trustees is raised with us as a general issue right across the board. I do understand the angle that you are coming from. I was just trying to establish whether or not there was special training that you people underwent as well.

Mr Short—From my own experience, one of the problems I found when I first came onto this board was that everyone told me when I raised a question, ‘Oh, that is unique to superannuation,’ when in fact a lot of problems in life are not unique. Commonsense covers a lot of things.

Senator SHERRY—I have just had a chance to have a look at this report in more detail. I think you said that Mr Parker became a director in 1992. He then, according to this report, commenced providing secretarial and management services for which he was paid fees in July 1997. Do you know whether there was a tender?

Mr Short—No, there was not.

Senator SHERRY—No tender for that?

Mr Short—The history of the fund was that they were very unhappy with the way that the National Mutual had administered it. Then when the National Mutual sold them to Suncorp they—

Senator SHERRY—Yes, I read that. So there was not a tender when Mr Parker was appointed to—

Mr Short—No.

Mr Rinaudo—As far as we know.

Mr Short—As far as we know there was not. They took over. With hindsight, they seemed to do a pretty good job. They did a much better job than the previous administrators had done.

Senator SHERRY—We can deal with that another time perhaps. What I find frustrating, frankly, is the employee trustees are not here and they would have, I would hope, a greater knowledge because they go back further in time than you do. Don’t you think it would have been appropriate for a tender process for the secretarial and management services?

Mr Short—Yes.

Mr Rinaudo—That is why we embarked on one last year.

Senator SHERRY—What was Mr Parker paid?

Mr Short—The administration fee, as I understand it, was pegged at what the previous administrator was paid.

Senator SHERRY—What was that?

Mr Short—I cannot give it to you now. I could take it on notice. It was the same as the Suncorp people had charged previously. It is more than we are presently paying the AMP. The fund has achieved a significant reduction in expense because of its recent change.

Senator SHERRY—I am looking at your expenditure under the heading ‘Other general administration expenses’ on page 30, which I assume is the category from which the payments are made. For a fund with a revenue of \$9,023,000 in 1999, to have ‘Other general administration expenses’ of \$560,000 is very high compared to a lot of other funds I am aware of.

Mr Short—Yes. I will not bore you with the details, but when you have 6,000 members and a great number of them are inactive, those dollars keep clicking up.

Senator SHERRY—Yes, but it begs the question as to why you would have a fund like this in the first place.

Mr Short—That is one of the things we are going to do next year. We are going to say, ‘What should we do with the fund?’ How do you balance the theory that a big fund is better against the reality that people do like individuality? People like personality in their fund and, sometimes, smaller funds do perform better than big funds.

Senator SHERRY—I am bemused by that. It is not evident to me, certainly, that the members of the fund, whose interests we should be concerned about, are going whoopee and doing handstands about individuality and being in the fund.

Mr Short—For myself, I cannot understand it. The only things I am concerned about with my superannuation fund are security and return.

Senator SHERRY—And return—exactly.

Mr Short—Personally, I think we came a very sad third in May. But I am told, particularly by the employee directors, that they have feedback from the members that they do need and want individuality.

Mr Rinaudo—It is a matter which we have under consideration. In fact, if it had not been for other matters that have directed our attention over the last 12 months, we would have considered it already. But we will consider it as a board in the next 12 months.

CHAIR—In hindsight, what are the lessons you think you can share with us? You seem to have done a pretty good job of bringing it back to a viable fund again.

Mr Short—My mother is the only person I know who has hindsight. What we have done is absolutely correct: we have made the fund more transparent in terms of its administration and we have put it out to competitive tender, and that has resulted in a reduction in administrative expenses. That, partly, is because computerisation these days means that funds can be done more economically—it is not a stroke of brilliance; it is just evolution.

Mr Rinaudo—One of the things we tried to do, certainly during my time and with Mr Short in the chair, is make sure that we deal with the little things, as it were—as Mr Short said, making it transparent. In other words, not taking some sort of expansionist approach but rather focusing on the fund, what it should be doing, what its core business is and making sure that we do maximise the security and the return.

CHAIR—Do you have a complaints register?

Mr Rinaudo—Not as such.

Mr Short—There is a procedure for that, but I cannot say what it is.

CHAIR—Why? It is required. Do you monitor your phone calls and identify them?

Mr Short—The AMP now administers it, so they do.

CHAIR—At each board meeting, do you get lists of complaints? Do you get a dissection of how many phone calls have been received in relation to the fund and what sorts of issues they look at?

Mr Rinaudo—No.

CHAIR—You should. Perhaps that should be on your agenda for the future.

Mr Rinaudo—I have taken note of it.

CHAIR—Do you have risk management statements that you have to comply with as a trustee?

Mr Short—Yes.

CHAIR—At each board meeting?

Mr Short—Then at the board meetings there are exception reports of things that have gone wrong.

CHAIR—Do you go through your risk management statements at every board meeting?

Mr Short—No, not through the statements at every board meeting, but there are procedures that will throw up exceptions, which is a part of risk management.

CHAIR—You have a check list of items that, as trustees, you go through on a regular basis to make sure?

Mr Short—Yes, and there are regular headings in the board papers. For example, under ‘Impaired assets’, we look at any assets that have come under threat and that sort of thing.

Mr Rinaudo—We have a statutory compliance list as well to make sure that all statutory matters are dealt with in a timely manner.

CHAIR—Have you been looked at by APRA?

Mr Short—Yes. I do not know the history of it. I think they had a complaint from someone. They did investigate the fund and gave us a laundry list of things which they thought would be useful and we worked our way through it.

CHAIR—And each of those have now been satisfactorily signed off by APRA in terms of what has been required?

Mr Short—Yes.

Mr Rinaudo—To the best of our knowledge, they are happy.

CHAIR—Thank you very much for coming before the committee.

Proceedings suspended from 10.56 a.m. to 11.12 a.m.

[11.12 a.m.]

HEATON, Mr Geoffrey Graeme, Company Secretary and Resort Manager, Voyager Resort Ltd

CHAIR—I welcome Mr Heaton to this inquiry. We are looking at aspects of the EPAS superannuation fund and, because there is litigation in this area, I have to warn both my colleagues on the committee and also Mr Heaton to be very cautious not to impinge on any areas that might affect the outcome of that decision because the last thing the committee would want to do would be to abort that hearing.

Thank you very much, Mr Heaton, for raising the issues. You have certainly been instrumental in bringing this matter to a head. I think that is important not only for your involvement but also for the members of the EPAS superannuation fund, who have suffered such calamitous results in recent times.

Mr Heaton—The main reason I persisted in the matter was that in every area I looked for support in, whether it was a regulatory body such as APRA or the Australian Securities Commission or the trustees themselves, I was not getting any answers to the questions that I was asking. By pursuing the matter through yourself and through the newspapers, I was able to raise awareness of the problems that a superannuation fund can find itself with.

CHAIR—You mention APRA. Were they reluctant to respond to you?

Mr Heaton—I addressed immediate questions in early 1999 to a Mr Pat Hannon who was the state manager for APRA and who took quite some time to reply to me via another person in APRA. The answers that I was given at that time were not answers; they just referred me to someone else, saying that I should pursue my inquiries through the Australian Securities Commission rather than through APRA because they did not have the legs or the power to pursue the matters.

I also approached the Superannuation Complaints Tribunal at that time to be told that they had no legislative powers due to a court decision handed down some time before that. I was really left with nowhere to turn except to the representative bodies such as yourself and to the newspapers. That was the only method of keeping members of the fund advised as to what was happening. A lot of them had just given up on it. They thought they had lost their money and they were not going to pursue it any further.

CHAIR—You have outlined that you were not satisfied with the response from APRA. What about ASIC?

Mr Heaton—The Australian Securities Commission were very helpful in acknowledging information I handed to them, but they would not give any feedback. I guess that is the nature of the beast. When they are investigating a matter, you have a feeling that probably it has been put into a basket and left aside. Unbeknown to me, they were pursuing the matter and all the

information that was handed to them was taken into account in their deliberations. So I must say that in the end, after some six or eight months, I felt justified in pursuing the commission to the point we did.

CHAIR—How long have you been involved with this particular fund, if you have been involved, or have you been putting employees into the fund?

Mr Heaton—I took over the company secretary's job and the resort manager's job at Voyager Resort on 1 July 1993. The resort handed me papers to have three per cent of my wages paid in as an employer contribution to the fund. I did that on their advice. I believe that Voyager Resort became involved with EPAS through the hotel and motel association. To the best of my knowledge that happened in about 1989. The main contributions before that date were employees putting a portion aside every week or month.

CHAIR—Do you know very much about the composition of this particular fund?

Mr Heaton—The EPAS fund, I was told, was an industry fund representing people in the hospitality trade which had an obvious tie-up with the hotel and motel association. I believe that they were the only fund considered by the directors of Voyager in 1989.

CHAIR—Did you and your members get regular statements in a timely manner from the fund?

Mr Heaton—When you say a timely manner, I believe that the regulatory body set 31 December as the cut-off date for statements to be handed out each year, which is some six months after the end of your trading period. In 1997 and again in 1998 the statements were issued very late, in the second half of December. In 1997 we started phoning, probably in the middle of September, because two of the members were looking at retirement in that particular year. They are still looking at retirement, they are still working with the resort and they are still awaiting some form of settlement of the EPAS problem.

CHAIR—So there was delay in paying a retirement benefit, was there, and that was what made you concerned?

Mr Heaton—It was only a four per cent return on 30 June 1997, somewhat lower than other funds were handing out at the time. My wife is involved in a super fund run for the club industry called Club Plus. Somewhere around 15 to 17 per cent was being attained by their fund, and they were not on the extreme top of the market, so 4.3 per cent was considered low. I still believe the opinion of the people that were intending to retire was that they would wait another year and build up their nest egg a little further, and so we persisted. We were also told at that time that the federal government were looking at choice of fund legislation and that that could be a factor in staying with EPAS, even though the returns were not great.

Then 12 months later, on 29 December, we got a negative credit rating and it was 43 per cent of the total amount of the fund that had just gone. That wasn't the end of the bad news because when it was reassessed at the end of 30 June 1999, it was taking another 13.75 per cent, so, in

actual fact, the negative credit rating which related to 1998 was in fact 56.75 per cent, and that is where we stand at the present time.

CHAIR—What is the latest accrediting of the fund—the latest report? Have you got an annual report that you can give us?

Mr Heaton—No. The last information I got was in May. The last actual newsletter from the new trustee, Trust Company of Australia, was in May 1999. We received an annual statement which, as I said, reflected at the start of it an opening balance adjusted back by a further 13 per cent with a nil credit rating, and all the additional administration fees, federal tax and so on deducted.

CHAIR—So is it true to say that, in the last three years, going backwards, you have had a nil credit rating, you have had a minus 13, approximately, and you have had a minus 43?

Mr Heaton—And before that it was 4.3 per cent, I believe, so it has been quite a long time that the fund has been on a downward spiral. In fact, APRA papers that I have with me refer to 1995 when they were starting to look at the fund. The warning bells were there at that time, but the fund as an investment tool for retirees continued to travel in the wrong direction.

CHAIR—Are you confident that the fund is on a steady course now?

Mr Heaton—I honestly could not tell you what the fund is doing. The last correspondence I had with a Mr Anthony Pagent, who I believe is in charge of the trust company, was in August 1999. Numerous phone calls were not getting anywhere, so I sent him a letter and I got a reply to that letter. I asked a number of questions. My main one was: where are we? I also asked: what is happening with the realisation of the assets? Can you tell me what the trading figures are for O'Hara's Resort in Tasmania? I got the same old answer that that was commercially privileged information. That is the same answer that the EPAS trustees were feeding me from the time we had a problem with working out why the fund was not performing. Honestly, when I hear that answer, it gets my bristles up straightaway. Saying it is commercially privileged information to a member of a fund in which you have a vested interest is not good enough. O'Hara's Resort is the major milking cow, if you like; it has been absorbing the liquidity of the fund for something like three or four years.

CHAIR—It has been sold, hasn't it

Mr Heaton—I do not know. I have been told that the management rights were cancelled by the trustee.

CHAIR—I think it is subject to some litigation.

Mr Heaton—We have not been informed as members of the fund. Like I said, the last reply that I got from the current trustee said that it is commercially privileged information and you are not welcome to any of it—which I find completely unacceptable.

CHAIR—Do you know who the current trustees are?

Mr Heaton—The Trust Company of Australia in Melbourne and the person who signed the letter is Anthony Pagent. I have the original letter.

CHAIR—Essentially, the membership comes from Queensland, does it?

Mr Heaton—I believe so, but people tend to migrate in this industry and I believe—

CHAIR—Have you got local trustees representing that board of the trust company that you are referring to?

Mr Heaton—I do not believe so.

CHAIR—They are not employee members?

Mr Heaton—I am not aware of them.

CHAIR—Is it an industry fund?

Mr Heaton—It is an industry fund.

CHAIR—There should be employee and employer members, I would have thought.

Mr Heaton—The fund is frozen. Every bit of information that I have got is that Anthony Pagent from the trust company is basically an administrator or is trying to realise the assets, which seemed to me like he is a liquidator and probably has full control.

CHAIR—Have they closed off one fund, or are they starting another, or what?

Mr Heaton—This is another problem that I have. When EPAS was frozen on 30 June 1998, the fund was taken over by the secretary of EPAS, Mr Jim Aiken. I could not for the life of me, being a businessperson, work out how someone could take over a business and still conduct it without any goodwill passing. If EPAS is frozen and they are going to close this part of the fund and Compass administration continue to run the same fund with the same database—

CHAIR—Where are the new moneys going, though?

Mr Heaton—The new moneys go to the Compass fund. I pulled out of it for two reasons. It seemed to me that basically the same operation was continuing under a different guise. Although the trustees had been replaced, the secretary of the existing fund was taking over, as a commercial interest, the new EPAS fund. A lot of confusion related to it. They said that the money that was taken into the new fund would be put into a cash management account. Cash management accounts probably earn two to three per cent.

CHAIR—Not much.

Mr Heaton—Even so, when you ask if you can withdraw your money, a nil credit rating was applied to those funds after the other fund was frozen. So it would not matter if you continued on eight or 10 months after, the money was invested but was probably being absorbed by administrative costs. There was still a nil credit rating when I pulled out of the fund. It was presumed to be like a successor fund but I believe that on due diligence that was carried out, the successors that were selected did not proceed.

Senator SHERRY—I want to go through the process in a little more detail with your knowledge of the creation of the fund and how it operated at your resort. I called the hotel association about EPAS. They made it very clear they had nothing to do with EPAS. They believed it was the motel association. I do not know whether you can throw any light on that. I know there are two different employer organisations, one the hotel association, the other the motel association. Do you have any response to that?

Mr Heaton—Here is an original letterhead from the Hotel and Motel Accommodation Association. I am quite happy to table that.

Senator SHERRY—Could we have a look at that?

Mr Heaton—It refers to the EPAS fund. I have other correspondence from the Hotel and Motel Accommodation Association. I attended an annual general meeting, which is referred to in that particular letter. I asked questions of the fund chairman at the time about the freezing of the fund.

Senator SHERRY—Just before you go on. Do you know if this organisation is the Queensland Hotel Association?

Mr Heaton—I think so. It has changed. We dropped out of it because of its reluctance to pursue these matters with EPAS.

Senator SHERRY—In the conversation I had with the Queensland Hotel Association they denied any involvement with EPAS.

Mr Heaton—I believe that would be a different organisation.

Senator SHERRY—Fine. The Queensland Hotel Association is a registered industrial organisation which, as an employer organisation, has an interest in a number of other superannuation funds. I do not want us to get confused with them. They would be a bit concerned if there was some confusion.

Mr Heaton—That is the body identified on that letterhead.

Senator SHERRY—They are not the same body as this organisation on the letter, the HMAA of Queensland. Was it July 1993 that the fund was first introduced at the resort you are working at?

Mr Heaton—No, that is the date I joined the resort as the manager.

Senator SHERRY—When was it introduced?

Mr Heaton—In 1989.

Senator SHERRY—How was that done? Who contacted the resort? Who came along and gave advice about EPAS?

Mr Heaton—My inquiries to the management at the time were that they were members of this hotel and motel association, they had attended seminars where this had been put forward as a good idea for employers—

Senator SHERRY—Do you know who put this forward as a good idea?

Mr Heaton—I have no correspondence to verify, only that there were advertisements in the journals of the hotel and motel association at that time and they were a sponsor, if you like, of some of the activities of the hotel and motel association in relation to seminars or conferences.

Senator SHERRY—Who was the sponsor—EPAS?

Mr Heaton—Yes.

Senator SHERRY—So there was some relationship—we do not know the precise detail—between the Hotel and Motel Accommodation Association and EPAS?

Mr Heaton—Yes.

Senator SHERRY—Okay. There is an industrial award provision in Queensland that covers your particular workplace, isn't there?

Mr Heaton—Yes.

Senator SHERRY—Do you know the name of that?

Mr Heaton—The hospitality award. I cannot tell you the exact name of the award, but it is an industrial award in the state of Queensland and it applies to us. There is also a federal award in this industry, but we are outside that.

Senator SHERRY—And this particular state award does have a number of funds options, if you like, for funds for employees within the industry that covers your resort?

Mr Heaton—I believe so.

Senator SHERRY—I just wanted to know what you knew about this because it is important legally in terms of the fund that your employees have ended up in. My understanding is that there are four or five options, one of which is EPAS.

Mr Heaton—The only one that was presented and that we ever had any contact with was EPAS.

Senator SHERRY—You are not aware of how EPAS was put into that particular award provision with respect to superannuation?

Mr Heaton—No.

Senator SHERRY—I assume this mob, the Hotel and Motel Accommodation Association, could throw some light on that at a later date. So someone on behalf of EPAS urged—do you think that is a correct description?—this as the fund to be in.

Mr Heaton—I think they may well have suggested to the manager or the directors of the time that they possibly should join.

Senator SHERRY—You say ‘possibly’ and ‘suggested’, but if there are no other options presented it is effectively a fait accompli.

Mr Heaton—The people that made those decisions at the time are no longer available to be asked questions.

Senator SHERRY—They are no longer associated with your company?

Mr Heaton—No.

Senator SHERRY—How was this presented to the employees?

Mr Heaton—The employees were invited to contribute in the first instance. Then in 1993 when the three per cent legislation, the SIS legislation, was introduced, there was a mandatory contribution by us—

Senator SHERRY—The SIS legislation was separate from the superannuation guarantee legislation, which I think you are referring to.

Mr Heaton—Yes, I am sorry. When the guarantee was introduced we continued to put the guarantee amount in and the contributions—

Senator SHERRY—On behalf of all employees?

Mr Heaton—On behalf of all the permanent—

Senator SHERRY—The eligible employees.

Mr Heaton—Yes, eligible employees. Some of them contributed \$25 or \$50 a month in addition, as their own salary sacrifice.

Senator SHERRY—So there were substantial contributions from the employees themselves, which is different from the three per cent which was an employer payment?

Mr Heaton—Correct, yes.

Senator SHERRY—EPAS was the only fund to which the employer contributions were being paid on behalf of employees at your operation?

Mr Heaton—Yes, solely.

Senator SHERRY—Why is that? Is that because that was the recommended fund?

Mr Heaton—Certainly, speaking from my own point of view, superannuation to me was a gilt edged investment. I never envisaged any problem with negative returns or even returns less than a bank account could attract. I found it absolutely astounding when we got to the stage of having to ring up for our annual statements—

Senator SHERRY—I understand that, but what has happened is that all the eligible employees' three per cent contributions were paid in, by decision of the management back in whenever it was, and presumably new employees coming to work who were eligible were having their money paid in as well?

Mr Heaton—There was no choice given. It was purely that a decision was made and we followed it through.

Senator SHERRY—From an administrative point of view, do you see it as good to have one fund to pay into? If you were paying into 30 different funds for 30 different employees, would you see that as a problem?

Mr Heaton—I have spoken to many operators in this industry. They are quite happy to draw whatever cheques they need to at the end of each month. It does obviously incur extra work but it is nothing—there are very few people I know that are not on computers these days—to extract four or five different fund deductions and draw four or five cheques each month.

Senator SHERRY—It might be a lot more than that. It might not be just four or five. As an employer, you would also have to check to make sure that the fund to which an employee wanted you to contribute conforms. You would have to check to make sure that they conform legally with the superannuation legislation. Are you prepared to do that and accept the consequences if you do not do that properly?

Mr Heaton—I think that is a bit of an onus on any business operator. We would prefer to think that we could suggest four or five major superannuation funds to our employees and they could select from those.

Senator SHERRY—But that is not choice. That is a very limited, restricted menu. We have got a theory of choice. Why shouldn't an individual come to you with an account with

Westpac—or in Club Plus, for example, which your wife is in? Why shouldn't they say, 'I want the money to go into that particular fund. That is where the money should go?'

Mr Heaton—And the due diligence would come back on the employer?

Senator SHERRY—Some would.

Mr Heaton—Some?

Senator SHERRY—Yes.

Mr Heaton—I think that is pretty onerous and probably needs a bit more thought to it than that because we are all pretty busy with what we are doing without adding an extra chore. If there were a body that perhaps approved a selection of 20 or 30 funds, if you like, I think that would be far more acceptable than individual managers or directors looking at the funds when they are proposed by the employee.

Senator SHERRY—Do you know who founded EPAS? I think you referred to it in your submission.

Mr Heaton—Terry James.

Senator SHERRY—Did you have any contact with Mr James at all?

Mr Heaton—No, never.

Senator SHERRY—And you cannot recall the names of the people who were urging that EPAS be the fund?

Mr Heaton—I was not there at the time when it was first introduced so I could not comment.

Senator SHERRY—None of them subsequently visited the resort?

Mr Heaton—We had very little contact in those early days at all, except for sending returns in and receiving statements each year and newsletters from time to time. That is the only communication that we actually had.

Senator SHERRY—Thank you.

Senator LIGHTFOOT—Mr Heaton, what has been the fundamental problem as you see it in straightforward transactions that should have returned an adequate percentage or an annual percentage of return to the stakeholders but failed to do so? Where do you see the problem? Is there one or more problems associated with that?

Mr Heaton—There is definitely more than one problem. I cannot identify—

Senator LIGHTFOOT—Can you tell the committee those problems?

Mr Heaton—Some of them are sub judice.

Senator LIGHTFOOT—Do not mention those, but you may be able to brush over them in a generic way.

Mr Heaton—In generic form? I find that the investment ability of trustees is lacking; and on top of investment, do you classify lending as investment? I find that there are certain aspects of investment that you could be good at but if you are assessing lending money to people on a mortgage or whatever, they are totally two separate forms of business. I find it hard to fathom out why some good investment decisions were lacking on the one hand and why some good decisions on lending on another hand were lacking. That is a problem I still have not solved and I will pursue the matter until I find out the reasons those things occurred.

Senator LIGHTFOOT—There was ignorance on behalf of the investors in the superannuation funds and there was the problem with the fiduciary responsibilities, as well. Is that correct?

Mr Heaton—That is as I see it, exactly.

Senator LIGHTFOOT—What about the major flaw? This is happening right across Australia and cannot be construed as sub judice because it is happening at the moment in Perth in Western Australia with mortgage brokers who obtain assets—particularly land and buildings—at what can only be fraudulent prices. A valuer gives a valuation of those assets and they are extraordinarily high—in some cases, more than double their actual price. Do you see that as the start of a fraud?

Mr Heaton—If that occurs it is definitely the start of a fraud. In a superannuation fund that is so heavily involved in property, such as EPAS was, you would hope those types of things did not occur. We need to be satisfied that they did not.

Senator LIGHTFOOT—Yes.

Mr Heaton—I believe the first approaches from APRA came when they were concerned about the balance of business investment in property that EPAS was handling as a percentage of its total portfolio. I believe more stringent ratios of liquidity also need to be instigated in funds and controlled by either APRA or somebody to ensure that liquidity levels never go lower than a percentage—possibly 30 per cent.

Senator LIGHTFOOT—How do you stamp out the false valuations that cause a lot of these problems—when they are quite clearly false?

Mr Heaton—I do not know what body investigates these types of things besides the Australian Securities Commission. I believe there could be some form of legislation that would say that, if the superannuation fund is purchasing an asset in excess of five per cent of the total portfolio, the matter has to be looked at by some party who is definitely at arm's length from the

people negotiating the deal. Obviously, this has not occurred in the past but it is a matter that needs a very stern look at. Regarding control measures for property valuations, we have a body, Natural Resources, that specialises in valuations. That is a body run by the Public Service and we get our land tax assessed by it. Why can't that be the body that does these valuations? Why does it have to be an independent valuer? There is far too much autonomy given to trustees as it is, let alone allowing them to seek out valuations and then lend members' moneys out on those properties.

Senator LIGHTFOOT—You have made numerous suggestions, and I think they are exceptionally good, but what about the penal provisions relating to false valuations, which seem to be a significant, if not the major, problem with respect to certain fraud? What about the penal provisions with respect to, say, licensed valuers, who create problems of this nature by giving, quite clearly, false valuations? Should the penal provisions be increased?

Mr Heaton—I am not aware of what the penal provisions are, but I can assume that they are not sufficient to deter people from entering into this type of thing because, as you say, it is happening. It is a significant factor in the downfall of several superannuation funds already. We would applaud any deterrent that can be issued or given through legislation. I am in my 50s and I am looking at retirement within the next 15 years; I would hope that I am now in a fund that is not going to fall over. But the legislation as it stands is not sufficient to make me comfortable enough to put any more than I need to into superannuation.

The Australian Prudential Regulation Authority said on the *Money Show* on Channel 9—and I have it on tape—that, in terms of them, we are only a small fund in the big pool of superannuation in Australia. That might well be the case, but there are some 24,000 members who in some form or another are relying on that fund, whether it be a large amount or a small amount, to perform as part of their retirement or fully for their retirement. It is not reasonable to expect that superannuation is just considered as another form of investment. Because the government have set down firm guidelines that we must fund our own retirement, I find it very hard to accept the fact that they cannot say that regulations are far more stringent on superannuation funds and trustees and investments in those funds. Huge amounts of money are being thrown into these funds. Why aren't controls and legislation far more stringent than for an investment adviser or some other form of person who offers investment of your funds?

Senator LIGHTFOOT—I certainly appreciate your tenacity in pursuing this, Mr Heaton. I am sure it has been at some personal cost to yourself and I thank you for your evidence today.

Senator ALLISON—What sorts of discussions and communication have you had with other members of the fund?

Mr Heaton—I am being used as a springboard in some instances but a central point of communication in others, so that is why I find it very important to stay in touch with journalists and keep them informed of what is happening. The first good news was that Senator Watson made a speech in the Senate, and I very much appreciate what you did there, Senator.

Senator LIGHTFOOT—It was a very good speech.

Mr Heaton—It was; I have given it to everybody I can think of.

Senator HOGG—He is not being preselected in Queensland; it is Tasmania.

CHAIR—It certainly brought some action—retribution initially, then a good reaction.

Mr Heaton—The second good news was that the Australian Securities Commission had issued a statement of claim—a 152-page document lodged at the Supreme Court, Brisbane. That is the other good news we have had of recent times. But as far as members contacting me for information and updates are concerned, it would be in the hundreds, and I have a list of them. I phone them when there is something different happening, and they pass it down the chain, so we have got a bit of a group going now. But, in the early days when this first happened and we got the news that we were 43 per cent in negative, the main reaction was, ‘Well, we’ve lost our money,’ and I do not accept that as a proposition at all at any time. If I had invested in a share company that had pretty much performing assets, I would probably accept that and take it on the chin. If it is superannuation you are talking about, I think you have got to be tenacious about it. Because if you can get something corrected and if you can see things were not done right and you know people have told you that this happened and that happened and you do not pass it on and pursue it, they will get away with it. That is why I am not prepared to do that.

CHAIR—Unfortunately, there are still a lot of bad practices around. There are too many uninformed trustees, trustees who are not performing to their duties or requirements, and the whole thing does need a lot of tightening up.

Mr Heaton—The attitude of APRA, I must say, is that the trustees must have autonomy. If that is the case and the trustees do not have any training or knowledge of good investment, how in the heck is the fund ever going to perform?

Senator HOGG—I have just one question and that is on the issue of complexity. It has been put to this committee that the laws and the rules and regulations, et cetera, surrounding superannuation are really too complex; that we really need to simplify them. But based on the evidence that you have given to us today, you seem to be arguing the opposite; that, really, because it is an issue regarding the most important thing in your lifetime—that is, your retirement nest egg—it necessarily needs to be an area that is complex. Is that a fair way to sum it up?

Mr Heaton—I do not know that it needs to be complex; it needs to be clear cut in its natural form. You need to be able to understand the consequences. If you are a trustee of a fund, you need to understand that you have got a heck of a responsibility to look after members’ funds and you do not go out willy-nilly shaking hands and doing deals. How good is the business acumen of some of these people who are running funds with multimillion dollars in cash? It astounds me that they can utilise people’s funds and not use some sort of discretion and ability to pick a good investment from a bad one. Once this case has been brought to trial by the Australian Securities Commission, we will get a lot more answers than we are getting at the moment. I am certainly getting back a lot of information as to how these things occurred and I am quite willing to pass them on to anybody who will listen.

CHAIR—We cannot accept that today.

Senator HOGG—No, he accepts that. Do you believe that part of the problem is that some of the trustees do not understand that it is not their money? Do you think that because they may well be the employer representatives, some of them believe the money is really still the employers' money and they don't see it as having passed on to their employees?

Mr Heaton—I am sure that is the case. It happens in business, too. Some operators are quite blase when they are dealing with a company's funds, a private company, public company or whatever. Senator Lightfoot suggested that maybe the penalty should be harsher. I think that is a starting point. It would be better to train people and give them some sort of qualification in investment if they are going to be allowed to lend money, and they should not always lend on margins. I was a banker for 15 years and I am a Bachelor of Economics. I consider myself reasonably well educated, but there is no way that I would invest any of my money in anything that I did not have good knowledge about and that I did not have some confidence in. Anybody who makes those decisions is a fool. If they make those decisions with somebody else's money; those people whose money it is are the fools. That is where I put myself at the moment.

CHAIR—Mr Heaton, thank you for all you have done and for appearing before the committee today. Is it the wish of the committee that the document presented by Mr Heaton from the Hotel, Motel and Accommodation Association of Australia, the newsletter headed 'Important Notice to Members', be incorporated in the transcript of evidence? There being no objection, it is so ordered.

The document read as follows—

[11.54 a.m.]

SCHEIWE, Mr Daniel John (Private capacity)

CHAIR—Welcome, Mr Scheiwe. You have given us a very provocative statement. We welcome it. It is a challenge for the committee to receive such presentations, particularly from academics. We look forward, at every hearing, to having an academic make a presentation to us. I think it often raises the interest and the dimension of the inquiry. Thank you for taking time out to write to the committee. Unfortunately, you gave us so much information we had to do some editing.

Mr Scheiwe—I have actually reduced it to one sheet for today.

CHAIR—That is very good.

Mr Scheiwe—I am a university lecturer in accounting, auditing and superannuation. I appear in a private capacity. I became interested in superannuation about 10 years ago because I changed jobs. I was concerned about the malpractices which had occurred in the corporate sector in Australia during the 1980s despite the fact that there was so much regulation there. At that time, quite a few investment funds had been frozen. It therefore occurred to me that it was possible that there were malpractices occurring in the superannuation industry and I undertook a comparison of the rights and, therefore, the financial protection of superannuants, shareholders and members of investment funds. The outcome of that was that I found that the rights and therefore protection of superannuants was far lower than that for shareholders. I am still concerned about that situation. What I would like to do today, with your permission, is go through the statement I have here and then answer any questions.

CHAIR—Perhaps for the *Hansard* record we might incorporate this to facilitate readers' understanding. Is it the wish of the committee that the statement be incorporated in the transcript of evidence? There being no objection, it is so ordered.

The statement read as follows—

Mr Scheiwe—I have not shirked away from being provocative in the title of the statement I am going to make: ‘Australia’s extant superannuation system: a major organised crime—not a retirement income system’. That is what I believe. I also emphasise that the perspective I take is from the point of view of a member. I will get back to that point shortly because it is most important. I will give an overview of my short presentation. I will briefly justify the title I have adopted, give a prognosis for the extant system, explain how the situation we are faced with came about, present some research findings, make a statement of recommendation and then answer questions.

I have five points as to why I regard the present system for superannuation in Australia as an organised crime rather than as a system to provide for retirement income. Despite that fact that we force over 91 per cent of Australian employees into superannuation, many superannuants are being cheated by their own superannuation funds. To illustrate that, I refer to the massive cross-subsidisation that exists in some funds. Let me illustrate with regard to the major fund that I am already in. I am in six funds but this is a major one. It is a funded defined benefit fund. In one instance a vice-chancellor’s salary doubled just before he retired and because this is a defined benefit fund his superannuation benefits jumped enormously. Another example is of a woman who was on a mid-50s salary—\$55,000 in 1996—and two years later her salary had tripled. The problem with the defined benefit plan, particularly a funded defined benefit plan, is that the fund assumes that that person has been on that salary all the time they have been in the fund and therefore the employer and the employee have been contributing at an appropriate rate. Of course that is not so. Therefore, in these types of funds there has to be massive cross-subsidisation by some members of other members. That, in my opinion, is grossly unfair.

I also point out that discriminatory vesting schedules are still in use in superannuation funds despite the fact that we are assured that there are wonderful prudential safeguards in place. I say that the minimum benefit provisions in the SIS regulations are a farce, that the Superannuation Complaints Tribunal’s provisions are restrictive and therefore ineffective, and that consumer protection does not exist for superannuants in Australia.

Secondly, fund investment arrangements are deceitful and wide open to abuse. I certainly have not changed my opinion of that from what I have heard this morning. For example, many investment objectives are pitifully low. Despite the section 52 covenant that the trustees are required to formulate and implement an investment plan which gives effect to risk, liquidity and diversity, on the low end, if the trustees so choose, they can adopt a very conservative investment plan which will generate very low returns.

In fact, if you look at the investment objectives for a lot of funds you will find that they are only one or two per cent above the inflation rate. Therefore, the returns which they applaud themselves for can in fact be very low. At the other end of the continuum, once the trustees have addressed these criteria in section 52 they are basically at liberty to invest in any way they like. I believe that the regulator cannot do anything about that, and there was evidence to support that view given this morning.

Another important problem is that fund members are deceitfully encouraged to believe that the fund investment return is in fact their return. What the Australian accounting standard on superannuation funds encourages, and that the legislation also encourages, is the reporting of

the fund investment return. That can be very different from the return which is filtered through to the members. For example, I had a mature aged student who was in a fund which was operated by a large insurance company in Australia. That company was advertising on TV that if members had been in their fund for 10 years they would have more than doubled their money.

As one of his activities, this student then tried to reconcile that statement with his own return. He found that he would have doubled his money only if he ignored all the costs and charges which this company had imposed on him. So it was quite misleading. In fact, this practice still continues. People are lulled into a false sense of security by being told they are getting a good return on their superannuation when in fact the return that they are being quoted is before the charges that have been imposed on them by the fund.

There is no protection against cosy arrangements between employers and fund operators. If the employer puts their employees into a particular fund, what is to stop the fund operator lending the money back to the employer at commercially attractive rates?

CHAIR—That is illegal under SIS.

Mr Scheiwe—Is it effective?

Senator SHERRY—There has never been a case of that brought to our attention yet.

Mr Scheiwe—It would be very hard to prove it.

CHAIR—No, not at all.

Mr Scheiwe—The other point is that there is no requirement for trustees to disclose all their relevant remuneration. For example, what if you have—and this is a real situation—trustees who are then on the boards of companies as a result of the investment decisions of their fund? Who is entitled to the directors fees from the company in which the superannuation fund has invested? At common law it was decided that that money belongs to the fund, but I know of instances of where that money is going directly to the trustees themselves and therefore is not disclosed as part of their remuneration from the fund.

Another problem with investment is that there is no limit on vertical integration. If you have a look at the accounts and reports of some of these large insurance companies, as some of my students have done, what you find is that the members have a superannuation policy with the XYZ insurance company. That then has a subsidiary of that insurance company as a trustee. It also invests with another subsidiary of that insurance company. Therefore, all of these entities which are subsidiaries of the insurance company are collecting fees from the member. There is no restriction on it. When you look at the returns that members are getting from some of these public offer funds, they are absolutely pitiful.

Point three is that fund trustees are accountable to no-one. The legislation encourages—

CHAIR—Under the legislation they are accountable to the members.

Mr Scheiwe—I disagree. Let me explain why. The legislation encourages funds to have corporate trustees. Who owns the shares of that corporate trustee? In the case of my own major superannuation fund, the shares in the corporate trustee are owned by the universities throughout Australia. Therefore, when the corporate trustee has its AGM, the only persons invited along to the AGM are representatives of the universities, not the members. The annual general meeting of that corporate trustee then decides important things like the remuneration of the trustees. So basically the corporate trustees are not accountable to any of the members. We have heard some of the costs which are incurred by these corporate trustees today. How did these get so out of hand? The Law Society one is \$500,000 for 6,000 members. How did this occur if the trustees were accountable to the members? I think that supports my point.

With regard to the amount of information that is supplied to members, the industry says, 'There's just so much accountable under the present legislation that is tightly regulated.' But when you look at the information that has to be provided to members there are a couple of points to make. One is that a lot of the information provided is at the discretion of the trustees. The second point is that if members request information above and beyond that which is required by statute, then the information is supplied to individual members. Therefore, I argue that the principle of divide and rule prevails in the Australian superannuation industry. And because superannuation funds are not required by law, in the main, to have annual general meetings, superannuants in Australia are denied the synergism of annual general meetings. They have no power—

CHAIR—That is not right. No annual general meetings?

Mr Scheiwe—No annual general meetings.

CHAIR—That is not right.

Mr Scheiwe—I would be delighted to hear from you as to which section of SIS requires annual general meetings.

CHAIR—You have got to put an annual report in.

Mr Scheiwe—That is not an annual general meeting.

Senator SHERRY—Are you suggesting a gathering to which, at least in theory, all the members of a fund can go along once a year?

Mr Scheiwe—Yes. Why should they have any fewer rights than a shareholder of a company? They have got the right to go to an annual general meeting; it is up to them whether they go.

Senator SHERRY—Yes.

Mr Scheiwe—The point is if they go along to annual general meetings they can hear comments and questions from more informed members and therefore they can learn a lot about the superannuation fund and there would be a much higher level—

CHAIR—I take your point. You are quite right. I apologise.

Senator LIGHTFOOT—The numbers are of no consequence, Mr Scheiwe, are they? BHP shareholders can go along, Telstra shareholders can go along, and there are several hundred thousand in each of those. Yes, I take your point. It is a good point.

Senator SHERRY—Yes, except there is a practical issue, isn't there, because there is no provision for proxy representation or voting for members of the superannuation fund. So realistically, when some of the funds have 200,000 or 300,000 members around the country and effectively they are the shareholders, to gather them together in any sort of representative numbers would be extraordinarily difficult.

Mr Scheiwe—You do not need to have them all there, do you? You only have to have enough people who know what is going on and can ask intelligent questions, and you have then got proper accountability of the trustees.

Senator SHERRY—Well, you have got some accountability.

Mr Scheiwe—Much better than we have got at the moment because there is none.

Senator SHERRY—I do not accept there is none. You may improve it in some areas—I accept that—but I do not accept there is no accountability at the moment. That is just not right.

CHAIR—The trustee company is a corporation, of course, and under Corporations Law there is a requirement to have an annual general meeting. That was the point I wished to make. But your point was an opportunity for members per se to meet.

Senator SHERRY—Chair, I am sorry, I know I have indulged in this myself but we are going to be here for a long time if Mr Scheiwe goes through this, so perhaps it would be better if we could ask that he draw it to a close and we go to questions.

Mr Scheiwe—The superannuants of Australia think superannuation is such an important matter that it is worth while spending a little bit of time on it.

Senator SHERRY—Yes it is, but we have all got restrictions on time, Mr Scheiwe, and the critical issues is asking questions and getting your response and challenging where we think we need to. We have received a written submission from you. As far as I am concerned, having read your written submission, I am confident I can ask sufficient questions to take up our time.

Senator LIGHTFOOT—Could you indicate to the committee how long you may be, Mr Scheiwe?

Mr Scheiwe—Stop me at the end of 10 minutes—how is that?

Senator LIGHTFOOT—Seems okay to me.

CHAIR—We are in the hands of the committee, but we are required to adjourn at 12.30. You wish to go for another 10 minutes? Is that the wish of the committee?

Senator HOGG—It does not worry me.

Senator SHERRY—Mr Scheiwe, as far as I am concerned, is making a range of, at least in some areas, inaccurate and grossly misleading statements. I do not challenge your right to do that, Mr Scheiwe—that is your prerogative. What I want to do is to have a reasonable right to question and challenge some of those statements, and I do not regard 10 minutes of questions as sufficient time to do that.

CHAIR—We are in the hands of the committee.

Senator LIGHTFOOT—Perhaps we can sit beyond 12.30? I do not agree with my colleague incidentally, for the record, that they are grossly misleading statements.

Senator SHERRY—I said ‘some’, which should be challenged.

Senator LIGHTFOOT—But I do not agree with your statement, Senator, that they are necessarily grossly misleading.

CHAIR—Mr Scheiwe, you will have the opportunity to take questions on notice, so perhaps you could go on for another five or six minutes and then we might ask questions.

Mr Scheiwe—The fourth reason I regard the present system as an organised crime rather than as a system for providing for retirement income is that, despite the fact we force 91 per cent of Australian superannuants into superannuation funds, they are denied basic rights regarding superannuation. They have no choice of fund and they have no opportunity to change funds if they want to.

Fifthly, superannuants are denied basic democratic rights regarding superannuation. The members are largely ignored by in-fund decision making despite the fact that they are at law the equitable owners of the fund. You only have to look at the TV ads at the moment. Those ads regarding superannuation are pitched at the employers. They are not pitched to the members. The members are disregarded. The arrangements are between the employers and the relevant unions.

Skipping over to the prognosis for the extant system, as far as I am concerned, the retirement income objectives of many individuals and government will not be achieved because of the present system: the returns are too low. If choice of fund legislation is not introduced, then both the employers and the unions will be successfully sued for economic losses suffered by employees. I think Senator Sherry alluded to that earlier this morning.

How did this situation come about? This is related to a key issue: the perceived ownership and control of funds. Basically, there are four major groups who think they own and therefore should control superannuation funds in Australia: the employers, the fund operators, government and members. Comments made by one of the panel earlier this morning tend to

support that view. Why has the present situation come about? Because so far the industry's regulations have been largely written to suit everyone except the members of the funds. Despite the fact that they own the funds the rules have been written to suit everyone except those members.

The fund operators have been very well organised. They have many expert voices with vested interests and they are singing only one benevolent song—and that is self-regulation. Joining them in this chorus are the actuaries that work in the industry, the lawyers that work in the industry, the Australian Superannuation Funds Association and the Australian Institute of Superannuation Trustees. Basically, they all want self-regulation by the industry. Therefore, the rules are written to suit the industry, not to protect the members.

CHAIR—Not by this committee, if I can interject.

Mr Scheiwe—Okay. Thank you.

CHAIR—We have done more than perhaps anybody else to institute changes on behalf of members and to protect members.

Mr Scheiwe—For various reasons, most Australians do not take an active interest in their superannuation. Also, superannuation is a low political priority for government and so policy is determined largely by vested interests to whom government has contracted out the day-to-day management of funds.

I will not go through all these research findings. Let us just have a look at the first one. In a national survey I conducted, only four per cent of respondents believed that significant misappropriation is not occurring in some Australian superannuation funds. Only four per cent of the respondents in my national survey believe that significant misappropriation is not occurring in some Australian superannuation funds. They do not have confidence in the system, in other words.

Running through the recommendations, the first recommendation is that unlimited choice of funds legislation, not limited choice, should be available. The second recommendation is that fund members should have the same rights and therefore the same financial protection that shareholders have. In other words, they should have annual general meetings, they should elect the trustees, and they should set the trustees' remuneration. They are both investments; why should superannuants have less protection and fewer rights than shareholders? That was a point made by someone else this morning.

The third recommendation is that there should be mandatory reporting to members in a meaningful way. Most members do not understand the reports they are getting. What they need is more information on the returns that they are receiving, not the fund investment return. They need to have more benchmarking with respect to their return. In other words, how does their return compare with the industry's best? It may be worth considering having a standard reporting format.

The fourth recommendation is that we have effective minimum benefits regulations to eliminate the rorts which still persist in the system. The fifth recommendation is to put responsibility for superannuation consumer protection back where it belongs—with the ACCC. I have contacted them about the false advertising by superannuation funds. They said they are not responsible, it is ASIC. I wrote to ASIC and their response was totally unsatisfactory.

CHAIR—What was ASIC's response?

Mr Scheiwe—Totally unsatisfactory.

CHAIR—Table it for us.

Mr Scheiwe—I have not got it with me.

CHAIR—Take it on notice; we would like to have that.

Mr Scheiwe—Okay, I will send it to you. When I asked if I could speak to the person who is in charge of superannuation in ASIC in Queensland, I was told there is no-one looking after superannuation in ASIC in Queensland. When we had the ISC here in Brisbane, they had some very good staff and they had very good systems for monitoring superannuation. Most of those people now have left the regulator. They do not work for APRA; they have left. Recommendation No. 6, of course, then is to stop destroying the regulator—consolidate the regulator into one body, not three. I would be happy to take questions.

Senator SHERRY—Firstly, I must say I am concerned about your overall theme of a major organised crime. I just do not believe the evidence, even including the evidence we have received this morning in terms of the industry nationally, supports that claim.

Mr Scheiwe—Of course, they wouldn't. The industry is not going to say—

Senator SHERRY—No, I am not talking about the industry. I am talking about my reasoned observations about the industry over a long period of time. I cannot agree with your essential theme and I think it is, frankly, grossly misleading. But could we go to some of the evidence we got this morning and one of the comments you make here about union patronage? What interested me this morning with the three funds we looked at was that there was no union involvement at all. Do you accept that?

Mr Scheiwe—I am not sure. I will accept your statement that there wasn't.

Senator SHERRY—There is no evidence that there was any union involvement, certainly based on the three funds we looked at this morning, so how can you claim that union patronage is a particular problem?

Mr Scheiwe—Because what happens is, under the equal representation rules, generally the employee representatives are, in fact, non-representative union members.

Senator SHERRY—Yes but, Mr Scheiwe, in the three funds that we looked at this morning—and, frankly, these are probably the worst examples we have seen around the country, and it seems to be a particular problem in Queensland—there is no union involvement at all.

Mr Scheiwe—But that does not prove that there is not union patronage in the system.

Senator SHERRY—But it does not prove your case either. We have had no evidence put before this committee on funds other than the three we have had here and, in these three, there is no union involvement at all.

Senator ALLISON—What about the hairdressers, Senator Sherry?

Senator HOGG—That had no union involvement.

Senator SHERRY—No union involvement, none whatsoever.

Mr Scheiwe—I do not dispute the fact that the equal representation rules do not work. If I can just illustrate with my major fund, there are supposed under the trust deed to be eight trustees: half of them employer reps and half member reps. Under the trust deed and the legislation, they appointed an extra independent trustee, so then they had nine. That ‘independent’ trustee was, in fact, a former employer representative. They then approached the ISC and appointed a second additional trustee who, again, was a former employer representative. At that point you had four member reps and six employer or former employer reps on the board. This is for a fund of over 50,000 people. Two of those four employee reps were, in fact, no longer employed in the university sector. One of them was sailing a yacht around Australia and, from information I received, did not regularly attend meetings. Clearly then, we had effectively two employees out of a board of 10 representing over 50,000 members in that fund.

Senator SHERRY—Mr Scheiwe, wouldn’t you accept that if you are to make sweeping claims about alleged major organised crime of the system, you would have to do a proper representative survey industry wide of the sorts of issues you were talking about? Can you provide us with that representative survey?

Mr Scheiwe—No I cannot, but, by the same token, the fact that I have not gone out and done that does not prove that my statements are wrong.

Senator SHERRY—It does not prove you are right either.

Mr Scheiwe—What I am saying is that you can either regard the system as being morally wrong or you can take it one step further and say it is tantamount to a crime.

Senator SHERRY—But I am asking you where is your representative, detailed survey on which you can base the assertions you are making? Where is your representative survey to support the quite sweeping claim you make about the alleged pitiful returns? Every survey that I have seen and, frankly, that this committee has seen shows that the vast majority of funds in this

country are earning three to four per cent real rate of return, on average, long term. So where is your detailed material to support your assertion?

Mr Scheiwe—I will gather that information. I believe I have it in a paper and I will submit it to you.

Senator SHERRY—Thanks.

Senator LIGHTFOOT—I will be brief. Mr Scheiwe, I understand your terminology and I do not discourage or encourage the type of inflammatory headlines you have. However, I think you have the right to say that here. I take it as being something of a non-specific nature and I think we should look at it.

Senator SHERRY—I do not challenge his right to say it.

Senator LIGHTFOOT—I understand that. What I disassociated myself from was that it was grossly misleading. I understand what your motive is. Where licensed valuers are able to give valuations that are double and in some cases triple the real valuation or a valuation that you could obtain from the Valuer-General's office, and it happens so frequently and in disparate areas, there has to be something seriously wrong with the licensed valuers as an organisation. I am not saying all licensed valuers are tainted at all, and I want to be very specific and unambiguous about that. But there is a hard core of not dissimilar valuations given in every major city and in built-up areas—I am talking about Queensland in particular because it is so decentralised—that I have seen over the last several decades, and not just related to the superannuation industry.

But in my view the superannuation industry is being run properly. Returns are low, there is no question about that: if you look at the average returns of the stock market, the returns are low; if you look at the average returns in the stock market from just one industry, the banking industry, they are low; if you look at the aggregated returns on long or short bonds, then the returns in the superannuation funds are low indeed. If you look at the borrowing by governments and aggregate those borrowings alone over a 10-year period you would be far better off to put the money in government bonds and then you would not have any management problems either.

Mr Scheiwe—Could I respond to that?

Senator LIGHTFOOT—Yes, please.

CHAIR—I am not sure, Senator, that that is correct. Long term there are better returns under equities.

Senator LIGHTFOOT—But please respond.

Senator HOGG—Ask him about mining shares as well!

Mr Scheiwe—Regarding these valuations, I would see it as the auditor's responsibility to query any of these contentious valuations. One of the weaknesses in the present system is that

the auditors of superannuation funds are appointed by the trustees, they report to the trustees on the activities of the trustees. There is no annual general meeting at which the auditors report to the members. The members do not appoint the auditors and cannot ask questions of the auditors.

Senator LIGHTFOOT—It is flawed. I appreciate that.

Mr Scheiwe—One last point is about the information which is sent to members under SIS. They can send out unaudited, abridged financial statements unless the member specifically asks for audited financial statements. In the main they are getting unaudited financial information.

Senator LIGHTFOOT—Where do we go in a major sense—does it require major surgery to the legislation?

Mr Scheiwe—Absolutely. Until that major surgery is undertaken the system will continue to be in a state of flux.

Senator LIGHTFOOT—I would appreciate questioning you further but we are running out of time, so I will pass to my colleagues.

Senator ALLISON—Do you think it is a good or a bad thing that fund administrators have now become consolidated and there are relatively few choices in who you tender out your fund administration to?

Mr Scheiwe—That implies that you have to tender out fund administration. I do not see it is necessary, particularly in smaller funds. With regard to larger funds, I am not in a position to comment.

Senator ALLISON—You suggest that there should be no equal representation rule—that is, that you do not have equal numbers of member and employer reps. What is the ideal structure? Should they be all members as trustees and, if so, how do employers get some voice?

Mr Scheiwe—I start by saying that is just not my view. If you go back to 1992, I think it was Discussion Paper No. 50 from the Australian Law Reform Commission which said there was absolutely no justification in the case of defined contribution plans for having employer reps on the board and in the case of the defined benefit plans there was very little justification.

To answer the second part of your question, why can't we have the same situation in superannuation funds as we have in public companies where, basically, we have elected trustees? They can always get in their experts to advise them.

Senator ALLISON—Do you see the election process for trustees at present as being inadequate?

Mr Scheiwe—Absolutely. It is not an election. In fact, if you read the legislation they do not use the word election, they use the word 'appointment'. The employers appoint their representatives in some cases. What has happened, particularly in my own case, is that there has

been no requirement for the election of the employee representatives and so, in some cases, the employers were appointing the employee representatives. So equal representation was a farce.

Senator SHERRY—And yet this morning we had the Queensland Law Employees Superannuation Fund that at least have the election of two employee representatives and that did not seem to provide any particular check on the problems they have experienced, did it?

CHAIR—It raises the question of professional trustees, doesn't it?

Mr Scheiwe—That is a possible way to go.

CHAIR—Thank you very much, Mr Scheiwe. As a committee, we do have to disassociate from some of your flamboyant headings, but, underneath those, you do raise interesting issues that we will certainly look at. No doubt about it, it has presented us with a challenge. I thank you for coming. But, as I said, we must disassociate ourselves from those headings about crime.

[12.28 p.m.]

HENDERSON, Mr Paul, Principal, Paul D. Henderson

CHAIR—In what capacity are you asking to appear before the committee?

Mr Henderson—I am a solicitor of 23 years standing. I would like to beg special leave to address some procedure on the last bracket of evidence in this matter, on how it was conducted.

CHAIR—Would you like to put a submission to the committee and we will receive that?

Mr Henderson—Just a brief oral submission.

CHAIR—How long do you intend to speak?

Mr Henderson—Five minutes at the most.

Senator SHERRY—I am happy with that.

CHAIR—There being no objection from the committee, yes, leave is granted.

Mr Henderson—Thank you, committee. I have been a practising solicitor for 23 years in Queensland. I believe that the interjections of Senator Nick Sherry were totally out of order in relation to the last speaker. They exhibit ostensible bias and a reasonable apprehension of bias if he is to continue in any report based upon this today. I submit that either his comments about the last speaker are deleted from *Hansard*—

CHAIR—We cannot do that. Once it is on the *Hansard* record, it stays.

Mr Henderson—or I request him to disqualify himself on the basis of apprehension of bias in relation to the final report on this matter. Thank you.

CHAIR—I can respond on behalf of the committee. People in order to draw out a witness at times do ask leading questions. But perhaps I should give Senator Sherry the right of response.

Senator SHERRY—You are quite open to make whatever comments you like. It is a democracy. As far as I am concerned, I believe my comments were appropriate. I am entitled to make them and I will make what comments I believe I am entitled to make. That is my particular role.

Mr Henderson—I appreciate that. You see it as part of parliamentary privilege. I believe what you exhorted against the last speaker to be an abuse of that parliamentary privilege.

Senator SHERRY—I just do not agree with you. You are very fortunate to have had the time. I had agreed to hear your concerns, but I simply do not agree.

Mr Henderson—I appreciate the Chair generally.

CHAIR—Thank you for your presentation. On behalf of the committee I thank all witnesses who have given evidence and for their participation here today.

Committee adjourned at 12.31 p.m.