

25 May, 2002

Committee Secretary
Joint Statutory Committee of Public Accounts and Audit
Department of the House of Representatives
Parliament House
Canberra ACT 2600

Dear Chairman,

Re: Supplementary Submission
Corporate Review - Continuous Disclosure

Overview

Since sending my initial submission dated 23 April 2002 I have thought more about the terms of reference “the Joint Committee of Public Accounts and Audit wishes to explore the extent to which it may be necessary to enhance the accountability of public and private sector auditing. In particular, the Committee is keen to determine where the balance lies between the need for external controls through government regulation, and the freedom for industry to self-regulate”.

I am more convinced that the Australian Securities and Investments Commission (ASIC) and the Australian Stock Exchange (ASX) must adapt a zero tolerance approach towards continuous disclosure and reporting by listed entities.

All efforts must be taken to protect all stakeholders directly or indirectly through their present and future retirement benefits.

Examination of Directors

If one looks at the best possible way to make change then we must start with the one factor that crosses all areas, “the human element”. Future change must be made on the basis that where the “human element” is concerned, change be made by factoring in the worst case scenario.

The terms of reference must focus on the relationship between the Auditor and the Directors and making changes so that the Auditor is regulated totally to ensure independence.

The time has come for the area of board composition to be addressed and legislated. I addressed the issue of board composition in my previous submission and I am convinced that change is urgently needed in this area.

The evidence coming out of the HIH Royal Commission is disturbing and one notes the name of Mr Adler is mentioned on a very regular basis at this hearing, he is mentioned at the One Tel inquiry and has been found guilty of breaching his duties as a director in relation to a payment of \$10 million by an HIH subsidiary (HIH Casualty and General Insurance Ltd) to

Pacific Eagle Equities Pty Ltd, a company of which Mr Adler was a director.

Auditor - History to Dictate Future

The attached article headed “Andersen poised to settle Bond case” by Mark Drummond on page 3 of the Australian Financial Review on Tuesday 21 May 2002 discussed various cases showing the downside of auditing and is relevant when one refers to the terms of reference.

1. Possible settlement by accounting firm Andersen relating to Andersen’s 1988 audit of Bond Corp’s accounts. The liquidator had previously launched a \$1 billion claim against the audit firm.
2. In 1994 KPMG agreed to a \$136 million commercial settlement of a \$1 billion plus claim relating to its audit of the failed merchant bank, Tricontinental.
3. In 1997, KPMG and Price Waterhouse (now PricewaterhouseCoopers) paid \$120 million to settle legal claims totalling more than \$4 billion brought by the South Australian Government over the 1991 collapse of the State Bank of South Australia.

When one reflects on those past events and looks at the present collapses, then it is time to urgently change and try a new approach, self-regulation has failed. If one looks at the worst case scenario, a corporate collapse followed by a royal commission, both costing financially, emotionally and damaging to investor confidence then change must be made only by Government intervention and not by self-regulation.

Audit firms to a certain degree have tried some level of independence internally by having separate audit teams and tax teams, each with their own audit papers. This has failed and clearly a future approach of rotating audit firms with no audit firm undertaking both audit and professional work is a must. I think we need to go even further by setting up an Independent Audit Commission answerable to Parliament

In my previous submission on page 5, I recommended the setting up of an Independent Audit Commission as detailed under recommendation 5 - Independent Audit Commission. To recap, the market requires data and information with credibility and integrity, and consideration be given whereby all auditors be required to lodge a report on each listed entity they audit, reporting on all issues discussed, issues uncovered, issues discussed with management or at an audit committee meeting. The report would be lodged with an independent government body, independent of the ASIC.

The objective is that the Auditor will be able to report independently, and companies will have to accept the boundaries for “true and fair” to exist. Far too often we hear of companies arguing over various issues prior to signing audit reports. This change will allow for enhanced audit independence.

ASIC - Focus

Presently companies are able to lodge documents with the ASIC electronically. The future focus of the ASIC should be one of being proactive to protect the financial interests of all Australians. It is far better to change and take action now and be proactive, instead of examining the failures as they occur.

The following may assist in helping the ASIC become proactive. The Government should legislate so that all listed entities and subsidiaries of listed entities lodge all documents electronically with the ASIC. Some review may be needed for the process of lodging statutory accounts, but overall it must assist the information and disclosure process. If Government can legislate to require large employers to lodge their group tax electronically then they can legislate for lodgement of documents electronically to the ASIC.

Lodgement of Documents and Reporting to ASIC and ASX

The fees currently incurred by listed entities for the late lodgement of documents to the ASIC is minimal and does not offer an incentive not to lodge documents on time.

The fee to lodge an annual report is \$900 and a minimal late lodgement fee if lodged late. It would be far better to set the lodgement fee slightly higher and late fee of \$2,500 being incurred if lodged past the due date. The fee is minimal for listed entities and would be an incentive not to lodge documents late.

The following details may assist the Joint Committee in the examination and review of the lodgement process of documents by listed entities and be able to make recommendations for change. These changes may include an education process or a procedure for the listed entity to explain its procedures in consultation with the ASIC.

(a.) Australian Environmental Technology Limited

The attached media release by ASIC states that the ASIC has commenced proceedings in the Supreme Court of Western Australian to wind up Australian Environmental Technology Limited as the company has failed to lodge its outstanding annual accounts for the financial year ended 30 June 2000 despite court orders to do so.

(b.) Prudential Investment Company of Australia Limited

In my previous submission I referred to the Prudential Investment Company of Australia Limited and feel that the chronology of lodgement of documents and reporting as detailed below may assist the Joint Committee in gaining a further understanding of reporting by a listed entity. Copies of ASIC and ASX documents showing lodgement dates by this listed entity are attached.

Statutory Accounts lodged with ASIC

Annual accounts - Due 30/09/2001 - Not lodged on time, 15/11/2001

Half-year accounts - Due 16/03/2001 - Not lodged on time 21/05/2001

Annual accounts - Due 30/09/2000 - Not lodged on time 18/10/2001

Quarterly Borrowing Reports lodged with ASIC

March 2002 - Due before 30/04/2002 - Not lodged
December 2001 - Due before 31/01/2002 - Lodged on time 25/01/2002
September 2001 - Due before 31/10/2002 - Not lodged on time 15/11/2002
June 2001 - Due before 31/07/2001 - Not lodged
March 2001 - Due before 30/04/2001 - Lodged on time 30/04/2001
December 2000 - Due before 31/01/2001 - Not lodged on time 08/03/2001
September 2000 - Due before 31/10/2000 - Lodged on time 03/10/2000
June 2000 - Due before 31/07/2000 - Not lodged on time 09/08/2000
March 2000 - Due before 30/04/2000 - Not lodged on time 07/08/2000

Announcements to ASX

1. Suspension from Official Quotation - On 29 October 2001 the company was suspended from quotation due to the non lodgement of the annual report with the ASX as the listing rules require a listed entity to lodge an annual report within 17 weeks of the completion of the year end. The non-lodgement was due to an inability by the company to reach agreement with the Auditors, Ernst & Young, on certain matters.
2. On 5 December 2001 the company accepted the resignation of the Auditors, Ernst & Young.
3. On 26 March 2002 the ASX requested in writing to the company when it was aware that the profit of the company for the period ended 31 December 2001 of \$203k before tax represented a decrease of approximately 52% from the previous corresponding period (profit before tax of \$420k).

The ASX drew attention to the definition of “aware” in chapter 19 of the listing rules. The ASX further drew the company’s attention to listing rule 3.1 which requires an entity to give the ASX immediately any information concerning it that a reasonable person would expect to have a material effect on the price or value of the entities securities. The ASX also drew the company’s attention to the guidance note titled “Continuous disclosure: listing rule 3.1” states if on reviewing management accounts an entity becomes aware that the actual revenues and profits for the period may not meet the financial results for the previous corresponding period, disclosure would be required.

The company responded to the ASX on 28 March 2002 and advised that the information was available in the first week of February 2002. The company had clearly failed to follow the listing rules regarding “continuous disclosure” when it reported over a month later.

The above highlights an area where change can occur in that auditors advise the ASIC when the information (pre-tax profit) was first available thus requiring the company to advise an indicative profit/loss result to the market. Overall “continuous disclosure” may need to be reviewed as one would have to be very naive to think that all companies will follow the spirit to report to the ASX following the requirements of Listing Rule 3.1.

SUMMARY OF MAIN ISSUES HIGHLIGHTED IN SUBMISSIONS

1. A zero tolerance approach by the ASIC and ASX.
2. Safeguarding and protecting shareholder wealth, present and future retirement benefits of all Australians and potentially assisting in decreasing future outflows of Government expenditure.
3. The setting up of an independent Audit Commission.
4. All former Auditors of Listed Entities be banned from being directors of those entities for a period of say two (2) years.
5. Substantial increase in ASIC late lodgement fees for listed entities.
6. Change of culture at the ASIC to being a pro-active culture.
7. Compulsory electronic lodgement of documents to the ASIC.
8. Legislation to be put in place on the composition of board's of directors of listed entities with greater emphasis on independent directors.
9. Examination of the suitability of directors prior to board appointment of listed entities.
10. The implementation of a penalty system by the ASX on renewal of listing fees for previously suspended listed entities or listed entities previously in breach of Continuous Disclosure.
11. Include in the Corporations Law a category of "Listed Entity".
12. Increase the budget of ASIC instead of potentially spending vast amounts on future Royal Commissions.
13. Anomalies in reporting between the ASX and the ASIC, particularly on the issue of "continuous disclosure".
14. ASIC and ASX increasing public awareness by advertising quarterly all listed companies that have been suspended or asked to respond to an ASX query.
15. Listed entities to report pre-tax profit quarterly.
16. Listed entities to report budget estimates when lodging yearly results with the ASX.
17. Legislating on the use of the word "accountant" and the unification of accounting bodies.

In conclusion, I would like to thank the Joint Committee for accepting and reviewing my submissions and hope they have assisted in this valuable process and look forward to the future changes that may eventuate to assist the financial future of all Australians.

Yours sincerely,

Rodney Bennett