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JOINT COMMITTEE ON CORPORATIONS AND SECURITIES

Monday, 13 July 1998

Members: Senator Chapman *(Chair)*, Senators Conroy, Cooney, Gibson and Murray and Mr Anthony, Mrs Johnston, Mrs De-Anne Kelly, Mr Leo McLeay and Mr Kelvin Thomson

Senators and members in attendance: Senators Chapman, Cooney, Gibson and Murray and Mr Kelvin Thomson

WITNESSES

Committee met at 9.09 a.m.

BOYMAL, Mr David Gary, National President, Australian Society of Chartered Practising Accountants, 170 Queen Street, Melbourne, Victoria 3000

PARKER, Mr Colin William, Director, Accounting and Audit, Australian Society of Chartered Practising Accountants, 170 Queen Street, Melbourne, Victoria 3000

HARRISON, Mr Stephen, Executive Director, Institute of Chartered Accountants in Australia, 13/47 York Street, Sydney, New South Wales 2000

REILLY, Mr Keith, Technical Director, Institute of Chartered Accountants in Australia, 37 York Street, Sydney, New South Wales 2000

CHAIR—I now open the hearing of the parliamentary Joint Committee on Corporations and Securities. I welcome all the witnesses who will be appearing before the committee this morning. The purpose of this hearing is to take evidence on the exposure draft legislation under the corporate law economic reform program. The committee has received 10 written submissions, which it will consider, along with today's evidence when it is considering its report.

The committee has already conducted a public hearing on this bill in Canberra, during which representatives of the Australian Council of Auditors-General and the Australian Chamber of Commerce and Industry gave evidence. The committee prefers to conduct its hearings in public; however, if there are any matters which witnesses wish to discuss with the committee in camera, we will consider any such request.

I welcome this morning the representatives from the accounting bodies who will be appearing before us. We have before us your written submission. Are there any alterations or corrections that you wish to make to that written submission?

Mr Boymal—No.

CHAIR—Do you wish to make an opening statement to the committee?

Mr Boymal—Yes.

CHAIR—I invite you to proceed and, at the conclusion of that, we may have some questions.

Mr Boymal—Because the sentiments of the two accounting bodies are very similar, if not identical, and because we do not particularly want to bore you, I will make an initial presentation on behalf of the Australian Society of Certified Practising Accountants and, if the Institute of Chartered Accountants in Australia have any contrary or additional points, they will add to or amend what I say. Unless this occurs, you can take it that the comments I make end up coming from both bodies.

Firstly, we would certainly commend the broad thrust of the legislation. For a considerable time the accounting bodies themselves have felt that it was important to get more participants in the accounting standard setting process. The research and report—the Pearson report—were prepared by the accounting bodies along those very lines.

There were self-interests on the part of the accounting bodies in that because, at the present time, the funding of the standard setting process primarily comes from the accounting bodies. They put up the largest amount of money. It is then followed by the federal government and in recent times for a special project the companies, through the Stock Exchange, have put up a single amount. But we have been very long-term funders and have felt that the burden should be much better spread around. So there is self-interest there.

There has been a considerable amount of consultation with the accounting bodies in this process. We are pleased to say that the vast majority of points that we have made to those drafting the legislation have in fact been picked up. So we are broadly very pleased with the final outcome. We have some comments to make nonetheless, but I think that puts it in the appropriate context.

In terms of some detailed comments, I think the starting point is the proposal in paragraph 2.3 of the regulation impact statement where the problem concerning accounting standards is first indicated. This is, I guess, what the draft legislation is intended to fix. It says:

> Australian accounting standards have been found to be too prescriptive and overly technical, imposing excessive costs on business. Business considers that the standard setting process—

I will stop there. We do not altogether agree that accounting standards are too prescriptive at the moment. The draft legislation itself does not suggest that there ought to be any watering down of the quality of accounting standards or the detail. We would point out that the most prescriptive accounting standards in the world—the most overly technical accounting standards in the world—are in the United States, which is the most highly respected capital market. Therefore, it appears to us that there is a relationship between the prescriptive nature of accounting standards and how well respected the capital market is, which in turn relates to the cost of capital.

When business considers that following all of these existing rules imposes an excessive cost on them—yes, there are costs involved in following accounting standards; there are costs involved in reporting. If you look at an annual report, though, and you see the number of pretty pictures, where there are voluntary costs incurred by the companies, it then is quite difficult to say that companies are objecting to the costs of financial reporting, because they actually spend a deal more than they really have to in producing their annual reports.

The important thing is that that cost, the cost of putting together the annual report, is minute compared to a couple of points change in the cost of capital, the cost of borrowing. The more highly respected the capital market and the more prescriptive the accounting standards, the cheaper the cost of capital. Therefore, the whole idea that there are excessive costs in this process is only looking at one side of the coin. I see Brian nodding, because I think we have probably said this same thing before. What it means, though, is that one does

have to be careful at the starting point. If the starting point is not quite right, then things that feed from it may not be right also.

The problem actually is not just that the standards currently are too prescriptive and that the whole exercise is too costly. The problem is that anybody who tells business what they ought to be doing, which is what accounting standards are, is not going to be all that well received by business. The whole point is that, in the long run, business itself understands that the more highly regarded are its financial statements internationally because of the stringency of those statements, the more highly regarded is the company when it goes out into the capital markets. That problem is very much only presented on a one-sided basis.

I think the accounting bodies would equally disagree with the next sentence:

Business considers that the standard setting process is captured by the accounting profession and that there is no real accountability to users.

The situation there is that the existing standards setting board, the Australian Accounting Standards Board, is an arm of government. The structure was arrived at by agreement between government and the accounting bodies, whereby the board would be an arm of government, but the technical support would be provided by the accounting bodies.

I am going to make another presentation later on in the morning because I am also Deputy Chairman of the AASB, but I can assure you that the AASB is an independent arm of government and the accounting profession makes its voice heard, but the independent board does not follow what the accounting profession necessarily wants. Therefore, the structure presently does have independence.

One would ask: how many times have the people who complain about the capture of the process by the accounting profession tried to influence the process? I can tell you just as an example—and I do not want to pick on them—that the Company Directors Association has never once replied to a single exposure draft on accounting standards. So it is fine for groups like the Company Directors Association to say, 'It is all captured by the accounting profession.' But, in fact, the attempt to influence the process by some of these groups has been non-existent or pretty pitiful. It is fine to complain, but many have not really made good use of the very open due process that currently exists there.

But it really is wrong to say that the accounting profession has captured it. The only way one could say there is that appearance is that, at the moment, all of the people on the AASB are accountants. You need to have that sort of skill to be there.

There was a time on the AASB when we said, 'This is no good; we've got to get a barrister.' We had a barrister on the board, and it just did not work. The barrister was fine when it came to matters of law, but did not understand what the drafting was all about in terms of matters of accounting. Those people have to be accountants. I will come back to that because that is also in the detail. That is the only way one could really say that the accounting profession has captured the process. If capturing the process means putting the money up, we are very, very happy to share that around, believe me.

Basically, what I am doing is querying, to a degree, the starting point. Again, we should not get that out of perspective because, whilst these sentiments are in the regulation impact statement, after the considerable consultation that has been had with the accounting profession, we do not find those sentiments coming out strongly in the legislation. We wonder, therefore, why they are still there in the impact statement in such blunt language, because we think the influence of those points has been resolved through the consultative process. Again, I do not want to get that issue too much out of perspective. I guess the starting point of any legislation is to read what we are trying to achieve.

One of the major thrusts of the draft legislation, in so far as accounting standards are concerned, deals with international accounting standards, international harmonisation. I think one has to understand what the current situation is. At the present time the Australian Accounting Standards Board has a project of international harmonisation well under way whereby probably, let's say, within the next 12 months a company complying with Australian accounting standards will be able to say that by complying with the Australian accounting standards it automatically complies with international accounting standards.

I have to explain in a little more detail what that means. International accounting standards contain choices. That is because they are written based upon international compromise. If two powerful countries sitting on the international accounting standards disagree, then you will find both of their approaches often appearing in the international accounting standard, saying, 'You can either do it by method A, or you can do it by method B,' because that was the way of getting both country A and country B to agree at that forum to let the document through.

So we have some quite different treatments for single transactions allowed in international accounting standards. Just to give you an example so that you have a feeling for it, if one incurs interest expense on borrowing money to develop or build big plant, the international accounting standard says that you can either expense the interest or you can capitalise it to the asset.

In Australian accounting standards we have never allowed this sort of wide range of choices. In Australia we chose one of those two methods. That means that compliance with Australian accounting standards can automatically mean compliance with one of the choices in the international standard, but some other country could have picked the alternative choice. So compliance with international accounting standards does not automatically mean compliance with Australian, because it could be following the other choice that Australia did not allow. Putting it simply, it is a one directional sort of harmonisation.

The Australian accounting profession is very concerned that, if there is a proposal that we just simply copy the international accounting standards, we would be allowing a wider range of very different choices into our financial reporting that we do not currently allow. We know full well that the reason for those choices was nothing that made any sense, other than that the document needed the two choices in order to get an international voter. Therefore, we do not really want there to be a scenario where the quality of our reporting gets watered down by simply copying the multitude of choices in the international standards.

So the current project for harmonisation is to ensure that Australian standards mean compliance with international standards. But the Australian accounting profession and the AASB will not have a bar of these multiple choices. So we are quite fearful, you might say—although that may be a bit too strong a word—or very concerned that, whilst there are these choices in international standards, if Australia were to sink a copy of the international standards, we would have a weaker set of standards than we currently have.

The whole purpose of there being standards is for there to be comparability between companies. When you look at the results of one company and at the results of another, you can just assume that they have all been derived in the same way, so those two results are comparable. If there are choices though, the results are not comparable, and it fails a fundamental test of good reporting. A great deal of the concern about copying international standards hinges upon this issue.

It will be a long, long while before the international standards no longer have choices, and that is because of the international politics involved in setting the standards. We basically have the view that the adoption verbatim of international accounting standards is still a long way off. Even though IOSCO, which is the International Organisation of Securities Commissions, might endorse the international standards, that in itself is probably still not enough for us to copy them.

When it comes to this issue, I believe that the United States is of importance. When the US market is prepared to adopt the international accounting standards, we will be quite happy in copying them—but not really until then. The US market is dominant. At the moment, companies are prepared to do more in terms of standards and disclosures to enter the US market. Everything hinges upon whether the American Securities and Exchange Commission is prepared to have any change to that—and at the moment there is no sign that it is. So basically the idea of copying standards is a good long-term objective, but it really has a long, long way to go.

The next point to make is in relation to the FRC, the Financial Reporting Council. The Financial Reporting Council has been put there as the group representing all of the interest groups, including the accounting profession, preparers of the financial statements and users.

The one thing that does concern us about the FRC is that, although there are statements in the document indicating that the FRC is not to have a controlling influence on the Australian Accounting Standards Board, we feel that the influence has the potential of being greater than it may first appear. That is because the FRC appears to control the purse strings; the FRC appears to control the priorities. Quite frankly, if one does control the purse strings and the priorities, there can be a considerable amount of influence over the AASB which is supposed to be independent.

So we find some conflicting language there. There are some statements that indicate the AASB is entirely independent, but we do see some potential for that to be watered down. That is in the detail, admittedly. We agree entirely with the broad objective and we do not have any problems.

We think that the FRC should hold its meetings in public. That would be one way of overcoming this problem basically, because if it wants to rearrange the agenda for a particular purpose to influence standard setting, public meetings would create transparency. We suggest that as the way of overcoming this one remaining glitch in the system. Needless to say, the accounting body is expected to be well represented on the Financial Reporting Council, and all indications are that they will be. We do not have any concerns that we will not.

Whilst talking about that issue, I might go on about the independence of the AASB. The draft legislation sets the new AASB up as an independent organisation. As I mentioned, there is the one glitch in its independence in its relationship with the FRC. There is another issue, too, and that is the question of the involvement of the minister. We do not really question the right of the minister to be involved. We believe that the AASB, whilst being an independent standard setting board, ought to be directed by the minister, but the legislation is rather strange because there is special emphasis placed on the right of the minister to direct the AASB in relation to when it should simply copy international accounting standards.

We wonder why that is given any special treatment. We are not really querying the right of the minister to direct the AASB. If the AASB do not like the direction of the minister, I suppose the way they would handle it is that they would resign and then it would be an issue that would come up in parliament.

This special reference to the minister being able to direct the AASB to copy international accounting standards seems to be given undue emphasis. It really makes one wonder whether—when one goes right back to the objectives of the legislation—the objectives really are not to end up with ultimate copying of international accounting standards. As I said, there are problems with that.

There have been safeguards introduced. The minister is to receive a report from the FRC on the advisability of copying the international accounting standards. A structure has been put in place that the minister is not likely to direct without due consideration. We really do wonder why the emphasis is given to that point in particular.

In relation to the membership of the AASB, the bill proposes that members should have knowledge of or experience in business, accounting, law or government. We do not really argue with any of those points of experience, but we know from the past membership of the board that, if they do not have experience in financial reporting, they are dead in the water. Therefore, we think that that little slice of legislation, that is section 236B, should actually say that the members should have considerable experience in financial reporting and knowledge of or experience in business, accounting, law or government. It just does not work if somebody who is a sound business person but is not an expert in financial reporting is on that board.

The next point is the Urgent Issues Group. The Urgent Issues Group is presently an arm of the accounting bodies and its job is to interpret the accounting standards where there is a need for a common interpretation in order to get consistent treatment between companies. The Urgent Issues Group is working very well at the moment and in our consultations with

the drafters of the legislation that is pretty much acknowledged. Therefore, the idea was that the Urgent Issues Group be picked up as is and put into the new structure.

The one thing that the new structure can do for the UIG which the accounting bodies cannot do is give the interpretations of the Urgent Issues Group the force of law. If the structure is going to be picked up from the accounting bodies and put into the new structure, we would suggest that the UIG consensus views be given the force of law, otherwise there is no need to even move it, because moving it does not do anything for it that it does not already have.

The secretariat of the FRC is proposed to be Treasury. The Accounting Standards Board will have its own technical support. The restructuring will mean that the accounting bodies will no longer provide technical support through the Australian Accounting Research Foundation. Therefore, there will be a technical secretariat as part of the new structure and part of the government providing technical support to the AASB.

It seems unnecessary therefore that the Financial Reporting Council, the body above the standard setters, uses Treasury as its secretariat, because the whole idea is that the FRC be somewhat independent and be representative of business interests. So we query the advisability of the FRC using Treasury as its secretariat.

Finally, there is the question of foreign domicile companies, which is an issue that we actually have not raised before. At the present time, foreign domicile companies do not have to follow Australian accounting standards; they can follow either international accounting standards or those of their own countries. It would appear to us that it would make more sense if all companies that want to list in Australia report using the same basis and that the bases used in other countries do not make for comparability.

We are a little surprised that in fixing all of this other standard setting the idea that all companies that list in Australia ought to subscribe to the one set of accounting standards ought not be an ultimate outcome. The interesting thing is that, with all of this suggestion for harmonising, a Hong Kong company could still list in Australia and use Hong Kong standards. It seems that the proof of the pudding is in the eating—if all of this will work, we should not be allowing these rebels any more; they should all conform to the one new and workable system. At the end of the day, the fact that the legislation does not require foreign domicile companies to conform to this new structure seems a little self-defeating when the new structure is really intended to obtain this uniformity.

Those are our only points. You can see that, interestingly, we started by not quite agreeing with the broad purpose. We agreed with most of the real thrust of the legislation because the consultation has been very good, and we have got a few comments in the detail at the end. It is a strange mixture, if you like, of comments that we have had to make.

CHAIR—Thanks very much, David. Do any other witnesses want to add to the opening statement?

Mr Harrison—I would like to make a couple of very brief comments. I certainly wish to reiterate David's introductory remarks that the two accounting bodies are very close to each

other in their views with respect to this legislation. We are very supportive of the direction it is taking and are very grateful for the amendments that have been introduced following our earlier comments. So, in general terms, we would hope that the legislation will proceed substantially intact, as it is.

I think that point is important to make in the context of our criticism of 234. We do not think the wording there is appropriate. In fact, the wording seems to be almost somewhat of a contradiction to the rest of the text of the legislation. Therefore, to that extent, whilst we are critical of that wording, it does not change our views about the legislation as it is currently drafted.

Harmonisation is clearly a key component of this whole process in the legislation. We have felt for some time that the development of one globalised set of accounting standards was an imperative for the accounting profession world wide. It is our view that the best way to proceed down that route is to strengthen the IASC set of standards, though that in itself does not solve the problem. If the IASC becomes dominant, we will still have the American standards and gap to address, but that is something that will probably be better able to be addressed—though no-one can say it with certainty—once IASC standards have much greater credibility.

Therefore, the profession in Australia has been working extremely hard to improve the quality of IASC standards, and I guess we have taken a lead through the international harmonisation project to demonstrate that, if you are prepared to commit yourself to that level, then probably the speed with which globalisation of standards will occur will be improved. So there is no reservation about international harmonisation of accounting standards but, perhaps, there is concern as to exactly how quickly that can be achieved. Therefore, we have expressed reservations about the suggestion that there be adoption of—if that is the right word—or a greater role for international accounting standards. Within paragraph 9.35 there are quite specific safeguards mentioned with respect to the speed with which Australia will move and the direction the minister might give. To that extent, we are very satisfied that the recognition of the elements outlined in 9.35 will provide us with the necessary safeguards as we move down that pathway to, hopefully, lead the world in developing one set of accounting standards.

Regarding the comments about the independence of the AASB, I think everyone accepts that a standard setter should have substantial independence. The FRC has been brought in, I think, to try to provide that check and balance exercise that some have said has not been in place to date—the ability to have the technical specialists on the AASB concentrate on the technical detail that is required to set quality accounting standards but to have the FRC sitting back and looking at it in its broader perspective.

That check and balance role between the FRC and the AASB we see as important because it allows both the technical expertise to be brought to bear as well as the safeguard of some sitting back and looking at the picture in a broader context. We would not wish the independence of the AASB to be undermined by that. Our comments on the FRC are not designed to suggest that there be substantial change but just to reflect that there is an important check and balance there between the FRC and the AASB.

On the final comment about foreign domicile companies, I am not sure whether it is in this piece of legislation or elsewhere in the Corporations Law that that should be addressed. I guess we need to bear in mind that if the IOSCO endorsement of core standards for IASC goes through, that is going to take us into another phase within which companies that are listing on more than one stock exchange will probably have a greater determination as to what standards they should use through that IOSCO endorsement, if that is then picked in each of the countries that participate in IOSCO.

CHAIR—Thank you very much. Can I ask, firstly, in regard to your concern about the international accounting standards—

Mr Parker—Could I make a comment?

CHAIR—I am sorry.

Mr Parker—I wanted to pick up on a couple of points that Stephen made, and to complement the points. Australia is taking at the present time a leading role in relation to international harmonisation. If you compare us with the US, the UK, Canada, New Zealand and South Africa, no other major capital market has such an aggressive harmonisation policy. This legislation would take us further down that path to ultimate adoption, more so than the major capital markets.

Our New Zealand colleagues are also looking at harmonisation. They are planning to look at the international accounting standards as a template or the Australian accounting standards as a template. They are going to use Australian accounting standards as their template for harmonisation, based upon the fact that our quality of standards is perceived to be better in certain instances than the international ones. That came out of a conference I attended recently.

In its proposals, the government wanted to receive a report from the Financial Reporting Council about the adoption of international accounting standards by 1 January 1998. Obviously that timetable was not met because of the legislative changes and the like. The regulatory impact statement still contains, perhaps, indicators that adoption of international accounting standards is in the near future rather than in the longer term. Paragraph 2.35 refers to adoption 'as soon as possible', and there is a contradictory reference to 'in the longer term'. So as to whose crystal ball will be better when we move to an international accounting standard language, I guess we believe it will be in the longer term and that references to 'as soon as possible' are a bit misplaced.

As to the concerns over the issues of harmonisation versus adoption, the submissions make quite interesting reading and they are alluded to in our detailed submission in which we did an analysis of 48 submissions. That indicated that the Australian market was, at this point in time, happy with our moves towards harmonisation but expressed concerns about adoption. It is good to see that the legislation has a safety valve in it that says that, once we move towards adoption, the Australian marketplace must support those moves.

David indicated some of the concerns that we had about the powers of the Financial Reporting Council vis-a-vis the Australian Accounting Standards Board. The parliamentary

committee should look in particular at the submissions of the Financial Accounting Standards Board in the US, the UK Accounting Standards Board and the submission of the AASB that indicate the concerns of the national standard setters over the respective powers of the Financial Reporting Council. Some of those powers do not exist in overseas jurisdictions and one must ask why Australia should be somewhat different in the respective powers between the governing or oversight body and the standards setter.

CHAIR—Keith, do you have any comment to make?

Mr Reilly—We are very supportive of the Financial Reporting Council as a concept. That is one of the major changes over the current system that we have, where the AASB does obtain some technical support from the accounting bodies but at the end of the day is an arm of government. We do not have a financial reporting council concept in place today.

That would be seen as being a significant benefit, particularly for those who have had some concerns over particular accounting standards, and we all share different concerns at times. At least the Financial Reporting Council is there and in place to provide a degree of accountability and also to provide support to the AASB, because when you are making rules you are usually subject to a degree of criticism along the way.

The other major point that is coming out of this proposed legislation is that the AASB will meet in public. I think that will take a lot of the criticism away; criticism that often is perhaps not as well based as it should be, but at least we will be able to see how the AASB operates in terms of setting accounting standards and in terms of debate as to whether one particular method is followed as against another.

CHAIR—With regard to the international accounting standards issue, you expressed concern about what you perceive as a mandatory adoption of international accounting standards. As I read the legislation, that does not seem to be the case, because clause 233 says:

The Minister may give the AASB a direction about the role of international accounting standards in the Australian accounting standard setting system.

Looking at the explanatory memorandum, there seem to be a whole lot of qualifications placed on the use of international standards. I am just wondering whether you are overstating your level of concern. Could you be more specific about the concern?

Mr Boymal—You are quite right, Mr Chairman. One has to understand the history of the drafting. The very first draft actually said that—and these are my words—come what may, on 1 January 1999 Australia would start adopting or copying the international accounting standards. Clearly, there were interest groups who had suggested that the quicker we get to copy these things, the better for us all. In the consultative process, that was changed.

I believe there still is an objective to adopt international accounting standards, because the FRC has to specifically advise the minister on whether or not this ought to be done. So,

behind the scenes, that objective is still there, but the timing of it is no longer specific and, if the FRC never recommends to the minister, presumably the minister will never direct.

If one understands the history of the drafting, one does see that perhaps behind the words there is the long-term objective to just adopt those international standards. Otherwise, the matter of adoption of international accounting standards would not have been referred to so explicitly. Nothing else about standard setting is referred to explicitly in this legislation. So the idea of adoption is something special, and I do not think that the government would really deny that that is the long-term intention. In due course it may be the appropriate direction to take. It is just that it certainly is not at the moment. If you understand the sequence of events, you will then know where it is coming from.

CHAIR—Your concern is about what might occur in practice under what the legislation allows rather than what the legislation actually mandates?

Mr Boymal—Yes, I think that is a fair comment.

Mr Harrison—It is important to recognise the significance of paragraph 9.35 in the explanatory memorandum. That is why the profession can now feel much more satisfied and content with the legislation. Paragraph 9.35 spells out quite explicitly three factors that the FRC have to take into account in giving advice to the minister whether it would be appropriate to move to a greater adoption of international accounting standards after the harmonisation project is complete.

It talks about IOSCO endorsement in the first case of the core standards of the IASC. It particularly talks about the level of acceptance of international accounting standards in the world's major capital markets, which is a point that we have been emphasising: we should be in step with the rest of the world. We cannot afford to lead the major economies but, on the other hand, we cannot afford either to follow behind them and that, when they give that level of acceptance, so should we. Third—and this is overall from a self-interest Australian point of view—is whether the adoption of international accounting standards would be in Australia's best interest. Those three safeguards, we believe, are fundamental and certainly in the context of this legislation lead us to lend support to it because they are now quite explicitly mentioned.

Mr Parker—Those safeguards that Stephen mentioned are a very positive feature of the revisions. It is pleasing to note that they are inclusive, so there could be other safeguards that are also built in over time as situations change. Also one other safeguard that may be worthy of consideration is the Australian involvement in standard setting internationally. I am not too sure if we would like to take rules from overseas that we have not had a seat at the table on, but those rules could be crafted in over time.

CHAIR—You referred to the benefits of the AASB hearings being conducted in public, and Keith mentioned that as a benefit. You have also expressed concern about the FRC's decision making process in terms of accountability and transparency. Do you think that the FRC's meeting should be public in the same way that the AASB will operate?

Mr Boymal—I cannot see any downside in that and it would certainly alleviate concerns that the FRC is behind the scenes trying to unduly influence the AASB and interfere with its independence. Experience has shown us that a lot of the concerns about the process are not well founded—that sort of a conspiracy type of theory, that all of these secret things are going on when no such thing is happening. Open hearings will overcome that problem.

If, on the other hand, the theory of conspiracy is just moved from the standard setting board to the supervising body, the FRC, then those sorts of comments may still persevere. The simple solution would be to have both of those organisations meeting in public. Neither of them should have anything to hide. The legislation is reasonably silent on the whole funding process and the FRC is going to have to raise money from different groups in order to make this work. If any group only contributes money on condition that it gets its own way, that could really influence the process and, therefore, I personally believe that it is probably in the best interest of the whole process that both the AASB and the FRC meet in public so that we can do away with this idea of conspiracies in the process once and for all.

Mr Harrison—The explanatory memorandum, section 225, paragraph 9.2, refers to the FRC. It says:

In performing its functions and exercising its powers, it is expected that the FRC will operate in a manner that is open and consultative in nature.

I think that leads us to concluding that to do so in public would probably be the best way of satisfying that particular clause.

CHAIR—Do you see a need for both the FRC and the AASB, or do you think there is an element of overlap and duplication and bureaucracy involved in having two separate bodies? Do you think one body could perform the functions that are designated for each of these?

Mr Boymal—No, the FRC is essential. If not for the FRC, the new structure would mean that AASB would be an arm of government with no influence from other interest groups at all. Where the complaints—although we believe them wrong—are that the accounting profession has control of the process, the complaints would later be, 'The government has got control of the process.' So the complaints will have been moved, but the problem will not have been resolved.

The important thing is that—and it is from an influence point of view—the different players in the process should feel some ownership of it and the different players in the process should make a financial contribution. The FRC is important, both to get the financial contribution from all of those who have sufficient interest and to make them believe that they do have a say in it. Really, I think you might as well stay with what you have if you do not introduce the FRC.

Mr Harrison—I can certainly live with that. I think it provides the leaders of business a role in the setting of accounting standards which they could never play if they were on the AASB. The people in AASB have to have technical competence, they have to understand financial reporting at a level of detail that is quite specific, but the FRC allows business

leaders to come in and oversee that process and play their role. As I mentioned before, it is the check and balance between the technical expertise and the overall perspective of what is good for business and the Australian capital markets and capital raising that you need to have in place, and therefore the two working in tandem, I think, are essential.

Senator GIBSON—I will ask you a question about the long-term strategy with regard to international accounting standards. Are we really seeing the process whereby the rest of the world is trying to influence the SEC to end up, in effect, adopting American standards internationally, because after all it has half the capital market of the world? What do you think is going to happen in five years time?

Mr Boymal—That is a good question. I believe that, in five years, the SEC will relent and allow conforming with international accounting standards to be the prerequisite for a US listing. I think, though, that would only happen if, within that five years, something more happens to the international standards so that they are not necessarily closer to the US but they have the same level of stringency that the US has.

The problem with the international standards at the moment is that you have got a set of words there but it is damn hard to know what they mean. You have no-one to turn to, to ask what it means or to ask what the drafters intended. You cannot get answers to any of these basic questions. The IASC needs to have a structure which provides answers. At the moment, the set of words can be interpreted in so many different ways. The standards are not really satisfying the object of comparability between companies because the ability to interpret it all that differently is too wide.

That is a different situation from the alternatives that I mentioned. The alternatives are clear-cut choices: you can do it this way; you can do it that way. But then, if you cannot understand what method No. 1 means either because the wording is too loose, there you have another problem. The IAS standards at the moment are riddled with those problems, as the AASB has found, as it has tried to harmonise. So considerable improvements would still have to be made but, ultimately, I think the SEC will relent.

Senator GIBSON—Some of the cynics are saying, 'Why don't we stop mucking around and adopt the SEC standards?' What is the disadvantage of that?

Mr Boymal—Very clearly, the international community is just not likely to go along with that. As soon as you mention copying America, Europe and Japan automatically object. It is national sentiments, I suppose, and the idea of copying an international set of standards is far more acceptable than copying any particular country. If you put it in a legal context, we may copy a piece of law that is international law but would we copy the American? No way, just because it is American and we do not copy another country. The international politics gets in the way.

Senator GIBSON—You mentioned earlier the secretariat and the proposal for Treasury to provide the secretariat. I must confess I have not done enough homework to understand where the technical support is coming from. I assume your bodies are not going to provide the technical support in the future that you have provided in the past or that you are providing today?

Mr Boymal—Our understanding is that one of the major purposes of this legislation is to take the technical support from us because that is how it is said that we are too much in control of the process. We have assumed that will happen because it seems to be the starting point for the legislation. Nobody has said to us, 'Would you be prepared to provide the technical support?'

Senator GIBSON—I am surprised about that. Why not?

Mr Boymal—Why have they not asked?

Senator GIBSON—Yes.

Mr Boymal—I think because they believe that the way in which we have excessive control of the process has been through us currently providing technical support. It should not be me saying this because we would have a different argument, but our belief is that part of the purpose of the legislation is for the AASB to have its own technical secretariat and there no longer be the current agreement between the accounting bodies and the standard setters for the accounting bodies to provide technical support and, thus, we will not have this undue influence any more.

Senator GIBSON—But the accounting bodies will still be lent on to provide the dollars to run that technical support?

Mr Boymal—Presumably, yes. The extent to which we may or may not do that is still an open question. I am not saying that we will not, but the extent to which we will be called upon to do that is still very much up in the air.

Senator GIBSON—So there is still some room to manoeuvre and to tidy up how that is going to work?

Mr Boymal—Yes. These are matters of concern for us, because we employ a group of people and if they suddenly become redundant we may have costs. The explanation that has been given to us is that, until the FRC is in place, we really have nobody to negotiate this with. So we have to be patient until it is put in place.

Senator GIBSON—Are you suggesting that foreign companies working here should be set in law or that it should be left to the ASX to control?

Mr Parker—It is currently with the ASX where it allows overseas domiciled companies to list on the basis of IOSC standards or IOSC equivalents. I guess, following the logic of our argument, it should be in the province of parliament to set the accounting requirements rather than a listed company itself.

CHAIR—Concern has been expressed, which I believe is also reflected in your submission, regarding the lack of recognition of public sector accounting. In the legislation—and therefore I assume in the process of standard setting—how do you see that being redressed?

Mr Boymal—The way to redress it is quite difficult. In the earlier drafting, there was basically no reference whatsoever. Again, I need to explain this for you to understand. At the present time, accounting standards applicable to corporations have the force of law through the Corporations Law. But accounting standards applicable to other entities that are not covered by the Corporations Law are mandatory only through the rules of the accounting bodies. So we say to our members, 'If you are preparing a set of accounts that are for reporting entities or'—if you like—'for public consumption, then we mandate upon you as a member of our accounting body that you must follow the accounting standards.'

That is how at the present time the accounting standards apply beyond just the private sector. It is we who have them applied to not for profit entities, and it is we who start the process of having them apply to public sector entities. We have a separate board, a Public Sector Accounting Standards Board. Apparently the objective or the intention is to roll that board into the AASB, so the one standard setting board will be responsible for setting standards across the board. Apart from simply saying that, the legislation does not deal with that in any detail.

So far as the public sector is concerned, the various governments are the ultimate deciders as to whether the standards will be applied. So, if you are talking about a particular state, it is the state that decides. So there is a problem in dealing with that in federal legislation, of course. But I think what it means is that, in the first instance, our making the standards mandatory upon our members is still a necessary starting point, once you are dealing outside of the corporate sector. Therefore, we are very important players in the process because, whilst all we can do is kick one of our members out if they misbehave, just the very threat of it seems to work to get the standards adopted overall.

Therefore, I am really saying that I do not know what else Commonwealth legislation can do about that. The explanatory material does say that the expectation is that we, the accounting bodies, will continue to make these standards mandatory and that will be the mechanism to achieve this. But if a particular state says, 'We're just not going to conform,' we may sanction the members who are employed in that government but the government still will not do it. So it is very much a cooperative effort at the end of the day, and there is no simple solution because of the states rights issue.

CHAIR—You think it needs to go further than simply the provision in the legislation to have government and public sector bodies represented on the FRC?

Mr Boymal—I believe the intention would be that there will be public sector interests on the FRC and that, in choosing the AASB, I think it would be appropriate that there be some people with particular public sector interests there too. But our expectation is that that is going to happen.

Mr Harrison—Without the need for it to be reflected in the legislation. Paragraph 9.14 in the explanatory memorandum, I think, picks up our concerns for specific reference to the setting of standards other than those for the private sector. But I do not think we would see it as being necessary to specifically refer to those groups being formally represented on the FRC and/or the AASB.

Senator MURRAY—The relevant sections of the bill say of the membership of the FRC:

The members of the Council are appointed by the Minister in writing. The Minister may appoint a person . . .

. . . . . .

The Minister must appoint one of the members to be Chairman . . .

Then with the appointment of members of the AASB:

The Minister appoints the Chairman . . .

. . . . . .

The FRC appoints the other members of the AASB.

In other words, the minister appoints the FRC, and his appointees will appoint the rest of the members. So it is pretty well a controlled and managed body, from a ministerial direction point of view. The question is whether the legislation should be more prescriptive than it is as to who should be on there—and you have mentioned already that it says the people should have experience in business, accounting, law or government—or whether there simply should be an advisory note that the legislators would intend there to be a broad mix.

The check list I have, as a result of the discussion we have had this morning, is that at the very least you would have a mix of representation from the public sector—for very obvious reasons—from the private sector and from non-profit organisations. They are three very different kinds of bodies which need to be reflected.

What we have not discussed, but what I think is implicit, is that you would need accounting people with experience in SMEs, for instance. They would have entirely different perspectives and needs to, say, multinationals who would need to be represented. I am talking about people with financial reporting experience in those areas and possibly in the medium range of companies.

Then Mr Parker made the good point about New Zealand: if New Zealand is going to ride on our back, and if as two economies we are so integrated with New Zealand, would it be appropriate to have a representative from New Zealand there? My instinct is that it would be unwise to be prescriptive in the legislation, but it might be wise to give guidance to the minister in a note. I would like your reaction to the concept of the mix of people who should be in there, given that we must accept that they need financial reporting experience.

Mr Boymal—Yes, that is a multifaceted question. The first point is that at the present time—and this is under the legislation—we have an observer on the AASB from New Zealand, and we send an observer to the New Zealand Accounting Standards Board. This is basically part of the closer economic relations situation. I suppose it still exists, but it certainly has not been given any emphasis of late. So that is already there in the existing structure. I guess it is reasonable to suggest that, if it has been working well, why do away with it? That is point 1.

Point 2 is that the question of small and medium enterprises raises quite a hornet's nest, because it raises the question of where you draw the line about the applicability of all of the accounting standards. The standard setting process is especially designed for financial reporting that is out in the public arena. I think it is fair to say that most of the small to medium enterprises keep their accounts to themselves and, therefore, the standards do not necessarily apply to them.

But the question of where the cut-off is raises a whole series of other issues about whether the cut-off be determined on a size basis, which is in effect what the present legislation has, or whether it be more conceptual and dependent upon whether the information is of any need to other users, which is what we call the reporting entity concept. So within your question you have raised another key issue, but it probably is another topic. Basically, these accounting standards do not necessarily have to apply to small and medium enterprises because they are not reporting in the public arena.

Senator MURRAY—I understand that. But you do appreciate that often there is a flow down in terms of the standards?

Mr Boymal—There certainly is. The real difficulty we have in that regard is with information. That is considered these days to be essential in terms of public reporting for an entity that—let us make it clear—is listed or has debenture money and is raising money from the public. The level of transparency in that organisation is expected to be a lot greater than the level of transparency in a small to medium enterprise that is just minding its own business. There is a flow down, and we have a lot of difficulty in knowing where to draw the line.

At the moment there are no reporting rules for small and medium enterprises if they are not out there in the public arena. The Corporations Law says that the accounts must show a true and fair view; they must comply with accounting standards. The accounting standards say, 'These accounting standards only apply to reporting entities.' So, whilst the legislation seems to lock them in, the standards throw them out again. So all you have is the accounts being required to show a true and fair view, which is a concept that has just not been defined by the courts.

Senator MURRAY—Within your existing structure, do you have representatives of SMEs as observers, for instance, because of the flow down effect?

Mr Boymal—The AASB has a consultative group. You name the interest group, and their representative is on the consultative group. So, yes, at that level, but not observers to the standards setting meetings or anything like that. So, in the same way that other interest groups are permitted to consult, yes, but not as direct observers, no.

Senator MURRAY—Would my understanding of your response be that it would be inappropriate to consider them in any formal or even observer role in this process?

Mr Boymal—No, it is not correct to say that it would be inappropriate. I think it is fair to say, though, that it gets quite difficult, because the interests of investors in investing and

using information in the public arena is so different that our difficulty is where to draw the line.

It is not difficult to have them involved. But, at the same time, a lot of what is discussed would not be relevant to their interests, other than the extent to which accounting rules flow down to smaller enterprises. They flow down in an uncoordinated, ad hoc type of way. No rules force these accounting standards on those small enterprises, but that is not to say that they do not follow them in time. So it is a very vague area.

Senator MURRAY—In this process of appointment which really flows from the minister, earlier you made remarks about business concerns, and any concerned interest group would probably have that concern, that is, about potential capture of any board. There are two forms of capture: one is by a particular profession or interest group; and the other, of course, is by a particular flavour. I do not mean in this instance a political flavour, but perhaps a philosophical flavour.

If the FRC and the AASB were packed with traditionalists and people with an old-fashioned approach, as opposed to people with a global or international view who are interested in new accounting concepts, leading edge, et cetera, how within this process do you see the minister being capable of arriving at the correct blend of modernity and tradition and experience, and getting the appropriate range? The legislation does not attempt to proscribe that, and probably quite properly because it is very difficult to do. I would just like your reaction as to how that would happen.

Mr Harrison—In that respect, one has to rely on the fairly extensive consultative processes that are envisaged and have certainly taken place with the profession and all the other stakeholders in the development of the legislation and in dealing with the general discussion about the setting of accounting standards.

You are quite right in saying that the legislation should not be proscriptive. I do not think that is going to help at all. To ensure that there is an appropriate balance between traditionalists and those who have a more modern view between various interest groups, I think you can only rely on the person who has the ultimate authority—in this case the minister—consulting widely in taking that advice and making sure there is an appropriate balance. I do not think anyone has a monopoly on wisdom in this area. One just has to rely on that process to arrive at that correct balance in the end.

Senator MURRAY—Unless anyone else has questions, I would like one more question to follow up. Mr Harrison, on the secrecy issue, I thought the reactions from the witnesses were dead right, that it should be open and so on. I could not conceive of any situation in which there should or might be a need for secrecy in these matters. Perhaps you could indicate if there is any instance?

Mr Parker—First of all, the FRC will be making appointments to the AASB. So there will be CVs to consider and to make a choice over one person vis-a-vis another. That may well be done in private. The other matter that immediately comes to mind is that the staff are engaged by the FRC. There might be salary negotiations there that are also kept private. Those are the only two areas that I would carve out of public meetings.

Senator MURRAY—Any others?

Mr Harrison—We have argued that at some stage in the future, but not now, the FRC might take a role in monitoring compliance with standards in financial reporting. If that were the case, then I can envisage there will be situations in which the FRC should therefore meet in private as it debated whether a particular company has complied. There are precedents for this in the United Kingdom, where the panel in the United Kingdom looks at compliance and has taken very effective steps to ensure that compliance is put in place.

We are not arguing that that should be done now, but that is something for the future and, in those circumstances, I think you could imagine there will be some needs for closed hearings as well.

Mr Boymal—When the topic being dealt with is a general topic, then it is fair enough that it be in public. Once it starts to deal with particular individuals or particular companies, irrespective of what the topic might be, but away from the generic dealing with negotiations, breaches and the like, one can see justification in that not being public.

Senator GIBSON—Does the UK body publish its minutes of meetings? Do minutes of meetings come out?

Mr Boymal—I do not know the answer to that. I am sorry.

Mr Reilly—The draft legislation 236A(2) states:

> If a meeting of the AASB, or a part of one of its meetings, concerns the contents of accounting standards or international accounting standards, the meeting or that part of it must be held in public.

I think it is envisaged that there might be some parts of the business of the AASB concerning staffing, for instance, that would not be public as such.

Australia in fact has probably taken to some extent a lead in arguing that accounting standard setting should be in the public arena. However, the Financial Accounting Standards Board in the US does in fact meet in public, and the experience that we have had with our own Urgent Issues Group meeting in public is that it has overcome some of the perceptions that deals were being done in private. That is why we are quite supportive of meetings being held in public.

Senator MURRAY—I have one last question. If I understood you correctly, Mr Boymal, you said that when the minister makes a direction, if the members did not like that direction, their only recourse would be virtually to resign or kick up a public fuss. In much other legislation, if a minister makes a direction, there is an appeal mechanism in some way. Frankly, I could not conceive in this instance who you would appeal to. Rather than have people resign because they are miffed at the particular minister, can you conceive of any appeal mechanism whereby a minister's direction might be appealed before being confirmed?

Mr Boymal—I have difficulty. The area that we are most concerned about is a minister saying, after receiving lobbying from a group, 'It's time we went international. AASB, go do

it. I don't care what the FRC says. Go do it. I've got the right.' For some strange reason it is a right that is specifically written into the legislation, rather than it just being part of the minister's normal ability to influence a minister's committee.

As I explained before, some of it comes from the earlier drafting, but the ability of the minister to direct the AASB to simply adopt those international standards seems to put an undue emphasis on that particular topic by itself. Our suggestion is that perhaps that just should not be there and then we would not have concerns.

Senator MURRAY—But the parliament may consider that it should be there, in which case the usual mechanism of parliament that applies is an appeal mechanism. So the minister should have the right, because he may get impatient with a particular board or authority and may need them to get on with it.

The appeal mechanism within legislation is usually to the Administrative Appeals Tribunal, isn't it? I am not sure, given the nature of your work, that they would necessarily be a competent body. If the parliament decided that they should support the minister having the directive role, the next question is, should there be an appeal mechanism really? Rather than get you to answer on your feet on this one, you might want to give some thought to that.

Mr Boymal—Yes, we will give that some thought. We had not addressed that as a particular issue, but we will take it on board.

Senator COONEY—In schedule 2 of the reform bill in section 224 it states:

The main objectives of this Part are:

(a) to facilitate the development of accounting standards that require the provision of financial information that:

. . . . . .

(vi) is readily understandable; and

(b) to facilitate the Australian economy by:

. . . . . .

(iii) having accounting standards that are clearly stated and easy to understand; . . .

During the very comprehensive account that you gave us of the standards, you said that, at times, lawyers cannot quite follow the matters that you put to them. In discussion with Senator Murray, it become apparent that the AAT might not be the appropriate body to attend to the matter that he was raising. I understand that probably one of the reasons he was saying that was the fairly technical nature of this.

Then you spoke about the international standards, the problem that there is in reaching those and the difference that we have between the United States, Japan and Europe. Clearly, the work that the accountants do is absolutely fundamental in giving the public an appreciation of how a company may be functioning or investing.

Do you think accounting standards and financial information can be put in a way that is readily understandable, with accounting standards clearly stated and easy to understand, or do you think the best we can do is to establish your profession as one that is going to give information that can be reliably counted upon? We can understand the laws about traffic and why we say we should keep to the left. It is quite apparent. You do not need a lawyer to explain that to you. In having a heart operation, you would not understand it, but you have got faith in the doctor. In trying to achieve what the bill seeks to achieve—that is, to make these accounting standards and financial information readily understandable and clearly stated—do you think there is a reality in that hope?

Mr Boymal—The financial statements of publicly listed companies can only truly be understood by people who understand the accounting rules that sat behind the preparation of the accounts. It is a highly technical subject. For example, balance sheets do not necessarily show values. The public may ask why not. One has to understand the historical cost accounting rules to understand why.

I think the profession is trying to serve two masters. One is the highly sophisticated analyst who understands the rules, looks at the minutiae of detail and gets very important messages from the minutiae. The other is what one might call the mum and dad type of investor, the relatively unsophisticated investor, who will want to see something, some basic information—for instance, 'Has the company I have invested in made a profit or a loss?' They could not care less about the detail that the analyst finds critical. The solution to that which has actually been built into very recent legislation just passed is the provision of concise financial information for the relatively unsophisticated investors.

That concise information is not established using a different set of rules. It is simply presenting information so that unsophisticated investors can see the bare bones—was there a profit or was there not?—rather than how the detail of this profit is determined. The way in which that problem is being resolved is not to make the accounting standards more and more simple, because that is not seen to be in the interest of sophisticated investors, but to separate off detailed information in broad brush and provide the different information to the two markets.

Senator COONEY—As far as the general public goes, and I would certainly include myself amongst that, there really is not a process by which we could have accounting standards that are clearly stated but easy to understand. Would that be a difficult objective to achieve?

Mr Boymal—If we are talking about being easily understood by the general public, that is quite difficult. I am not sure that the wording meant 'easily understood by the general public'. I think it probably meant 'easily understood by the people who use the information'. That is a different issue, because if the sophisticates cannot understand it either then there is a problem. I think it is really addressing that issue, rather than the unsophisticated readers.

Mr Reilly—The particular provision in the draft legislation, which is section 224, is taken directly from existing statements of accounting concepts that have been on issue by the accounting bodies for some time. We were very pleased to see that the government actually incorporated those provisions. Before that, those provisions were not there. To some extent,

it is a bit of a holy grail but, on the other hand, it is important to make sure that the standards that are being issued, as they are today, retain the degree of understandability to someone who has some background into the issues.

Senator COONEY—It ends up in (c) by saying that the main objects of this part are to maintain investor confidence in the Australian economy, including these capital markets. I am gathering, from what you say here, that the best way of doing that is to ensure that the accounting standards amongst the profession are clearly stated and are easy for them to understand. Then the public can see that is properly and correctly done and they could have confidence. That is what you would see. If all of this was done in the public arena rather than behind closed doors and if the public could see that the matters and the processes were being properly attended to, that is how the confidence would come. It is a bit like a court of law where you might not understand the law, but if you can see it in process you can have confidence in it.

Mr Reilly—And the other important thing is that we have the urgent issues group and that is designed to provide interpretation on accounting standards. That is also a good mechanism to go back to the board and say, 'They have produced this accounting standard. At the time it seemed as though it was going to work. There are now some question marks. We are getting some feedback as to whether it should be amended.' That is the other mechanism which you have in place and that meets the public.

Senator COONEY—Can you think of any other way, other than what you have already spoken about, where you could ensure investor confidence? Perhaps not now, but if you could think of any other way that would be very helpful.

Mr Boymal—There are some other issues in connection with that. Accounting standards are not the be-all and end-all in terms of giving confidence to capital markets. Accounting standards are one of a group of things that have to go together. Firstly, you have to have the rules and that is what the standards are. Secondly, you have to have a mechanism whereby those rules are followed—a sort of mandatory nature to them—or they are just rules. Thirdly, you have to have a regulatory regime which, if you like, imposes penalties on the wrong-doers, because if you can get away with it and pay a $100 fine then you will get away with it—$100 is not enough.

You have to have a strong enough regulatory regime that really hits the wrongdoers. Even in between that, you have to have a strong auditing profession because things can go on behind the scenes. When you read accounts, a reader cannot tell; it is only the person who is allowed to look behind the scenes who will ever find it out. You need all of these things to work together well.

You could have the best accounting standards in the world, but if the auditors were not doing their jobs, if the regulator was not doing their job, if they were not made mandatory, it still would not work as a complete system. It must be a total package, and there is no way that we would ever say that the standards themselves are the be-all and end-all to solving the whole problem of reliable accounts and proper reporting. The question of whether the regulator is doing his job is clearly as important as that of whether the standards are good ones.

CHAIR—In terms of the FRC membership, I note that in the final draft there is still no mandating of nominees of the accounting bodies. Do you have a view on whether that is necessary and, if not, have you had any informal advice that nevertheless the associations will be represented? Secondly, should other stakeholders such as accounting academics and auditors be represented on the FRC?

Mr Boymal—I will answer the last part first. We would see the accounting bodies as being representative of the academics, the auditors and the preparers. So probably, so long as the accounting bodies are represented, all of the different groups within the accounting profession are being reasonably represented. As to whether we would like to see it specified in the legislation, I suppose, if we had our choice, the answer would be yes to make sure that we have a voice, but we do not have concerns that we are not going to be represented. Although we would prefer to see that, we are not concerned or worried about that because being such large contributors, both in dollars and the purely physical effort that goes in, far surpasses the dollar contribution. It is only while we are properly represented that all of that will not remain forthcoming, so we do not really have concerns that we will be excluded and, if we are, our contribution and our effort would dissipate, which would be a pity, but we do not think that that is ever likely to be the case. So, preference, yes, we would like to see ourselves mentioned there, but we do not regard it as critical.

CHAIR—There being no further questions, I thank each of you for your appearance before the committee this morning and your evidence and your answers to questions. It has been very extensive and useful for the committee.

Proceedings suspended from 10.47 a.m. to 11.06 a.m.

BROOK, Mr Bruce, Past National President, Group of 100 Inc., 170 Queen Street, Melbourne, Victoria 3000

CHAIR—Welcome. Are there any alterations or corrections you wish to make to your submission?

Mr Brook—No, but I wondered whether you wanted me to tell you just a little about the Group of 100.

CHAIR—I was going to move on to that. If there are no formal changes to the submission, I invite you to make an opening statement. At the conclusion of that, members will probably have some questions to follow through.

Mr Brook—Thank you. The Group of 100 is a representative body: it represents just over 100 organisations—listed companies and corporatised entities. It has an association with the Business Council of Australia. It is not linked in any other way but that the Group of 100 often has the same member companies and members tend to be CFOs or people heading up the accounting function in companies or corporatised entities. We would then liaise closely with the Business Council to make them aware of issues that we are covering in the accounting standards setting and corporate regulatory environment.

The Group has a National Executive which represents each of the states. There are chapters in five of the states, and the national executive is drawn from the participating chapters. The idea of the chapters is that they are very involved with members: they run training, discussion issues and workshops. All submissions that we prepare are usually handled by one of our chapters. The National Executive's role is to be the policy making part of the Group of 100, and it considers the final submissions from chapters.

We obviously take the preparer perspective. Our emphasis is on best reporting practice. We look for consistency with international practice, and the whole purpose behind the Group of 100 and its role in the accounting standards setting review of standards and Corporations Law is to aim for this best practice to get lower cost of capital so that Australia's view in the international community is one of a positive, strong, robust set of standards in a regulatory regime.

Some of the things that we have been involved with over the last few years include strong support for the international harmonisation program. That is carried through in conjunction with the Australian Stock Exchange, whereby a levy on listed companies has created a million dollar fund over two years. That program is aimed at harmonising all the Australian standards with the relevant international standards.

I work for a company—Pacific Dunlop—as do all the other representatives of Group of 100 entities. We are salaried employees of our companies. Our time and effort is put in there so that we can contribute from the preparer perspective to the standard setting process. I have also been involved with and am a member of the institute and society, and I have been on the institute's council. I am also on the ASX's Monitoring Committee. The three people on the Monitoring Committee oversee the release of funds to the Standards Board and the

research foundation to ensure that the harmonisation program is kept on track both as regards time and quality.

We support the thrust of all of the proposed legislation. We believe that it is very important that the standard setting process meets the broader Australian community needs. We obviously recognise that we can put forward our perspective, but there is a valid perspective of users, regulators, community groups, professional bodies. We see the separation—and it does not exist at the moment—between an FRC and a AASB as being highly appropriate to the governance, on the one hand, of the whole process through the FRC and, on the other, the technical capability residing in the AASB.

We believe also that the funding issue is important; it will be one of the major challenges facing the FRC. Our own view broadly is that funding should come from a range of sources, including directly from preparer groups, user groups, the professions and from government in terms of the broader public interest. We believe that generally the composition of the FRC should follow the sources of the funding.

We remain active. We see the period ahead as being one where there will be a convergence around the world of standard setting. It is really important that Australia play its part in that. Therefore, it needs that funding; it needs the best people involved on the technical side. Accounting standards, as I heard a previous speaker say, is a very important part of the whole set-up. But it is not everything. So we keep ourselves involved with issues like a form of management discussion and analysis, on which we have been working with a number of other groups. The disclosures, the rules, the regulations all come together to promote the kind of environment which we think is extremely important for corporate Australia so that, with our cost of capital in this country, we are not in any way disadvantaged. That is really what we are on about.

CHAIR—Thank you very much, Mr Brook. You indicated that you are linked in with the Business Council, and I think you also said that you had been involved with the executive of the accounting bodies. Are your links with the Business Council formalised in any way? And, similarly, does the organisation, apart from you, have any formal links with either the Institute of Chartered Accountants or other accounting bodies?

Mr Brook—Yes. The relationship with the Business Council is not a formal one; it is a relatively informal one. A few years ago the Business Council felt that it was not establishing enough expertise within its own ranks on accounting standard setting and the new developments, and it set up an accounting standard subcommittee within the BCA. We then met—this is probably seven or eight years ago—with the BCA and said, 'Look, the people that you are putting on to that subcommittee are the same people who represent your organisation on the Group of 100. Leave the two separate; we will give regular reports and input.'

For example, we summarise all of our submissions to the standards board in a bimonthly report to the BCA. We tell the BCA of the sorts of new developments that have arisen, and we tell it what viewpoint the Group of 100 has put up. So that is the relationship with the BCA: it is a flow of documentation from us to it. Also, for example, if the BCA were asked

to nominate a senior accounting person to a body, it will often talk to the Group of 100 and say, 'Well, who's got strong technical expertise?' and that sort of thing.

In relation to your other question about the accounting standard setting bodies, I was on the Victorian Council of the Institute, and that was a separate issue. The Group of 100 does enjoy sponsorship from the Australian Society of Chartered Practising Accountants. The ASCPA provides us with administrative support and, I guess in return, the Group of 100 always thanks the ASCPA but maintains a completely independent perspective on all the issues we comment on.

CHAIR—So the Group of 100 focuses specifically on accounting issues; it does not deal with broader issues?

Mr Brook—Accounting standard setting, corporate law reform, issues like management discussion analysis—those are the parameters. We do not go beyond that into trade practices, taxation or anything like that.

CHAIR—The issue of operational independence of the AASB from the FRC has been raised in evidence with us. I am just wondering whether you have any views on that.

Mr Brook—As we see the model, very definitely the FRC is there for the governance side of things. It should be the body which is broadly representative of the community—the preparers, the regulators, the users. Its role is to set some broad parameters and determine, for example, whether the status of international standards is of such a quality that the standards board should move to a replication versus a harmonisation type approach. Those broader strategic issues—the funding, the appointment of people to the standards board—would all rightly be, in our view, the province of the FRC.

The standards board should be the people with the technical capability. We do not see there being any necessity to try and represent the community again within the standards board. In the composition of the standards board, because of the expertise it would have to have in terms of private and public corporations, it would need to appoint a range of people. But they would not come with any representative capacity; they would be there because they technically would be the best people to deal with the issues that would need to be dealt with.

CHAIR—You indicated that your particular interest is on the business aspect and promotion of the business accounting standards. Given the structure of the FRC and the focus on business representation there, do you see a problem arising whereby the accounting standards will be biased in favour of the private sector and public sector requirements will be ignored?

Mr Brook—I do not know whether they would be biased in favour of one or the other. I think that is where there is a control mechanism between the standards board and the FRC. The FRC would be broadly representative and would not permit that situation to arise.

CHAIR—As you heard this morning, there is also some concern about the way in which international accounting standards might be adopted in Australia. Do you think the legislation, as currently drafted, is sufficiently flexible to ensure that we do not rush unduly

headlong into adopting international standards; or do you see there being a danger that that could occur?

Mr Brook—This question of the international accounting standards has been around for years: do we move towards the US standards, or the international standards? If we took an extremely narrow view, many of the larger companies could say, We'll simply file in the US; therefore, make life easy for the larger companies and go for US standards.' We do not think that is a realistic goal. We do not think that really reflects the broader community need.

Some time back we took the view that ultimately the politically feasible way of getting a global set of standards was to foster a global standard setting that was not tied to one particular national jurisdiction. The International Accounting Standards Committee at the time was the best possible vehicle for that, and that committee also did not have very good standards at that time. Our view back then was to support it both financially—and the Group of 100 has been giving financial contributions, not massive but helpful ones, to the IASC for some years—and by giving it technical contributions.

I think over the last four or five years the level of IASC standards has risen dramatically. Largely that has been because of the close engagement of people like the Australian Standards Board, the US and the UK, and you are seeing a convergence. To a certain extent, it does require a leap of faith that people will continue to do this. But so many people in so many countries have a real interest in this coming about that I think the timetable might blow beyond what was intended. There may be some compromises on the way, but ultimately there will be a qualitative set of global standards.

In Australia we definitely need to maintain the flexibility to determine when that time has arrived. I think the legislation, as outlined, gives the FRC the capability to make a broad determination of whether or not that time has arrived and to recommend accordingly. So that was the long answer to say yes.

Senator MURRAY—Whilst listening to you talking and probably during the evidence of earlier witnesses, I was amusing myself in remembering that America is described sometimes by some countries as 'the great Satan'. I can just imagine the accounting boards in those countries describing it as 'the great accounting Satan'. That leads me to the view that harmonisation is sometimes regarded as driving towards the lowest common denominator; in other words, something that everyone will agree with is the lowest set of standards. I think, given the statements by the previous witnesses and confirmed by you, we might have the largest common denominator working here; in other words, the United States is so powerful and dominant that we are all being pushed in that direction.

Isn't it possible that the government has merely accepted reality and that the only way in which we can internationalise our systems, as it were, is to accept the inevitable and follow, broadly speaking, other people's models, whether American or the large European models, and that really we just need to find a way to do that process as easily and as smoothly as possible? Is it really possible for a country which I think comprises one per cent of world GDP to try to retain any real independence and authority in these areas?

Mr Brook—Because we are dealing with accounting standards here, I think we are actually dealing with principles, and accounting standards really become the practical implementation of principles. A big jurisdiction like the US with a highly developed economy will have a high number of new developing trends and issues. So it will probably have a lot of expertise in, say, derivative instruments or something like that. But with globalisation all of these issues move around the world so fast that the development of the principle of how to account for it is not really tied to one nationality or another.

There is this organisation known as the G4 plus 1, which might have been mentioned—the big four countries plus one—being the international standard setters. I think it is evident that you can have a relatively small country, like Australia, in economic terms being large in terms of technical capability and the ability to formulate and articulate the way that accounting standards should be set from the principles.

There are a lot of difficult things that all of us as preparers and users do battle with. Measurement in accounting is a great big difficult issue. We are torn between our love of historical cost accounting, because it is so obvious that you have paid for something and you can write it in a book and it is concrete, versus the developing market related pricing of companies through into their balance sheets. We are conscious then of all the tensions and how this all goes through in the profit and loss. One person may be more balance sheet driven and another more profit and loss driven.

These are complex issues, they need a lot of work, and nobody actually has a mortgage on them. In that sense, the cooperative capabilities that are coming through in organisations like that, and ultimately through the IASC, I think are bringing about a regular improvement.

The one thing we as preparers in the Group of 100 have often said is that, because you are dealing with these complex issues, you can sometimes have two approaches. While we may have a preference from the technical perspective for approach A, we have often been prepared to say, 'Well, it's better to have the entire world and everybody preparing their accounts on approach B than for one of us to be in isolation on approach A and thinking that we are more technically correct but being no longer comparable.' So I think that is a reason for the globalisation.

Senator MURRAY—Senator Cooney in his somewhat indirect way I think was driving at the essence of accounting standards earlier, and that is that it is all about preventing fraud and misrepresentation. At its heart, it means that investors and those involved in business do not misrepresent the reality, as subjective as that reality may be, in the marketplace. Really, that is the essence of accounting standards. It is not a question of simply presenting the information in an understood fashion; it is so that people can understand exactly what is happening with their money. As you would know, in the United States currently there is a claim against Al Dunlop, Chainsaw Al, that he may have presided over a company by presenting the accounts in a fashion which misrepresented the reality of that performance to its investors.

Do you think the bill and its processes will in fact contribute to less fraud and less misrepresentation in the way in which it is envisaged that accounting standards will be dealt with? The other day, strangely enough, I was reading the 1986 False Claims Act of the

United States, with its amendments, which very much attends to the issue of fraud and misrepresentation. That act is deemed to have been responsible for the direct recovery of billions of dollars from both public and private sector enterprises. With these huge amounts of money, the link between ensuring that there is less fraud, less misrepresentation and that we can have greater trust in the system in fact resides in a body supposedly as technical and dry as the AASB with a vital role to play in probity.

I am not so much interested in whether it is cleaner, better understood or easier for accountants to deal with, and all that sort of stuff; I am interested in whether it will produce a system whereby our capital markets not only work more efficiently and more cheaply but in fact the potential for fraud and misrepresentation is reduced. That is what I want to know from you: whether, in your judgment, this process will contribute to that for Australia and be in Australia's public and national interest.

Mr Brook—I think it will because there are a number of structural issues that are being addressed. The present system has produced a lot of good output, but the present system requires that the AASB both govern itself and be the technical body. I think the split into an FRC and an AASB really helps to address that representation versus technical issue. That is important because it releases the AASB to really focus its attention on the clarity of the standards that it produces.

All of these rules that are formulated only work in conjunction with the rest of the apparatus—and that is the regulator, the professional bodies and a vibrant accounting community, which I think essentially we have in place. To my mind, it is that focus, getting the best technical expertise in the right place and allowing the FRC to take a broader perspective.

The AASB, because of the number of issues and developments that it has faced over the past five or so years, or for some time, has had to deal with the technical developments as well as the whole change in the way that business is being done with globalisation. So it has had to deal with the policy issue of international harmonisation as well as the technical issues of harmonising. It has not dealt, for example, with the point I mentioned—the directors' discussion and analysis, or management discussion and analysis, which we think is a really important thing. It is something which is mandatory in the United States. It is voluntary in the UK. It is done in Australia by a lot of leading companies because they are seeking to put in a best practice approach.

What we have done, in conjunction with a number of other people, is put together the guidelines for discussion and analysis. That we think really is a part of the whole of the review of operations in the financial condition of a company, and it plays a very important part in giving any investor an insight into exactly what a company does and the risks—because a lot of it is about reviewing risk—inherent in a company.

I would suggest that, if five years ago we had had in place the system that we now will have in place or perhaps will have in place, there may have been more capacity for issues like discussion and analysis to be thought about, and like concise financial reporting which I think is also extremely important to be thought about. But they have not been because of the narrower focus of a single AASB on both broad policy issues and technical issues. That is

why I think the proposals will result in a better outcome in terms of the way the rules are written, their application, the level of knowledge and the reduction of fraud and misrepresentation in the community.

Senator COONEY—In the bill at 225(2)(h), it says that the FRC's function is:

. . . to seek contributions towards the costs of the Australian accounting standard setting process . . .

and I think you were talking about that financing. Do I gather correctly that you have said contribution should be sought in terms of the ability of people to pay? What did you say?

Mr Brook—I think there should be, broadly, some correlation between the representation on the FRC and the financial support that different parts of the community give.

Senator COONEY—I think that is the sort of thing that does happen in professions. But is there not a problem there that you will tend to get the FRC skewed—and I do not say that in any evil way—in favour of people who have big resources, big companies, big international companies? May that not lead to an appearance that the standards have been written—again, not in any evil way—nevertheless to suit them?

Mr Brook—I do not think it necessarily follows. For example, my organisation represents the top 100 companies or so. These are the companies that tend to have overseas listings and all of the complexities that arise. But we are only 100 companies. So I do not think any one of our member companies would be saying that they want to give a disproportionately enormous amount of money so that we can control the process whereas further down there are thousands of other listed companies and further down from that there are all forms of other entities who, because of their number, can give relatively small amounts of money and yet make up a significant budgetary base. The entire budget for the standard setting process is not so enormous that we are looking for enormous amounts of money from different people. So I think it is likely to come to being fairly evenly spread out.

Senator COONEY—But there are two things here. The first thing is the perception—and the perception is all it would be, because I would have thought anybody on this body would do their very best according to their conscience—and you have just spoken of that perception. The second thing is the interests. Here, when I speak of the interests, I do not mean the financial interests, but the matters that concern, say, the people that you represent are different from the matters that may concern others. As a result of this, you have a council that perhaps does not address the totality of the issues in a way that is best calculated to make the act work. Has your organisation thought about that?

Mr Brook—Yes, we did. I guess that in a way we reflected upon the Group of 100, and the fact that it is representative of some very different types of organisations—manufacturing companies, resource companies, banks, et cetera. Really, the focus of the national executive, which is the policy setting part of the organisation, tends to be on best practice and long-term goals. We have in the past taken a policy initiative that probably removed a preferential treatment with which a particular industry would have gone against the particular sectoral interests of one of the industries.

We would envisage a council with the kind of broad representation that we would see it as having. So there really would be no one dominant force. It would comprise people with backgrounds drawn from right across the community and they would have the economic and financial interests of Australia at heart. Those people are going to take that longer-term, broad picture view and leave behind, when they enter that council chamber or whatever, the specific issues of their own body.

Senator COONEY—Senator Murray was asking before whether perhaps there ought to be another body—to be defined—perhaps like the AAT. The AAT is funded from consolidated revenue and, therefore, does not have the appearance that a body funded from the profession might have. Do you have any thoughts about that? If you were to have a body like the Financial Reporting Council, should there be a judicial or quasi-judicial body above that to at least see that its decisions were made according to law?

Mr Brook—I have not thought about that. I guess that the one thing which we saw as counterbalancing the need for that was the holding of proceedings of the AASB in public; we regarded that as a great step forward.

Again, I come back to saying that there are issues of principle and interpretation here. It is a question of whether you give X disclosure or Y disclosure. There is some quantitative debate between different parties about the extent, say, of a disclosure rather than any fundamental disagreement.

Most of these issues, broadly speaking, are accounting issues. They do not have the capacity to drive a lot of emotion when they are broadly in line with everybody else. The only time we see emotion arising is when one finds a particular treatment in one country and a different treatment in another country, and companies say that they are being unfairly dealt with because there is no level playing field.

Senator COONEY—Except that I think there are value judgments and standards that are involved. As Senator Murray asked you before, 'Would this reduce it to the lowest common denominator?' and you have answered that. It just seems to me—and I will raise it as a legislator—that there are some problems where a body that will be quite powerful, such as the Financial Reporting Council, is set up according to contributions from various sources. As you said—and I think it is a reasonable proposition—the contributions ought to reflect the power, if you like, of the particular bodies concerned.

The FRC can appoint members of the AASB—and I think this was raised by earlier witnesses—and that is a fairly significant power. It can determine the AASB's broad strategic direction. It can give the AASB directions, advice or feedback on matters of general policy. So it is a fairly powerful body. As we are talking about globalisation and finances around the world, it just seems to me to be a matter that ought to be looked at. Would the Group of 100 like to have a further think about that or are the people in that group satisfied with their answer at the moment?

Mr Brook—I think it is worth taking on board to think about. I am just trying to run through in my mind what the practice is in other jurisdictions. If any standard is made and it

appears to be that wrong, then some aggrieved person can always go to the courts over it ultimately, I suppose. But I do not know enough about that, and I would like to follow it up.

Senator COONEY—Talking about courts, I think your suggestion for it to be held in public so that it is all open is clearly a very significant issue. This also is a difficult one: if you say that big organisations should only have a small part in it, then I think they have a legitimate complaint when they say, 'Look, we represent those with most resources, and we should not be in this position.' You can understand that. On the other hand, if all the standards are going to be written from the point of view of those with the biggest resources, again there is a problem. So I do not know what the answer is.

Mr Brook—I think the power to have differential reporting, which is in there, is important because there will be times when you would require more disclosure for a large listed company than you would want for a small enterprise. I think that is entirely appropriate.

Senator COONEY—This is the other question I would like answered: in all good time, would it not be better simply to have it funded publicly from the public purse than perhaps for the minister to appoint the AASB? That might have problems with it too. If you could give us those answers, I would be very pleased.

CHAIR—Are there any further questions? As there are no further questions, Mr Brook, we thank you very much for your appearance before the committee and the way in which you have answered the questions this morning. With those particular issues that have been raised, will you get back to the committee in writing?

Mr Brook—Yes.

[11.45 a.m.]

PHENIX, Mr Paul, Senior Consultant, Australian Stock Exchange Ltd, Level 3, 530 Collins Street, Melbourne, Victoria 3000

SHAW, Mr Alan Joseph, National Manager Market Integrity, Australian Stock Exchange Ltd, 530 Collins Street, Melbourne, Victoria 3000

CHAIR—Welcome. Do you wish to make an opening statement to the committee?

Mr Shaw—Thank you, Mr Chairman. I just want to identify a couple of things that we are still concerned about, arising out of what has happened in the draft legislation that was recently released compared with the submission that we made on the earlier version of the draft legislation. But just before doing that, and perhaps just to identify that the ASX is a co-regulator with the Australian Securities and Investments Commission in the securities markets, our focus is on listed companies and the impact that these provisions will have on the capital markets with which we are concerned, and they are essentially the listings area for listed companies, some derivatives markets for options and warrants and so on, and clearing and settlement areas. It is important, I suppose, to note that, although we are often painted as representing the big end of town, it must be borne in mind that there are 1,200 listed companies approximately and that many of them are quite small entities.

Having said that, perhaps I could usefully identify the areas that I want to touch on and then come back and very briefly talk about them. In the fundraising area, I am interested in the coverage of warrants and the section 1031A exemption from secondary sales; in the area of director's duties, the question of the onus of proof for statutory derivative actions; in the area of takeovers, one of the conditions in particular in relation to mandatory bids and the question of whether other listing rules should be picked up in the law and not left to the listing rules to be regulated; and, lastly, in the area of accounting standards, which Paul will speak about, the international accounting standards area.

In relation to the coverage of warrants, the legislation is as per the draft legislation—that is, that all deliverable call warrants are caught by the fundraising provisions. Our submission was that the CLERP paper No. 6 entitled 'Financial markets and investment products' was a better place in which to regulate the disclosure requirements for derivative products, firstly, because it would be consistent for all derivative products and, secondly, because it seems very odd to pick up in the legislation some derivative products but to have in mind that the ASIC would grant a class order to exempt them out again while the position under CLERP 6 was reviewed.

There is at least one fragile assumption in the proposal to rely on an ASIC modification, and that is that ASIC has the power, given that the parliament will, when the bill becomes law, have specifically spoken on the subject. All the people we have spoken to in Treasury and in ASIC, so far at least, believe that the power will still exist, but of course, if that assumption is wrong, there is a problem.

A couple of particular issues in relation to the split regime include that there is a seven-day period for prospectuses under the fundraising regime, and that is a rather long period in the warrant market for not being able to issue the product. Secondly, you are not allowed to issue securities under the fundraising regime until they have been admitted to quotation, and that framework does not quite fit the warrant market very comfortably.

On the question of section 1031A of the current Corporations Law, that is a provision that effectively deems the secondary sale of securities to require a prospectus if that happens, currently, within six months of the original issue of securities. In other words, if they are issued with an intention that they be onsold, whatever documentation they are issued with is deemed to be a prospectus. That period will be 12 months under the current bill, and an existing carve-out for secondary sales on the seats system is not included in the legislation. The explanatory memorandum says that there is a potential problem that the deletion of that carve-out is solving, although it does not identify what that potential problem is and, so far as we can ascertain, it remains perhaps a potential problem but not an actual one. So it seems to be rather a step too far to completely delete the exemption.

The particular problem that we identified in our submission, which remains because the exemption was not picked up, is that the placements market will be affected in that institutions take placements of listed securities, perhaps not with an intention to resell them, but circumstances might change and they resell them within the 12-months period, and then there is a prospectus problem.

In the area of directors' duties, it was our submission, and it remains our position, that the statutory derivative action should have the onus very clearly placed on the applicant making an application to bring a statutory derivative action because, otherwise, of course, the potential for the action to undermine the business judgment rule is quite significant. In our view, that requires two things more to happen than are in the current bill: the first is that there are additional safeguards against abuse, and we set them out on pages 12 to 13 of our submission; secondly, that the interaction of section 111 (2) and (3) of what were the draft legislative provisions could be clarified. In particular in that area there was a rebuttable presumption that seemed to complicate where the onus of proof lay. In the mandatory bid area, section 614 of the Corporate Law Economic Reform Bill has a condition:

> (c) . . . from the time of the acquisition until the end of the bid period for the proposed bid, the target may:
>
> (i) issue or agree to issue securities . . . ; or
>
> (ii) declare a dividend;
>
> only if authorised to do so by a resolution . . . passed in general meeting;

It was our submission that that condition, which in fact was picked up out of the listing rules—or at least partly so, because the listing rules do not address dividends but only issues of securities—should apply to all takeover bids, not just mandatory bids. One of the complications of making it a condition only of the mandatory bid is that it might make bidders prefer mandatory bids because they get the advantage of that provision.

I indicated that there are a number of other listing rules set out in our submission under 'Other Issues' in the takeover provisions, and we would like to see those picked up as a matter of law rather than as a matter of listing rule regulation. I will ask Paul if he will address the accounting standards question.

Mr Phenix—As Alan said, the Exchange supports the harmonisation process and, through the Group of 100, we have been supporting it with, at the moment, half a million dollars, and there is another half a million coming. The reason for this dates back a number of years. The Exchange is exposed to the internationalisation of the capital markets, perhaps more so than most organisations in Australia, and the concern is that we need a common standard. When I say 'we', it is not just the exchanges that need a common standard, it is also the companies, and most of the discussion you will have heard is about companies. Also, just as importantly, it is very important for investors to have a common standard. The question is which standard to use, and there was some discussion about using American standards. I will come back to that in a minute.

In our view, the main game in town is International Accounting Standards. You would be aware that the International Accounting Standards Committee and IOSCO, the body which puts together all the securities commissions, including ASIC, the American SEC and the British FSA, have a program where the intention is to adopt International Accounting Standards for cross-border listings. There are some difficulties, as was mentioned this morning, but, basically, the bulk of the world will support these International Accounting Standards as the basis for cross-border listings.

There are some problems with the Americans. The three major bodies which do not adopt IASs in total are the FASB, which is the American body, the Japanese and the British. The reasons for this are mainly political. They are not so much to do with the quality of the standards, it is the political realities in those particular countries. Japan has a Napoleonic Code way of doing things; it does not have accounting standards as such. The British, for their own political reasons inside Europe, will continue to write their own standards mainly because the standards act as a buffer between their common law system and the EU's Napoleonic Code system. The Americans, for their own reasons, have written standards—they were the first people to start writing standards in the 1930s—and they have their own reasons for continuing to do so. It is a $US25 million business in the United States just in terms of the FASB budget. What is happening is quite clear: the standards all over the world are coming together, and you will see the common theme—the common body, the common strand—is International Accounting Standards.

The other thing to consider is the companies which use IASs. There are not any accounting standard setting bodies in most of Europe, apart from the UK and Holland. There are some being formed in Germany, et cetera, but, in the last six months, the German, Italian, French, Belgian and Luxembourg authorities have been allowing their companies to use International Accounting Standards for group accounts, consolidated accounts, which is what you and I see, what investors see, and what regulators regulate. So the day is dawning very quickly.

Look at companies which use them: Anglo-American, Bayer, Nestlé, ASEA, Hong Kong and Shanghai Banking Corporation, Deutsche Bank, Peugeot, Fiat, the World Bank, United

Nations, International Federation of Stock Exchanges, IOSCO—which is the securities commissions' organisation—and, given it was the World Cup yesterday, Adidas. Basically, all Swiss and Swedish companies have been using them for many years. Major capital markets the size of Australia—Switzerland, Holland and Hong Kong are about the same size—all use International Accounting Standards. That is one of the reasons why we have pinned our faith on this and, with the Group of 100, put some money behind it.

The thrust is that Australia should support these international standards rather than trying to do it ourselves. Firstly, the cost of doing it ourselves is horrendous, and secondly, you lose comparability. Basically, people ask, 'What are Australian standards like?' If you say, 'They're IASs,' they say, 'Fine. Not a problem.' People understand exactly. It is not just companies looking to list in the States, it is also, as I keep saying, investors. They look to invest, and they pour this through funds-managed investments into Australian companies. If they are told that they use International Accounting Standards and are audited by international accounting firms, they are basically okay.

What we would warn against is changing horses. We think that any move away from this program we have embarked on would be a major mistake. Changing horses midstream would put everything back two or three years to the detriment of the capital markets of Australia, and obviously this is our major concern. This is basically a capital-poor country, and accounting standards is one small brick in the wall which allows us to increase the amount of capital which can be raised by Australian companies.

CHAIR—From what you have said and from your submission, I take it that your main concern with the fundraising aspect of the legislation is the treatment of derivatives rather than the other issues?

Mr Shaw—Yes, I think that is right. There were a number of meetings that took place between Treasury officials and members of the listing department to sort out questions like admission to quotation and how that was to be reflected in the law, because it had never quite picked up the difference that ASX has had between listing and quotation. I notice that there is now a definition of admission to quotation that will require some change to ASX's procedures, but, at the end of the day, I think our main concern, from a theoretical and practical point of view at least, is the coverage of derivative products.

CHAIR—Do you have specific amendments to the legislation proposed that would deal with that issue, or is it a more generally expressed concern?

Mr Shaw—No, I do not. Our proposition was that the warrants should be excluded from the operation of the fundraising provisions because they are, at present, already covered by the business rules of the Stock Exchange. Once the CLERP 6 financial disclosure regime is set up, and proper integration between that and the securities fundraising provisions is established, then the right place for warrants could be determined. It might be that, at the end of the day, deliverable call warrants continue—or end up back in—the fundraising provisions but, until you have established the entire framework, it is rather curious to put them in now and hope that the ASIC has the power to exempt them while you make other decisions.

CHAIR—Before we move on, are there any questions on the fundraising issue?

Senator MURRAY—Yes. I have a broad question, Mr Shaw. I think the understanding of both the parliament and the community would be that the fundraising provisions by and large contribute to the better raising of capital—to the easier and less costly raising of capital. Does it in any way advance the ability of Australian companies to raise venture capital?

Mr Shaw—Are you identifying, perhaps, the offer information statement modifications—any in particular?

Senator MURRAY—Yes. I am really asking in a kind of indirect sense. The major issue with capital in Australia—and it is regarded quite widely—is that the greatest weakness is in the venture capital area, not in the more formal or short-term capital areas. I want to know if this bill, in your view, in any way advances that particular program and need? It does not try to deal with it specifically, I acknowledge that, but it is a major need for Australia.

Mr Shaw—I think two particular changes might assist in the venture capital area. Firstly, the clarification of the 20:12 provision. You are able to raise capital from 20 individuals. Having made 20 offers now, other offers would cause you to be in breach. That is an improvement in the position. Secondly, we did not support the offer information statement provision because, theoretically, it does not fit either a prospectus or no prospectus regime, and there were better ways to address that point. We had some concerns with the offer information statement. Problems we had pointed out have been corrected—allowing only one, for example. I think, therefore, there may be some assistance given to venture capital that wants to raise money by way of an OIS.

Although, from our point of view, the transition from being a venture capital company to becoming a listed company might be quite difficult because the listing rules require a prospectus or, if no capital is raised for three months either side of the listing, an information memorandum—which is, effectively, according to the rules that we require of it, the same disclosure standard as a prospectus. A venture capital firm that was raising capital under an offer information statement would not automatically qualify under the listing rules for a listing. Quite how we deal with that circumstance we have not yet worked out.

Senator MURRAY—I am aware that the government and probably all political parties are looking at the venture capital area in greater depth, without trying to do that job in a bill which might not be appropriate for that function. As an institution significantly involved in these issues, if you could think of any way in which any of these bills provisions may be in fact advance venture capital needs, could you perhaps advise the committee?

Mr Shaw—Yes, certainly.

Mr KELVIN THOMSON—In that fundraising area, how important is it that the disclosure of all information relevant to the future commercial plans of an organisation is revealed to shareholders in a prospectus for a right's issue?

Mr Shaw—I am thinking about how best to address that. It should not make any difference because the continuous disclosure requirements would have already required disclosure of existing plans that were complete for the disclosure in the normal course. There

should not be anything in a prospectus that had not already been disclosed to the market. In fact, while the collection of material into a single document in a prospectus is sometimes useful in itself, when we look at a prospectus we do not expect to find surprises in there because, for listed companies, we expect that anything that is in a prospectus should already have been disclosed to the market.

Mr KELVIN THOMSON—I will give you an example of what I am interested in and somewhat concerned about and of which the ASX, I think, has some knowledge. On 19 December last year, Crown told its shareholders when it was engaging in a right's issue that the company expected to commence development of what was called the proposed Southern Hotel Tower, or the second hotel tower, by mid-1998. Then the rights's issue closed on 4 February and Crown told the Victorian government, three working days after that, 'We can't proceed with the southern tower of the hotel,' but the market was not informed until 16 February. The issue here is the government being informed ahead of shareholders being informed. I guess the question is: is this a matter of concern for the ASX and, if so, how do you deal with it?

Mr Shaw—Perhaps I can answer the question this way. It is not something that is a problem in the legislation or a problem that the legislation needs to address. If there was an issue there—and I really would not like to comment on the specifics of the case—that issue would be in just when the requirement for making disclosure arose and then its interaction with the fundraising prospectus—the rights issue prospectus. There are two questions. There is a question about the continuous disclosure listing rule and there is a question about, once the information under that listing rule would be required, whether, if there was a prospectus open, that would in turn require a supplementary prospectus. Whether it would require a supplementary prospectus or not is a matter on which ASX never comments to a listed company.

There are often occasions when, in a new capital raising, for example, the Stock Exchange requires pre-quotation disclosure of something that is not in a prospectus. Our concern is essentially for the secondary market, and we require that pre-quotation disclosure without insisting that a company issue a supplementary prospectus. Our view is that whether the company needs to issue a supplementary prospectus is a decision for it and its directors. Provided we get the pre-quotation disclosure, then that is our concern satisfied.

Mr KELVIN THOMSON—In terms of the disclosure principle, if the company is making a disclosure to a state government, it ought to be making a disclosure to the shareholders at the same time, on a matter which was clearly quite important to the rights issue that it had been engaged in?

Mr Shaw—No, that would not automatically follow, in our view. The company would only be required to make a disclosure if listing rule 3.1, which is the continuous disclosure rule, required it and they did not have the benefit of the carve-out from that listing rule. The mere fact of talking to a minister does not necesssarily mean that it loses, for example, the benefit of the carve-out if we assume that the information is otherwise disclosable. But again I really do want to emphasise that I am not commenting on the Crown case in particular but as a general proposition.

CHAIR—I have a question in relation to the sophisticated investor provision whereby an offer can be made through a licensed dealer to a person that is in effect regarded by the licensed dealer as a sophisticated investor even if they do not meet the other criteria in terms of income and assets. Do you see any possibilities there for abuse or scope for abuse of the sophisticated investor provision?

Mr Shaw—I suppose theoretically that there is always the possibility of abuse, but I do not expect that the system would be abused because the ability of a company to rely on the securities dealer is really quite fundamental. The ongoing relationship between them is going to be quite important and I think the system will work for that reason. It will not be abused for that reason.

CHAIR—Moving on to the directors' duties issues, you have expressed concern about the lack of adequate safeguards to protect against vexatious actions under the statutory derivative action clause. The explanatory memorandum to the bill states:

Appropriate checks and balances will be provided in the legislation to prevent abuse of the proceedings and to ensure that company managements are not undermined by vexatious litigation and that company funds are not expended unnecessarily.

Does that meet your concerns or do you see the need for additional provision in there?

Mr Shaw—We felt that some additional safeguards could be spelt out in the legislation, as I have set out in the submission. For example, specifically the court should be able to look behind the applicant's stated motives in determining whether the applicant was acting in good faith; specifically the courts would be directed to look to other remedies apart from the derivative action as a relevant consideration, and also the onus of proof question that I mentioned before. The section in the draft bill is 237, and one of the provisions that the court is directed to look to is that it is in the best interests of the company that the applicant be granted leave. But then when one looks at subsection (3), it says:

A rebuttable presumption that granting leave is not in the best interests of the company arises if it is established that . . .

and various things happen, which essentially are that the business judgment rule has been complied with. The difficulty with that is that the only people who will be able to establish whether or not the business judgment rule has been complied with, in all probability, are the company or the directors individually.

That then caused me some difficulty knowing quite who it was who had to discharge that obligation. It is our submission that the obligation to satisfy the court that there should be a statutory derivative action should rest and continue to rest on the applicant and should not perhaps shift on to the directors to decide or establish whether the business judgment rule has been complied with before being thrown back to the applicant.

Senator COONEY—I understand and have a lot of sympathy with what you say, but you have said that the people who are likely to know the details of this are the directors themselves. If you were going to float what would be a civil action, how would you establish that if the peculiar knowledge is within the domain of the directors? Isn't what is

being said, 'Look, on the face of it, there seems to be a cause of action,' and then it is up to the directors to produce evidence which would rebut that and then the applicant has to go ahead. It is not an unusual approach. If the knowledge is peculiarly within the directors' domain, why would this be a bad thing?

Mr Shaw—I suppose the difficulty with it is that—and it may be just a timing one—the principle perhaps is right: it operates as a sort of defence to the applicant bringing a statutory derivative action. But, because it raises a rebuttable presumption, it is not clear at what time that needs to be established. So do you launch an action and then it is thrown to the directors to establish the business judgment rule, and then it comes back; or does the applicant have to make their case before the directors are even called on?

Senator COONEY—You would like that clarified?

Mr Shaw—Yes.

CHAIR—Are there any further questions on issues of the directors' duties? Are there any questions on the accounting standards?

Senator COONEY—I think this has been raised before. If you have international standards, as you see it, what real effect would Australia, Australian companies or Australian people have on them? Alternatively, are we as a country necessarily simply going to accept what others say because of our size and influence?

Mr Phenix—Perhaps I can say this fairly, as a new immigrant: Australia has been remarkably successful in the IASC, the International Accounting Standards Committee. The amount of attention paid to Australia's input is greatly disproportionate to its economic size. In fact, Australia has done very well, and hopefully it will continue to do that. Our view is that, given that the name of the game is IASs, it is important that Australia get involved at the start, from the starting gate, and is able to shape them to its own particular needs—and it has been very successful in that.

Senator COONEY—Can I take it that the ASX is confident that, if it went to an international standard, Australia would have sufficient influence to make those standards reasonable?

Mr Phenix—Sure. Standard setting is a political process. It is not so much a technical process but a political process.

Senator COONEY—That is why I am asking the question.

Mr Phenix—Once IOSCO has endorsed them, the politics inside the standard setting system will settle down a bit and, therefore, the technical ability and the persuasiveness of the Australian situation will become much more important. The trouble is—and you are right—given that it is a relatively small country, it tends to get sidelined, but it is still listened to remarkably well; it carries a lot of weight. It has a reputation for integrity and getting things right, basically.

CHAIR—You raise concern about the lack of legislative backing for the urgent issues group, although this is addressed in the explanatory memorandum. Do you not believe that the way in which it is dealt with there is sufficient? Do you believe that it needs formal recognition in the legislation? Perhaps you could expand on your concerns there.

Mr Phenix—I think the view was that it is a very successful operation at the moment. It was mentioned in the explanatory memorandum but not in the actual law. So we just felt that it should be flagged to say that we hope the UIG continues as it is. At the moment it is a statutory body of sorts. We would not want it to be just a subset; we want some kind of weight behind it.

CHAIR—Are there any further questions on accounting standards? On the issue of takeovers, do you have particular concerns about the approval of nominees in respect of takeovers, as proposed in the bill? Can you perhaps enlarge on your concerns there? You simply what that provision removed, I gather.

Mr Shaw—Yes, it is our view that the approval of nominees is a function of ASIC rather than of the Stock Exchange, for a number of reasons. As a matter of principle, matters relating to takeovers should be handled in the law and by ASIC. Also, we do not have the expertise to be able to approve the nominee in those circumstances. We are being asked to do something and required—because the law requires it—to do something, but it is not really something that is within our skills set.

Senator MURRAY—There are two separate issues there. One is whether you are appropriate to appoint the nominees—and that is a separate issue. The other one, as I understand it, was a concern that you would have no statutory protection against legal action by any aggrieved parties in that regard. I probably need some assistance from Senator Cooney, as our resident lawyer. But the ASX has a statutory role. I would assume that you would have had qualified privilege in that respect and would be protected. Perhaps I am wrong.

Mr Shaw—Yes, ASX has qualified privilege in limited respects, but it is not so much a qualified privilege question. Section 246 of the Australian Securities Commission Act, as it was—and I am not sure what provision it now is—said essentially that, for any act done by the commission or its officers in good faith, they were not challengeable. So basically on any ground, no matter what it was, provided they acted in good faith, essentially they would not be able to challenged and sued.

But the Australian Stock Exchange does not have a provision like that. So, if we are appointing a nominee and do so in some error but in good faith, there is no legislative provision, for example, that stops someone suing ASX. If the Securities Commission was to make that decision, there is a legislative protection for it.

Senator MURRAY—The follow-on is that, if the parliament and the government believed that it was appropriate for you to make a nominee appointment, you therefore would ask for the protection of qualified privilege, at least with regard to the exercise of that duty.

Mr Shaw—Yes, at least.

Senator GIBSON—In your submission you say that the panel will not be able to make a declaration of its own volition, which will limit its flexibility and perhaps its usefulness. Would you care to expand on that a bit?

Mr Shaw—The point there was that there will not be an opportunity for the panel to see that something was not going properly under a takeover and to commence the process; it is reliant on someone bringing something before it. So it takes a very passive role in the way takeovers run.

Senator GIBSON—What would the Stock Exchange prefer to see?

Mr Shaw—It seemed that it would be a useful ability for the panel, if it noticed that something was not going properly in a takeover, to be able to commence the process of deciding whether it was an unacceptable acquisition or whatever and not simply rely on the parties to enliven it. So you would have a proactive panel in takeovers.

Senator GIBSON—Is it likely the panel would have the expertise to actually do that? You are doing that yourselves, aren't you, and ASIC would be too?

Mr Shaw—I do not believe that we are a party that can bring an action to the panel. It is an aggrieved person, a target, a bidder or ASIC, but the Australian Stock Exchange is not going to be one of those.

CHAIR—Are there any further questions?

Mr Phenix—I have comments in response to Senator Cooney's question. It is quite clear to me that if Australia does not adopt ISs its position in the IASC will be threatened. I know there are countries in the Far East, where I have just come from, that will say, 'Why is this country in the board? Why is it on all these committees if it does not use ISs?' The politics of the board are like that.

CHAIR—If there are no further questions, I thank both of you for appearing before the committee this morning and for your evidence and answers to questions.

Mr Shaw—Thank you for the opportunity to come along.

[12.26 p.m.]

BOYMAL, Mr David Gary, Deputy Chairman, Australian Accounting Standards Board, and National President, Australian Society of Chartered Practising Accountants, 170 Queen Street, Melbourne, Victoria 3000

MICALLEF, Mr Frank, Senior Project Director, Australian Accounting Research Foundation, 211 Hawthorn Road, Caulfield, Victoria 3162

CHAIR—Welcome. Do you wish to make a statement to the committee?

Mr Boymal—Yes. The Australian Accounting Standards Board is generally in agreement with the broad intentions of the draft legislation. The chairman of the AASB has been frustrated for quite some time over the existing arrangement, because it leaves the AASB in a position of being a standards setting board but without control of any resources of its own. It does not employ anybody and it is dependent upon what you might call the goodwill of the accounting bodies to provide the technical resource.

Whilst the resources have never actually been withheld or rationed, nonetheless the Accounting Standards Board is in the most unusual position of being dependent upon the arrangement rather than being in control of its own resources. It certainly agrees with the thrust that the board be reconstituted and that it can employ its own people and have its own resources, rather than having to hand the bills into another organisation to have them paid on its behalf.

There are two broad areas of problem, though, as the AASB sees it. The views that I will present, you will see, are a little stronger than they were earlier this morning because the AASB feels more strongly on the two issues that I am about to raise than do the two accounting bodies. The two issues relate, first of all, to the question of adoption of IASC standards and, secondly, to the question of the independence of the new AASB from the FRC.

I will start with the IASC standards question. There was a meeting two weeks ago of the leaders of the accounting profession in Scotland and the Secretary-General of the International Accounting Standards Committee said that he is observing with great interest the existing Australian harmonisation program with international standards—the one that is going on at the moment—because it is unique in the world. I say that because you may have an impression that all the other countries are merrily going away harmonising more quickly than Australia, but that is absolutely not the case.

You hear about other countries being quoted as saying they are following international standards. The truth is they are following them to the extent that they want to. So they are following them where it suits, not following them where it does not suit. Australia is actually already at the forefront of harmonising, with hardly any exceptions. It would be wrong to say there are none, because we are coming up with a couple, but we are already leading the world in terms of truly harmonising.

The harmonisation that is going on at the moment is not copying the international standards word for word; it is using Australian lingua, but it is intended to achieve the purpose that if a company follows an Australian accounting standard then it is automatically conforming with the international. The rest of the world is looking on with a lot of interest at how we are going.

The idea, though, of copying international standards is a different issue altogether. I must say I was the Australian representative on IASC for a period of 2½ years in the late eighties, early nineties, so I can be seen to have no negative feelings against international standards, and in fact have a lot of experience in relation to them. It really was never the intention that international standards be just purely and simply picked up by corporations. The intention was that the international standards be picked up by countries.

The effect of that is that when an international standard contains a number of choices a country will choose which of the choices to take and it is not then up to an individual corporation within the country to take choice A and another company to take choice B. That was never the intention of the drafting. IASC has no jurisdiction; it cannot impose its requirements upon anybody. It is national standards setters which tell companies within their country what is to be followed.

So the IASC standards were written in such a way as to be picked up not just by individual companies but by countries' standards setters—be they the law makers or the accountants or whoever it might be who set standards—and the whole idea was that the national standards setter use the IASC standard as the starting point.

From there on, though, it depends very much upon what happens in an individual country and who the standards setter is. Sometimes the standards become part of the law and therefore they have to be written in legalese; at other times the accounting profession has complete control of them, as in Canada; and at other times it is a hybrid, as it really is I suppose in Australia.

The wording in a particular country depends somewhat upon all of these different national structural situations and also upon attitudes in the country. We know in Australia that the attitude is that if you can find a way around the law that is what you do. So the laws then get written in a certain way, not that the expectation is that people will always, if you like, do what is right, but they will do what they see written down and so you have got to be very careful in the way you write it.

International standards cannot accommodate all of these different situations. The idea of copying international standards and saying, 'There we are, that is it,' is seriously not a proposition because there are too many national or local overrides to that. But that is not to say that the international standards are not an appropriate starting point for the drafting and that is not to say that there will not be uniformity throughout the world in the application, but to copy is not a realistic proposition.

Two weeks ago, the Secretary-General of the IASC was asked, 'What does this endorsement by IOSCO really mean? It appears a little like the pot of gold at the end of the rainbow. Once the international securities commissions say, "Okay, you have got an

acceptable set of standards," does that mean all of a sudden cross-border listings throughout the world will suddenly accept international standards?' The Secretary-General of IASC said no. He acknowledged that IOSCO itself has no way of enforcing this upon its own membership of securities commissions. Even with an IOSCO endorsement, the securities commission in each country can still do whatever it chooses. There is nothing mandatory about it. The Secretary-General of IASC said that in truth the IOSCO endorsement is more symbolic than anything else.

Basically it means that the whole process, the idea of the whole world doing the same thing and all following the same set of rules and each country therefore accepting a set of accounts from anywhere else drawn up under IASC, is still a long-term objective; there is a long, long way to go. We have to ensure that Australia does not beat the gun and is the only country that says, 'Right, let's go for this,' when the major capital markets in the world are far from it. The major capital markets in the world are the United States, the United Kingdom and Japan. If you add those three up, you have about 75 per cent of the market capitalisation. You have heard from another speaker that those are the three which are least likely to be going along with this. That is basically the capitalisation of the world, so there is a long way to go.

You should also not believe that the other countries are just going to go along with it. They are picking up the international standards only to the extent that it suits them. At this meeting I was at, it was pointed out to me that a very well-known Swiss drug company, which is a household name, is also a very large investor in other companies. It purported to produce a set of accounts drawn up in accordance with international accounting standards but it did not produce segment information. Nobody is policing international accounting standards, so it just got away with leaving out segment information and yet purporting to conform to international accounting standards.

What we have is a set of international rules that is an excellent starting point for national standards setters but is not the be-all and end-all and the only way of going about the process. If the rest of the world adopts them verbatim, of course Australia should too. But if the rest of the world does it differently then Australia should take its time and watch what happens.

In trying to harmonise with the international standards at the moment—and this is getting into the technicalities of it—the Australian Accounting Standards Board is having quite a job. It is having difficulty understanding what the standards say; it cannot get answers from the IASC about what the intent is at times. The standard setters here know that to use language that you cannot really understand in an Australian context, where we know people set out to find a way around rules, would diminish the quality of Australian standards in the Australian environment to a very considerable extent.

In many respects, that worry we have found in our international harmonisation program is basically the same sort of concern that the Securities and Exchange Commission of the United States has when it is looking at the same thing and why the SEC seems somewhat reluctant. It may well be that, at the end of the day, copying the standards will be the way to go, but it is not going to be in my time as a standard setter; I am sure of that. So the question of adoption of the IASs is certainly not agreed with by the AASB. The AASB's

present program of harmonisation, which is to get the intent of those international standards built into Australian standards, seems far preferable for our environment.

The second area is the question of the independence of the AASB from the Financial Reporting Council. The AASB certainly agrees that there should be a financial reporting council because there is a need for broad oversight and there is a need to separate the detailed standard-setting process from the broad objectives. But there is at the same time a concern that the specific wording of the bill fails to ensure the technical independence of the AASB. The concern is that, if there are technical proposals being developed by the AASB that are a worry to the FRC, in the guise of setting priorities or allocating the funds the FRC will have the opportunity to have a greater technical influence than appears to be the intention. Therefore, the AASB believes that the specific terms of reference of the FRC need to be further addressed to further ensure that the technical independence of the AASB is not too greatly influenced by the FRC.

I think those points really deal with the two major concerns; it becomes too repetitive otherwise. Those feelings are quite strong on the part of the AASB. It is fair to say that when the AASB wanted to have control of its own finances and employ its own people it did not suspect that it would be wiped off the face of the earth and replaced, and that probably does introduce some concerns about transition. You have a whole set of projects that are under way and, at a point in time, all of the people working on that are potentially just put aside and another group started. How in practice that will work without some reasonable transition is still an open question.

Probably the legislation itself does not need to deal with that, but there do need to be some practical solutions so that particularly the present impetus for the international harmonisation project is not lost or delayed in the change. We do have a risk that the changeover could lose six months to a year without any difficulty if the transition was not handled very carefully. Frank, is there anything of consequence that I did not cover?

Mr Micallef—If I could just have a minute or two to try not to cover any of the ground that David has already covered but to perhaps set the record straight on a couple of important points, David has mentioned the issue of who complies with international standards at this point of time. It is an important issue because Australia should not be doing anything in isolation of what is happening in the rest of the world. Rather than perhaps characterising the present situation as there being a rush for countries around the world to adopt international standards, I would probably more describe it in the way that countries are now starting to take some note and to consider international standards when they form their own positions, which is a different thing to everybody rushing to pick up international standards. Many of the countries and the companies that are said to adopt international standards have in fact retained their sovereignty in that area and consistently use that sovereignty to override or depart from international standards in key aspects. I think that is an important fact which needs to be remembered.

It is also important to note that, whilst there will definitely be a continuing search for a set of international standards, the jury has not come back yet on which set of standards the international standards will end up being. I think the AASB has made its own calculation at this stage that it is perhaps more likely to be the IASC standards, and that is why it is

committed to the harmonisation program. It certainly hopes that it will be the IASC standards, but that is a far thing from being assured at this stage. It is not only the American standards which provide competition to that.

One of the earlier speakers, I think Bruce Brook, mentioned the G4 plus 1. That is probably a code speak to anyone except an accountant up to their neck in accounting standards, so I will try to explain it to you. It is what many people consider to be the four pre-eminent national standard setters in the world: that is, the US, the UK, Australia and Canada. We are very fortunate to be one of those. Obviously, we have a big influence on that group and, through that group, on the IASC, because the G4 is probably the most organised and respected grouping of national standard setters.

If the IASC push to create a global set of standards falters for some reason, then the G4 is an alternative route to achieving that. We already have countries like Germany seeking membership into this group. So there are other alternatives and other options if the IASC does not work out. The other thing that needs to be remembered about the IASC is that it comprises members of the accounting bodies of the different member nations—not the national standard setters, the accounting bodies. So what you have in most cases—for example, in the US and most European countries—are people turning up to the IASC and making their best deliberations but having no authority, power or relationship to take those deliberations home and turn them into national standards. So, in fact, they can walk away from the standards when they go home. In Australia, we have that relationship formally, but we have been able to work through that informally, and the accounting bodies have made sure that members of the AASB have in effect been represented as the Australian representative on the IASC. But that is very different from the situation in other countries.

There are not a lot of incentives for the national standard setters in a country like the US and the European countries and all the other countries represented in the globe to buy into and commit to the process at the moment. Unless the ISC can fix that problem, I am not sure that those countries are going to rush to commit themselves to the ISC either. The ISC is trying to address that problem, but it has a very big political problem on its hands in trying to do that, because there are many countries who want a say in what is happening and what is going to happen at the ISC. There are also the existing accounting bodies who do not want to give up their power to the national standards setter.

In many countries there is not a close relationship between the national standards setter and the accounting bodies; so there is an intra-national power play before you even get to the ISC. Unless the ISC can resolve those points, there is no surety that it will in the end be the body that is able to set international standards which will be adopted around the world, if they are going to be international standards in all manners and not just in name. That is quite important.

The thrust of all that—and I am really repeating what some others have said—is to not commit to the adoption of international standards before we can see that is the way to go. Doing so would be injurious to the reputation of our capital markets. Even less dramatic than that, but important nevertheless, it may be injurious to our powers and our influence on the International Accounting Standards Committee. The AASB does take international account-

ing standards seriously. We are undertaking the harmonisation program. We have a commitment to harmonise, which is more than most other countries have.

If everybody knows that Australia is committed to international standards, whatever the outcome, then you might hypothesise that there is less incentive for others to listen to our position. Our position, in part, comes from our strong technical background and independence and integrity on a technical front. If that is seen to be compromised, you may well ask who is going to really bother about the views of a country the size of Australia and whether we will be able to punch above our weight as we have to date.

We would be saying that, even though the explanatory memorandum to the bill talks about not moving to international standards too soon, the legislation leaves it quite open and does not provide enough safeguards, in that it needs to be examined as to whether any more safeguards can be built in. The explanatory memorandum notes that the minister may require a move to international standards and the legislation talks about the minister having to take a report from the FRC on that, but there is no onus on the minister to take any specific consideration on the recommendations in that report.

Hypothetically, the FRC could say it would be against Australia's interest to move to international standards and the minister, under the bill as it is now, could nevertheless require a move to international standards. There is no appeal mechanism and no other mechanism to review that position. So that is a major concern.

CHAIR—In terms of practical operation, how different do you see a new AASB being from the existing board in the personnel making it up and proposals that it is likely to promulgate and so on?

Mr Boymal—It is difficult for us to answer because we are not sure what influence we will have on appointments. It will probably be very little. Practicality, though, would require that, even if all of the existing board members are to go off, they should not all go off at the one point in time and leave a void in terms of past experience.

I have been on the standards setting boards and predecessor boards since 1982, which is a long time, and I am really an old hand at it. The ability to recall what the objectives or the purposes of changes were many years back is quite important to the board even to this day. That is just speaking for myself. If we were to lose that sort of experience, because the community said there were problems with these standards so those people were not much good, we would really be set back a significant period of time. A change will have to be handled with a deal of care, but I am presuming that the care will be taken. Until the FRC is in place, there is really nobody to talk to about those practicalities.

CHAIR—Given what you have said there, and the concerns that you and others have expressed about the international standards and the qualifications on the adoption of the international standards that exist in the explanatory memorandum, why do you believe it is necessary to have a stronger legislative safeguard in there about that? You have said there is nothing in the legislation that prevents the minister from directing international standards to apply, but in what circumstances is the minister likely to do that, given that all of the advice and opinions coming out of the relevant sections of the community would be against that?

Mr Boymal—I think what you say is fair comment. It would take an unusual set of circumstances for the minister to avoid the advice and then go and do something exactly the opposite. I must say, though, that there are quite strong influences for the wholesale adoption of international standards. Where did the Treasury get the idea of adopting it all by 1 January 1999? There are influences there, and I do not think that we can pretend that there are not, but I agree with the point that it would take a pretty strong lobby group to convince the minister to do something different from what the FRC has suggested.

I guess the point, though, is whether these sorts of safeguards were worth putting in the explanatory memorandum. We seem to have a whole set of additional criteria in the explanatory memorandum that you do not see at all in the legislation, and that is quite unusual. Explanatory material normally explains the legislation and does not add to the conditions and rules, yet that is what we have. So it is the structure of legislation vis-a-vis explanatory material rather than our really saying the minister is likely to do some of these things.

It is an unusual explanatory memorandum. I think it comes about because people did not like the initial drafting and additional things were put in to placate the respondents. We therefore perhaps do not have inconsistency between the legislation and the explanatory memorandum but seem to have absolute add-ons in the explanatory memorandum that you do not find in the legislation, and that is somewhat unusual.

Senator COONEY—Following on from what Mr Boymal was saying, if you look at section 227 of the 1998 bill, it says:

(1) The functions of the AASB are:

. . . . . .

(b) to make accounting standards under section 334 of the Corporations Law for the purposes of the national scheme laws; and

(c) to formulate accounting standards for other purposes . . .

That leaves it up to the AASB to do that. If you go to section 233, it says:

The Minister may give the AASB a direction about the role of international accounting standards in the Australian accounting standard setting system.

That would seem to bear out what you are saying about powers given to the AASB in section 227—as far as accounting standards go. But, where international accounting standards are involved, there is a specific provision there which enables the minister to give directions. As you say, before giving a direction under this section:

. . . the Minister must receive and consider a report from FRC . . .

So, in a typical case, the minister must take that report into account but does not have to follow it or, indeed, give it any considerable weight—just as long as he does give it some consideration. That does seem to be a very interesting way of structuring the legislation and does seem to bear out what you are saying. Have you thought of writing a report about that?

Mr Micallef—We have addressed the same concern—I am using 'we' as a staff member of the AASB, so I mean the AASB—in all of our submissions on the proposals as they have come through.

Senator COONEY—Do you know what the source for this is?

Mr Micallef—I do not think we know the source necessarily. It is probably not our place to be concerned about the source. It is a proposed piece of legislation, so we can comment on that. I guess it has to be left to wise counsel—like yourself—to analyse it and do what you will with it.

Senator COONEY—It might well be a political problem. I do not say that in any sort of derogatory sense. As you say, there are countries around the world that take political approaches to it and perhaps it is, in the proper sense of the word, a political issue.

Mr Micallef—You have to look at the whole thing. In the accounting body's submission and evidence to you earlier this morning, part of what they are trying to say is that this power and the move to international standards seem to have been singled out for special consideration in the legislation. They have their own place. The minister has powers. He has nowhere else to direct the board to move in this direction.

Given that that is the case, the question needs to be resolved as to when that power would be used, how it would be used and what safeguards there are in its use. The powers are quite wide here. The safeguards are discussed in the explanatory memorandum; they are not incorporated in the legislation at all. I do not know what circumstances might give rise to a direction. To me, it would be fairly obvious that, without that piece in the legislation, if the FRC, the general corporate community and the government were all firmly of the view that it would be in Australia's interest to move to international standards, it would be untenable for the AASB not to move that way. It would just be untenable.

Further, the minister and the FRC have the ultimate power of determining who the members are, so they can always effect change through that avenue. If the weight of opinion was firmly moving that way, I cannot see how the board could resist that. I am not sure why this particular provision is necessary. The AASB has never operated in a political vacuum—it never can—because of the nature of standard setting and rule making. As members of the legislature, you know that pressures come to bear and things cannot be done in isolation of general community opinion. It is the same for the AASB. What I and the AASB are saying is that if it has got special attention here and there are special powers here in relation to this aspect, then perhaps their use should be safeguarded.

Senator GIBSON—If section 233 were not in the bill—this is the international accounting standards and ministerial direction thing—would that remove your concern, and your second major point, David, about lack of independence of AASB?

Mr Boymal—They are related but not quite separate. If 233 were removed—which I think would be appropriate—there is another section that also deals with cost/benefit analysis. If you copy an international standard, you do not have to do a cost/benefit analysis;

if you write your own, you do. There is one other section also with a strong bias towards copying international standards—so maybe both of those ought to be removed.

To your question about whether that would solve the independence of the AASB entirely, no, not entirely, because the FRC, if it does not like different standards altogether—nothing to do with international harmonisation—could still say, 'We know where you are heading and we do not like where you are heading. It is now the very lowest priority, so it will never get completed.' There is a question of the independence of the AASB from the FRC which stands altogether separately from the international accounting standards question.

Senator GIBSON—But, on the other hand, how can the AASB—in practical terms—be made independent from the FRC when the FRC is raising the funds for it and appointing the people to it?

Mr Micallef—That is exactly right. It relates to the point I made before, that if there were broad opinion one would assume that the FRC, being broadly constituted, would reflect that and the board would not be able to ignore it. But, by the same token, especially if you had the membership of the FRC being determined to some extent, on funding for example, then there would need to be a check in place to make sure. The legislation—or certainly the explanatory memorandum—says it is vital that there should be a check to make sure that the FRC cannot determine the technical output of the AASB.

From my practical perspective as a staff member—and David will tell you from his view as a board member—the best way to stop something from happening is to change its priority, because there are always more accounting issues to deal with than we could ever get around to with our resources. If one lobby represented on the FRC did not like the way a particular standard was going, the best way to deal with that would be to change its priority and, if something is a low priority, it will never get on the actual agenda.

Senator COONEY—That cost/benefit analysis was 231 I think, Mr Boymal.

Mr Boymal—Yes. To summarise it, in international accounting standards, although these have been watered down from the original drafting, there is still a bias towards ultimate copying of IASC standards. That really is still there and the AASB is concerned about it, notwithstanding that it was certainly watered down from the first drafts.

CHAIR—Can you just clarify something for me. Under section 231(1), it says that the cost/benefit analysis does not apply where the standard is being made or formulated by issuing the text of an international standard. Then section 231(2) says that the AASB must carry out a cost/benefit analysis of the impact of a proposed international standard before providing comments on the draft or proposing the standard for adoption. Is there a conflict there?

Mr Micallef—My interpretation of what that is saying is that the cost/benefit analysis has to happen at an earlier stage in relation to the international standards or at a different stage. I think under section 1—let us say where it has got nothing to do with an international standard—you have to have a cost/benefit analysis at the stage that you are proposing the

standard, which I guess we would call 'exposure draft stage' where we go out for public comment.

Subsection 2(a) says that we would have to do the cost/benefit analysis before, for example, we have made comments on the international standard. So, if the International Accounting Standards Committee had an exposure draft and the board's normal practice was to provide input into that process—to respond—it would need to determine the cost/benefit analysis from an Australian perspective before it finalised its comments and sent them to the IASC. It might then take another six months to a year, or even longer, before we issued our own exposure draft.

Senator MURRAY—Has anyone done a cost/benefit analysis of the cost/benefit analysis? As a genuine question, what I can see happening is that to actually establish a cost/benefit analysis would require an extensive survey of the likely effects on companies. That has a time consequence, but it also has a cost and research consequence. I am one of those who very much like that approach, but nevertheless this is a privately funded body. That potentially could result in expenditure of hundreds of thousands, maybe millions, simply to do appropriate and credible analysis.

Mr Boymal—I think the explanatory material basically says you do not have to do that. There actually is something of a contradiction between the bland words of section 231, which says you do a cost/benefit analysis, and the explanatory material, which starts to water that down.

Mr Micallef—In fact, subsection (3) actually says it has only to comply with the cost/benefit analysis to the extent to which it is reasonably practicable to do so in the circumstances. That is further discussed, as David said, in the explanatory memorandum. As Senator Murray points out, and in the sort of way that he is talking about, I do not believe any standard setter in the world does that sort of cost/benefit analysis.

In fact, in some cases it would be impossible because, if you are proposing, for example, the disclosure of new information, you do not really know what the benefits will be. You have a feeling about the benefits that are going to be gained by people using that, but the proof is in the pudding in some respect. That is where, hopefully, you have the right set of members on the board to make that judgment. It is very hard to put dollars on that before the event.

Senator MURRAY—Perhaps the legislation should be qualified by stating that it is an indicative analysis.

Mr Boymal—I believe so. I actually also think that 230(12) just cannot work. Before we can comment on something to IASC—and it may be that they propose something that is utterly ridiculous—we cannot say that it is utterly ridiculous until we have done a cost/benefit analysis. So 230(12) seems to actually preclude us from saying our piece on a timely basis, when the issue may have nothing at all to do with costs or benefits. I think that section probably needs a fair amount of attention.

Senator GIBSON—Perhaps it would be useful for you to consider that and then give us advice as to what you think would be an appropriate response.

Senator MURRAY—This is just for the committee's understanding. You have told us that the big four on international standards are all English speaking countries, the USA, the UK, Canada and Australia, which might make the non-English speaking countries a little irritable. There are around 200 countries in the world. How many countries are represented on the international standards body?

Mr Boymal—The board of IASC is made up of 13 representatives. I was about to say 'country representatives', but I think at least one of those is not a country. International Financial Analysts is an organisation and not a country. So I think that makes 12 countries, plus the financial analysts.

That 12 is a shifting, moving 12; it is not the same 12 all of the time. But there are hard-core members who have been there since inception and Australia is one of those. At the peripheral, particularly with Third World countries, they come on for a period of time and then go off and another country replaces them. That is also the case with European countries. Europe, potentially, could swamp IAS but they tend to rotate on and off. It is the 12 plus the financial analysts who make the decisions.

Senator MURRAY—The parliaments are used to the provisions of treaties or conventions whereby a series or set of countries will sign up to them but, generally speaking, they are negotiated on a genuinely multilateral basis. If it is the intention of Treasury for us to rush off to international standards, can you indicate to us if, in fact, there is international support—not just of the four or the 12—for these international standards?

Mr Boymal—Generally, no. This is the problem, as Frank indicated: even when a country sits on an IAS and votes that, yes, this standard is a good thing, that does not bind that country because these were members of accounting bodies who said yes and the standard setting organisation can just thumb its nose at it. That is even for the 12.

Senator MURRAY—What about American, South American, African and Asian countries?

Mr Boymal—None of them is bound. The rules of IAS are that the member bodies, which are accounting professional bodies, shall do their best endeavours to have international standards applied. But if you are not the national standard setter, your best endeavour is to say to the standard setter, 'Hey, how about it?' But you have no power.

Senator MURRAY—If I can interrupt: I want to get a specific answer. What happens to all the Australian companies operating in Indonesia, Thailand, China and Korea? When they present their accounts for those countries, what standards are they using?

Mr Micallef—It depends. Are you asking about their financial reports here or in those other countries?

Senator MURRAY—In those other countries. One of the things that each company has to look at, from a company's point of view in terms of costs, is whether its assessment for analysis can easily be used in other countries. Part of the attraction of international standards is that that is so.

Mr Boymal—At the moment—if we can narrow the question down to the Australian companies that are listed elsewhere—not too many companies are listed on the Indonesian stock exchange and therefore it is a non-event. If an Australian company is, let us say, listed in Hong Kong, my understanding is that at the present time the Australian accounts are acceptable. Am I wrong? Maybe I shouldn't have mentioned Hong Kong.

Mr Phenix—Yes, sorry David, you should not have mentioned Hong Kong. Perhaps, Mr Chairman, I should explain that, until I came here, I was No. 2 in charge of the Stock Exchange of Hong Kong and Chairman of Financial Accounting Standards Committee in Hong Kong. Hong Kong listed companies can use Hong Kong SSAPs (Statements of Standard Accounting Practice) which are based on IASs or use pure IASs. The Hong Kong SSAPs are gradually picking up IASs as in 1993 they started an IAS harmonisation program and they are gradually picking up all the IASs. As you said, Mr Boymal, it depends on the accounting standards in those particular countries. Most far-eastern countries use IASs.

Mr Boymal—If the Australian company is listed in London, which is a large market, the Australian accounts are acceptable. If the Australian company gets listed on the New York Stock Exchange—and here is the crunch—then the Australian accounts are not acceptable, but they are accepted as the starting point. There then has to be a reconciliation from Australian profit to US gap profit and from the Australian equity position to the US equity position, which actually is not a great burden. I will come back to that in a moment.

But on top of that again, the detail of disclosures called for in the United States have to be an add-on to the Australian disclosures. They are substantial and that is where the additional cost is. So, the cost is actually not so much in the reconciling of one gap to another, but it is the additional disclosures. They are monstrous, because, if you do not have the right accounting system to extract the information right from the beginning, you have enormous difficulties

CHAIR—Does the same apply with NASDAC listings or is there a variation there?

Mr Boymal—For NASDAC listings, I do not believe you need a US gap.

Mr Phenix—There is no distinction made in the United States if you are registered with the SEC or not. If you register with the SEC, you have to follow US gap. American standards only actually apply to a small proportion of American companies. For instance, if BHP wished to be listed there, at the back of BHP's financial statements, which are IAS compatible, they would have two pages of reconciliation to the American gap. It is only if you register with the SEC, which is the commission.

CHAIR—Otherwise you do not have to?

Mr Phenix—Otherwise in the States there is no requirement for audits and there is no requirement for compliance with the American standards.

Senator MURRAY—If I may summarise what you are saying, because I think we need to move on. The adoption by Australia of international standards would make Australian listed companies more acceptable in more countries, but would not make them acceptable in all countries?

Mr Boymal—I think that is a fair comment. If I could add one thing though. If the current Australian harmonisation program is completed—and it is about two-thirds of the way there so the end is in sight—and we are in a position to say that compliance with Australian standards is automatic compliance with IAS, then even production of the Australian accounts in Hong Kong will be acceptable, not because they are Australian accounts, but because Australian accounts are automatic. Therefore, the point I am making is that the existing harmonisation program will achieve the purpose. You do not have to copy the international standards to achieve the purpose.

Senator MURRAY—And your other point is that, if you continue down the harmonisation road, you maintain your leverage and bargaining process whereas, if you automatically accept the international standards, you just become a side player. Is that right?

Mr Boymal—Yes.

Senator MURRAY—I have one more area of concern. How much does it cost to run the AASB presently?

Mr Boymal—I would have to take that on notice.

Mr Micallef—I would, too. I would not want to give the committee the wrong answer. Off the top of my head I cannot answer that accurately.

Senator MURRAY—I would guess it is at least a million or more.

Mr Micallef—It is more than that.

Mr Phenix—It is nearer $4½ million.

Senator MURRAY—Thank you for the answer. I thought it might be. The questions of transitional provisions and independence are always tied up with money. Would it be an appropriate thing for the government to consider one of two courses of action? Firstly, to always guarantee a portion of core funding, so that at its most basic level meetings could be had, people could get together, et cetera. So that, if the FRC was unable to raise funds for whatever reason, at least the body set up by statute could be maintained. I guess that might be a couple of hundred thousand just to guarantee a minimum secretariat and meetings.

Secondly, if there is to be a transitional period in which it might not be certain that the funding could continue for the FRC on the same basis that it continues for the AASB at present, the government in fact guarantees a year's worth of funding at a certain level to

ensure that the new body gets up with some weight whilst it finds its feet in terms of establishing a fund raising system?

Mr Boymal—I believe that that probably is appropriate. There are further problems though, and that is that the standard setting process has to have some certainty in relation to its funding. If the FRC is simply going to ask interested groups for donations, if the interested groups have a bad year, what happens to the donation? If the interested groups do not like the product, what happens to the donation? You can imagine the process will have an element of uncertainty to it.

At the moment, there is certainty because the amounts that the accounting bodies are putting in is a sum certain. The amount that the government is putting in is a sum certain. The amount that the large corporations through the Stock Exchange is putting in is a sum certain. We know within what sort of budget to operate. We cannot write standards in the hope that people will pay later. It just will not work.

Senator MURRAY—I would like to request that you do the following, if you would. You are the only body with experience as to what it costs to run these things. I think the committee would welcome an indicative budget for the new body, if it was to proceed similarly to the previous body. You must have a historical cost basis to do that, so hopefully it is not too much of an imposition. Secondly, in your view, the minimum core funding necessary for the government to at least abide by its statutory obligations, which to my mind would be at least to indulge it in the international liaison and that sort of thing.

Mr Boymal—Yes, I will undertake on behalf of the AASB to do that. I would venture that for the organisation to be at all productive, we are talking about sums much greater than a couple of hundred thousand.

Senator MURRAY—Yes.

Mr Boymal—To keep it doing something, rather than just sitting doing nothing.

Senator MURRAY—Yes, but the committee cannot recommend to parliament that it should pass legislation if the fulfilment of a statutory function is entirely dependent upon fundraising for which there is no guarantee that that will be present. We could, but we have not imposed a levy on the ASX or anybody else. We would need to know those figures.

Mr Micallef—We will undertake that.

Senator COONEY—If you look at section 225(2)(c), it is up to the FRC to approve and monitor the AASB budget, business plan and staffing arrangements. You are in the difficult position of trying to ascertain what your ultimate budget will be, because it has to be approved by the FRC. Your staffing arrangements have to be approved by the FRC.

Mr Boymal—Indeed. With our experience in standard setting, we certainly have the historical information of how many people have been needed to be employed to run the program up and until now. It gives a fair indication of what the scale of the ongoing will

have to be. We do have a lot of information that has to be a first indication of the budget setting for the FRC.

Senator COONEY—Yes, but what if the FRC cuts you? I suppose there is not much you can do about that, is there?

Mr Micallef—The FRC is effectively the board of directors, if you make an analogy with a company. The FRC is the oversight body and it would be doing that after making a judgment that that was appropriate. I do not think that causes a problem in itself.

For example, if the whole world moves in the next two years to adopt a set of standards—whatever they are—and we really do not need as much standard setting capability, it would be fair enough to make fairly drastic cuts to the AASB's budget. You would not expect the FRC to cut the budget unless the circumstances were appropriate, because effectively it is cutting itself.

Senator MURRAY—And at the same time the other interested groups have been saying they want a greater influence. The accounting bodies have said, 'Okay, we understand that; we do not want to be the only contributors.' So the expectation out of this restructure is that there will be more money available than is currently available because there will be more players in the game and, irrespective of just how the new players do make a contribution, the expectation is that there will be a greater contribution than there currently is because very few of them make any contribution at all. So the whole idea is that more resources ought to be available in the new structure than currently exist. But you do not actually find that spelt out too clearly.

Mr Micallef—One anticipates that, in trying to seek a broader base of funding, the FRC would explain to people that certainty of funding is fairly important and they will try to at least get some kind of commitment on more than an annual basis from those who do commit to funding.

Senator COONEY—It will be interesting to see how it ultimately works. It has got to monitor whether or not international accounting standards are developing and develop the AASB in broad strategic directions. There are interesting times ahead, I suppose.

Mr Micallef—Certainly.

CHAIR—Any further questions? If not, can I thank both of you for appearing before the committee and answering our questions.

[1.33 p.m.]

BROWN, Mr Robin Michael Gwynne, 12 Denman Street, Yarralumla, Australian Capital Territory 2600

CHAIR—I now welcome Mr Robin Brown. Do you wish to make any alterations or additions to your submission?

Mr Brown—I think what I will be doing is adding a few comments and perhaps—

CHAIR—Yes. That will come in your opening statement. There is nothing specific to change in—

Mr Brown—In the written submission, no.

CHAIR—I invite you to make an opening statement, at the end of which we may have some questions for you.

Mr Brown—I am not aware that the committee has heard from consumer representatives to date. I am not sure whether that is the case or not. I have been involved in the consumer movement, as you will have noted from my submission, but I am not here representing any consumer organisation. I have actually tried to determine the views of consumer organisations in relation to these matters, but without a great deal of success. But I do not think that the views that I am expressing diverge greatly from the views held by consumer organisations.

A bit of water has flowed under the bridge since I made the submission, so I think that some of what I said in the submission is not entirely apposite any longer. My submission, I think, clearly expresses my greatest concern that the overall consumer protection regime which we have enjoyed in this country for a number of years is under some threat, if you like. I think the Trade Practices Commission, and the ACCC since then, and the Trade Practices Act have been viewed by consumers in Australia as operating to the great advantage of consumers in general, and I think we are envied by a number of other countries around the world in this respect.

I think quarantining part of the economy from the reach of the Trade Practices Act and the monitoring and regulatory activities of the ACCC is, in principle, undesirable. I would like to think that, with a little time in the future, that could be looked at again.

I do understand the arguments that were made in support of those changes or those moves. My main point there is that I would like to see the committee noting that there is some concern expressed and that, in the future, a re-examination of the exclusion of certain elements of the Trade Practices Act be undertaken. I do not think I need to go into the other arguments that I have written down in support of that general position and principle.

There are some things that I think could be looked at and should be looked at in the near and immediate future which are a consequence of the changes in legislation in the regulatory regime. As I understand it, insurance as a class of transaction is now, in general, beyond the

reach of the Trade Practices Act or, certainly, aspects of it. I am not sure that that is entirely intended. I think that there may be certain kinds of insurance that still should be under the purview of the ACCC that the ASIC would not necessarily want to be dealing with and perhaps could not effectively deal with.

I also understand that it is not clear that now foreign exchange transactions are adequately covered. I further understand that the recent amendments to the Trade Practices Act in relation to unconscionable conduct as it relates to small business are not reflected in the new legislation. I ask that the committee have a look at those areas of concern.

Given the regime that we now have, I think that there are some things that the committee could consider to make the ASIC the kind of effective consumer protection regulator that it should be. One is that it should have powers to mandate and enforce codes of conduct. It has the function of approving and monitoring codes, but it does not have a provision for mandating codes. There is not a provision that would allow the ASIC or any other body to take action for breaches of codes as there is under the Trade Practices Act in section 51(d).

I think also the ASIC needs to be patched in as well as the ACCC was, or still is, with the overall regime of consumer protection in the country. In other words, it needs to be setting itself up to work closely with state and territory consumer affairs bureaus. It probably needs to have some formal operating agreements between itself and those agencies.

As part of that, I think the ASIC should be represented at various Commonwealth-state regulator forums that try to coordinate consumer protection throughout the country—for instance, the standing committee on consumer affairs and the fair trading operations advisory committee. At the same time, it should be involved internationally with developments in consumer protection policy at the OECD level and in a thing called the International Marketing Supervision Network.

I would also like to see the ASIC have regular formal and informal liaison arrangements with citizens consumer organisations. There may be some sort of a consultative committee at which consumer representatives could advise the ASIC and learn better what it is on about and so on.

I have said in the written submission that I thought that the ASIC should have a commissioner who had particular experience and expertise in consumer protection. The kind of consumer protection that the ASC has done in the past is different from the kind of consumer protection that it is going to have to be involved with in the future. This is because of the profile of the consumers that the ASC was seeking to protect. It is now going to have to worry about a much wider range of types of consumers, and I do not think it has necessarily at the moment got the expertise to do that, and I think that expertise should be reflected at commissioner level.

In addition, I am not satisfied that the ASIC has a clear enough guideline, requirement or ability to undertake research to consider further reform of the law, to undertake education and compliance functions in relation to consumer protection issues.

Finally, I want to turn to the role of industry dispute schemes—non-formal industry dispute schemes or quasi-regulation as I think it is now called. I understand that the idea is that the ASIC will rely fairly heavily on these non-formal industry dispute schemes to deal with individual consumer complaints. I do not think that is a bad thing in principle, but I think the capacity of those schemes is open to overestimation, having been involved in setting up a couple of them and having been directly involved in the running and operation of a couple of them. They do a pretty good job, but I think they have got quite a way to go. I think that there could well be a gap between what the ASIC does and what these industry schemes do.

I have made the suggestion to the committee that it should now consider pushing for the establishment of a comprehensive financial services industry ombudsman scheme. I imagine that there is a well-founded economic argument that different dispute resolution schemes can be a factor of competition amongst different parts of the financial services industry, but I think in practice ordinary consumers would not factor those things into the competitive decisions that they make. I think there are stronger arguments in favour of a comprehensive financial services industry scheme. It would need to be a scheme which had specialist elements to deal with various particular parts of the financial services industry.

The fact is that the schemes that we have at the moment do vary in a number of respects. They vary in their structures, in their procedures, in the standard or level of assistance that consumers get in prosecution of their complaints and in the sorts of complaints that are covered and those that are not. It was very satisfactory that recently the banks decided to give the banking ombudsman scheme coverage of all small enterprises, whether they are incorporated or not, so it has now moved towards what some of the other schemes already did.

As long as there are these separate schemes—on paper—for separate elements of the financial services industry, we are going to have confusion amongst consumers. We are going to have complaints that fall in gaps. We are going to have problems because we are going to have bundled products and you are not going to know whether it is a product that the banking ombudsman scheme or the life insurances scheme should look after, or whoever it might be. So I would strongly urge the committee to consider whether it could and should push for a single financial services industry ombudsman scheme.

CHAIR—Thank you very much, Mr Brown. Your concern seems to be about the lack of expertise within the ASIC to deal with consumer issues in relation to securities investments. My understanding is that a section of the Trade Practices Commission or the Australian Competition and Consumer Commission that deals with this area is in effect being transferred across to the Australian Securities Commission to handle those issues. Are you aware of that?

Mr Brown—That is not my understanding, but if that has happened then that is gratifying.

CHAIR—That is what I understand Alan Cameron in our last hearings indicated. If that happens, that would address your concerns?

Mr Brown—In part, but I think it is also important that there be leadership at the top of the commission. I think a commissioner that has particular expertise and background would still be very desirable.

CHAIR—You made the comment in your submission that an industry regulator can become too closely aligned with the industry interests at the expense of consumers. Can you give examples where that has happened?

Mr Brown—I do not know whether I can give specific detailed examples, but I think that the Insurance and Superannuation Commission was a body that carried out its functions and took its prudential functions pretty effectively, although I do not think it did a particularly good job as far as consumer protection was concerned. That was in part, I suppose, because the prudential problems had much wider implications and so its attention was perhaps rightly diverted to those. But I think it would be widely felt amongst consumer organisations that it was a little overly concerned with the financial health of insurance companies and not adequately concerned with the position of individual consumers dealing with those companies. There were a number of issues that it did not deal with adequately which were in fact picked up and dealt with by the Trade Practices Commission as it was then. For example, the work that the Trade Practices Commission did in relation to sales of insurance to Aboriginal communities was quite inappropriate. I think that is an example of a regulator that was not able to see the wide perspective that it should have.

CHAIR—I suppose that depends on its terms of reference and what it is required to do. It may well argue that, if it is looking after the health of the insurance companies in terms of their prudential arrangements and so on, that in effect is protecting the consumers who have policies with any of them.

Mr Brown—Consumers want insurance companies to continue to exist so that they can pay their claims. That is clearly important. But it did have the other function and I do not consider that it performed that other function adequately. That is history now and the new arrangements are very satisfactory in that we now have a single regime. Time might prove my fears quite unfounded, but I think in principle a regulator that is concerned only with one industry is not desirable. It would mean it is concerned with one industry when there are not measures to keep it aware of what is happening in industry in general. It could not ensure that the way it regulates that industry is equitable and not anticompetitive in relation to industry in general.

I am not suggesting that it is not appropriate for there to be a specific industry regulator, but I am saying that it would be more appropriate for the industry-wide competition and consumer protection regulator to continue to have a formal role so that we get the best of both worlds and you can overcome the problem of duplication, as was my experience when I was on the board of Austel, through operating agreements between the two agencies. I think you can provide adequate certainty to industry players by that mechanism.

Senator MURRAY—It is not so much a question as an observation that it is appropriate for every regulator to have a consumer bias. Your response, Mr Chairman, was that they do. Even when the Reserve Bank lays down minimum deposits and capital adequacy rules for banks, the desire is to protect the consumer, the depositor. I am all for the spread of

consumer ideology amongst the regulators. The question is whether, as the chairman properly outlined, the terms of reference and the funding accompany that obligation and the culture that is there. Our impression from Alan Cameron, the Director of the ASIC, is that he does intend to drive up the consumer side of their business. As you rightly pointed out, we will have to wait and see whether it develops appropriately. I must say I would prefer everything not to reside in one regulator or another; I would like to see the culture go right across.

Mr Brown—I have no doubt at all about Alan Cameron's intentions. It is a question of being able to understand the kind of position that an ordinary consumer is in in dealing with a large financial institution or the agent of a financial institution. It is not an easy thing to do to put yourself in that position unless you have been exposed to those sorts of complaints that people have and you have dealt with those sorts of complaints over a period of time. I would like to see people that have that experience directly involved in the ASIC.

Senator MURRAY—I think that is so.

Senator COONEY—Following on from what Senator Murray was saying, have you got any concept in mind how the ombudsman would operate? As I understand it, you want an ombudsman that would look at the whole range of financial services.

Mr Brown—Yes.

Senator COONEY—There is no problem constitutionally about that?

Mr Brown—We are talking about grey letter law, or whatever, here. I do not think that there is a constitutional problem. If there is, then we have already got it with the ombudsman schemes that we have got at the moment.

Senator COONEY—You have got the banking ombudsman, there is no problem about that. I think that in fact is set up by the banks. Did you have an intention that the ombudsman would be set up by the financial institutions themselves?

Mr Brown—Yes. Perhaps as a result of a licence requirement, and that is what we do with the Telecommunications Industry Ombudsman. The telecommunications companies, if they are to be given a licence, are required to agree to be part of an industry ombudsman scheme. Perhaps there is a constitutional problem, but so far I do not think it has been challenged.

Senator COONEY—Telecommunications is all right, because that is specifically federal stuff. I think your idea is great, but I was just wondering whether you had teased it out at all, because I think there is a spread of powers over financial institutions between the state and the Commonwealth. I am very interested in it and I was just wondering whether you had worked through it at all. Perhaps you could just have a think about it.

Mr Brown—Yes. Most of the institutions we are talking about are already regulated at the federal level anyway, aren't they? For those that are not, there may well be—

Senator COONEY—Would you include such things as pawnbrokers and things like that?

Mr Brown—I have not thought about the detail. It may well be that you would need state governments to agree to hand over the relevant power here.

Senator COONEY—I think it is a good idea. One of the problems people have is not specifically with finances but where you have got a complaint—say, an injury and you want some sort of compensation for it. You go to the Department of Social Security or to a workers compensation insurer or what have you, and that division is a real problem. If you had one ombudsman that could look after all that, it would be very helpful. I thought the idea that you had that you would have an ombudsman looking after all the financial problems that people might get into was a good one. I am just wondering about the structure of it all.

Mr Brown—Not all the financial problems but all the commercial financial services that they take now.

Senator COONEY—Yes, you are right.

Mr Brown—In respect of pawnbrokers, what it would probably require is that the state licensing authority would issue a licence to a pawnbroker with the requirement that that pawnbroker be part of a national financial services industry ombudsman scheme. That is the device that you would use. At the end of the day it is going to require the industries that are involved to agree to do this, because if they do not agree to do it they cannot be forced to do it since you would then have constitutional problems. I think that moral persuasion could be quite powerful enough.

CHAIR—If there are no further questions, I thank you very much, Mr Brown, for appearing before the committee, for your submission and for answering our questions. That concludes the hearing. I thank committee members for their attendance.

Committee adjourned at 2.00 p.m.