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JOINT COMMITTEE ON CORPORATIONS AND SECURITIES

Reference: Statutory oversight of the Australian Securities and Investments Commission

THURSDAY, 14 JUNE 2001

SYDNEY

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JOINT COMMITTEE ON CORPORATIONS AND SECURITIES

Thursday, 14 June 2001

M embers: Senator Chapman (*Chair*), Senators Conroy, Cooney, Gibson and Murray and Ms Julie Bishop, Mr Cameron, Mr Rudd, Mr Sercombe and Dr Southcott

Senators and members in attendance: Senators Chapman, Conroy, Cooney, Gibson and Murray

Terms of reference for the inquiry:

Statutory oversight of Australian Securities and Investments Commission

WITNESSES

Committee met at 9.12 a.m.

CHAIRMAN—Today the committee is conducting its public hearing into the Australian Securities and Investments Commission. The parliamentary Joint Statutory Committee on Corporations and Securities is required by statute to oversee the functioning of ASIC. This hearing is part of that oversight process.

Before we commence taking evidence, may I reinforce for the record that all witnesses before the committee are protected by parliamentary privilege with respect to the evidence they give. 'parliamentary privilege' refers to the special rights and immunities attached to the parliament, its members and others necessary for the discharge of parliamentary functions without obstruction and fear of prosecution. Any act by any person which operates to the disadvantage of a witness on account of evidence given by him or her before the Senate or any of its committees is treated as a breach of privilege. I also wish to state that, unless the committee should decide otherwise, this is a public hearing and, as such, members of the public are welcome to attend.

[9.13 a.m.]

DIPLOCK, Ms Jane, Executive Director, Infrastructure and Strategic Planning, Australian Securities and Investments Commission

DRYSDALE, Mr Mark, Executive Director, Public and Commercial Services, Australian Securities and Investments Commission

JOHNSTON, Mr Ian, Executive Director, Financial Services Regulation, Australian Securities and Investments Commission

KELL, Mr Peter, Executive Director, Consumer Protection, Australian Securities and Investments Commission

KNOTT, Mr David, Chairman, Australian Securities and Investments Commission

MACKINTOSH, Mr Ian, Chief Accountant, Australian Securities and Investments Commission

SEGAL, Ms Jillian, Deputy Chair, Australian Securities and Investments Commission

TREGILLIS, Mr Shane, Executive Director, Policy and Markets Regulation, Australian Securities and Investments Commission

WOOD, Mr Peter, Executive Director, Enforcement, Australian Securities and Investments Commission

CHAIRMAN—I welcome the witnesses from the Australian Securities and Investments Commission. Do you wish to make an opening statement?

Mr Knott—No, Chairman. If one or two matters are raised, we will have statements to introduce other commentary. Generally we have no opening statement.

CHAIRMAN—We will move to questions then.

Senator MURRAY—Mr Knott, good morning to you.

Mr Knott—Good morning.

Senator MURRAY—The briefing notes I have here state in the second paragraph:

ASIC is an independent Commonwealth government body established by the Australian Securities and Investments Commission Act 1989.

What constraints are there on your independence?

Mr Knott—We are by law subject to direction in appropriate cases. You would be aware of that part of the law.

Senator MURRAY—From the Treasurer?

Mr Knott—Yes, the minister. Apart from the normal accountability that we have through this committee and others and that power of direction, our independence is generally unfettered.

Senator MURRAY—With regard to your own independence, what is your security of tenure? What is the length for which you are appointed?

Mr Knott—I was appointed for a five-year term.

Senator MURRAY—Do you in any sense report to the Secretary for the Treasury?

Mr Knott—No, I do not report. We do, of course, deal quite extensively with the Treasury, particularly in relation to policy matters, but we certainly do not report to the secretary.

Senator MURRAY—So he would have in no sense the same sort of jurisdiction over you and your commission as he would have over his department?

Mr Knott—That is correct.

Senator MURRAY—I assume that you are requested or sometimes required, probably most often requested, by the minister to provide advice to him on issues. Does the Secretary to the Treasury also sometimes request you to provide advice to the Treasury on policy matters which affect your areas of jurisdiction?

Mr Knott—The best example would be progressing legislation and draft legislation from a policy stage through to legislation. In that context, we quite regularly provide advice or comments to the government through the Treasury.

Senator MURRAY—Does that mean that once you are requested to do that—having given them such advice—you are then constrained or prevented or in some way quarantined from reusing that advice, which is obviously private in the normal sense, as we understand it, of interaction with government? Are you constrained from using it in a public sense? Do you get a peculiar situation where you may take a view on some matter—naturally, it is a matter of public interest—and you provide that view to the Treasurer or the Secretary to the Treasury and then you are cut off from pursuing it afterwards?

Mr Knott—It depends a little on the circumstances. If a draft proposal is out for public comment, it is unusual for us to make a public comment. However, once a proposal has gone through that stage and has effectively become government policy by being represented in a bill, for example, we would not generally comment publicly any further.

Senator MURRAY—If it remained, however, a matter of public interest—and I would think that, generally speaking, those things that you are asked to give advice on are continuing issues; I would doubt that they would fall away often—would you feel, as an independent commission and as a person with independent tenure—at least for five years—at all constrained in pursuing it in other ways, if you felt, from a public interest perspective, that you should?

Mr Knott—Where issues are of concern to us and we have gone on the record with them and expressed our viewpoint, we have to recognise that governments may form a different view. Parliament may form a different view on a particular issue. Our responsibility in those circumstances is to accept that and implement the law.

Senator MURRAY—You know, as we do, about your statutory relationship with this committee. We have a function which is different and distinct from a normal committee. You have a relationship with us which is different and distinct from, say, your relationship with an estimates committee. Would you feel constrained, if you had been providing policy advice to either the Treasurer or the Secretary to the Treasury, in discussing those matters with this committee, even, if necessary, in private hearings and not necessarily in the same form? Is there any sense of quarantining your opinions?

Mr Knott—We would always attempt to be open and frank with this committee and, indeed, all committees of the parliament. I can envisage situations where we had put a point of view—we were publicly on the record as having that view, not walking away from that view—and it may not have been adopted as government policy. In those circumstances I do not think it would be helpful for us to be maintaining a strong public stance when our view has clearly been articulated and the government has reached a different position. It is all on the record and open for people to see.

Senator MURRAY—But there might be the odd position—I suppose 'odd' is the wrong term—where the parliament in its voting capacity might agree with your public position even if the government of the day rejects it.

Mr Knott—That has probably happened. I think in the past there have been cases where ASIC has stated a position, the legislation has proceeded down a different road and the parliament, as the legislation has proceeded, has made amendments which may or may not fully have adopted an ASIC position but might be closer to the ASIC position. So I think that can happen from time to time. It is not common I think.

Senator MURRAY—You would appreciate that is one of the reasons I am pursuing this line of questioning. The government is favoured in its advice from a professional body such as yourselves and so is the parliament, and we would be influenced. Indeed, Senator Conroy and I were influenced in the recent matter of accounting standards by opinions that ASIC and other bodies held. So I think it is important, through this committee in particular, that we are informed.

The area I want to pick on, where there may be some dissidence, is that of resources. It is the duty of the government of the day to give you what they can afford and what they think you need, and to make the hard decisions. That is so for any government. You would have your own view on the resources necessary to do the job that you do, but I think increasingly there is pressure on all of us from the community which wants regulators to do a bigger job than perhaps the government, parliament or even regulators foresaw. APRA is the most recent example, but Ombudsman officers have those pressures and there is a limited pot of money. How constrained do you feel in expressing an opinion about whether resources are inadequate to do a particular job?

Mr Knott—It is not so much feeling constrained. I think it is a matter of judgment about when it is appropriate to be airing those issues publicly and when it is more appropriate to be pursuing those issues privately with the government. One must form a judgment about the likely outcomes. I am quite happy to discuss this matter specifically. My predecessor, in the annual report that we are here this morning to discuss, I think made some quite frank observations about pressures faced by this agency. Last week Ian Johnston made it clear to another committee that we are stretched. Since these original comments were made we have gone into a new market environment. There are additional matters of some complexity, and that are resource intensive, which have added to those pressures.

I think there is a general understanding that we are under resource pressure. We are about to embark on a pricing review with the department of finance in the second half of this year, which we are hopeful will result in a reappraisal of our resourcing. That is the forum we have elected to work through over the next six months in the hope that it may be recognised that our circumstances have changed and that some additional funding is warranted.

Senator MURRAY—I am blessed by also being a member of the Joint Committee of Public Accounts and Audit. The Auditor-General by statute is responsible to that committee and makes very clear his budget needs, where he considers there to be shortcomings and so on. That committee acts in a non-partisan manner in going to bat for the Auditor-General when necessary, whilst bearing in mind the government's responsibilities. I raise that issue with you because you are well aware that certainly the Senate do not have the power to initiate financial change—we can cut budgets, but we cannot increase them—and, therefore, advocacy on a non-partisan basis from this committee would carry some weight. I just wanted to be assured by you that you had the same view of this committee as perhaps might be expected of the Auditor-General of the JCPAA and that you would use us for advocacy when there were issues which you thought genuinely required a different set of ears perhaps to a parsimonious Treasurer or finance minister.

Mr Knott—I am grateful for those observations, and I certainly take them on board. As I said, we are in a new environment. We need to work through our needs, looking at the new environment and trying to project out over the next couple of years. That is not something I want to rush into, but it is clearly a job of work that needs to be done. We will not be reluctant to discuss those matters with this committee.

Senator MURRAY—Yes, because activism costs money, frankly. I will move from being a dispassionate non-partisan person to more my own field of portfolio interest, and that is some of the current issues—HIH, One.Tel and others. I suspect Senator Conroy will shift into the shadow mode for his portfolio. I really want to refer to some political remarks I have made—and I couch them deliberately in that sense because they were political and deliberately provocative—about ASIC's failings to come good on a public interest requirement to be more voluble about auditors and their independence.

I refer you to the record, going back probably at least five years, of discussions that this committee and I have had with your group, and probably you, on this matter over time. It is really why I began my remarks as I did, because, knowing the quality of the officers that preceded this group and the quality of the officers before us, I would be very surprised if an issue such as that was laid idle. Therefore, I feared that, in fact, you had had discussions with

Treasury and government and they had not progressed it and it had been let lie. That may or may not be true, and I do not really need to know whether it is true or not. What I need to know is where we go from here.

My essential case is that, whilst there should be a debate about solutions—and I can see many different points of view on that, and I am quite happy to concede that; I have a particular point of view, but there are others—I am searching for an acceptance by ASIC of the problem. My own readings, including of luminaries such as Trevor Sykes, who gets a mention in these circles—and I happened to live in WA with WA Inc.—and my following of corporate affairs in Australia over the last two decades have indicated to me that consistently at the heart of corporate failure has been the failure to report financial statements, assets and liabilities situations, accurately, particularly on the part of valuers, who get off far too lightly in this debate, and particularly on the part of auditors, from Rothwells through to HIH. They are right in the firing line.

I have a great deal of experience with auditors. I know Australian auditors to be well trained and are an extremely capable, professional group of people as a class. Therefore, I have come to the view that there is nothing wrong with their abilities but that there has to be something wrong in the way in which they were either appointed or their independence is constrained or in some way they are subject to influence or pressure which distorts their view of things—particularly, of course, when you are dealing with these massive international companies, and you are dealing with partners of great experience, both in international and local.

I say there is a problem. I have mapped out a set of solutions but neither I nor most people—I would suggest—in parliament have the resources and capabilities to look at this thing in its all of its ramifications with the real in-depth examination that either you or an independent body would be able to do. I have deliberately given you a long lead-in so you understand my perspectives on the record. You have had some remarks from me off the record. I would like your response on that, both on problems and solutions and how ASIC sees itself in developing a productive debate with a productive—not a political—outcome, which perhaps minimises the chances of corporate failures a little more.

Senator COONEY—Just before you answer that, I want to add something to what Senator Murray has said. From information recently received, I proceeded here. It was said yesterday at another meeting that what is happening in this whole area is that the big four accounting firms, or ones that pick up corporate failure and corporate crime, are the ones that really know about it. They do not do it necessarily to prepare a brief, they just prepare it to show the companies they are working for what is happening. In any event, the way they get to the information is such that it makes any evidence that would be capable of being put before the court very doubtful in its character. To follow on from what Senator Murray said, the proposition—and I might be overstating it—is that the official regulators, as it were, are not the main forces in this field but that the private companies are. They just sort of show a company that there have been some problems and that it is: it is left swinging in the air. It may be a good thing that it is swinging in the air, but that is it. That seems to be the sort of thing that Senator Murray is saying. So I just add that in thecontext he has created.

Mr Knott—I am not sure that I quite understand that, Senator. But we might come back to it.

Senator COONEY—Perhaps I had better explain. What was said was how many prosecutions does the Federal Police take—and I am not for prosecutions, may I say—how many prosecutions does the NCA or ASIC take? If you look at all that, not all that much fraud is investigated—that is, fraud against the Commonwealth or generally—compared to what goes on. But it is there and the fact that it is there is shown by what is revealed by the auditing and the work done by these four big companies. I think it shows that a lot of crime is committed in the corporate sector which just goes straight through to the keeper. Very little of it is picked up.

Mr Knott—I must say, on that point, I am quite surprised.

Senator COONEY—I will get you the transcript.

Mr Knott—Yes. If the point is being made that auditors are uncovering fraud or prima facie evidence of fraud, the question is: why aren't they bringing it to our attention?

Senator COONEY—Yes, that was asked. I have to make it clear that what was being said was that it is not only auditors, that these companies are the effective investigators in this area. I will get you the transcript. They are the ones that do this, the other bodies like the AFP and the NCA have not got the resources—they are taxed with what they can do and so this area is left lamenting.

Mr Knott—If we are talking specifically compliant with the Corporations Law—I am interested to see the transcript—I do not understand the argument. We would not expect the Federal Police or the NCA to be in that area, you would expect us to be and we are. We have just fewer than 200 active investigations under way at present. That is pretty typical in any year. We have over 80 cases in the criminal courts. We have about 35 cases in the civil courts as well as a whole series of administrative actions we take. But auditors are under a legal obligation to report breaches of laws.

Senator COONEY—I would not wed myself to the concept of auditors. As I understand the argument, people go in there to see what is going on and they are the ones who uncover problems, and that might well be so.

Mr Knott—In terms of a pre-investigation by ASIC, again, I would not be surprised by that. I have made the point more than once, and quite recently to another committee, that, as is clear from the annual report, we receive over 5,000 complaints from the public every year. To investigate a complaint can take a week, several weeks or several months. It is quite clear that when you are getting that level of complaint you can only do a very small proportion of investigations. Then only a proportion of those investigations will result in admissible evidence of the type that would enable a prosecution. In the sense that auditors and others are at an earlier stage, uncovering issues within companies does not surprise me—in fact, it is what should happen. One of the answers to Senator Murray might be that they do not do enough of that.

Senator MURRAY—I feel as though I have been hijacked here! Perhaps we can go back to the question.

Senator COONEY—I think there might have been a misunderstanding.

Senator MURRAY—Senator Cooney is exceedingly lovable and very effective!

Mr Knott—I am tempted to say that I have forgotten your opening comments, but I haven't. I actually welcome them because I think it is clear from what you said that you accept that we might differ in terms of outcomes and approaches. As I understand it what you are really saying is that you would like us to be more active in the debate in terms of the role of auditors in Australia and the independence of auditors in Australia.

Senator MURRAY—If I may say so I think you have a seminal role to play. I think you have to be in fact not a participant in the debate, but a source of much of the thoughtfulness, research and alternative views, not because you are exceptionally resourced, because you are stretched, but because you are the only independent body without an axe to grind. You do not represent the accountants, you do not represent the politicians and you have a vast experience within your organisation. Effectively what I have done over the last five years is said to you: this is the problem as I see it, this is the solution I have arrived at from my reading and my life experience, you tell me what to do. Do you accept there is a problem? If you do not, there is nowhere we can go in this discussion. If you do, are you capable of accepting the role of researching this thing as well as you can internationally and domestically and saying, 'These are the alternative ways in which this can be dealt with.' That is really what is at the heart of what I am asking.

Mr Knott—I think I can give you a substantially favourable answer in the sense that you are looking for us to play a role. The recent collapses that you have mentioned will inevitably require us to look at the role of the auditors in those particular instances. I do not want to talk about those specifically today.

It seems to me inevitable that the royal commission into the collapse of HIH will have to look at these issues. That will give us an opportunity to take into account the circumstances that are revealed and to formulate suggestions for any reform that might take place. I, personally—and, I think, the commission—would welcome the opportunity to do that. We can make a commitment to you that we intend to be more active on these issues. There was quite a lot litigation resulting from the series of collapses that came out of the 1980s, as you will recall. Most of it was settled and, of course, that denied us and the community generally some precedent out of court in terms of obligations and the like. We, ourselves, you might recall, took civil proceedings in relation to the collapse of Adsteam, which were settled last year and which are mentioned in this annual report. The terms of settlement are available on our web site, and have been publicised, and do address some issues of auditor independence and rotation.

The reason I was pleased that you were not particularly pushing a single solution is that I am not persuaded, at this stage, by the solution that ASIC should appoint auditors. Indeed, I go further and say that, whilst independence is a key issue and we should look at it, independence is a means to an end. Independence is a means to try to ensure that we get the best quality audit that we can. If we think that they are somehow being compromised by conflict, independence will help to achieve better quality. The starting point may be—and I posture this only as a suggestion—to look at the role and extent of audit requirements and form a view as to whether they are adequate. You will know that the audit requirements themselves are not part of the law. Unlike accounting standards, which are part of the law, the requirements that extend to scope of audit and the role of the auditor are in the separate auditing standard and that is a professional standard. The starting point would be to look at those issues, at whether the requirements in

relation to the conduct of audit ought to be part of the law and whether the requirements in relation to the conduct of audit are sufficiently specific. This would raise quite difficult issues in terms of the extent to which we expect auditors to independently carry out investigatory audits as distinct from relying on information provided to them by management, for example. Depending on the outcome, it could have tremendous implications in terms of cost which would have to be factored into the equation. I would have thought that that was the starting position. By saying that I do not mean that we should ignore issues of independence—I think they are important.

Senator CONROY—You would welcome the liability issues that might flow?

Mr Knott—The liability issues should be looked at. Coming out of the 1980s collapses there was quite a discussion about capping liability. I believe that occurred in some jurisdictions.

Senator CONROY—If you made the appointments you would be potentially liable.

Mr Knott—The appointment issue is exactly the issue that I would want to raise as the primary question. There would be huge moral hazard to ASIC and therefore to the system if we were appointing auditors and an audit failed. The question would be somehow that ASIC had got it wrong. It can never be that we could be responsible for the conduct of auditors.

Senator MURRAY—I must make it clear that my proposition was for auditors who are accredited under the professional standards to be registered with you, and for companies to select a shortlist of auditors which they would be happy with. That would be a small number not less than three or five. You would simply give them one of those three or five. In other words, you would act like the attractive couple in Pools—the balls out of the Lotto spinning thing.

Mr Knott—I would be happier if you were pulling the balls out.

Senator MURRAY—As soon as I have a trust—I am actually worthless in my individual capacity—I would not mind doing that.

Senator CONROY—You are too harsh on yourself, Senator.

Mr Knott—Nevertheless, there would be moral hazard issues even with that formula.

Senator MURRAY—You do appreciate too—I should put it on the record if we are having this discussion—that an alternate to that is the corporate governance board proposal, which allows for a separate entity to carry out the job of appointing auditors—not the main board. The corporate governance board is specifically elected by shareholding, not shareholder. But there are many ideas. My real point is this: if we get bogged down in my ideas versus yours, we unnecessarily taint the debate. I am really asking that, within a reasonable period of time, ASIC come up with a well researched position paper, which is made available to accelerate this debate. The issues of law you have picked on, the issues of capping, and the issues put forward by Senator Conroy, members of the government and members of my party are all grist to the mill.

Mr Knott—We will certainly take that on board. The climate is right for this sort of work to be undertaken. It needs to take into account specific experiences because they are always instructive. We make assumptions, I might also add. If we see a failure and there has been an auditor there, we make an assumption that the audit must have failed. We must be careful about that and we must look at what actually happened and draw the lessons of any shortcomings from the actual experience. But the climate is right to do that.

Senator MURRAY—My point to you—and I leave it with this remark—is that, although recent events heighten the sensitivity, to me they represent a decades-old problem and that is that the financial statements are not being properly reported. Values are most often overvalues and auditors are not properly identifying the assets, liabilities and cash position of companies. If you talk to insolvency practitioners, as you do, and as I do, and if you read the literature over the last 20 years, you see that that is a theme in all the corporate failures. I am not saying—and I do not think anyone will ever say—that you can stop corporate failures. All I am asking is that they be minimised and that the damage is less than it might otherwise have been.

Mr Knott—We have a common objective, obviously. We want the best possible disclosure that we can generate. The question is going to be whether the standards themselves are a problem or whether it is the way the audit work is conducted that is a problem, and that will vary from case to case. That is why I think the starting point would be to look at the requirements on auditors and the nature and the scope of their obligation to conduct, in a sense, independent investigatory audits. Does an auditor of a retail company have an obligation to go and look at the stock, the inventory, and form his or her own view about the carrying value of that stock or is that asking too much? Is the expectation that they should be able to rely on directors, and directors take the liability? They are the sorts of public policy issues that are going to be thrown up by this type of debate. We are definitely going to have the debate.

Senator MURRAY—Thank you.

Senator CONROY—There were a number of media commentaries over the last couple of weeks revolving around the royal commission and there were suggestions that the royal commission may encompass some of the ASIC investigation and/or that ASIC would not proceed with its inquiries until after the royal commission. Are you familiar with any of those media reports?

Mr Knott—I am not sure, specifically, about that last point. There have been a number of media reports about whether it would be possible for the two streams of investigation to continue contemporaneously. Certainly I am aware of that.

Senator CONROY—Do you have a view on that?

Mr Knott—I think it is unwise for me to express any view in relation to the royal commission or the HIH matter in view of the fact that, as you know, I have stood aside from that matter. My colleagues may be able to help.

Senator CONROY—I am happy for Mr Wood or Ms Segal to respond. There have been reports that ASIC may either defer its investigations or have some of its areas rolled into the royal commission's terms of reference. Obviously, you cannot comment on that because they

are not public yet. Are there any circumstances where ASIC could not proceed with its investigations?

Ms Segal—As the chairman indicated, it is unwise at this stage to comment because, as you said, we have not seen the terms of the royal commission. That will be the key as to how they encompass the existing ASIC investigation. If they envisage that investigation continuing then we are certainly minded to continue, but that will need to be worked out in terms of the actual terms of the royal commission and the approach of the royal commissioner. It is very hard to speculate until all that is known publicly.

Senator CONROY—Drawing on Senator Murray's opening commentary, you are an independent statutory authority charged with looking after corporate law. Are you suggesting that the royal commission can cause you to not fulfil your statutory obligation? Can it cause you to defer, delay or not investigate some issues?

Ms Segal—I will ask Mr Wood if he has anything to add on that. My understanding is that letters patent to the royal commission are similarly an issue of instructions from the parliament and can encompass very broad ranging investigations that might mean other things are delayed. It is within the scope of a royal commission to look at broad issues and then to refer matters. They might look at potential criminal behaviour and then seek to refer that matter to an independent investigative agency like the DPP to further investigate and then possibly prosecute. Similarly, it may choose to assess matters and refer them on to ASIC. It is very hard to speculate on the appropriate obligations of everybody until the terms are made public.

Senator CONROY—Thank you for that answer, but I will ask you the question again. Can the royal commission stop you? Can you be instructed not to proceed with your current investigations?

Ms Segal—I do not know the answer to whether it can stop us, but if the terms of the royal commission are so—

Senator CONROY—If you do not know, who would know?

Ms Segal—It depends very much on the terms. If the terms of the royal commission are so broad as to encompass everything that needs to be investigated then I do not know that it would make sense for multiple investigations to be continued simultaneously. It may be that, as I said, the royal commission looks at certain things and then refers them on.

Senator CONROY—I accept that it may not make sense, to use your words, but that is not what I am asking. Mr Wood is champing at the bit to get to the table so I am happy for him to kick Mr Drysdale off the table, as we have a very small table.

Mr Wood—Thank you for your invitation, Senator.

Senator CONROY—Not being a lawyer, I do not know the answer to these questions so I am hoping ASIC can help.

Mr Wood—As I understand the question, it is this: can a royal commissioner direct ASIC not to carry out statutory functions?

Senator CONROY—Or the government.

Ms Segal—Or the terms of the royal commission itself.

Mr Wood—We are very much in the area of speculation here. We do not know the extent of the terms of reference, but it would surprise me that a royal commissioner would have that power. I would have thought that the royal commission would be acting within the limitations imposed by the Royal Commissions Act and the limitations as to jurisdiction that flow from the terms of reference. As far as ASIC is concerned—

Senator CONROY—You said a royal commissioner could not direct you or say you must cease your investigation. Does the government have the power to ask you not to proceed with the investigations because there is a term of reference that may encompass some of the issues that you may be investigating?

Mr Wood—I am sorry, it is a question of law and I am not really able to answer that.

Senator CONROY—The Corporations Law is a tricky thing.

Ms Segal—To pick up an earlier point that the chairman made right at the beginning, the government does have the power to give us directions so, in a theoretical sense, the government could direct us to stop our investigation pending the royal commission doing its work and the royal commissioner making recommendations pursuant to the terms of reference. We are talking theory here but, as I understand it—and I am very much only speaking from what I have read in the newspaper—the public statements have been that it is everybody's intention that matters that ASIC is investigating hopefully will continue and there will be a royal commission that will look at matters that are the subject of the letters patent. So we are just continuing with our work at this point and will continue until we see the terms of reference and are able to react accordingly.

Senator CONROY—I am trying to come to an understanding of the law. I think we have agreed that the royal commissioner cannot stop you, so the only possible authority that could stop you—and I would be very interested if this was actually the case—is a government of the day if it could direct you not to proceed with your investigations. I find that an extraordinary proposition.

Ms Segal—I think I have said we are subject to direction in theory but, on the point of law in terms of the interaction of the Royal Commissions Act and the ASIC Act, we would be happy to take that on notice and come back to you on the technical matter. If I could just talk practically, I think that it will very much be a question of the terms of reference because it makes practical sense in the way investigations work for there to be primary people conducting the investigation, and you cannot have people running between different rooms, answering questions at the same time of day to two people. As a practical matter, if the royal commission and ASIC's investigation is to continue it will need to be part of the terms of reference to enable that to take place.

Senator CONROY—Can I just clarify that: you said if the ASIC investigation is to continue it will need to be part of the terms of reference? I thought that is what you said.

Ms Segal—The terms of reference is a key—that is what I am saying. On a practical basis—I am not dealing with it as a matter of law—it is very important for us to wait to see the terms of reference.

Senator COONEY—What Ms Segal is saying is that it is a practical matter. If you have an inquiry into a drug deal and you have two or three authorities all separately going about the one investigation, you are likely to get into all sorts of trouble and people tip other people off, not intentionally but as a practical effect. I think what you are saying is, 'Look, if there is going to be an investigation, let us have a coordinated investigation,' and you cannot have a coordinated investigation until you know what the terms of reference are.

Ms Segal—Exactly.

Senator CONROY—There have been a number of suggestions that the royal commission may impair your investigation. It has been suggested in newspapers that some of the evidence that may come out in the investigation may in actual fact impair your investigations. What would be the circumstances that would lead to that?

Ms Segal—Mr Wood, would you like to answer?

Mr Wood—I am just trying to think of those circumstances, Senator. I would have thought if there was a direct overlap between the investigation being carried out by ASIC and that being carried out by the royal commission, there would be problems with lines of inquiry and matters even under investigation being released prematurely by two sets of investigators interviewing the same witnesses about the same matters. But, short of that situation arising, I should not think there would be any great difficulty between the two things.

Senator CONROY—So none of the evidence tendered in the royal commission could—

Mr Wood—I guess I am assuming that we would have separate investigations, that ASIC would proceed to investigate transaction a, and one would hope that the royal commission would be looking at b, c, d and the other transactions. There would be so far as possible a clear delineation of the areas of interest and investigation between the two bodies.

Senator CONROY—In the course of the royal commission, if there were any deals done to obtain evidence and the deals were for no prosecution, would they come across the line so that you could not prosecute some individual in the future? I actually do not know the answer, not being a lawyer.

Mr Wood—I think you are probably referring to the granting of indemnities against prosecution.

Senator CONROY—Yes.

Mr Wood—Unless there are some powers in the Royal Commissions Act—and I am not aware of that—I would have thought those matters would have to go to the Commonwealth Director of Public Prosecutions, who would exercise the same function in relation to our investigation. So I suppose, in that sense, there would be the one person granting indemnities and there should not be any conflict in terms of who is indemnified as against what evidence.

Senator CONROY—Wouldn't that depend on what the priorities of the royal commission are as opposed to the priorities of your investigation? I appreciate that obviously you do not know the terms of reference, but if the priority of the investigation of the royal commission is into a different area—and you are saying that hopefully there is a delineation—and indemnity is granted on X and Y over activities A, B and C because they want to get to a different outcome necessarily, could that impact on your investigation if indemnity is given, even though they may be criminal acts that they have been given indemnity for?

Mr Wood—Again, we are presupposing a certain set of circumstances and a certain line of investigation. I guess you are postulating whether a person might be an indemnified witness in relation to one transaction and perhaps a potential accused in relation to another. My experience—and I have worked with the Commonwealth DPP for quite a few years—was that the director is very careful before he grants indemnities and he demands to know the full circumstances surrounding that.

Senator CONROY—Would they come and consult with you and say, 'Look, there is this suggestion that indemnity might be granted for this individual over these transactions if they testify in the royal commission.' Is that what would happen?

Mr Wood—Clearly, I have got no practical experience of the situation.

Senator CONROY—We have not had many federal royal commissions, have we?

Mr Wood—We work very closely with them. It is the one company collapse under review. I would expect the normal course of events—we have regular liaison meetings and there is everyday contact between our people and the Commonwealth DPP. I would be surprised if that sort of basic negotiation were to take place with ASIC being in ignorance of them.

Senator CONROY—Is there any evidence that is tendered in the royal commission that would not be available to you? I know that material that is spoken about here under privilege cannot be tendered in a court of law under the law of privilege. Is there a similar situation in regard to a royal commission?

Mr Wood—Again, I have to plead ignorance of the law in that area. Whether the commissioner can sit in a closed session, I am not too sure.

Senator CONROY—I am just drawing on the recent experience of the Queensland royal commission into electoral issues, where—

Ms Segal—The royal commissioner can sit in camera. But I think the overarching thing is that, for ASIC's investigation to continue effectively and for the royal commissioner to satisfy whatever the terms of reference are, from a personal perspective I think it will be important that

there is a considerable degree of communication and cooperation. I think that is the case in many transactions in life: if you have got multiple overlapping or potentially overlapping issues, that will be essential. It is important that the terms of reference envisage the ASIC investigation and that the royal commissioner and ASIC—through counsel assisting or however is appropriate—maintain appropriate cooperation and communication.

Senator CONROY—Mr Woods described the delineation between different transactions. Is that sort of discussion taking place? Presumably, you are looking at all of the transactions at the moment that would have led to the collapse.

Mr Wood—Yes.

Senator CONROY—By definition, a royal commission will look at some of those transactions as well.

Ms Segal—No discussion has taken place because we have no knowledge of any royal commissioner.

Senator CONROY—Presumably, though, they will be looking at some of the similar transactions to yourselves, by definition? They cannot investigate HIH and how it went under if they do not look at some of the transactions.

Ms Segal—We would imagine that, but not having seen the terms of reference, it is to some extent speculation.

Senator CONROY—Mr Woods described it as a delineation between you looking at these transactions and them looking at these ones.

Mr Johnston—That was one possibility.

Ms Segal—That is one possibility.

Senator CONROY—You are looking at them all. For the royal commission to proceed, commonsense says that they must be looking at some, so there is an overlap. I do not think anyone has tried to argue that there will not be an overlap—it is how you practically deal with it. Is it your position that, for transactions that overlap which are the subject of the royal commission, you would cease your investigation into those transactions?

Ms Segal—No. We have no position at the moment because I think it is wise to wait and maintain an open mind, particularly as our investigation is progressing. Each day we know more in terms of what are appropriate matters.

Senator CONROY—But to use your phrase ‘practically’, there is no point in having people running backwards and forwards giving the same evidence. So, practically, you are saying that when the royal commission encompasses some of the transactions—maybe not all—practically to you it makes no sense. You would continue to investigate those transactions while the royal commission is looking at those transactions because it is practically—

Ms Segal—No. I think, practically, it is going to be important to establish working protocols. What those working protocols mean in relation to any particular investigation or any particular transaction will very much depend on what happens at the time. It is very hard and, indeed, very dangerous to speculate at this point. We just do not know.

Senator CONROY—The reason I am asking you is because a number of media commentators, who have some expertise in the area of Corporate Law and royal commission law, are suggesting that your investigations will probably be curtailed in some way. 'Curtail' is not a word that I am trying to put into your mouth, but they are suggesting that your investigations will be curtailed, and I am just trying to establish, as a matter of fact, how you will conduct your investigations once the royal commission terms are announced if there are some overlapping transactions. I understand that there has to be cooperation and there has to be protocols but, fundamentally, will you still be proceeding with investigating transactions that are the subject of a royal commission?

Ms Segal—Your question as to how particular investigations that we are conducting might be curtailed is a highly theoretical issue until we see the terms of reference and the working protocols that we look forward to establishing with the royal commission. Then we will be able, perhaps in another forum, or the media will be able, to comment on exactly what is being looked at by either the royal commission or by us or, indeed, by both. We are saying that practically there are difficulties, and there are, but it may be that one area is looked at by both with us assisting each other.

I would not want to say that it is necessarily the case that parts of an ASIC investigation would stop if the royal commission were interested in it. There are ways in which we could assist each other in pursuing a particular part of the investigation. I think it will very much depend on, firstly, the terms of reference and, secondly, the approach of the royal commissioner and the protocols that we can establish. We have common objectives, in a sense, in that, as you say, we are looking at that single collapse and presumably wanting to understand it. It is very hard, at this point, when we do not know the identity of the royal commissioner, we do not know that person's approach and we do not know the terms of reference—

Senator CONROY—I am just trying to ensure that the funds the government has given you for the collapse of HIH are not siphoned off, in effect, by your joint arrangements to assist the funding of the royal commission.

Ms Segal—I see.

Senator CONROY—Basically, you are doing the legwork and paying for it for them.

Ms Segal—That is a slightly different question. If you would like reassurance that we will be using the funds in pursuing our investigation, I can definitely reassure you on that.

Senator CONROY—Which resources would you then be using to cooperate with the royal commission and perhaps jointly investigating?

Ms Segal—It would be part of ASIC's investigation to come to particular courses of inquiry, et cetera. If that same material is of use to the royal commission, it does not in any way diminish the appropriateness of ASIC conducting its own inquiries.

Senator COONEY—I suppose you have worked with DPPs in the past, and they are reasonable people. Mr Wood might say you need more evidence and you would go and get him more evidence. Is that right? In other words, you are talking about the working protocols and it depends on each case as to how that goes. Until you establish those, and until you establish, frankly, who the royal commissioner is and what the terms of reference are, as you have been saying, you really cannot do anything but wait and see what happens.

Ms Segal—Yes. We are certainly not not doing anything. We are pursuing our investigations full pelt.

Senator COONEY—But as far as the royal commission goes, you cannot deal with something that has not been set up.

Ms Segal—Exactly. We cannot deal with something we really can only theorise about.

Senator COONEY—So in the meantime you just go along in the normal fashion until something happens?

Ms Segal—Exactly. And then we look forward to understanding the terms of reference and trying to work out the most practical way to deal with the issues.

Senator CONROY—I will happily move on from that issue for the moment. You would be aware that a number of consumer associations have written, possibly even to yourselves, about some appointments and some question marks about some of the consumer appointments recently. I understand that they have asked you to look at it. The minister was on radio a couple of mornings ago suggesting that you had investigated this matter and had 'cleared' him. I asked Mr Conolly yesterday morning if that was the case, if you had advised him. He explained that he was having his first physical meeting with you tomorrow, I think he said. He was somewhat surprised to see the minister announce that he had been cleared by ASIC. Could you clear this up for us? Have you investigated and cleared the minister?

Mr Kell—We have not formally investigated these appointments. An investigation is simply not relevant in these circumstances. We are however meeting with the consumer representatives and, indeed, scheme representatives about this issue. We will obviously discuss their concerns. I might add that we do not propose to suspend the approval of the schemes, which is what we were asked to do. In fact, we are continuing to advise consumers that they should use these dispute resolution schemes. It is essential that consumers have a place to go to, to get their complaints dealt with. There is an opportunity under the FSR consultation process for stakeholders, including consumer organisations, to provide submissions on some of the standards that apply to dispute resolution schemes.

As you would be aware, there is a proposal under the FSR framework for all licensees dealing with retail customers to belong to an external dispute resolution scheme, a proposal we strongly support. We have released a policy proposal paper on the implementation of those dispute

resolution requirements and the sorts of standards that will apply. Scheme governance is one of several issues that we will be looking at in that context. The bottom line here is that nothing has changed in terms of our approach to scheme decision making. We have never tolerated and will not tolerate any poor quality or biased decision making under schemes. We will continue to make sure that that outcome is achieved under our policies in relation to the ADR area.

Senator CONROY—So when Mr Hockey says that ASIC have cleared him, you have not completed your investigations of this issue firstly and you have not communicated to Mr Hockey—I am using his words and not trying to put words in your mouth—that he has been 'cleared' by ASIC.

Mr Kell—The issue of clearing someone in relation to this matter is not the relevant issue. We have not formally investigated. The issue of clearing does not come up. We do not intend to go in and necessarily examine the appointments by a minister. That is not our role. Our role is to look at how the schemes work and whether the schemes are complying with the standards that we have set out in our policy. One of those standards goes to whether they are complying with the requirement to be independent. As you know, under our policy statement 139, there is a requirement for a scheme governing body to have equal numbers of industry and consumer representatives and an independent chair.

Our policy then goes on to set out that consumer appointments can be made by the minister with responsibility for consumer affairs or through another means, by the scheme itself. In the finance sector, you have ADR schemes that take both of those routes when it comes to appointing consumer representatives. That is the framework in which we are examining this issue. The bottom line for us is that consumers continue to require access to these schemes and we will continue to ensure that they meet the standards in this area.

Senator CONROY—So you have not communicated with Mr Hockey in any means to indicate to him that he has been 'cleared by ASIC', to use his words?

Ms Segal—I believe ASIC has communicated with Mr Hockey and we have communicated with the consumer representatives. We have said the same things to both.

Senator CONROY—The consumer representatives do not believe Mr Hockey has been cleared and Mr Hockey says he has been cleared, so somebody seems to have—

Senator MURRAY—been unclear.

Senator CONROY—Thank you, Senator Murray, for clearing that up.

Ms Segal—Perhaps I can doubly clear it up now. We do not believe this is a matter, as we have said, for clearing or investigation. The specific issue of appointments is not something we are looking at. We are concerned about the schemes and their overall governance and compliance with our policy. We have said, as you indicated, that we are happy to talk further to the consumers. We have also discussed with them that the issues they have raised are appropriate matters for consideration within our PPP, and they have said that they understand that. As far as I understand, this is what we are further to discuss tomorrow, as you indicate. We, the minister and the consumer associations all have a common interest in ensuring that the

schemes operate properly to provide consumers with the appropriate venue for alternative dispute resolution.

Senator CONROY—Does Mr Hockey have any basis for his statement that he has been 'cleared by ASIC'? Those are his words.

Ms Segal—I cannot comment about those being his words, but his understanding that it is not a matter for us to investigate and it is not appropriate for us to look at these individual appointments is correct. We are focused on the scheme governance as an overall outcome. I understand that to be now everybody's understanding.

Senator CONROY—There are a string of questions that arise from that last statement, but I will move on.

CHAIRMAN—Are you satisfied with the way the scheme is operating currently?

Ms Segal—I will again ask Mr Kell, but I think it is fair to say that we are in regular contact with the schemes about their operation because they have to operate pursuant to our policy, and there are various interactions between the scheme and ASIC in terms of information they provide us, their own governance, et cetera. So it is not as if we in one sense approve a scheme and do not have any further contact with them; we are in fairly regular contact with them and are seeking at times more information from them.

Mr Kell—We are talking about two schemes here—insurance inquiries and complaints, which covers general insurance, and the financial industry complaints service, which covers life insurance, financial planning and the managed investment industry. As Jillian Segal just indicated, we are in regular dialogue with those schemes. They are required formally to report to us on a regular basis as a condition of their approval. We raise issues with them fairly regularly about the particular ways that they are working, such as whether they could provide more information to us in their reports. That is something that we have raised with them quite recently. Overall, we are confident that these schemes can work well.

CHAIRMAN—How is your own Consumer Advisory Panel appointed?

Mr Kell—It is appointed through the selection of a mix of individual representatives and also representatives from particular consumer and investor organisations. We write to a set of investor and consumer organisations asking them to nominate someone to the panel, and that takes up six of the appointments. That includes people from the independent retirees, the Consumers Association and community legal centres, and we rotate those appointments over time.

We also select a group of people to serve in an individual capacity based on their expertise in financial services and consumer affairs. That is three of the appointments, so that takes it up to nine. And then we have an independent chair, who does not have a particular background in the consumer sector.

Senator CONROY—Mr Knott, you got some publicity recently over corporate governance issues at NRMA. Could you outline what your concerns were at the time?

Mr Knott—We have a current investigation into that matter, so I will be very broad—

Senator CONROY—Sorry, I had forgotten that you actually had that.

Mr Knott—We have announced in relation to that that we were looking at certain corporate governance issues, certain disclosure issues, and we are continuing to do that.

Senator CONROY—Does that investigation on governance issues encompass the minister phoning various directors of NRMA seeking to pressure them into keeping Mr Dodd as CEO?

Mr Knott—I think if we were to pursue these discussions, we would need to do it in camera.

Senator CONROY—You are aware that it has been publicly reported and not denied by the minister? In fact, I think he might even have confirmed it, but it certainly has not been denied. In fact, I have had it confirmed to me that it is the case: the minister did make a number of phone calls to NRMA directors seeking to encourage them to retain Mr Dodd. Are you aware of that?

Mr Knott—I think if you would like to discuss the matter—

Senator CONROY—That is a matter of public record. Are you aware that that happened?

Mr Knott—I have read the press in relation to this.

Senator CONROY—That is all I am asking. You are aware that the minister has either not denied that or in fact I think he may have even confirmed that he did that.

Mr Knott—I have not discussed the matter with the minister.

Senator CONROY—I am talking about in terms of the public record.

Mr Knott—I have read the press reports.

Senator CONROY—And you have not seen any denial by the minister publicly?

Mr Knott—Not that I can recall, no.

Senator CONROY—Have you spoken with the minister about this in terms of your governance investigation?

Mr Knott—If you would like to discuss these matters, Senator, I think we should go in camera.

Senator CONROY—I will not stop us now but we may, at the end, go in camera to hold a discussion on that. We received some evidence yesterday from Mr Foster from the Life Agents Action Group in relation to an investigation on the Financial Sector Reform Bill. I have got a

transcript of that evidence. I am not sure whether Mr Johnston was here, but I will just run through it. It says:

> My business partner attended a recent meeting which was also attended by Pauline Vamos from ASIC and Senator Ferguson, who was a guest speaker. Both confirmed at that meeting that, if you are a sole independent operator ... I am taking my definition of a 'sole independent operator' from how they read the current legislation: if I am an AMP agent and I have no other agencies except AMP or alliances, I do not have to disclose commission at all, including investment products, because there is no bias in the advice.

Ms Vamos is not here but, Mr Johnston, are you the right person to address the question to?

Mr Johnston—Yes.

Senator CONROY—Could you take me through this interpretation of the current read of the current legislation? Are Ms Vamos's remarks correct as far as you know? Even if you are not aware of them, could you give me your interpretation of the current legislation?

Mr Johnston—My recollection is that it is the new legislation that they were referring to—the bill. I believe that the issue that would have been addressed there is commission disclosure in the various forms in which commission has to be disclosed under the new legislation. It is a somewhat complex matter. Without seeing the whole of the speech, I can only speculate as to what the observation was. But I imagine that it would have been in relation to the disclosure of risk products specifically.

The way that the legislation will work is that it contemplates that products disclosure will be in a document called a 'products disclosure statement', which will be prepared by a product issuer. There has to be disclosure made in that document by the product issuer of the costs of obtaining the product. Commission has to be disclosed in that document but only to the extent that the commission influences the return on the product. So if you are talking about a risk product—a general insurance policy, for example—there would not be any impact on the return or the benefits that you gain from the product that you have purchased. Therefore, there would be no disclosure in a product disclosure statement in respect of risk products.

If an adviser, be it an insurance agent, is then giving personal advice to a consumer, then your legislation will require that the adviser has to give a document called a 'statement of advice' to that consumer. In the statement of advice, there is a requirement to disclose all commission which the adviser receives as a result of the advice, but only commission where the advice that you are given is influenced by the commission you receive. So there is at least an argument that says that, in respect of risk products, if you are a sole agent—a tied agent, as they tend to be called in the industry—then you may not have to disclose commission in respect of those products. The reason is that, if you are a tied agent, you only have one product that you can sell—if you are tied to a risk insurance company, for example, or a general insurance company.

So if I am an agent acting for one of those companies and it is a plain vanilla, if you like, house and contents policy that I am selling, and I only represent one company, then there is an argument that says, 'I only have one product to sell you, therefore I am not influenced by the commission because this is the only product I can advise on.' So, in those circumstances, it has been observed that that person may not have to disclose the commission. I am sorry that that was a somewhat complicated answer.

Senator CONROY—No, that was actually very succinct. That leads me to a number of questions. Are you familiar with the recent legislation passed about alienation of income?

Mr Johnston—No, I would not pretend to be overfamiliar with the tax income. I am familiar with the general thrust of it but I do not pretend to be a tax expert.

Senator CONROY—Okay. Are you familiar with a number of High Court cases about the question of an independent contractor and a superannuation entitlement?

Mr Johnston—That is even further removed from my area of knowledge.

Senator CONROY—All of these are now established issues about what the definition of an employee versus a tied contractor is. Are you confirming to me that the way in which ASIC intend to interpret the law is as you have described? It was put to us in this statement that it was confirmed by Ms Vamos and Senator Ferguson that this would be the interpretation that ASIC were going to follow. Are you putting to me that that is going to be ASIC's interpretation of implementing the FSRB?

Mr Johnston—I suspect that there are actually two different issues. The issue in relation to disclosure of commission would apply to someone giving that advice regardless of whether they were an employee, an authorised representative or a licensee. The issue would be the same. I do not think it would make any difference at all.

Senator CONROY—I am not sure that is consistent with what you have said. I accept that in the PDS there is no requirement, and there is no argument that there is no requirement to disclose commission. You suggested that because you believed that a tied agent was in actual fact an employee then—

Mr Johnston—No, sorry: a tied agent may be an authorised representative but not necessarily an employee. They could still be an independent agent running their own business, but they have an agreement with a product provider that they will represent them and they are licensed. The licensee perhaps was the product provider and the adviser might well be an authorised representative of that product provider. I do not think the issue of the commission disclosure goes to whether or not the person is an employee, a representative or a licensee.

Senator CONROY—Can I put it to you that I think you are splitting a hair and that there is a string of tax law cases that actually run in the complete opposite direction to the way you are creating a loophole with your interpretation. With this interpretation, you are allowing thousands of agents to escape the intent of this bill—which is, as the minister has repeatedly stated, to provide in the statement of advice disclosure of commission. Your interpretation flies in the face of a string of tax law cases—High Court cases—over superannuation.

Mr Johnston—I cannot comment on the tax cases because I do not pretend to be familiar with them. I do not think we are intending to create any sort of loophole. This issue is about what has to be disclosed in a statement of advice. The bill as it stands—we do not know whether it will be the final form or not—says that anyone who advises—be that a licensee, an authorised representative or anyone giving financial product advice that is personal advice—in the statement of advice has to disclose commissions where that commission influences the

recommendation that they make. So we would be expecting and we would support full disclosure of all commissions by everyone down the chain. In our submission that we made in respect of the bill, going back some 18 months, we argued strongly for full disclosure of all commissions.

CHAIRMAN—Would it not be fair to say that tax law is about whether a person is an employee or an independent agent running an independent business; what the FSRB law and your interpretation of it is about, is whether a person is tied to one product or can sell a multiplicity of products?

Mr Johnston—Yes, that is right. We are not having any regard to the tax status of the person.

Senator CONROY—They are not tied to a product.

CHAIRMAN—Well, tied to a product provider.

Mr Johnston—The law is the same regardless of whether the person is tied, is independent, or is a licensee in their own right.

CHAIRMAN—So it is not a loophole. You are saying that if they are tied to one product provider, obviously there is no bias in their advice because they cannot provide any alternative.

Mr Johnston—They are not allowed to provide any other product and therefore there is at least an argument, and I am conceding, Senator, that it is an argument. We are not necessarily saying that this is how it will be interpreted.

Senator CONROY—It was put to us yesterday that Ms Vamos had said that it was. I am seeking for you to clarify whether Ms Vamos has been verballed. I accept that she is not here so that is a little hard. You are in charge of the interpretations and you are putting out a string of guidelines at the moment for comment so your interpretation here today is an important guideline to thousands of Australians engaged in this industry. I am intrigued by your concept that, because you are tied to one product provider, that means you have no incentive based on the size of the commission for different products from the same supplier. There could be two products provided by AMP and one has a greater commission than any other.

Mr Johnston—In that case we would say the illustration does not apply because if there are two products that it is possible to provide and if they provide essentially the same—

Senator CONROY—This is financial advice.

Mr Johnston—If they provide essentially the same benefits and cost to the client then you would imagine that the commission that is paid would be an influencing factor and would have to be disclosed.

Senator CONROY—I appreciate you have narrowed it fractionally there. But I put it to you that the whole giving of financial advice is not just saying, 'There is this life insurance policy that you can have until you are 55 or this one you can have until you are 65,' and they could be

defined in the way you have described as a 'like product' and therefore there is disclosure? Can I put to you that financial advice includes saying, 'You have a choice about doing this, or you have a choice about doing this'. A consumer should know whether or not the commission for going down this path, as opposed to this path, is influenced by your commission.

Mr Johnston—Absolutely; we agree with that.

Senator CONROY—If you were to say to me that all the different products that are available have the same rate of commission then I think your position could stand.

Mr Johnston—Can we go back a step? In relation to Ms Vamos's comments, I did say that I was not familiar with exactly what had been said and we would need to check exactly what the question was that she was asked or whether it was made in a speech, and exactly what her comment was.

Senator CONROY—Does she do many travelling road shows with Senator Ferguson?

Mr Johnston—She does many travelling road shows. We do not do them in conjunction with Senator Ferguson.

Senator CONROY—I am pleased to hear that.

Mr Johnston—He may have been on the same platform but invited by someone else. The purpose of the statement of advice is that, where an adviser provides personal advice to a client, the client has a right to understand what relationships the adviser has to distributors or product providers and what incentives the adviser is acting under. Most importantly, in the statement of advice, the adviser needs to take into account the needs of the client and give advice that is appropriate to the needs of the client. I think I said that if we were talking about a plain vanilla general insurance product, where it was very clear that there was a cost and a benefit to the client and there was no other choice that was available, where there was only one product that the person could offer, it may be argued that the commission does not influence the advice that is given.

Senator CONROY—Can I put to you the fact that he is tied so he can offer only one product. It implies completely that the only reason he is offering that product is because of the commission. He is not offering it for any other reason. I am not allowed to offer you any other product because if I do I lose my commission, therefore I am offering you one product.

Mr Johnston—The adviser would have to disclose that that was the case with the product being offered. The product would have to be researched in terms of the neat analysis that has to be done in respect of the client—that is an earlier client rule. The adviser then has to say, 'This is a product that is suitable for your needs, here are the costs and benefits to you in obtaining the product.' But we would argue that full disclosure should be made as a matter of good practice in any event.

Senator CONROY—I am not interested in what you think is good practice, I am interested in what you are going to enforce as the law—and they are two very different things.

Mr Johnston—There is an argument that has been put to us that you may not need to disclose commission in that respect, but it is something that is under our notice.

Senator CONROY—Thank you; I have at least got the admission that you have not finalised your position on it.

Mr Johnston—I think I did say it was an argument that had been put.

Senator CONROY—As I said, there will be a lot of people reading this transcript—many thousands of people I am sure are going to be advised about this transcript—and having a good look at it. I come back to this question of knowing your client. When you are sitting there working through the financial advice and you are offering a menu of options which is by and large what will happen in these circumstances they could say, 'There's a managed trust here, there's this here.' In that circumstance do you believe that there are alternative paths that can be gone down and that the client is entitled to know the level of commission?

Mr Johnston—Absolutely.

CHAIRMAN—On investment.

Senator CONROY—I take Senator Chapman's interjection that that is largely investment.

Mr Johnston—If there was a choice with respect to risk products we would make the same argument because the client then does have a choice. The investment adviser or the agent, whatever type of person it is, is providing a choice to the client based on the needs of the client; should do a full needs analysis; should say, 'Based on those needs your objectives, your risk profile et cetera, here is a suite of products that might well be suitable for you, here are the relationships that I have in respect of these and here is the commission I might receive.' We would support that strongly.

Senator CONROY—Do you think that the only situation where in the SOA there may not be a need—I am just seeking your view, not your final position—is if there is only one product for, say, car insurance? I am just picking a product.

Mr Johnston—That is the type of product where that argument is put.

Senator CONROY—Or life.

Mr Johnston—That is the type of product where the argument is put. It is where there is nothing that influences the adviser in respect of that particular product.

Senator CONROY—Can I put to you a comparable situation. Many people will look at the home loan market at the moment and say, 'Here's your basic product'. Wizard, say, has a basic home loan product that goes bang. If you take that you get the lowest possible rate. Some critics in the industry would argue that you can find almost nobody on that minimum rate because by the time the guy has finished talking to you on the phone or face to face he has convinced you. There are a whole variety of bells and whistles in alternative offshoots to the product that you

can take, so it is not the plain vanilla, if I can borrow your phrase. The same applies to insurance. It is what is covered, how much is covered.

Mr Johnston—I agree with that.

Senator CONROY—No company has one vanilla product per se for any car or anything like that. They have a variety of different products. I would find it quite extraordinary if suddenly the car insurance offered by one company collapsed into one product. So there is almost no circumstance where individuals would only have one plain vanilla car insurance product to offer.

Mr Johnston—It is not for me to argue on behalf of the industry. They would argue probably that there is one car policy but there are variables in terms of the excess, how you pay the premium et cetera, which costs more.

Senator CONROY—Which costs more and has different commission levels. In your view, if there is that variety of excesses and those sorts of things, is that still all within your definition of one vanilla product?

Mr Johnston—It is a matter of fact as to whether there is one product or more products that a distributor can offer, we would say that.

Senator CONROY—I am looking for the bells and whistles on the plain vanilla.

Mr Johnston—We would need to take that on notice because we have not thought right down that path as to the variables that sit within one product. We have not considered that.

Senator CONROY—I accept that you have still got that under consideration. It was put to the committee yesterday. Ms Vamos confirmed what Senator Ferguson had said. I accept that that could be a verballing—

Mr Johnston—Yes.

Senator CONROY—and I accept your caution. Thank you on that. I was wanting to finish a conversation I was having with Ian in terms of BHP Billiton and the accounting standards issues. We were having some discussion the week before at estimates.

Mr Mackintosh—In relation to this subject, I have prepared some notes and I wonder if it would be useful if I read them.

Senator CONROY—I would happily accept them tabled or if you are able to or allowed to—

Mr Mackintosh—They are not all that extensive so I could read them.

Senator CONROY—That would be great.

Mr Mackintosh—The subject is accounting for dual listed companies. There are two bits. There is a quick summary first and then a lengthier explanation. With respect to the summary of financial reporting considerations for DLCs, in determining financial reporting requirements for Australian companies entering into dual listed arrangements ASIC has, firstly, worked within the existing Australian accounting framework and has not used its discretionary powers to waive any substantive requirements of that framework. Secondly, ASIC has had regard, as far as the standards allow, to substance over form. Thirdly, where the arrangements are not in substance and acquisition for the purposes of Australian accounting standards, ASIC required the Australian company to prepare combined financial statements for the entities concerned in Australian dollars and under Australian GAP. Fourthly, ASIC required the Australian company to continue to prepare consolidated financial statements for its group, and parent entity financial statements for itself, again in Australian dollars and under Australian GAP. So that is the brief summary.

Just a bit broader: in recent months ASIC has given considerable attention to the financial reporting requirements for Australian companies which are proposing to enter into dual listed company arrangements. This includes the recently approved DLC arrangements between BHP and Billiton and the proposed arrangement between Brambles and GKN. At present there is no accounting standard dealing specifically with the financial reporting requirements for Australian companies in DLC structures. We have requested that the Australian Accounting Standards Board undertake development of appropriate guidance to clarify the accounting treatment for DLC structures as a matter of urgency. The AASB have put this matter as a high priority on their agenda and we have every reason to believe that they will deal with it expeditiously.

Until the AASB has issued an accounting standard or other appropriate guidance, ASIC has been working with those companies proposing to enter into DLCs as to how we expect the existing requirements of the law, including the accounting standards, to be applied to their proposed DLC structures. ASIC is aiming to provide draft guidance on our view of the issues in the next month or so. ASIC is seeking to act in a constructive manner in relation to DLC arrangements, however we also have a responsibility to safeguard the interests of shareholders and other users of the financial reports of Australian companies in DLC structures and consider it important to maintain as far as practicable a level playing field between Australian corporates.

I would just like to run through, briefly, the features of DLC structures—so what it is we are dealing with. DLC structures typically bring two listed companies together in a manner in which neither company acquires shares in the other. DLC structures are formed by way of agreements between the two listed companies and amendments to their constitutions. The shareholders of each company will have to approve the DLC arrangements between the companies and the changes to the constitutions of the companies. The key features of the DLC structure proposals put to ASIC include: firstly, arrangements to equalise dividends and other distributions by the companies; secondly, the creation of a common shareholder voting pool achieved by using special purpose entities holding special voting chairs; and, thirdly, separate boards appointed at separate shareholder meetings but with common directors.

My next heading is ‘Acquisition and consolidation.’ ASIC has given particular regard to the application of acquisition accounting and consolidation requirements to listed companies entering into DLC structures. ASIC considers that certain DLC transactions and structures may give rise to acquisitions and control in substance, for the purposes of the relevant Australian

accounting standards, not withstanding their form. In these cases, assets of the aquiree would be recorded by reference to fair values, including goodwill. Where there is an acquisition in substance, ASIC considers that all the normal requirements of Australian accounting standards should be applied to the DLC transaction and structure. There are various factors that ASIC is likely to take into account in determining whether a DLC structure involves an acquisition in substance and control by one listed company over the other. These may include: the magnitude of differences in the relative sizes of the two listed companies at the creation of the DLC structure, and the nature of the contractual and other relationships between the entities. Our response in any particular case will be based on the facts provided to us.

With respect to other reporting requirements, if there is no acquisitional control, ASIC would expect that combined financial reports, for both the entities concerned, will be prepared by the Australian company and included in the company's normal financial report. ASIC considers that the normal Corporations Law requirements relating to consolidated financial statements and single entity financial statements would continue to apply. We expect these financial statements, and the combined financial statements, to be prepared in accordance with Australian accounting standards and in Australian dollars. ASIC will consider proposals to provide additional information in accordance with foreign reporting requirements and in foreign currency. So that is broadly the situation.

Senator CONROY—Thank you. That was an excellent summary. I know you have changed your schedule substantially to be here today to deal with these issues and I appreciate that. It is disappointing that the minister would not allow a briefing paper to be given to the opposition on this matter, which would have perhaps also meant you did not have to be here today but I will not expect you to comment on that.

I have always argued, that accounting standards are to try and get to the economic substance of a transaction, not the fiction necessarily put to auditors or accountants about what the bosses of a company want the transaction to look like. I am a little concerned when you say, 'we will accept the facts as provided to us.' I am sure you have seen the transcript and read the exchange between myself and Mr Alfredson, which was a robust discussion, again, going to the heart of this matter. I think, in the end, Mr Alfredson said, 'Look that is not a policy decision that we can make.' The facts provided to you by BHP Billiton is that it is not a take over; reverse or otherwise.

Mr Mackintosh—An acquisition.

Senator CONROY—It is not an acquisition. I put it to you that that is a fiction by management and that any attempt to put a fair value on their assets puts the value of BHP well past 60 per cent, even after they have sold BHP Steel. I am interested to know how you are going to deal with this problem?

Mr Mackintosh—In regard to it being a fiction, we have to work within the accounting framework that we have. We have a standard on acquisition and we have a standard on consolidation. We then have to take the facts that are given to us and it is my belief that BHP have been open and honest with us, as far as I can determine.

Senator CONROY—Have they given you some information that they did not give to the market?

Mr Mackintosh—No. But the discussions went on for a long time and I think they were open to us in disclosing the type of arrangement they were anticipating entering into to. We had to take that situation and contrast it to the standards and see where it fitted into the standards. It was our judgment, in that situation, looking particularly at the acquisition standard, that you could not fit that situation into the acquisition standard, even, as we have said, taking a strong substance over form view. That standard is a piece of law in the Corporations Law and we still have to operate within the law. You could have an opinion that perhaps the standard is not broad enough or that perhaps—

Senator CONROY—No, I do not think that there is a problem with the standard. What I am looking to find out here is whether Don Argus, who got away with bullying most of the investment houses in this country, is doing it to you as well.

Mr Mackintosh—Personally I did not feel bullied, although I did not deal with Mr Argus personally either.

Senator CONROY—Can I put to you that, of those that have tried to do an independent valuation of BHP assets, no-one has come in at 58:42 and that most have come in substantially higher than that based on a fair value of their assets. When BHP points to all these analysts around the world that have supported it, all of them supported the DLC structure but none of them or few of them made comment other than the paid company that provided the valuation. Few of them made comment on the actual valuations, though a number here in Australia did. None of the ones that had an independent look at the valuation here in Australia—in other words, had a look at the fair values being attributed by BHP Billiton to their assets around the world—came close to 60:40. In terms of the UK market, 60:40 or above means acquisition accounting. The question here is: do we have a similar economic substance position?

Mr Mackintosh—There are two parts to this. The first one is determining whether you think the deal that has been done is a good deal for the shareholders, and that is the analysis that has been done on whether the 58:42 is a fair deal for both sides. Your claim is that the analysts have looked at it and said, 'No, BHP is worth much more that 58 per cent of the two put together.' The shareholders had to agree to this deal. It is not something that was imposed on them. It is a proposition that has been put to them with proper documentation and that is their decision. Our decision then related to the accounting treatment, which comes out of that arrangement. The arrangement is 58:42 and we took that into account when we determined the substance of the transaction.

Senator CONROY—On what basis of a fair value of assets have you made the decision? Or have you just accepted what BHP have told you?

Mr Mackintosh—No, our decision is on the basis of the deal that the shareholders have accepted.

Senator CONROY—The fact that the shareholders have accepted it and management has said that this is the valuation that we are giving them is not the question. You have not looked at

substance over form. The fact that it has been voted for and that BHP shareholders of Australia were prepared to transfer $5 billion to their British counterparts should not influence the economic substance over the form that is being argued. In Britain it is 60:40; do we have a similar—

Mr Mackintosh—Yes, we have that as a broad guideline.

Senator CONROY—We have a 60:40 guideline, so you are accepting the assets that BHP sold off and that BHP's own internal process agreed to—BHP has this internal management process that says, 'How do we value this? What is our takeover?' They actually have guidelines about how to take over and how to value assets. BHP chose not to adhere to their own internal mechanisms. BHP asked initially for a valuation of the Billiton assets and was told, 'If you want a valuation, there is no deal.' This is all on the public record, and so I am putting to you that substance over form does not deliver a 58:42 ratio and you should account for it in a way in which is fairer and not the way you are being told to by Don Argus.

Mr Mackintosh—I would not agree with you, Senator. I think we should view the deal as it has been consummated between the two companies. I think a separate and distinct point is whether that is a fair deal. That is up the shareholders to decide.

Senator CONROY—No, they have made a decision and the fact that Australian shareholders have been prepared to transfer $5 billion to British shareholders is not the substance of this discussion or the substance of the transaction.

Mr Mackintosh—I would say the substance of the transaction is the transaction and that is what we judged it on.

Senator CONROY—No, they voted on whether they wanted a DLC because Don Argus said he would quit if they did not vote for it.

Mr Mackintosh—And they voted on 58:42.

Senator CONROY—But that is not the economic substance of the transaction. That is just an agreement between two boards of management.

Mr Mackintosh—It is the reality of the transaction.

Senator CONROY—And the purpose of accounting standards is to get to the substance of the economic transaction, not to accept the form that is being proposed. The form that has been proposed was accepting a valuation method which almost nobody else in the world is prepared to cop, and if BHP had actually adhered to their own internal processes, they would not have copped it either. So the question is what accounting standard is going to apply. You are saying you are simply going to accept whatever you are told by management and, because management can blackmail enough institutions in this country, that you are going to roll over.

Mr Mackintosh—No, that is not what I said at all. In fact, it is not even close. I said what we accepted was the reality of the deal, and the reality of the—

Senator CONROY—No, you have accepted a shareholders' vote, which is not about the economic substance.

Mr Mackintosh—The transaction has been done and exists. That is the reality.

Senator CONROY—Just because management and shareholders say, 'This is the value we are prepared to accept' does not mean it is a true and fair valuation.

Mr Mackintosh—But in terms of how the two companies interact to work as a dual listed company, the voting is 58 to 42. That is the reality.

Senator CONROY—But the asset base—and your job is to get to some economic substance of this entity, not to just accept two numbers—

Mr Mackintosh—I understand your point. We are having a difference of opinion on what is the economic substance of the transaction. You are claiming that we should go back behind the transaction—

Senator CONROY—Yes.

Mr Mackintosh—And we are saying no, we go to the substance of the transaction.

Senator CONROY—Therefore, you are accepting whatever management puts to you. You are not looking at substance over form.

Mr Mackintosh—We are. We are looking at the substance of the transaction that has been approved.

Senator CONROY—You are looking at an outcome. That has got nothing to do with the substance over the form, Mr Mackintosh.

Mr Mackintosh—I think it has.

Senator CONROY—There is no point in our arguing about this for the rest of the morning. It is just disappointing to see that the accounting standards in this country are going to be collapsed just when big business tells you to collapse them.

Mr Mackintosh—I do not concede that.

Senator GIBSON—Senator, that is an unfair allegation.

CHAIRMAN—Perhaps there is another question.

Senator CONROY—I am happy to cede to someone else.

Senator GIBSON—Mr Knott, your annual report from last year canvasses what has happened with staff. I looked at the staff page, page 50, which shows you have 1,200-odd people—954 permanent staff; 253 temporary staff; 52 contractors and 15 consultants. Five years

ago there was a lot of talk in the marketplace that there were not enough street smart people in your organisation. I have got to say that today I do not hear any of that talk. So I congratulate the organisation in overcoming that hurdle. You have done that, I believe, by producing results.

My query is this: do you believe the organisation now is attractive enough for top quality people in the marketplace to want to spend some time with your organisation as a real plus to their CV for their longer-term future? In other words, have you reached a goal whereby ASIC is a place that every young person in law, accounting or in financial markets would like to spend a few years in, as a real plus for their longer-term future?

Mr Knott—Senator, I am glad that you refined your question there by adding the word 'young'. I was inclined to answer it personally, but I will now talk about it in the—

Senator MURRAY—If this is an ageist discussion, does it mean that I will have to leave the room?

Mr Knott—We might all have to! I think the answer is basically yes, although I have to add that we cannot be competitive with private sector remuneration approaches, as you would know.

Senator GIBSON—I know that, and that is why it is important to have this other attraction.

Mr Knott—The experience is that we attract people for some time—that may be for some years but we do have a reasonable turnover of good people going into other pursuits. We find that people are attracted for a variety of reasons, but in the main these people who come to ASIC are committed to the public policy role that we play.

The work itself is extremely interesting and gives people exposure to a variety of work they would not easily find in the private sector. To some extent we can offer some flexibility of workplace conditions that might not apply in the private sector, although in that respect I must say that people who come to us thinking that life might be a little easier are quickly disillusioned. That is a realistic assessment of the way that people are working in our organisation. They work extremely long hours that in my experience would compare with any demands that are being placed in the private sector.

Senator GIBSON—Is your expectation that you will increase your amount of contract and consultant staff in forthcoming years, or is the current level about right? Do you have any views on this?

Mr Knott—It depends to some extent on the seniority of the staff we are talking about. We tend to bring more senior people in under the contracting type provisions rather than the APS provisions. That reflects the fact that they may be term employees joining us for around three to five years. But of course other recruitment still continues through the APS structure.

Senator GIBSON—If I may switch to the balance sheets, I guess you are not happy to have a negative net equity position for 30 June 2000, but I do note that has largely come about due to the abnormal item—getting out of a lease—of $4.7 million. I assume therefore that your expectation is that in a couple of weeks time you will have a net equity position back in the black.

Mr Knott—I am not sure that I could give you that assurance, Senator.

Senator GIBSON—But am I correct in assuming that the main abnormal item was that $4.7 million?

Mr Knott—It certainly was the main abnormal item.

Senator GIBSON—That is obviously the thing that stands out, when looking at the accounts, and that is keeping you back in the wrong direction.

Senator MURRAY—So you are not trading while insolvent?

Mr Knott—I am pleased we are not trading!

Senator MURRAY—Good answer.

CHAIRMAN—You will be aware of the joint committee's report on transparency of electronic banking transactions. ASIC also has a working group working on that. In our report we indicate—

Senator COONEY—You cannot assume that.

CHAIRMAN—I was referring to the committee's report on electronic banking transactions and ASIC's working group on the same matter. In that report we indicated that as a committee we would monitor on a quarterly basis the progress being made towards full up-front transparency of electronic banking. I think our recommendation was that there should be a move towards that somewhat more quickly than ASIC has indicated that they were working towards it. Can you give us a report on progress towards transparency in electronic banking?

Mr Kell—As you know, we put out our draft guide to bank fee disclosure a little earlier this year. The timetable for the acceptance of submissions only ended about two weeks ago. We are currently assessing those submissions. We are pleased to see that there is a lot of support, generally, for the sorts of disclosures that we have set out in that guide. Indeed, some institutions have already moved towards disclosing things such as fees at foreign ATM machines. For example, if you are a Commonwealth Bank customer using a Westpac ATM, how much is that going to cost?

The issue of real-time electronic disclosure is still the most contentious issue. In particular, the time frame around that issue is still contentious. That has certainly come through in those submissions. We have not had a chance to go through them all in depth as yet, but it is probably not going to come as a big surprise for you to hear that we still have quite a significant divergence of views between the institutions and consumer and other organisations on that point.

In terms of going forward, we are aiming to come out with a final guide to fee disclosure in August. We may be doing some consultation before then, and I would say the most significant issue we are going to have to address is the issue of the time frame of real-time disclosure and

when that can realistically be introduced. Obviously, we would like to see it come in as soon as possible and we appreciate the work that came through in the report from the committee that you chaired, but that is something that we will be talking to our various stakeholders about in the next month or two, and we are happy to have a discussion with you on that point.

CHAIRMAN—Mr Knott, have you had an opportunity to reflect on the issue I raised with you in the context of another committee on Tuesday, and that was the article by Trevor Sykes and his proposals in relation to major collapses: that the investigator's report be made public, and that the investigation and the committal proceedings be rolled into one? What might be the efficacy of that?

Mr Knott—I have not had much opportunity, in view of other events since we last met, to add to that. I do not think I can add much to the answer I gave at the time. I do intend to talk to that journalist and explore his thinking a bit further. At this stage, I have not had an opportunity to add to those matters that we discussed on Tuesday—the issues of confidentiality and protecting rights on the one hand and, in terms of the investigation, the factors that support the existing ASIC leading to DPP prosecution, on the other.

Senator GIBSON—A recent BRW article, 'Fair exchange is no robbery' on 25 May, by David Crowe, makes reference to electronic format information for both the ASX and ASIC. In effect, the recommendation is:

> It is time to change the law: ASIC should require companies to post sensitive information on their own Web sites as soon as possible after releasing it to the market or filing a document to Asic.

Do you have any comment to make?

Mr Knott—I have not read that article, but my immediate reaction is, firstly, to refer to the law in terms of continuous disclosure. If we are talking about listed companies, we know what the law is on those and, if they are issuing material anywhere of a price sensitive nature that falls within the continuous disclosure requirement, they should be immediately making it available to the exchange. In terms of what goes onto their own web sites, of course you will be familiar with the quite extensive debate in Australia last year on the so-called 'heard it on the grapevine' policy that we released. That policy, which is, in a sense, a best practice policy that is outside the law, encourages companies very strongly to do exactly that. It is not so much because it is intended to make price sensitive information available which is not otherwise available; it is to address the perception that, if companies are having one-to-one discussions with analysts and the like, the substance of which is not available to other shareholders, there is a more favoured group of recipients of information. We have strongly encouraged companies, when they are discussing company affairs with particular groups, to put the substance of those discussions up onto their web sites. Many of our best companies are doing that, and the practice in that area has increased quite substantially, even in the last 12 months.

Senator COONEY—Presuming that the community wants to get good corporate life flourishing in Australia, a variety of issues come up, some of which you handle. I was asking before about the Australian Federal Police and the National Crime Authority. Does ASIC come together with groups that might also be helping in this area, like the ACCC and the APRA and all these others? Do you ever have conferences in beautiful Sydney, or anywhere else for that

matter? I will not say it in such a jocular fashion, but do you get away and have a talk about how corporate life in Australia is going?

Mr Knott—Yes, we have quite strong lines of dialogue with other regulatory and enforcement agencies. We meet regularly, for example, with the DPP. We have upgraded the level of those meetings in the last few months so that they now involve direct meetings between the commission and the DPP as well as meetings at other, more operational levels. We have, of course, a strong connection with APRA. Until quite recently, we had a member of our commission on the board.

Senator COONEY—A very eminent member, I thought.

Mr Knott—My predecessor will be pleased to hear it.

Senator COONEY—When I saw that person go, I lost faith in the APRA board from then on. I said, 'The best has gone here.'

Mr Knott—In relation to other law enforcement agencies, there is a forum called HOCLEA, which is the Heads of Commonwealth Law Enforcement Agencies, which we attend. We have MOUs with most of the relevant agencies, including the ACCC that you have mentioned. We meet with them also on a reasonably regular basis. The coordination of our law enforcement agencies in Australia is good and the cooperation is good.

Senator COONEY—Leading on from that, you could get the idea that all ASIC is about is law enforcing or regulating. But it has also got a facilitating function. Could we hear a bit about that? Sometimes you hear complaints—I am sure they are unjustified. For example, ordinary shareholders or somebody trying to find out about companies might want to get in touch with your organisation but has a lot of trouble getting through on the phone. Do you have those press button phones where you press button A, B or C depending on the information you want?

Mr Knott—There is a chorus of noes resounding in my ears. Mr Drysdale, in addition to being our regional commissioner in Victoria, is the national director in charge of our public information 'programs', so-called. That is the whole range of activities whereby companies are registered, changes are notified, et cetera.

Senator COONEY—Exactly.

Mr Knott—Of the 1.2 million companies, over 60 per cent of them deal with us online, but perhaps Mark could help you.

Mr Drysdale—We have an info line, which has a 13 number that people call in increasing numbers. The percentage increase in calls on that is double figures each year. Much of our information is now available through our web site, with free searches on the Internet, which have grown exponentially over the last couple of years. We have various publications that we put out regularly, such as *ASIC News*, to various stakeholders in which we outline not only our enforcement outcomes but also our policies—some of the things you have asked about today in terms of financial services review and policy development, et cetera. We have an active outreach program. Other areas that you may be referring to, which occupy the regional office,

include the work that we do with companies that are seeking to list in initial public offerings, the applications for licences that we get from securities dealers and proper authority holders, et cetera, and the work we do with those people to get them to an acceptable standard. They are all examples of the sorts of things we do that are not enforcement related.

Senator COONEY—Are there any of those press button phones?

Mr Drysdale—When you ring the ASIC info line you speak to humans.

Senator COONEY—But do you get to the humans through the buttons or does somebody pick up the phone and say, 'Hello, it's a lovely day in Sydney, today.'

Mr Drysdale—That is right. Somebody picks up the phone. Our info line is based in the Latrobe Valley, where it is always a lovely day.

Senator COONEY—I should not say this, but haven't you cut down on your staff in the Latrobe Valley recently?

Mr Drysdale—We have.

Senator COONEY—The local member rang up and I said, 'They're really nice people,' and I had to talk hard to convince him that you were.

Mr Drysdale—That is an interesting story. There has been a cut back in the information processing centre total staff. That is essentially because of technology change—people are now able to electronically lodge annual returns and electronically register companies through the different systems that we have brought in and which are available through information brokers. The actual volume of processing work that the processing centre has to deal with has been declining at a faster rate than the number of companies has been increasing—if you can follow.

Senator COONEY—Yes. You are satisfied that the human face is still there, that people who cannot manage these machines—infernal machines, some of us would say—can, nevertheless, get service from your organisation?

Mr Drysdale—I am confident of that. The stakeholder feedback surveys that we do support that. We get very strong positive numbers on things like the reliability of the information, the access to it, the support that people get when they contact us.

Ms Segal—I would like to add one small thing, if you can forgive us for sometimes patting ourselves on the back. In terms of the electronification that Mr Drysdale spoke of, we have in this last year won the Australian Information Industry Association National Awards for Excellence through Information Technology because we have provided an electronic company registration service which was a response to the perceived need of people—obviously not everyone, but there was a request from a range of people to provide that electronically so people did not have to lodge everything in person. That was awarded for excellence and outstanding achievement. We really are trying to provide service and listen to people wanting to provide new services.

Senator COONEY—What was that award—you ought to put it on the record?

Ms Segal—The Australian Information Industry Association National Awards for Excellence through Information Technology for our electronic company registration service.

Senator COONEY—When you have to make people redundant, do you do it tenderly, if you can do that tenderly? What did you do? Did you look after them well?

Mr Knott—We are essentially a public sector agency and, as you would know, Senator, the public sector does manage these things as humanely as possible. It is never an easy process but we follow all the procedures that you would expect a good employer to adopt.

Senator COONEY—There is a danger that I am being very parochial here—and I would probably be proud of that. The Latrobe Valley—

Senator MURRAY—Where is it? Victoria?

Senator COONEY—The Latrobe Valley is one of those sort of depressed areas and this is a very important organisation down in Latrobe Valley.

Senator MURRAY—Mr Charles is the member for La Trobe.

Senator COONEY—Not the Latrobe Valley. You are a man who needs to be educated. You are a man who needs to be introduced to people.

Senator MURRAY—Many say that.

Senator COONEY—Well, that is right. Clearly, you talk about the regulatory aspect of your organisation, as we have heard. What about the internal, almost soul searching, examination of how you go about servicing companies and the community and being the facilitator? Do you have discussions about that too?

Mr Knott—Yes. To put it in context, and more detailed information is in the report, only about 25 to 30 per cent of our budget and work is enforcement related.

Senator COONEY—That is what I thought.

Mr Knott—We have a huge commitment to delivering other services to the community. Public information services we have just been talking about, but there is also a range of regulatory areas. The whole fund raising area we have not spoken about today—there has been huge activity over the last 12 months or so in that area. More recently there has been consumer protection, and there are mergers and acquisitions. The policy side of our business is an extremely important and quite vibrant side which deals daily with people seeking modifications, exemptions or variations of the law in order to make commercial transactions work, and we have a huge commitment to that.

Senator COONEY—The picture often is that you, along with other law enforcement agencies, are a dark cloud over the corporate sector. That is how it is often painted. Whereas what you are doing is trying to clear the sky so it is nice and blue.

Mr Knott—That is not the picture that is fed back to us. If anything, the criticism of ASIC in more recent times is that the enforcement side has not been as dark and cloudy as you would paint it. We do survey stakeholders periodically to try to see what people are saying about us. I am not sure that there are a lot of other agencies that do that with the rigour that we have done it. The people who know and deal with us best are the people who rank us highest. That is good because it is suggesting to us that our customers are basically happy with the service that we provide. Like all organisations, there is always plenty of room for improvement. But, overall, business does not see us as a draconian, difficult, non-accessible type of agency.

Mr Johnston—To amplify that somewhat, there would not be a week go by in which we do not have some sort of liaison activity either with an industry group, a distributor group, a managed investment group or a consumer group. We meet on a weekly basis with various groups around the country, nationally and regionally, discussing with them issues on law reform, how we are performing, how we can facilitate their business and how we can assist. That happens on a week by week basis also.

Mr Kell—I can give some very quick examples. Yesterday, we announced that ASIC on the consumer side is helping consumers in getting out to investors. You mentioned that not everyone wants to access things electronically. We announced yesterday that we will be going out to Bunbury and Busselton in Western Australia. Last week we were out in Burke talking to consumers and in Albury talking to consumers in southern New South Wales. We have just recently held a very successful investment seminar in Adelaide and we have just been to Albany in Western Australia. As Mr Johnston said, going out and talking to people on the ground is something that we take very seriously and perform very regularly.

Senator COONEY—The only state you have left off is the state of my birth Tasmania. What is wrong with—

Mr Kell—I am sure Mr Drysdale has been over there!

Ms Segal—In terms of the policy work that we do—the guidance in the form of policies, which as the chairman mentioned takes up quite a lot of time, and the FSR policies we have released is just one example—we have received lots of feedback that people do value that process. It is a transparent process. We go out there with draft policies or policy proposals and seek comment—and not only written comment: we have meetings, round tables and workshops—and try to understand the issues that a particular policy raises for business and then translate that into a final policy. People have particularly commented on the process itself being an excellent one in trying to reach people, to understand and to seek information so that we can then base policy on an understanding of business.

Mr Johnston—I hope you do not mind if we take advantage of a rare opportunity to say some positive things about ourselves.

Senator MURRAY—I have got some more questions, so do not use up all the time.

Senator COONEY—We bring them in before these committees and say, 'Why haven't you done this? Why haven't you crushed so-and-so's toes? Why haven't you twisted his arm up his back?' Give them a go, I say.

Mr Johnston—One other example that may be worth highlighting is that we regularly also issue media releases and investor adviser alerts warning consumers about some of the types of scams that are around and types of investment opportunities that arise, and trying to educate consumers as to how they should reject those types of investment opportunities and how to identify them. We publish lists on our web site of those types of activities as well. We try to actively inform consumers about some of the pitfalls that they should best avoid.

Senator COONEY—I suppose you would be able to say that there is the odd law abiding and successful company in Australia as well?

Mr Johnston—Very many ofthem, and we try to facilitate their business.

Senator MURRAY—Odd as in unusual?

Senator COONEY—Senators on this committee like to go after the sensational thing and what the dreadful crime has been. It is nice now and then to say, 'People do all right.'

Mr Knott—Thank you, Senator.

CHAIRMAN—Senator Murray.

Senator COONEY—He wants to ask some nasty questions!

Senator MURRAY—Now you know why he is much loved—and I mean that. I need to deal with a matter that was put before us—a letter that the secretariat has circulated. Can I ask that it be tabled and then I can give a copy—

CHAIRMAN—I think it was tabled at one of our private meetings.

Senator MURRAY—I have to ask questions from it, and if it can be tabled that would assist. Could I refer it to anyone who deals with prospectuses generally? If you could just quickly read that letter I will ask you my question.

Mr Knott—While Mr Tregillis is reading the letter, may I volunteer a comment nevertheless? I think it is appropriate that Mr Tregillis deal with any detailed issues. I want to say that the policy change or clarification that we introduced earlier this year in relation to prospectus disclosure is something that we feel very strongly is in the interests of Australian investors and financial consumers. Our position arose out of a quite comprehensive review of the dot com experience in particular, as well as some consideration for the so-called agricultural schemes. One of the things we determined was that there had been an excessive use of hypothetical assumptions to substantiate investment outcomes. We all know that the more hypothetical assumptions there are, the more a house of cards is being constructed because in the end the experts say, 'I have looked at that. If those assumptions are correct and that is the

experience that results, this will be a viable and profitable enterprise.' But, of course, if the assumptions are not correct and the whole thing collapses people then stand back and say, 'We made it clear that these were assumptions.'

That is the background. It was our view that the dot com raisings in particular—but, as I say, some agricultural schemes as well—have overly relied on hypothetical assumptions. We say that forward looking financial information is very helpful to investors and we seek to encourage it. But it must be reasonably based. We say that the more hypothetical the assumption, the less likely it is to be reasonably based. That is the core of our thinking, which we will now be discussing in more detail. I do think it is important to get on the record why we have adopted this approach.

Senator MURRAY—Before I move to the officer concerned for some specific remarks, I should respond to you. Firstly, I agree absolutely with your proposition. In fact, recently in estimates I asked the Treasury to do the very same thing and, in fact, to go back to previous forecasts of financial results and explain why they are different from the modelling they put. I have long thought that the law should require those who put up prospectuses—say, three years after the initiation of the project—to indicate any differences from that which was forecast and to account for them. I think, in building up such case files, you will discover the boosters as opposed to the realists. I accord with that.

Before I move to the officer concerned, I must make it clear that I am raising this as a Western Australian senator. I do not know Mr Mangano, who has written to me, and I have no connection with, or interest whatsoever in, Australian Growth Limited, and neither does my party. However, I thought it was pertinent to bring it to this occasion because it reflects a general concern. It is not particular to this person or this company and I would like a view as to the remarks made. The particular point that really is apparent here is what anyone who understands business and finance knows: that different kinds of industries have different rates of return and payback periods.

In many respects, if you enter into a mining venture, you might not get a payback sooner than eight years; in pipelines, it can be 15 years; in retail, it can be six months. It does depend on the particular situation. Can I indicate for the record that the prime concern here is that this is a plantation timber project—and there are many of these—and the returns at the time of harvest range, according to the information before us, from 10 years for blue gums to 25 years for pine trees. It is very long term, and they say that they are being required only to put prospectus estimations for two to three years.

The one last thing I should say in covering this is to declare that I am a participating member of the committee which is looking into the tax investment scheme problem, so I am very much acquainted with that side of things. I understand your reactions and sensitivities. After that long lead-in perhaps you could give me your views.

Mr Knott—I might also invite Mr Johnston to participate in this discussion because, as you would be aware from the committee you have just mentioned, he also has had involvement in the so-called agricultural or tax related schemes, so he is also quite aware of this sort of situation.

Senator MURRAY—Please be aware that we will use the text of your response as the response to this person who has written to the committee.

CHAIRMAN—It would probably be best if you could outline the policy position.

Mr Tregillis—I cannot comment on the particular matter, because I am not personally familiar with this entity. I can really only make a couple of comments about the general policy.

As the chairman has clearly outlined, what we are requiring and what the law requires is that forward-looking statements have a reasonable basis. The policy position—and I will read the key issue here—is that 'the statement that goes beyond two years is hypothetical and hence misleading'.

Our approach is that that is one of the indicators. There is no strict rule that a forward-looking statement going out beyond two years is, by its very nature, unreasonable or not justified and misleading. What we do say is that if it is for less than two years, then it is more than likely that it can be substantiated and reasonable. In our review process we take that into account.

There are other ways in which we say that people can demonstrate in their prospectus documents that a longer-term forward-looking statement is reasonable. Some of the examples are where you have locked-in contracts. As you say, it actually does reflect the nature of the different businesses, and there is a whole range of different circumstances that we take into account. If there are clearly forward contracts that are locked in, then they can provide best-estimate revenue assumptions.

We have also said that where an expert is prepared to make a positive statement that the revenue and forward-looking statements are reasonable, we will accept that. We have accepted a range of other sorts of circumstances where people demonstrate the fundamental proposition that there are reasonable underlying assumptions and that therefore the forward-looking statement is reasonable.

The two years is really a rule of thumb. If it is under two years then we say that normally, subject to scrutiny, a test is somewhat easier to satisfy that it is reasonably based. Beyond two years you need to demonstrate that there is a reasonable basis for the revenue and the projections or the forecasts, and that can be done in a number of different ways.

Senator MURRAY—I interpret your response to mean that you do take a case-by-case attitude.

Mr Tregillis—We do take into account that there are a variety of different industries, and this applies—again, as the chairman said—from new start-ups to rural schemes to building property schemes, all of which have different factors. But the fundamental thing that I think we need to be clear about is that we do insist, and the law requires, that there is a reasonable basis for the forward-looking statement.

We have set out in discussions and elsewhere how people might meet that. Particularly in this area, if an expert is prepared to make a positive statement and back that up in terms of assumptions that the forward-looking statements are reasonable, we have accepted that, and

there are experts in forestry and other areas who are currently making those statements and justifying them.

Mr Johnston—Senator, I might just add: neither am I familiar with this particular company, but obviously aware of the issue as it affects the timber industry. As Mr Tregillis said, we are aware of experts who have given reports that have gone into prospectuses to support such forward-looking statements. What we have also attempted to do to assist people is advise them of some of those experts who have been prepared to prepare such reports. We have tried to facilitate that where we could. To go back to your question: you asked whether we do it on a case by case basis. We do, and in some cases where people have come to us advising they have a problem in this area we have said, 'Well, there are a number of experts, and here is a list of them, whose reports have appeared in prospectuses of a similar type to yours.' So we have tried to facilitate in that way.

Senator MURRAY—So, broadly speaking, you have an industry sector response. You develop a series of understanding about a particular industry, of what its typical estimates and prospects should be—I do not mean in a very specific sense but in a broad sense.

Mr Johnston—In a broad sense that is true.

Senator MURRAY—You are able, therefore, not to fall into the trap of one size fits all?

Mr Johnston—That is certainly our intent, and that is why we look at it on a case by case basis. As you have indicated, we understand that there are differences across the different industry types. Hence we have suggested reference to panels of experts' reports that we have seen.

Senator MURRAY—The criticism here is essentially, if I interpret it correctly, is that this is one size fits all and your judgments do not suit projects such as this which have long-term returns. Is that criticism inaccurate?

Mr Johnston—I can repeat my answer, in terms of the fact that we have tried to help people find ways that they can demonstrate a basis on which those statements are reasonable. I quickly perused the letter. I guess I am hesitating because—

Senator MURRAY—Let me put my question a different way. You do take into account, don't you, from what you have said, industries whose rates of return vary over a time period?

Mr Tregillis—We do take into account that different industries have different pay-back periods, returns, differing commercial structures. The clear example, which is the easiest one to give, is that we have looked at a number of property schemes in some states. They raise different issues in terms of how you might actually have a reasonable basis for assumptions, so clearly we have put forward that where you have got locked-in contracts, long-term commercial leasing, that is the type of basis for reasonable assumption. In other industries we recognise that different experts are required. So we have taken those industry differences into account. I would add that, in terms of the process, we have had a senior officer actually go to Western Australia and Queensland to have direct face to face discussions with not only some of the participants involved but also some of the experts involved, to discuss the issues. If the accusation is that we

have not gone out there and talked to people in the industry or the experts, then that is not correct either.

Senator MURRAY—I think, Mr Knott, the public interest aspect of this—and this is just one example out of many I could take—is simply that your job is undoubtedly to limit as far as possible the number of shonks and shonky views that can emerge. We would all applaud that. But equally you do not want to be an impediment to legitimate capital raising for productive projects?

Mr Knott—That is completely right, and that is a balancing act which is difficult. There are some countries that simply will not allow this sort of thing. You would know that. We are more liberal in this country, in terms of allowing these sorts of capital raisings from the public. It is a question of demonstrating to us that the revenue projections are reasonable, and I do not think anybody should have an objection to that stance. In practice it becomes difficult with long lead-time projects. It is true that that is a practical problem.

Senator MURRAY—Thank you for taking the time to explore that. Unless there is anything further on this, I have just got one last issue. You raised an acronym earlier, in speaking with Senator Cooney, for the meeting of heads of law agreements. How do you spell that?

Mr Knott—That is Heads of Commonwealth Law Enforcement Agencies—HOCLEA.

Senator MURRAY—I will tell you a story out of school, but I will not name the senator. At a Senate hearing, at which matters of trade with Japan were being discussed, Osaka was mentioned several times and, at the conclusion of an interchange, the senator was heard to say, 'Osaka, Osaka, what is that? I am sick of all these acronyms.'

Mr Knott—You could not work for ASIC if you did not have a love of acronyms.

CHAIRMAN—Can I ask a little bit about your international activities? As I recall, several years ago ASIC was involved in advising China about setting up their regulatory regime for the equities market. Is that support still being given to China, in particular, and any other countries?

Mr Knott—Yes, it is.

CHAIRMAN—If so, does it generate revenue for you, or is it done purely on a goodwill basis?

Mr Knott—I wish. There is a serious aspect to it, in truth, because the demands being made of us for assistance from our own region, in particular, are growing all the time. We do what we can, but there are obviously some limitations on what we can do at our own expense. It is not always at our own expense. There have been, from time to time, government grants that have been made available to provide assistance, either from this country or other countries. We are extensively involved in international work, both through IOSCO, of course, but also more bilaterally. There is quite a major corporate governance initiative known as ACORN, in which we have played a lead. It is sponsored out of our Western Australian office, in combination with one of the universities there. That has seen us provide assistance on corporate governance issues to Vietnam and other countries in South-East Asia. We are, in fact, active in that area.

CHAIRMAN—What progress is being made in those countries, in terms of the efficacy of their markets?

Mr Knott—I do not want to mention any countries, so I will divorce this answer from the previous one. There are, I think, increasing signs throughout the Asia-Pacific area that a strengthening of their institutional base and of their regulatory base is absolutely critical if they are to play a part in globalisation. It is that factor that is driving them more than anything else. It is becoming more difficult all the time for any country to be stand-alone. Obviously some of them have a long way to go. You can put a regulatory structure in place very quickly, but unless your institutional structure is sound and has a history to it, it is obviously more fragile. For a number of countries, that just means this will take time and they are going to have to continue to work harder.

Ms Segal—As an example of that, late last year we hosted, as one of the initiatives with aid to the region, or assistance in this regard, a week-long view of all the institutions so that it was not just a matter of coming to visit ASIC, but of gaining an understanding of the Institute of Company Directors, the Stock Exchange, the court structure, the Securities Institute of Australia and all the institutions that go to make the governance framework. Representatives came from many of the countries in our region. In fact, it was a very sought after week that we hosted to enable them to have a look at the entire structure so that they could go back and, in each case, look at particular needs that they might have had in terms of furthering an Institute of Company Directors or furthering some other institution. That was through APEC.

Mr Knott—The week-long summer school that we run, of which there was another very successful one last summer, which this year focused on regulation relating to retail products and the evolving markets in retail financial products, also attracts attendance from overseas parties, both from our region and, indeed, from around the world. We continue to be active.

CHAIRMAN—You have recently released several PPSs in relation to the Financial Services Reform Bill and have sought responses. Have you had any significant response back on those yet and, if so, can you perhaps give us a feel for what is coming back?

Mr Johnston—Yes, we have. I could not tell you the number thus far because we issued one tranche and the closing date for submissions is just now. The second tranche we issued recently and not until the first week of July does that close off for submissions.

In relation to the first tranche we can make some comment about the types of input that we have received. Firstly, I think it was the deputy chair who said earlier that we have received very positive feedback in terms of the process that we are actually following and the fact that we say that this is what the law says and we will now try and give you guidance as to how we interpret the law. Those policy proposal papers then go into a number of specific matters covered by the bill and say, 'Here is how we think. These things might be interpreted but please tell us whether you agree and where you think the gaps are.' So the process has been applauded.

In terms of some of the specific comments we have received, as you would expect there is a range of responses, sometimes allied to the sector of industry that is responding to us. For example, in respect of our PPP on product disclosure, there is a range of responses—some people saying, 'We think ASIC should be more prescriptive in terms of what it thinks ought to

be in a disclosure document.' Other areas of the market are saying, 'We think you should not be prescriptive and that you should give only very minimal guidance to us.' So there is a range. But there is nothing that is standing out as a very strong negative issue that we think we need to look at at this stage, but it is early.

CHAIRMAN—Any further questions? If not, I thank you, Mr Knott and commissioners and your staff, for your appearance before the committee this morning and for your answers to our questions.

Proceedings suspended from 11.48 a.m. to 12.05 p.m.

JACKSON, Mr David John, Director, Australian Shareholders Association Ltd

ROFE, Mr Alfred Edward Fulton, Chairman, Australian Shareholders Association Ltd

CHAIRMAN—Welcome. Do you wish to make an opening statement before we proceed to questions?

Mr Rofe—I would like to raise a number of issues, if I may. As I mentioned yesterday, David is the ASA's representative on ASIC's Consumer Advisory Panel. He is also our representative on the Financial Reporting Council. Thank you for inviting us to be here today. As you would know, on a previous occasion I expressed my surprise that ASIC's stakeholders have not taken the opportunity to participate in this annual review of ASIC's performance. To me it is a little bit analogous to the phenomenon we experience in relation to company AGMs, where shareholders criticise a company's performance but do not bother to attend the AGM, vote or appoint proxies to question the directors and vote against their excessive remuneration packages. However, as usual we are here today to represent individual investors and to ask the difficult questions.

Before I start I would like to give a few bouquets to ASIC in confirmation of some of the things they said earlier today. Their role in monitoring prospectuses recently has been needed and very beneficial to investors. They have played an important role in monitoring managed investment schemes and their compliance plans. A lot of the information I have about this is anecdotal, but I think there is evidence of it in some of the enforceable undertakings published on the web site. More generally, the use of the new power in the Corporations Law to accept enforceable undertakings is proving very useful. They have also had some successful investigations. Simon Hannes, and Geoffrey Dexter and the Wattle Group, are good examples. I would also like to confirm what Jillian Segal said in relation to electronic lodgment. I have certainly had some experience with it, and I think it is fair to say that ASIC has been leading the field in its use of electronic commerce in recent years.

On this electronic area, I would like to comment on two of the points mentioned by Mark Drysdale. Certainly the info line is very useful. As we said in reply to Senator Cooney, you do not have to press buttons; you do actually get a human being, who I have found always very helpful. Sometimes recently there has a bit of a delay. I hope that is not a function of a reduction in staff down there in the Latrobe Valley. Certainly I think it is a very good and useful initiative.

The other thing to comment on is the ASIC web site. Again that is very useful. But I would comment on some other remarks by Mark Drysdale. He referred to free searches on the Internet. I am afraid that is a bit of an overstatement. If you go onto the ASIC web site you get a chance to search its register, so you can find if a company is registered, but you cannot find out any more details. We would strongly argue that you should be able to do a full search of company details on the web site. ASIC is encouraging consumers to take advantage of the web site when they are dealing with, let us say, the bloke that has come to do the gutters, to do a search to see whether the company really is registered and who the directors are. You cannot yet do that for free on the web site. Indeed, if you try and make use of some of these electronic services you can easily run up a bill of $100. We would argue the information is already there in ASIC's

electronic records; the marginal cost of making that available on the web site to consumers would be very small and a significant public benefit. Certainly retain the fees for people who do paper searches, who go in to the office, but I believe that as part of helping consumers to have do-it-yourself protection, that would be a very important public benefit.

I would like to move to the funding of and cost recovery by ASIC. In the past we have been critical of ASIC's response to complaints by the ASA and our members. It became quite a standing joke at one stage that if you made a complaint to ASIC you would get a form letter back saying, 'Thank you for bringing this matter to our attention. Unfortunately, due to our limited resources, we really cannot do anything about it,' and that was it. I must say that over the last year or two ASIC's complaints handling procedures have markedly improved and we are certainly not aware of that problem to the same extent. But, on the other hand, we believe that the question of ASIC's funding continues to be a major issue. I think it is very clear, if you look at the additional responsibilities which ASIC has been given in relation to licensing, managed investment schemes and consumer protection, obviously they are doing a lot more work. They need a lot more resources to carry out that work. And of course the workload is going to be further increased by the FSR Bill.

In addition, at the present time, ASIC is currently engaged in a number of major investigations, including in particular Harris Scarfe, HIH Insurance and One.Tel. I think it is essential that these activities not be inhibited by any lack of funding. I know that, at one stage, I think it was the Prime Minister announced additional funding of $5 million for the HIH investigation, and then subsequently there was some speculation in the media that that $5 million might in fact be diverted to the royal commission. I certainly hope there is no truth in that suggestion because obviously there is a big job being undertaken and, as I say, I think it is essential for investor protection and the public interest that ASIC not be inhibited in any way, including by lack of funding, in fully pursuing these investigations.

That leads me to a current inquiry by the Productivity Commission into cost recovery by Commonwealth agencies. Of course it covers a very wide field, but submissions have been made by participants in the financial services sector, including in particular APRA, IFSA, ASFA and NRMA Insurance, and I appeared before the commission last week. Appendix F of the commission's draft report deals specifically with cost recovery by ASIC and APRA and raises a number of significant issues. APRA has lodged a submission with the commission, and I am surprised that ASIC appears to have neither lodged a submission in response to these issues which have been raised, nor to have indicated its intention to appear before the commission. Let me refer to some of the figures here which I think are significant and which I think do call for a review.

If we take the figures from last year's ASIC annual report, we see that ASIC collected, mainly from fees and similar charges, $361 million. Of that $361 million, $132.4 million was used to fund ASIC's operations, $135 million was paid to the states and the Northern Territory, and $93.6 million was retained by the Commonwealth. We have referred to this in the past as a form of company taxation. I am interested to see that in appendix I to the Productivity Commission's report the Australian Government Solicitor confirms this view. It is a form of company tax for the benefit of the states, and it is an unfair tax. For example, if we look at the number of registered companies, something over a million companies are proprietary companies for which the annual return fee is $200. In other words, nearly two-thirds of the collection is

being collected from proprietary companies. It is an excessive and unfair tax on small business in Australia. It needs to be rectified. I will not go further into the detail.

We made some suggestions to the Productivity Commission about some reforms which could be made. That will appear in the commission's transcript. There are a couple of issues I would like to raise. Firstly, in relation to the funding of the Australian Accounting Standards Board, you might question whether this is quite within the terms of reference of the current hearings but in fact, under the ASIC Act, the AASB is an integral part of the regulatory scheme.

One of our arguments is that it should be funded through ASIC's collections. We are concerned that currently the AASB is funded still to a major extent by the accounting bodies and by the ASX. We are also concerned by suggestions by the Treasury that we might follow a US model and seek funding from private corporations. I think that would be a retrograde step. It would at least be perceived to affect the independence of the FRC and the AASB. It would be very undesirable if there were some implication that the weight of the vote of a member of the FRC was in any way affected by the extent of the contribution by the nominating body to the funding of the FRC and AASB. The major benefit of the standards produced by the AASB applies to public companies and in particular disclosing entities, which already pay fees to ASIC. Obviously there is a great deal of margin in the total fees collected by ASIC to cover the cost of the AASB which currently is about $3 million a year. David, do you want to add anything to that?

Mr Jackson—I agree with what Ted is saying. Given that there appears to be a surplus of $93 million, the funding of the FRC, which is very largely or almost entirely funding the AASB, should come directly from the ASIC collections. I do not see any reason why there should be—as I have said in the past—a cap-in-hand approach, going to accounting bodies and corporations to fund the production of accounting standards which are the lynchpin of producing reports and information to shareholders which is absolutely vital. It is a trivial amount in comparison with the total sums that we are looking at here.

Mr Rofe—One of the problems is that there seems to be an unrealistic approach by Treasury to suggest that there should be private funding. For one trivial example, members of most of the statutory and other bodies under the ASIC Act like CASAC and the Consumer Advisory Panel, in most cases have sitting fees paid or at the very least are reimbursed their travelling expenses for attending meetings. In the case of the FRC, David and other members have to fly down to Melbourne at their own expense to attend meetings. It is just an unrealistic approach and downgrades the status of those bodies.

I would like to say something in relation to transparency and accountability in relation to ASIC's annual report. There is a lot of detail there on what they do. There are conventional financial statements in the form of a statement of operating results and a balance sheet and a cash flow statement, but there is no useful detail of the costs of the services which they provide. The example I gave of the fees paid by proprietary companies is one illustration, but I think if you look at the CLERP 7 document it is clear that there is no appropriate relationship between fees charged to different industry participants and the services provided. I think, for example, it is clear in relation to those fees charged to proprietary companies, that the small end of town is in effect cross-subsidising the big end of town, and it is acknowledged here that fees for takeovers, prospectuses and so forth are far below the actual costs. I think it is something that

should be rectified. I was disturbed to read in the company's fees bill in about section 6—I thought I had it here but I do not seem to have—a statement that there should be no necessary relationship between the fees charged for services provided by ASIC and the cost of providing those services. I think it is a complete reversal of what should be the appropriate relationship.

I will move on to some other points. Regarding auditors, some comment was made earlier today about problems with audits, and in fact one of our members made the following statement to us. One firm of accountants signs off on a set of accounts which shows that the assets of a company substantially exceed its liabilities and that the accounts give a true and fair view. A couple of months later another firm of accountants who have been appointed as administrators reveal that the company has in fact been insolvent for the last three years, or that the inventory records have been falsified for the past six years. I think investors and the public are entitled to conclude that there are deficiencies in the performance of auditors and the quality of audits.

I know that on each occasion this issue is raised the accounting profession makes vague references to the so-called 'audit expectation gap,' and I note that there were recent statements attributed to Stephen Harrison, Executive Director of the Institute of Chartered Accountants in Australia, that there are relatively few problems with audit reports, that there are only three or four of these company crashes. Of course, the answer to that is that a cut price, poor quality company audit is just as satisfactory as a cut price insurance policy from HIH Insurance. So long as you do not need to make a claim on the policy it is fine; it is only when the company collapses that the quality of the audit is tested, and I think we have had enough tests now to question the quality of the audit function. I do not subscribe to Tony Harris's suggestion that ASIC should appoint auditors, but I do think there is a role to play similar to the role that I mentioned earlier that they had been playing in relation to managed investment schemes. They should do checks and, if there is some question about the quality of the performance, they should get another firm to do an independent review, and of course the costs there are passed on to the company so it is not a burden on the public purse.

Secondly, I think there is a role for ASIC to play in issuing something of the nature of practice notes or perhaps policy statements dealing with the conduct of auditors. Recently we had some correspondence with ASIC about the audit of forecast financial statements and our comment was that the relevant auditing guide appeared to be concerned more with protecting auditors from potential liability than with ensuring that useful information was provided to investors. I think that same criticism could be levelled at some of the auditing statements and guidelines issued by the Auditing Standards Board—a board, I think it is fair to say, that is dominated by the profession, that a lot of these statements are more concerned to protect auditors from potential liability than they are in ensuring that investors receive financial statements on which they can rely. As I say, I believe there is a role which ASIC could usefully play there.

On this question of accountability and transparency of ASIC, in the Productivity Commission draft report there is reference to three of the recommendations of the Wallis committee dealing with regulatory agencies charges, how they are set, and whether they should be off budget. I think there are two other recommendations which could be reviewed, re-examined. The first is recommendation 108, that regulatory agencies should have boards with majorities of independent directors. I think there is an argument that there are not adequate mechanisms in place to review, firstly, the accountability of ASIC in a financial sense. As I said earlier, the

annual report has a lot of statements of what they do, which I think are very valid, and there are these conventional financial statements, but there is no useful information published of the cost of ASIC providing those services.

One mechanism to provide some sort of accountability would be to have independent, part-time members of the commission. There is already provision in the ASIC Act for up to five part-time commissioners to be appointed. I think it would be worthwhile having another look at that provision. That is the first point that might be served there—accountability. The second is the priorities and policies of ASIC. I have no great complaint at the present stage as to what ASIC is doing, but I think it would be useful to have some formal input from industry as to areas that they should be focusing on and how they are going about things. I think that is something that is worth a second look.

I notice that in one recommendation it was suggested there should be cross-membership of boards, including APRA. I guess one could say of that that it seemed a good idea at the time but, just as with public company boards, cross-membership sometimes has its problems. With respect to recommendation 109, that regulatory agencies should improve their reporting, I have already mentioned that. I think it should not be limited to just what you might call conventional financial accounting, but reporting on the cost of the services provided. Yesterday I said something about problems with dispute resolution schemes. I do not think I need to repeat that today.

Another inquiry by the Productivity Commission concerned an inquiry into the SIS legislation at which we also appeared. There is only one point I would like to make about that. I mentioned yesterday the increasing convergence of superannuation and managed investments and the increasing importance of superannuation as a long-term investment medium. The suggestion we made to the Productivity Commission was that ASIC's role in relation to superannuation should be similar to its role in relation to managed investment schemes—you might say that is addressing the consumer aspects of superannuation, the honesty, integrity and accountability aspects, and perhaps leaving to APRA prudential supervision and the monitoring of national retirement incomes policy.

One other point I would like to mention—and it was again mentioned earlier today by ASIC—is ASIC's role in granting modifications of the Corporations Law. We have got a concern at the extent to which that power is now used. I do not think nowadays there is any takeover which does not involve some sort of modification of the law. I think one problem with that is perhaps a problem with the legislation. It is arguable that in a sense parliament has lost control of legislation. There is such a volume of legislation coming through now that in many cases there is not sufficient time and opportunity to get the details right, and I think in some cases ASIC is forced to step in and fix up the problems. But also I think there has been a tendency for ASIC to go further in granting exemptions and modifications without, in many cases, adequate review.

I will give one example. You may recall the debate and our concern about the new compulsory acquisition power which was introduced into the Corporations Law. I think the Labor Party and the Democrats got together and said, 'We have got the solution. We will have this six months time limit.' Well, we have had a situation recently where ASIC has said, 'We are

going to amend the law. We are going to take away that protection. We are going to, in the case of a particular company, give them extra time to have another bite at the cherry as it were.'

I think it is a problem that you have got parliament at one level making the law and another body enacting another system of law behind closed doors—I do not think it is a good thing.

Senator CONROY—I think the Democrats and the government agree to a six months time limit.

Mr Rofe—We said there would be problems with that thing. I think the only benefit it has produced is more money for lawyers. We have seen already a number of opportunistic offers: Equatorial Mining, share price at $2.50, the company makes an announcement, AMP comes in with an opportunistic offer of $2 a share; a similar thing happened with Western Australia Diamond Trust. I think it was badly conceived; there were already mechanisms in the law to buy out minority shareholders. It was unnecessary and, as I say, I think we have been vindicated on that one. David, are there any other issues we should raise at this stage?

Mr Jackson—No, I do not think so.

CHAIRMAN—Are there any questions?

Senator MURRAY—Yes. Going back to your remarks about AASB, I think you are on the right track, if I might say so, but there are more tracks down which you should go. Firstly, you are aware, are you not, that nearly all—it might be all now—Australian governments, all nine of them, are on the accrual system. That has meant that accounting standards matter that much more because there is a consistency between the private sector and the public sector, and in accounts presentation in many respects—not in all respects.

There is also another massive non private-sector sector which you have not remarked on, and that is the not-for-profit sector. It is simply huge—much larger, I might say, than the Valuer General accords their assets to be and much larger than appears apparent in the national accounts. The new tax system has started to throw that up because they have had to get up to speed with introducing accounting systems into these massive church organisations which formerly did not have them and so on.

Senator CONROY—That would be because of the GST.

Senator MURRAY—Because of the new tax system. The upshot of that is in relation to the source of funding for the AASB and the composition of the AASB. It is a deficient body in the sense that there is insufficient public sector input in there in my opinion. There are literally hundreds of government agencies, if you count up the nine departments affected, with massive assets affected by accounting standards, and hundreds of thousands of non-profit organisation entities and subentities all over the country.

Mr Rofe—Some of those are incorporated under the Corporations Law.

Senator MURRAY—Yes they are, but their particular needs in terms of accounting standards are remarkably different from even a proprietary company, never mind a public company. So

my question to you might be more of a suggestion: from your particular perspective, have you given any thought as to how proper funding and representation of the FRC and the AASB should be considered, with due regard to public sector and not-for-profit sector proper involvement? Because the implication behind my question is that, if you are going to go to a user-pays situation, all the users need to pay and all the users need to be represented, do they not?

Mr Rofe—Yes. I would certainly acknowledge that under its current role, as you say, AASB is responsible not only for companies but also for the public sector and not-for-profit sector, although—and I guess this is really acknowledging the point you raised—up to now a major part of the activity of the AASB has been in relation to company accounts. I wonder though, in the overall perspective, whether we are talking about a major amount of funds. If the present budget of the AASB is $3 million, even if we double it, $6 million is not that large a figure in relation to ASIC's budget.

I agree with the user-pays principle and certainly that would be an argument that, rather than ASIC stakeholders, through fees collection, making a $300 million contribution to the public sector, the public sector should perhaps be paying something to cover the cost of these accounting standards—and indeed it does, as there is a minor contribution from them.

Mr Jackson—It is quite substantial, actually.

Senator MURRAY—And the odd air fare or two I would have thought.

Mr Rofe—That is right—I have got the figures here somewhere. I agree with that but I think there is a problem in what you might call the direct user-pays approach insofar as there might be any perception that the content of particular standards could be influenced in any way by the amount of the contribution provided by a particular industry or segment or something like that.

Senator MURRAY—The other strong point you make on the funding side is that you support the Productivity Commission's conclusion that fees and charges should be relative to the costs of the organisations which raise those fees and charges and should not be excessive and therefore providing general tax revenue. I am sure, as a practical person of some experience, you would recognise that, if you adopt that policy, then those incomes, those revenues, have to be raised by the government in some other form or they have to cut services. You accept that, don't you?

Mr Jackson—Yes, certainly.

Mr Rofe—I must say that, going back to the GST, I am disappointed. My understanding of the sort of principle behind the GST—

Senator CONROY—You are not the only one, let me assure you.

Mr Rofe—I do not want to abolish it—I think it is a great tax, myself. But there should be a level playing field with no exemptions.

Senator MURRAY—Let's not get distracted.

Mr Rofe—No, but my understanding was that the revenue generated from the GST was to be paid over to the states and at the same time a number of state taxes were to be abolished. I am just disappointed that the opportunity was not taken to abolish this—that what was originally a $102 million tax indexed in perpetuity was not abolished at the same time.

Senator MURRAY—You are almost requiring hypothecation—namely, that the fees and charges raised are used entirely for the purpose for which they were raised. We have heard evidence throughout this hearing about the cross-over between regulatory agencies—APRA, ACCC, ASIC, ASX, Reserve Bank, ombudsmen—and they all at one time or another have a finger in the pie. If you are a supporter of hypothecation, do you think it is better for that not to be narrowly defined? In other words, you raise money for an ASIC but, to be broadly defined, the fees and charges raised by the various regulators form the pool from which they are funded. There are presently complaints by people such as me—and I will not speak for my colleagues; some of them may or may not agree—that some of the regulators are underfunded. I think APRA is. I do not think APRA can possibly do its job as it is presently constituted and funded—it is impossible. And I take the view that ASIC is stretched in regard to its budget in certain areas of its jurisdiction.

Mr Rofe—As I said earlier, if you just look at the work which ASIC is doing compared with what it was doing a few years ago, it is obviously doing a lot more, it has got a lot more calls on its time, but its appropriation has not been significantly increased—

Senator MURRAY—So my question to you really is—

Senator CONROY—Its core funding is actually decreasing in real terms.

Mr Jackson—That is right. If you go back to 1995, they actually received $138 million and it in fact has been dwindling since then. I think 1999 was—

Senator MURRAY—I accord with your view and I understand that, but I am not the government. But the point I am asking about is this: I am short cutting my understanding of your remarks to mean that you support hypothecated tax—namely, what is raised specifically through fees and charges should be applied to the institution concerned—but I am merely asking you if you would take that through to its nth degree and whether you want that narrowly defined or broadly defined. In other words, should all regulatory moneys which affect the sector which you are concerned with—APRA, ASIC, ASX in cases, ACCC—be pooled?

Mr Rofe—You referred to my supporting the conclusions of the Productivity Commission. In fairness, this is only a draft report, and secondly the issue is more complicated than simply taking an agency and saying it should be self-funding. Obviously, that is more feasible and more appropriate in the case of some agencies than others.

Obviously that is more feasible and more appropriate in the case of some agencies than others. In some agencies where there is a direct relationship between the service provided and the benefit to the stakeholder—the clients, I suppose you would say, of the agency—that is fairly straightforward. In other cases, of course, there are questions of public benefit, and I know that applies in the case of ASIC also. On that point of other agencies, in the CLERP 7 paper at paragraph 7.4.1 there is reference to the fact that the fees collected by ASIC need to

cover what they refer to as national scheme related costs of bodies that, while not part of the national scheme, perform functions arising out of the administration and regulation of the scheme, and examples given are AAT, the Australian Federal Police, the DPP and the Federal Court.

Senator MURRAY—I am not accusing you of it, but what I see often is an inconsistency. People demand more money spent on whatever is of interest to them but at the same time complain about tax and revenue rises. Senator Conroy clearly understood this issue the other day—

Senator CONROY—Mr Rofe wants the tax people to stay away. He hasn't got a problem on this.

Senator MURRAY—in his interaction with a young man. Essentially, I am saying that if the Productivity Commission continues down that track it is going to twist the tail of either this government or the next government to actually refrain from raising excess revenue through the present system, and people will applaud that. On the other side everybody is saying, 'We want ASIC to do more, we want APRA to do more, we want the ACCC and the AFP to do more.' And this costs money. And the government of the day, whoever they are, are going to quite rightly say, 'Where is that money coming from?' I am suggesting that you either take the amount of money which presently goes into general revenue and use it to boost these areas—such amounts as you wish—or you have to raise the fees and charges which already apply at the various levels to fund those. I think people who argue for lower taxes—which you did; you said let us not have that charge across proprietary companies—

Mr Rofe—No, it is not as simple as arguing for lower taxes.

Senator MURRAY—No, I know it isn't, but I want you to give the committee more guidance as to balancing out the job required and the amount of money that needs to be spent sometimes to do the job required, and how the money should be raised.

Mr Rofe—I think it depends a lot on the function of the particular agency. I think in the case of ASIC you can define fairly well a range of bodies which benefit directly or indirectly from the services which ASIC provides. For example, if you look at the costs of the fees which ASIC charges to companies, they are in effect passed on. For example, in the case of a company to its shareholders, some of those shares are held by superannuation funds, so in that way the costs are ultimately passed on to members of those funds. In an agency like ASIC you can to a very great extent—although not completely because as I acknowledge there is a public benefit in some cases—relate the burden to the benefit there. On the other hand, there are some areas, I suppose in particular health and education, where you cannot do the same thing. But, having said that, I do not think it is reasonable that proprietary companies should be taxed $200 a year to provide $300 million to the states to provide services which are quite unrelated to proprietary companies.

Senator MURRAY—That is all I have, Mr Chairman.

CHAIRMAN—Thank you very much.

Senator COONEY—What you are really saying is that you do not mind paying a fee but you do not want to pay a tax, as it were. If it is a general revenue tax that is one thing and if it is a fee for service that is another, is it?

Mr Rofe—That is right. If I am going to pay a tax to support hospitals or schools or something like that I would prefer to pay it as a tax, not because I happen to have a proprietary company.

CHAIRMAN—Thanks very much, Mr Rofe and Mr Jackson, for appearing before the committee. We will take into account your comments in preparing our report on ASIC.

Committee adjourned at 12.50 p.m.