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JOINT COMMITTEE ON CORPORATIONS AND FINANCIAL SERVICES

Reference: Regulations and ASIC policy statements made under the Financial Services Reform Act 2001

THURSDAY, 23 MAY 2002

MELBOURNE

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JOINT COMMITTEE ON CORPORATIONS AND FINANCIAL SERVICES

Thursday, 23 May 2002

Members: Senator Chapman *(Chairman)*, Mr Griffin *(Deputy Chair)*, Senators Brandis, Conroy, Cooney and Murray and Mr Byrne, Mr Ciobo, Mr Hunt and Mr McArthur

Senators and members in attendance: Senators Chapman, Conroy and Cooney and Mr Ciobo and Mr McArthur

Terms of reference for the inquiry:

To inquire into and report on:

The regulations and ASIC policy statements made under the Financial Services Reform Act to ascertain the extent to which they are consistent with the stated objectives and principles of that Act.

WITNESSES

Committee met at 9.30 a.m.

BOARD, Mr Michael Gordon, Director, Derivatives.com.au Pty Ltd

CHAIRMAN—I declare open this public meeting of the parliamentary Joint Statutory Committee on Corporations and Financial Services. I apologise for my physical absence from this meeting, but it was called at short notice with the view of giving members of the committee the views of those who made submissions prior to the regulations being dealt with in the Senate. On 20 March this year the committee agreed to inquire into the regulations and the ASIC policy statements made under the Financial Services Reform Act, to determine whether they are consistent with the committee's understanding of the objectives and principles of that act. The legislation, which commenced on 11 March 2002, introduced a uniform disclosure, licensing and regulatory regime for the Australian financial services industry.

The act clearly states that its main object is to promote:

(a) confident and informed decision making by consumers of financial products and services while facilitating efficiency, flexibility and innovation in the provision of those products and services; and

(b) fairness, honesty and professionalism by those who provide financial services; and

(c) fair, orderly and transparent markets for financial products; and

(d) the reduction of systemic risk and the provision of fair and effective services by clearing and settlement facilities.

The committee advertised the inquiry on 6 April in the *Weekend Australian* and the *Australian Financial Review*, calling for written submissions to be lodged with the committee by 3 May 2002. The committee has received 23 submissions. This is the first public hearing planned for this inquiry and the committee expects to hold further hearings within the coming weeks.

Before we commence taking evidence, I reinforce for the record that all witnesses appearing before the committee are protected by parliamentary privilege with respect to evidence provided. Parliamentary privilege refers to the special rights and immunities attached to the parliament or its members and others necessary for the discharge of parliamentary functions without obstruction or 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 this committee is treated as a breach of privilege. Unless the committee should decide otherwise, this is a public hearing and, as such, all members of the public are welcome to attend.

I now welcome to this hearing Mr Michael Board. The committee prefers that all evidence be given in public, but should you at any stage wish to give any part of your evidence in private you may ask to do so and the committee will consider your request. The committee has before it your written submission. Are there any alterations or additions which you would like to make to your submission at this stage?

Mr Board—At this time, I make no changes to my original submission.

CHAIRMAN—I now invite you to make a brief opening statement. Following that, I am sure the committee will want to proceed to questions. Welcome to the hearing, and we look forward to your statement.

Mr Board—Derivatives.com.au Pty Ltd is a licensed futures broker and a participant of the Sydney Futures Exchange Limited. I am a director of that organisation. We are also quote vendors. By that, I mean we disseminate financial information in realtime provided by the exchanges, like the Australian Stock Exchange and the Sydney Futures Exchange.

Our interest in ASIC policy statements, in particular policy statement 172—which concerns the operators of an exchange such as the Sydney Futures Exchange—stems from a view held by us that the Sydney Futures Exchange custom market is not being operated in a fair and orderly manner. The details of that are in my original submission. We asked ASIC in mid-2001 to investigate the way in which the SFE custom market operated; in particular, how it operates in a fair and orderly manner—and, to date, we understand they have chosen not to investigate our claim.

Further, as outlined in our submission, the commencement of the Financial Services Reform Act raises the requirement on an exchange operator that now they must ensure their marketplace is also transparent. This new additional requirement of transparency is a positive one, and we believe it will have positive ramifications for the investment and trading community in Australia at large. In particular, section 792A(a) specifies that an exchange in brief now must 'do all things necessary to ensure that their marketplace is operated in a fair, orderly and transparent manner'. However, we were concerned to read ASIC policy statement 172 and, in particular, part 83 of that statement because, in our view, it sought to weaken the original intent of the legislation by requiring an exchange only to achieve a fair balance between 'fair, orderly and transparent' ideals.

The idea of a balance was outlined in the explanatory memorandum that accompanied the original text of the bill. That explained that, on occasion, 'fair, orderly and transparency' may be in conflict and, as such, a balance is needed between these three objectives. The text of the original bill, as presented, reflected that, in that it required that 'fair, orderly and transparency' be consistent with each other.

That act was subsequently amended, and the idea of consistency between 'fair, orderly and transparency' was removed. In our view, that placed 'fair, orderly and transparent' back as singularly and equally important objectives for an exchange operator to maintain. We do not believe they can be in conflict with each other; we believe they are complementary. We see no valid reason as to why an exchange cannot comply with such requirements. We feel those are base requirements that an Australian exchange operator must adhere to. Offshore, such requirements are adhered to: fair, orderly and transparent. A marketplace's strength comes from the fact that its markets operate in a fair, orderly and transparent manner.

We believe that the removal of part 83 of policy statement 172 will have lasting ramifications and will force exchanges, both new and old, to meet their obligations as set down in the legislation. That is, to promote fair, orderly and transparent markets as singular objectives. That is my additional submission.

CHAIRMAN—Mr Board, thank you for your evidence. We will now proceed to questions. Senator Cooney, perhaps you might like to chair the question session.

Senator COONEY—Senator Conroy is going first.

Senator CONROY—Thanks for your submission, Mr Board. In your view, has what ASIC have done actually returned the intent of the legislation to the original intent before it was amended by the Senate?

Mr Board—In my view, the wording of the policy statement, and particularly part 83, is very similar to that of the wording in the explanatory memorandum. Aside from my belief that the ideals promoted in that explanatory memorandum were not correct, I believe that the amendment that was made in the Senate removed—

Senator CONROY—Clearly the Senate felt the same way you did.

Mr Board—Yes, I believe so. I believe that my view, and the view of the organisation I represent, is consistent with that of the Senate.

Senator CONROY—But you believe that the ASIC policy note is inconsistent with the Senate amendment and consistent with the original intent.

Mr Board—In my view, yes.

Senator CONROY—Probably because the same people helped draft them.

Mr Board—I cannot comment on that.

Senator CONROY—I have had a quick read of your submission. You said, 'It is not transparent.' Could you take us through why the market is not transparent if this interpretation is followed?

Mr Board—At present there can be a view in the marketplace that the information pertaining to some transactions that take place on an exchange does not need to be, or is not for other reasons, disseminated to the wider marketplace via a quote vendor such as our organisation or another quote vendor such as Reuters, Bloomberg et cetera. I believe that all information about financial transactions that take place on an exchange must be disseminated to the wider marketplace. It gives the investment public, professional and otherwise, a far greater understanding of what is taking place in that marketplace and allows them to enter into the marketplace with confidence, without the additional fear that a bid or offer that they put into the market may not be consistent with the transactions that are actually taking place. What can in fact happen is that instruments that are being traded are not, in effect, showing up on the screens—that is what we would call it. So a trader working in an organisation—

Senator CONROY—Is this during the course of the day, or is this only after the market closes?

Mr Board—This is in real time, during the course of the day. Every day, traders price instruments when asked, or take positions in instruments of any kind, largely based on information in front of them.

Senator CONROY—Was this happening before this legislation, or has it developed subsequent to the legislation? In other words, given that the test used to be 'fair, orderly and transparent', was this taking place under the original legislation and in breach of the original legislation?

Mr Board—In my view, transparency was not in the original legislation. I feel that exchanges were operating, rightly, in that there was no legislative requirement on them—there might have been an ideal or a regulation— that I know of, to act in a transparent manner. Now there is. I believe that is an ideal that should be welcomed by the investment and trading community in Australia, and I believe it is reflected in the legislation.

Senator CONROY—I think you are the only organisation that has raised this. Are you just not part of the club?

Mr Board—I would consider myself part of the broker community, which might be slightly diverse from what I would call the investment community of, say, fund managers. More information available to the broker community means that we are able to do our jobs more effectively and provide our clients with more information. The broker community has, in my view, shrunk with the advent of electronic trading over the last four or five years, and I think that there are not the numbers of personnel looking at these compliance issues. I think it would be fair to say that a lot of the broker community may be lagging. I do not mean that in a negative sense; they may be waiting for the outcome of this or waiting until further into the transitional period of the commencement of the FSRA.

Senator CONROY—So this was a problem that pre-existed the new FSR legislation because there was not a requirement for transparency previously?

Mr Board—Agreed.

Senator CONROY—This was a problem within the market already. You then saw a chance for it to be fixed and you now think it has been watered down, back to the original position?

Mr Board—I believe there were prior opportunities for Australian marketplace operators to operate their markets in a more transparent manner to bring them in line with other countries. The legislation amended that situation and now, I believe, the policy statement has slightly weakened it.

Senator CONROY—Had you or other brokers raised the problem of a lack of transparency about these trades taking place off screen with ASIC, the government or the actual market? Had you complained previously during, presumably, the last 10 years?

Mr Board—It has only really been a matter of concern—in my view, but I am only talking about the futures market because that is all I can speak for—since the closure of the Sydney Futures Exchange trading floor. On the trading floor, all information was in the pit, so to speak; there was no trading outside the pit. All that information was disseminated via the quote

vending systems. They literally had human beings with microphones who told the market what was going on. Since that closure, the technical vagaries of some of those trades were let slip and that information is now not being disseminated to the information vendors. We have raised this matter with the Sydney Futures Exchange and ASIC.

Senator CONROY—Is it easy to fix? Is it just an instruction to all the players that they have to put these things on the screen? Is it that simple?

Mr Board—The system itself, the trading engine, does not disseminate the information to the quote vending systems.

Senator CONROY—Does it require a software change or is it already there requiring a button to be pressed and the information is suddenly on the screen?

Mr Board—I cannot speak unilaterally because I do not know the technicalities of the complete system, but it would be somewhere between those two points. It would require a software patch or some intent by an exchange operator to provide that information. The participants enter the information into the system and they comprise fewer than 30 organisations who have that information available to them. It is the wider group who do not have the information.

Senator CONROY—Which companies are the 30 in the club? Are they large institutions?

Mr Board—They are large organisations; that it correct.

Senator CONROY—I am trying to get a sense of who we are talking about.

Mr Board—The top 10 investments banks in Australia, the big four—I am not saying all of them are participants, but one or two of them are. I do not want to name names expressly.

Senator CONROY—I am not trying to get you to point the finger at anyone because I understand that they would not be—

Mr Board—They are not outside what you and the committee would consider to be an investment or a financial service provider, so you are looking at banks and large broking houses—a large US broking house, for instance.

Senator CONROY—What benefits do they gain from this information not being available to the broader community?

Mr Board—I do not feel that they look to gain a great deal. I think it is an aberration that exists and, therefore, they hold a little bit more information than the rest. I do not believe that they have set out to achieve that end. I believe that the aberration exists and they are comfortable with it.

Senator CONROY—When did the pit close? When did you go online?

Mr Board—Late November in 1999. It has been an ongoing situation for the last 2½ years.

Senator CONROY—But FSRs have been taking place over the same period since then? People could have said, 'No, we will fix that in FSR.'

Mr Board—That may have been in their minds, yes. In my case, we are a relatively small organisation and we need to keep on top of legislative changes. As such, this is an issue that has popped up. If the policy statement is amended back to the legislative form, in 15 years time when there are new operators in the market the investment and trading community will be better served.

Senator CONROY—Your concern is that the 'composite' phrase would fail a legal test? Would it mean that you could discount one saying, 'Oh, you can't do that because these other two would be—

Mr Board—If you allow the same instrument to trade, in effect, out of sync—in that an instrument is trading at a lower price than the actual bid—I do not believe that is a fair marketplace. If that is not transparent, then that may be able to occur. So I believe that the ideals of transparent, fair and orderly are all complementary. I do not believe that it is a composite one where some may argue that a highly transparent market may reduce the amount of liquidity in the market. But I believe the legislative intent is there to provide an efficient market. A liquid or illiquid market does not necessarily mean the market is not efficient.

Senator CONROY—I am surprised. I thought most argue that transparency leads to more liquidity at the end of the day because of investor confidence.

Mr Board—I feel very strongly about that. Those are the sort of statements that are made generally globally. The more transparent a market can be investor confidence et cetera just flows on; it builds its strength from the marketplace. So any attempt to water down what I believe are very important things, like transparency, will ultimately have a negative effect.

Senator CONROY—Have you taken any legal advice? I know you have said that you have looked at it. Have you got a legal opinion that by making it composite it has watered it down? Because, as you can see, the Senate intended it not to be watered down.

Mr Board—I have taken no legal advice on the ASIC policy statement. I have taken no legal advice that the word 'composite' means one thing or the other. I have only looked at what the explanatory memorandum said prior, what the amendment was, and now what the policy statement was.

Senator CONROY—Clearly there has been movement in words, and there has been movement in words for a reason. That is the reason the Senate amended them to be a different form than in the original bill. We will seek clarification from ASIC.

Mr Board—On a final note, I think it is a highly achievable ideal. To me, it is not outside the realms of the normal practices of a market operator.

Mr CIOBO—With regard to taking it as a composite versus each having a specific objective, do you foresee issues arising where there may be inconsistency between trying to reach each of the three elements?

Mr Board—I do not see any inconsistency if an organisation strives to achieve those three things singularly. In my experience, I cannot see how any one of those objectives would detract from each other, if that was promoted that way.

Mr CIOBO—Why would you foresee that they would look at reverting back to a composite structure?

Mr Board—Why would they take it back to a composite phrase as opposed to a singular? I just believe the status quo is in place at the present time with the exchange operators, and I believe that that is the way they would like it to remain.

Mr CIOBO—It is one of comfort rather than—

Mr Board—I believe it is one of comfort rather than intent.

Mr CIOBO—Finally, you make a statement in your submission that the operation of the 'policy statement only serves to weaken the terms of the underlying legislation'. In summary form, what is your basis for saying that?

Mr Board—That just goes to my original statement. In my professional view, if an operator today and in the future is allowed to only achieve a balance between those three things, then an exchange could operate that 80 per cent of our marketplace is transparent, and then five, 10 or 15 per cent is not; therefore that is an appropriate balance. But I feel that that five, 10, 15 or 20 per cent of the marketplace is a very important part of the overall market. As such, they should all be transparent, all be orderly and all be fair.

Mr CIOBO—Do you see that those as tending to be the multicomponent transactions?

Mr Board—Yes, I do. But it would not, in my view, limit the exchange at some later date introducing an instrument that they felt may not need to be as transparent as another due to the complexities of it. By that, I mean they could develop an instrument—I do not know what it may be—and they could deem it is of such complexity that they do not need to disseminate the information pertaining to it and just let the participants who are able to deal in that instrument trade between themselves.

Senator COONEY—Do you have no problem getting to ASIC, or do you say there is some delay in being able to get to ASIC to put your point of view?

Mr Board—We have had reasonable written dialogue with ASIC on the matter of the fair and orderly provisions. They do not feel the same way that we do about the fair and orderly provisions. What worries me is that they do not feel the same way about the fair and orderly provisions in that there is a new heightened requirement for transparency. From the outset there seems, in my view, to be a weakening of that provision. Therefore, I feel that ASIC could be more rigorous in enforcing the intent of the legislation.

Senator COONEY—So it is a difference in philosophy, and if you want to knock on their door they will let you in but not—

Mr Board—I have had no problem in actually initiating a written dialogue with them. I believe that if they were to investigate and use empirical data, my view would be borne out.

Senator COONEY—Mr Chairman, did you have a question?

CHAIRMAN—Yes, I will follow that up. What do you believe informed the original draft of the legislation, which now seems to have reappeared in the policy statement, as against the amendment that went through? I assume your view is that it was ASIC's influence on the drafting of the legislation, but perhaps you could enlarge on how you believe that original drafting came about and on the way in which ASIC still seems to be ignoring the amendment to the legislation.

Mr Board—I believe that the legislation came about over a long period of time. It stems from the FSI, and that was six or seven years ago. I feel that the ability of some of the exchanges to adhere on day one to this sort of regime of fair, orderly and transparent, particularly with the technological change et cetera that took place in the last two to three years, is what allowed the policy statement to, in my view, revert back to the text of the original memorandum. It just fell through the hole, really. I do not have any knowledge of any real intent by ASIC, an exchange or a marketplace operator to make sure that was actually there.

When it was originally drafted—and this is only my view, because I have no working knowledge of the way in which the text of the bill or the explanatory memorandum were brought into being—the mechanisms that ran, in particular, the Sydney Futures Exchange involved an open outcry system, which I explained in my submission. That enabled, in my view, the market to be operated in a fair, orderly and transparent manner all the time. It was only later that they realised that some of those ideals may require some technological changes in their systems which may be expensive and may yet need to be developed, in their view, and that is why that was slipped back in. I do not think those are valid reasons, but they are there.

CHAIRMAN—In your view, does it indicate that ASIC might not be quite up to speed on the development of technology in the industry?

Mr Board—I think as a general statement the industry has been able to promote itself as a sophisticated, well-regulated, self-regulated type of industry. As such, I do not think ASIC necessarily has kept up with the day-to-day real workings transactionally of the marketplace. To look at a market in a snapshot way—for instance, at the end of the day or at the end of the month—you get one view of the market, but I think ASIC needs to focus on looking at it in real time, at the transactions and the real workings on a day-to-day basis, as most clients and most participants in a marketplace are doing. I do not believe that they are doing that at the moment.

CHAIRMAN—With respect to the sorts of transactions that you are referring to that are affected by this policy statement, are they transactions that are undertaken by professionals or would private individuals also be directly involved in those sorts of transactions? Or is this an area of the market that is virtually limited to professional—

Mr Board—I believe those transactions are taking place by professionals, if you are referring to professionals as institutions. I believe institutions—

CHAIRMAN—Or agents for clients—people operating on behalf of private clients rather than the individual small clients doing it themselves.

Mr Board—Private clients of a more risk-preferred nature are looking to trade very similar instruments and contracts to those of any institution in Australia. There is no reason why they cannot have the same access.

CHAIRMAN—I suppose the issue I am getting to is this: if there is a move away from the policy statement as promulgated by ASIC to the sort of wording that you prefer, there is no issue here of consumer protection that would arise?

Mr Board—I am sorry?

CHAIRMAN—If the change that you are advocating was made—in other words, the move away from ASIC's policy statement to the position that you are advocating—is there any issue of a lesser level of consumer protection that would arise as a consequence of that?

Mr Board—No. I believe that, on the issue of consumer protection—and I use the word 'consumer' for all—they would be protected in a greater manner because they would have more information available to them to make decisions about some of the instruments that they were getting themselves involved in—some of the trading instruments that they inherently acquire through various investment schemes that are operating in the marketplace.

CHAIRMAN—That concludes my questions. Are there any further questions from any other members of the committee? If not, thank you very much, Mr Board, for appearing before the committee. We appreciate the evidence that you have given and your answers to our questions.

Mr Board—Once again, thanks for the opportunity and I hope to speak to you all again soon.

[10.03 a.m.]

ANDERSON, Dr Michaela, Director of Policy and Research, Association of Superannuation Funds of Australia Ltd

PRAGNELL, Dr Bradley John, Principal Policy Adviser, Association of Superannuation Funds of Australia Ltd

CHAIRMAN—I welcome Dr Pragnell and Dr Anderson from the Association of Superannuation Funds of Australia Ltd. The committee prefers all evidence to be given in public but should you at any stage wish to give any part of your evidence in private, you may ask to do so and the committee will consider your request. The committee has before it your written submission, No. 5. Are there any alterations or additions you would like to make to the submission at this stage?

Dr Anderson—No.

CHAIRMAN—I now invite you to make a brief opening statement, after which I am sure there will be questions from members of the committee.

Dr Anderson—Thank you, Mr Chairman. Our submission and the comments here today relate only to the operation of superannuation funds and the FSRA regulations and ASIC policy statements. ASFA supports the principles underlying the FSRA, in particular the need for informed decision making by consumers. I would like to briefly highlight the main areas of impact of the regulations and policy statements. These are more fully set out in our submission. Then I would like to outline some of our remaining concerns.

The first area of impact is disclosure. The act will require practically all superannuation funds to prepare new up-front disclosure for fund members in the form of product disclosure statements to replace the old key feature statements for public offer funds and member booklets for non-public offer funds. Unlike other financial products, the content of the superannuation PDS is prescribed in regulations. We support the need for this standardised disclosure requirement for superannuation funds. However, we feel that there are some critical deficiencies with the current requirements, in particular the use of the ongoing management charge, the OMC, which we will talk about in more detail later if required.

The second area is licensing. Many superannuation fund trustees will be required to obtain or operate under an Australian financial services licence. All public offer funds will be required to hold an AFSL and non-public offer funds providing financial product advice will also need to either hold or operate under a licence. While approved trustees offering public offer funds have been required to hold a security dealer's licence, the licensing regime and dealing with ASIC will be a new experience for many public offer superannuation funds, which include many not-for-profit industry, corporate and church funds.

I would like to turn now to the making of regulations and policy statements under the FSRA and our experience. ASFA has been deeply involved in the consultation process, dealing with

Treasury over the regulations and with ASIC over the policy statements. Our submission outlines the generally positive and cooperative nature of that consultation process to ensure a smooth transition. As I said before, a lot of superannuation fund trustees will be dealing for the first time with a new regulator. Examples of our concerns that we raised with ASIC and with Treasury during the consultation period included competency requirements for licence applicants and confirmation of transactions. I think to a large extent we got a good hearing and the outcomes are much better than we probably expected.

Despite our genuine satisfaction with the regulatory process and outcomes, we still have some remaining concerns. These concerns are in the regulatory framework and go to the objectives of the act, in particular the need to promote confident and informed decision making by consumers of financial products. ASFA supports the need for clear, concise and effective disclosure and the need for comparability. However, we strongly believe that the current approach is deficient for numerous reasons and may not assist this objective. The ongoing management charge, the OMC, is of particular concern to us. It is significantly flawed as a measure. Notably, it does not include entry and exit fees that may dramatically affect a member's benefit. It fails to demonstrate the actual impact of fees and charges on a member's benefit. ASFA strongly recommends that Treasury replace this OMC requirement in the superannuation PDS requirements with an expense measure and examples that will better enable comparability. We also believe that this new measure should be tested for its comprehension by consumers to ensure that it is able to be understood by those consumers.

Our second concern relates to the position of the Superannuation Complaints Tribunal as an external dispute resolution mechanism for consumers. One requirement of holding an AFSL is to have adequate means of addressing and resolving consumer complaints. This is done through ASIC requiring the licence applicant to have suitable internal and external dispute resolution processes. Meeting the external dispute resolution requirements is generally done through membership with an ASIC approved industry run body, such as the banking ombudsman or the Financial Industry Complaints Service. The Superannuation Complaints Tribunal, as a statutory body, is outside this regime of industry bodies approved by the regulator. The strength and independence of a statutory body—rather than a self-regulatory industry body—is supported by ASFA as suitable for the special nature of superannuation. Superannuation savings are compulsory and a central feature of the national retirement income policy. The need for confidence in the system is paramount.

ASIC recognises in policy statement 165 that it cannot approve the SCT but notes that if all the activities carried out by the licensee applicants are covered by the Superannuation Complaints Tribunal they do not need to join an approved scheme. However, if the applicant carries out activities outside the Superannuation Complaints Tribunal's jurisdiction then a superannuation fund trustee may need to join another dispute resolution body such as FICS. Neither ASIC nor Treasury have provided any clear and detailed enunciation as to their understanding of the limits of the tribunal's jurisdiction and how this might impact on licensing and the possible need for a superannuation fund to join another dispute mechanism.

ASFA's preference remains to have the Superannuation Complaints Tribunal cover the field of superannuation fund trustees activities. This was always the intention of the legislation that established the tribunal. Therefore, if the jurisdiction problem alluded to is within the current legislation we feel it is incumbent upon government to resolve it. If superannuation funds are

required to join other schemes it is likely to prove confusing to members of superannuation funds and thus less than conducive to the FSRA's objective of promoting informed and confident decision making by consumers. It will also be costly for funds who already pay for the tribunal through their APRA-ASIC levies if they also have to pay membership fees for another scheme such as FICS. What we would recommend is that government, Treasury and ASIC ensure that the Superannuation Complaints Tribunal remains a one-stop shop for consumer complaints regarding superannuation fund trustees and fund activities. Thank you.

CHAIRMAN—Thank you very much for your opening submission. We will now move to questions. Senator Cooney will again chair the question period.

Senator CONROY—Your submission touches on a number of topics. Can I get your opinion on this: are you comfortable with the ASIC policy statements accommodating the trustee system in the industry funds? There was, as I am sure you are aware, a lot of debate around the intent of the words. Are you comfortable that it meets the test?

Dr Pragnell—From the feedback that we have received today from our members it would appear as though ASIC has sought to accommodate the trustee system and member representatives in policy statement 164, in particular enabling the appointment of responsible officers who may not necessarily be members of the trustee board themselves. To date, we have not received any concerns that those funds are unable to meet those requirements.

Senator CONROY—So in terms of making sure all superannuation funds have the necessary skills and expertise to maximise the returns for their members, you are comfortable that these regulations and the laws that have been passed meet the intent of the legislation?

Dr Anderson—We are, because the skills have to be there, and that is the bottom line. With respect to how they are there, there are a number of mechanisms for putting them there, and we are comfortable that that will not upset the equal representation mechanism which has a lot of very commendable features in terms of safety of superannuation.

Dr Pragnell—The SI(S) Act and initiatives within the industry itself have generally meant that the level of competency is relatively high. If trustees themselves do not necessarily have the skills internally, they are more than able to access them externally. We feel there is actually a pretty high level of competence generally within the industry that trustees are able to source. With respect to some of the other concerns that other industries may have regarding 164, we have not heard those kinds of complaints to date.

Senator CONROY—Were you involved in the ongoing management cost debate with ASIC? Did you raise concerns as they were developing this?

Dr Anderson—We did raise concerns with Treasury a number of times, and we continue to raise concerns.

Senator CONROY—I am pretty simple and straightforward. I would have thought the simplest way to deal with this is just to have a requirement that the cost to customer has to be a calculation and, in that way, calling something a fee or whatever captures all the elements of cost to the consumer. Is that your view?

Dr Anderson—I think the intent is there. What we have ended up with—

Senator CONROY—The intent by ASIC, the intent by the legislation?

Dr Anderson—Probably the intent from all sides is there. What we have is an outcome which will not help the consumer. I think the intent was good. I do not think any of us would say that there was not an intent to capture all costs and to show them to the consumer. The problem is that the consumer will probably burst into tears when they see what they have got that is supposed to help them to compare funds.

Senator CONROY—I am concerned that when you say the intent was there, the word 'ongoing' clearly to me does not say that the intent is to capture all costs because, as you correctly identify, one-off costs are not ongoing.

Dr Pragnell—There are deficiencies in the ongoing management charge with the entry and exit fees. What Dr Anderson was indicating was that the decision to try to introduce the ongoing management charge into the product disclosure statement requirements was aimed at trying to create some degree of comparability so that members could compare fund A with fund B on some sort of common basis. They could do it on a percentage basis, on a historical basis or on a flat dollar amount basis. From a very high level, those principles are very commendable. Our concern is that the OMC itself, as you rightly indicate, does not include some of those one-off costs, so it is deficient there. But the way in which the regulations have been developed will basically create a maze of impenetrable numbers so that no consumer will be able to get any kind of clear indication as to whether this is an expensive fund or a relatively inexpensive fund. They will just see this mass of numbers that will be generated. They will be folding out A3s, Excel spreadsheets. I do not think that aids informed and confident decision making by consumers. That is our main concern.

Dr Anderson—If you look at the process you can see that what was happening towards the end was that there was pressure to get things finished, to get regulations in place, with time running out. What we got in the end was, 'We have to get something there.' Probably we need to stand back and say, 'We've got something there but we may as well not have it.'

Dr Pragnell—The ongoing management charge to begin with was probably a pretty imperfect mechanism but it did exist in the key feature statements for public offer funds, so it was something that was there and that Treasury could build on. But they had a deficient indicator to begin with and then they started bolting on all these other requirements—the five-year historical, the splitting of non-investment and investment, breaking it down for all investment charges. Those are all commendable from a high-level policy point of view but, when you actually try to implement it, it is a disaster.

Senator CONROY—I am sure that if Senator Sherry were here we would be applying his famous Burnie pub test in Tasmania.

Dr Anderson—It would fail.

Senator CONROY—From the sound of it, those punters in the Burnie pub are in for a very long evening trying to understand it.

Dr Pragnell—It fails that test. We were concerned that Treasury were developing standards and we kept raising, 'Have you tried to consumer test this?'

Senator CONROY—So at no stage did they indicate that they consumer tested it?

Dr Pragnell—No, I do not think Treasury did any consumer testing or comprehension—

Senator CONROY—Do you think Treasury have ever met a consumer?

Dr Pragnell—I will take that one on notice. Never met a consumer they did not like.

Senator CONROY—I will not ask a question about ASIC, in deference to the audience. In the absence of other questions, I will keep going. You basically think this should be scrapped and started again.

Dr Anderson—Yes. We have tried just tinkering with it to see if there is a way of doing it. It does not work. You have got to start again and you have got to then run what you end up with through some consumers.

Dr Pragnell—And that is part of the thing, that people can come up with the magic bullet to try to consolidate this down to, say, a single number indicator, but it is really important to actually go out and test it. We have been conducting over the last couple of years consumer testing of various disclosure document formats and we have been playing around with various formats in terms of their understanding. We did provide those findings to Treasury, but unfortunately it would appear that they chose to rely on what was already there in the tried and true rather than try to do a bit of a break from the past.

Dr Anderson—And I do not think it was tried and true that they were relying on. We always knew that it was in fact not working in the key feature statement. Our understanding right from the beginning was that the key feature statement items on cost were not good. Our understanding was that we would go back and we would have something that was developed and tested. That did not happen. I think to a certain extent you can say time ran out, but I do not think that is good enough for consumers.

Senator COONEY—Is it the structure that is the problem or do you think if you had different people filling the positions in these structures there would be an improvement? You have got two things whenever you have got a regulatory system: you have got the structures themselves, the tribunals and everything else, and you got the people that fill them. You can get problems from both those areas. Are you saying that it is the structures that are the problems here?

Dr Anderson—Within the departments?

Senator COONEY—Yes. And generally across the board, as distinct from people who you might have filling the tribunal and other bodies as well.

Dr Anderson—I think most of the development of the regulations here was from Treasury. Perhaps the expertise may not have been there in this, because you are talking about communication as well as law. I think that is something you might look at. That is why we say to go back and see if it works; go to the consumer and see if it works.

Senator COONEY—But you are definitely saying that you have to have the right people to make it work.

Dr Anderson—Yes.

Dr Pragnell—I would have to say that most of the people we dealt with at Treasury when we were involved in consultations over the regs were very professional, very competent, and I think that for the most part they tried to be responsive to industry concerns along the way. I think that when work was actually passed down, probably to individual officers within Treasury, it depended on who got handed what portfolio at what time. Sometimes you had someone who was right on top of the issue and understood it and could work through it and other times you had people whose knowledge of superannuation, the SIS Act and all that was very shallow. So it was a bit of a mixed bag there, I would say, and there was a lot of education that we had to do to try to say, 'Let's start at first principles. Let's start at what funds currently have to do and the SIS Act and all that and let's work through this, and this is what the outcome is.' When you have only got, say, a two-week consultation period on draft regs, it is difficult to get people up to speed that quickly, so the time frames did make it difficult, given the patchy nature of some of the expertise in Treasury.

Senator CONROY—There has been a fair bit of debate about disclosure of fees and the form of them, as you would know. I am not as sanguine as you, Dr Anderson, about everybody being in the cart to get us a good consumer outcome here. I am aware that some in the investment community are passionately opposed to revealing fees, particularly in dollar amounts. I have been present when they have made speeches on these issues, calling those who seek to support it naïve and unhelpful. So I am not quite as sanguine as you; I come at this from the position of knowing that there is not quite 100 per cent support among some stakeholders to deliver these outcomes.

Dr Anderson—I felt that within Treasury and ASIC they perhaps understood why you should assist consumers.

Senator CONROY—I think AIST produced a research paper a little while ago which detailed how it was possible to come up with some dollar disclosure figures. I cannot remember the name of the academic who produced it.

Dr Anderson—Yes, it was the University of New South Wales.

Senator CONROY—I remember seeing a release from your organisation that was critical of it, which I was very disappointed to see. I was wondering whether you could take me through what you believe are the problems with dollar disclosure.

Dr Anderson—I don't think we had any problems with dollar disclosure. Our problem was with the methodology of the research work that was undertaken. We actually looked at the issues again and we were criticising the methodology and the outcomes.

Senator CONROY—What was your alternative methodology?

Dr Anderson—It was not an alternative methodology; it was actually pointing out that there were mistakes in the methodology, which I think the author has now acknowledged.

Dr Pragnell—Our principal researcher, Ross Clare, has been in contact with Hazel Bateman at the University of New South Wales and they have discussed a lot of the issues. It does come back to, as Dr Anderson said, methodological differences there. I think we are trying to reach the same principles; it is just how we actually do it. Coming up with the magic number is sometimes a bit of a concern. If you have a complex formula which then creates a magic number at the end, how meaningful is that number? How can you ensure the integrity of the people calculating that number and so on? We have been trying to look at forms that involve simple tables that are reasonably understandable by consumers, that do express the impact of fees and charges on a dollar basis. We are committed to that. I think it is just about a different approach.

Dr Anderson—Yes. Our consumer testing, which we have been very public about, says that the only thing that consumers understand is the dollar. They do not understand percentages. We have never been in disagreement. Most of our disagreement, as I said, was methodological, and the way it came out in the end seemed not to be showing the real differences that there were between funds. Most people who were getting the superannuation guarantee were in relatively cheap funds, even on a world comparison, but some funds were quite expensive. In fact, the research, to a large extent, did not highlight that range and who was affected by it.

Senator CONROY—Were you surprised to find that ASIC were only pursuing a disclosure standard for superannuation funds and not for the rest of the financial services industry?

Dr Anderson—No, I am not surprised because we have been the most vocal. We have the least financially sophisticated members of financial products. We have always asked for really good disclosure for those people, and there are a number of reasons why it is very important to get the disclosure for superannuation correct. We also think that probably, if you can get it right for superannuation funds, you can follow that model and get it right for the rest of the industry because probably our clients in superannuation are the hardest to work with because some of them do not take any real involvement in their investing.

Senator CONROY—On your reading of the legislation which passed through parliament, were you surprised to see that you were the only segment of the financial services industry that was picked out? Having read the legislation and then debated it in the parliament, it certainly was a surprise to me when I was informed that, no, it was only superannuation that was going to be covered by this particular requirement.

Dr Anderson—We could take that as a compliment to our good lobbying, that in fact we had said—

Senator CONROY—I should take it as a compliment that it is somebody else's good lobbying, I am afraid.

Dr Anderson—Yes, you could, too. Our concern is with superannuation and the people who are compelled to be savers. We have always said that we have to get it right for this group of people, and that means probably that you need, at least with this group, to have some prescription so that you can make it more—

Senator CONROY—I accept your point in terms of less financially sophisticated, though.

Dr Anderson—Yes.

Senator CONROY—There is an overwhelming case in your area.

Dr Anderson—That is the point. There is an overwhelming case, and it is hard to white ant.

Senator CONROY—To what extent do you believe the jurisdiction of the SCT needs to service a one-stop shop for consumer complaints?

Dr Anderson—This is a really interesting one. We have spoken to the chair of the Superannuation Complaints Tribunal about where are the jurisdictional areas that are a problem. We have spoken to ASIC and we have spoken to Treasury. We are going back to Treasury shortly to talk again. We are not really sure where the problem is, which is part of the problem. What we do find disturbing are the kinds of throwaway lines that we get from Treasury and ASIC at various forums where they say that because of jurisdictional issues some trustees may have to take on board another dispute mechanism. There it is left, and when we say, 'Please clarify', we get nothing. To be honest with you, we are quite sick of that. We would like someone to explain where the issues are. We really think there is a need for a one-stop shop so that people do not have to deal with trustees in two different dispute mechanisms.

Senator COONEY—Mr Chairman, we are finished here. Did you want to say anything?

CHAIRMAN—No. I have no questions. Thank you, Dr Anderson and Dr Pragnell, for appearing before the committee this morning, and for the evidence that you have given to us. It has certainly been most informative in relation to our consideration of the regulations and the policy statements.

Dr Anderson—Thank you for the opportunity to appear.

Proceedings suspended from 10.33 a.m. to 10.44 a.m.

HARDING, Professor Donald Edward, Partner, Freehills

McALISTER, Ms Pamela Ruth, Partner, Freehills

MacDONALD, Mr Ewan, Senior Associate, Freehills

CHAIRMAN—I welcome the representatives of Freehills. The committee has before it a written submission from Freehills that we have numbered 7. Are there any alterations or additions that you wish to make to the submission?

Prof. Harding—I have handed to the staff a further statement, which I propose to use, which deals with a number of points. I have given two copies to the committee—I only brought two copies with me—and I propose to speak to some of those points.

CHAIRMAN—Is it the wish of the committee that the additional submission presented to the committee by Professor Harding be tabled? There being no objection, it is so ordered. I now invite you to make a brief opening statement, and then we will proceed to questions.

Prof. Harding—Mr Chairman and committee, thank you for the opportunity to appear. It has also been quite useful for us to be able to put some thoughts together on paper. I should say that my areas of expertise are licensing, and securities and futures markets. My partner Pam McAlister is an expert on superannuation, which is a very highly technical subject, and Ewan MacDonald is an expert on managed funds. So we might field questions according to our areas of expertise. There are a few points which I want to make which do not appear in writing in the submission, and some of them relate to the regulations.

We have found that, in terms of their placement, the regulations have become extremely complex. I have a set on the table in front of me, which represents only some of it. They came out serially, and anyone trying to work manually with the regulations is finding considerable difficulties in integrating them, including legal advisers. There are online systems which integrate them, such as SCALEplus, but we find that there is another problem as to the placement of some of the regulations. For example, in the transitional provisions, you find—generally speaking—that a holder of an old securities dealers licence during the transitional period of two years is essentially treated much the same as a holder of the new AFSL. I had a meeting with ASIC just a week or so ago, and they said that there is still only one. But it is often very difficult to find where the regulation is.

I have had a particular issue in relation to the marketing of wholesale funds or securities, on which I advise a lot of people. I have found that there is a regulation, 7.1.33B, which deals with general product advice, but it only applies to AFSL holders and not securities dealers. Yet there is another one in regulation 10.2.39 which in effect provides that a licensed securities dealer in the old way can do the things in relation to dealing which the holder of the new AFSL can do. So there are still gaps. Treasury has obviously done an enormous amount of work trying to get all this fixed up, but we still keep finding little problems of that sort which cause the industry some concern.

The ASIC policy statements have involved an enormous amount of work on the part of ASIC, and I think it has done a superlative job in trying to make this whole regime work. But I am concerned that, because of the pressure of public opinion, ASIC feels obliged to leave no stone unturned. So we now have a much more complex set of requirements than we used to have, and obviously it is going to impose general costs on the industry. ASIC itself has been doing a stalwart job, but as I understand it, it has to handle some 9,000 transitions to new licences in the next couple of years. It is trying to handle that by doing it electronically, and dealing with it has become somewhat faceless. That may change, but where you have certain sorts of problems, it is very difficult to get the one-to-one contact one used to have.

The training requirements and the qualification requirements are also causing concern. I am currently acting for several clients who have had long experience in the industry, more than 12 years, yet they do not have the formal qualifications which are required. In effect, they have been required for some time, but ASIC was somewhat flexible about them, especially where you are talking wholesale. The general effect at present, although we have not tested it sufficiently, seems to be that that flexibility is gone and that everything is simply done electronically. So a significant question for some of my clients is: even though we have been in the industry for years, do we have to go back to school or get an individual assessment under the three options which ASIC provides? Also, in relation to retail advisers and others, the provisions of policy statement 146 have caused a lot of concern for anyone—and we mentioned this in the submission—who has been in the business for more than five years.

There are a number of other specific problems which are mentioned in the submission. One of them relates to listed trusts. Listed trusts and securities are treated differently. Securities, when they are offered retail to potential investors, require a prospectus, yet listed trusts such as Westfield will find that they have to do a product disclosure statement. In many respects it seems wrong that they should be different and that the requirements should be different. You also get situations where the offer is both of a stapled security and a unit in a managed investment scheme. There are problems there in that you end up having to do both a prospectus and a PDS, and that is a fairly expensive business.

There have also been some problems with respect to secondary sales in that they have now introduced an element of the intention of the person with whom the securities are placed. That also applies to financial products which are governed by the product disclosure statement requirements, such as listed trusts. ASIC has come to the party on some of that with the class order, which operates for six months in relation to securities, but there is none in effect so far in relation to a very comparable situation for managed trusts. They are the additional points that I wanted to bring out orally; thank you for letting me have the time.

CHAIRMAN—Thank you very much for that opening statement. Do your colleagues have anything they wish to add before we proceed to questions?

Mr MacDonald—No, we do not.

CHAIRMAN—Again, I will hand over to Senator Cooney to conduct the question period.

Senator CONROY—We intend to put a lot of your concerns to ASIC this afternoon. I was interested to note that you are silent in your submission on the issue of telephone monitorings in takeovers.

Prof. Harding—Yes.

Senator CONROY—It is an issue raised in a submission by IBSA and you, in your practice, would be involved in a number of takeovers in a given year.

Prof. Harding—Yes. I am not personally, but certainly some of the partners on my floor are. They do not like those provisions.

Senator CONROY—I was wondering whether anyone is in a position to outline the concerns about the impact of this particular new measure.

Prof. Harding—Fortunately, they now do not apply to the institutions, which is very significant. It is not something that really affects us, but it obviously can create all kinds of issues in terms of the spontaneity of conversations and, in effect, the reluctance of people to engage in conversations. I think that is a bit of a concern.

Senator CONROY—There was a heated argument on the floor of parliament about this issue.

Prof. Harding—Yes. I think some people feel that there will be avoidance measures or steps taken which circumvent them, but it remains to be seen. We have not had a lot of takeovers this last year because it has been a quiet year in that area. I certainly have experts who could provide you with more detailed commentary within the firm, if you want.

Senator CONROY—If you could, that would be very useful for the committee.

Prof. Harding—Sure. I think someone like Braddon Jolley, a partner of mine who works on the same floor as I do in Sydney, could do that. I will ask him.

Senator CONROY—Thanks. Your submission indicates that some of your clients have problems with the training requirements in policy statement PS146. I was wondering whether you could expand on that a little.

Prof. Harding—In effect, ASIC requires people who have been in the industry for a certain period to be reassessed or to do further training. For many brokers, for example, who are over the age of 50—I have some sympathy—it is a very daunting thing. Whereas, in my case, I have to do continuing legal education and I have to make sure that I am able to show that I have enough points of continuing legal education. I would have thought that that is a better approach than to actually require people to go back to school or to take a viva, which is a pretty intimidating experience. Indeed, in quite a few of the professions there are continuing training requirements, they are formalised and you have to meet them. I do not know where the idea of, in effect, requiring people to requalify has come from. It is something that ASIC produced in interim policy statement 146 quite some time ago, so it is not new; it is not just connected with the FSR. It strikes me as pretty draconian, with all due respect to ASIC.

Senator CONROY—Were you involved in any discussions with ASIC about the model you have suggested, the continuous training model?

Prof. Harding—No, I was not.

Senator CONROY—Do you know if anyone was? Were there any discussions?

Mr MacDonald—No, we have not raised that with ASIC at the moment. We have essentially received a lot of client feedback to the effect that the training requirements are not practical and that they unfairly discriminate against people who, say, picked up their qualifications five years ago. Those were the main points.

Senator CONROY—Five years ago?

Mr MacDonald—Yes.

Senator CONROY—It is a five-year test, is it?

Mr MacDonald—There is a five-year test for some qualifications.

Prof. Harding—It used to be 1995. We are aware that a lot of our clients have lobbied and put in submissions. I know they were very active about it.

Mr MacDonald—Essentially what we have done with this point is feed back client concerns, because it is not so much of a legal point.

Senator COONEY—It is coming through a bit in the submissions that there is a problem with having the consumer understanding things. I suppose one of the functions of the legal profession is as an interpreter of the law to the people in the street, if I can use those fairly loose phrases. Professor, you were talking about the whole situation being so complicated that you yourself had some difficulty—

Prof. Harding—Scary.

Senator COONEY—in working it through. You get there, but obviously you have had to spend time and effort.

Prof. Harding—Certainly, but that is my job.

Senator COONEY—I might be wrong about this but I get the feeling that you thought that you need not have spent such time and effort if things had been different. Do you have any comment on that? I am still just thinking aloud here but is there scope, for example, for the legal profession to have more input at an earlier stage with legislation as it is being drawn up?

Prof. Harding—There was plenty of opportunity to put in submissions. I think the Treasury were faced with an enormous task in that the legislation is covering a whole range of products which were not regulated before, particularly general insurance, and certainly the regulation of

superannuation is far greater. Derivatives as such which were neither futures nor securities were not really regulated. The Treasury have in effect had the task of trying to turn what was the Wallis committee recommendations, which were very general, into something concrete in terms of law. I happen to know one of the gentlemen who were seconded from ASIC who worked on it. They were faced with an enormous task. I do not have any simple remedy or panacea for how to deal with all of this.

One of the advantages of what the Treasury have been prepared to do is to react to the submissions as they have come in. For example, in relation to the regulations that were available last December, people put in all kinds of submissions and pointed out all sorts of problems and they reacted by producing further regulations on 14 February, further regulations on 28 February and further regulations in March, plus there was an amending act that went through parliament in relation to insider trading aspects and certain other things. So, in effect, both the legislature and the Treasury have tried to respond to all this. It is just that they seem to have ended up with an enormously complex body of law.

My concern in a sense is that ultimately the consumer will pay, because it will add to the costs of the operation and regulation of the industry. I realise that people want the industry closely regulated, but there is a question in my mind as to the extent to which this will add to the cost of the Australian financial services sector—which is quite an important sector in the Australian economy now. I think that is something that needs to be looked at. I would not want to use a specific word, but perhaps it is a question of rationalisation and seeing what can be done—a huge effort having been made—to make the situation a little bit more like a lot of the rest of the Corporations Act is now, after certain projects which took place a few years ago.

Senator COONEY—I suppose nobody is objecting to regulation, but it is a question of whether it is apt regulation. This is too simple, but if you go to a doctor, the doctor says, 'We're going to operate to cure you;' if you go to a lawyer, the lawyer says, 'We'll take you to court;' and if you to a parliamentarian or to a government, they say, 'We'll pass a law.' The message I am trying to get across is that you should operate or go to court if there is a purpose and if it is needed. The issue I am raising here is: how much of the regulations and the act are really pertinent, or could they be more pertinent? Do you have any feelings about that?

Prof. Harding—Given the fact that it was proposed and accepted by governments, as recommended by the Wallis committee, that there be regulation across all of these different areas, they in effect have had to put all of that in. I was legal adviser to the Senate Select Committee on Securities and Exchange a long time ago under Senator Peter Rae, and when we looked at the stock markets there were major problems and certainly a lot of that has been addressed. Regulation in that sense has achieved a much more honest market with much better disclosure—and that is still being worked on in a different respect—but somehow it seems to have ended up with an enormously complex and costly body of staff. Senator Ian Campbell, I think in a release that I saw yesterday, acknowledged that that may need to be looked at in terms of the cost that is imposed. In a sense a rationalisation or simplification process could possibly be of assistance, but I do not think anybody really wants to go and change it all just yet. We have all had quite an effort getting on top of the stuff that has just come out!

Senator COONEY—I suppose superannuation is a big problem because, as has been pointed out earlier this morning, that affects the whole population. People are required to go into super-

annuation, and you would have thought that the law regarding that was fairly understandable to everybody and not simply to those who are central to the industry.

Ms McAlister—Yes, and because superannuation is a fairly unique financial product, because it has a compulsory aspect and a very high public policy aspect—in the sense that it is the nation's retirement savings—there were some arguments put in the initial stages that superannuation should have its own separate regulation because there were many features of superannuation which were unlike other financial products. It has now been accepted that that battle has been lost, and so now we have to try to accommodate the unique features of superannuation within the constructs of uniform, harmonised legislation whilst still recognising its unique features. That is what creates some complexity, because you have the general principles that apply to all financial products in the act and then the regulations seek to deconstruct some of those general principles to the extent that they need to to apply to superannuation. Some of the issues that we still have with the regulations in relation to superannuation are whether that deconstruction has gone far enough and whether what we have ended up with is better for consumers than what we had before.

Senator COONEY—There is a whole welter of laws coming down. You probably feel sorry for Treasury and for ASIC, because there has been an avalanche and force for them to deal with. Can you think of any way that they might be helped in that task? If I can take you back to your previous occupation, Professor Harding, at the university, there was I think in your day still a willingness on the part of the academic world to help in this area if invited. Do you think there is any scope there?

Prof. Harding—Quite possibly, there is. Professor Ian Ramsay of the University of Melbourne has just done a major report on auditors, which is input. There is also of course a very important committee, CAMAC, which is created by the legislation. That produces very useful reports. For example, it did one not so long ago on insider trading. The report addresses some of the problems that have been hanging around in relation to insider trading prohibitions and laws for many years.

There are problems now with the market misconduct provisions. Joe Longo, who used to be the national coordinator of investigation at ASIC and is currently with the firm—although he is leaving—has suggested that one way to deal with that would be for CAMAC to do a report on it. Reviewing this area as a role for CAMAC is an issue—they do not really have anything as big as this—but it may be that some brilliant mind could work out a way of making it a bit easier. That has happened in the past. There are people at ASIC who could probably really help you.

Mr MacDonald—One problem we have been encountering with particular issues is the resource level at ASIC. A number of highly technical difficult issues have arisen because of the devil that is in the detail of the regulations. There is nothing wrong, generally, with the act itself—it is only fairly short—but as you know the regulations are enormous, and a number of very difficult problems have arisen. Clients are trying to implement new products or to amend products, and they are being frustrated by the effect of regulations which just do not work.

We respect the huge task that Treasury and ASIC have had, but there are mistakes and anomalies. We are finding that difficult issues are being put to the regulatory policy group of

ASIC but are getting swallowed up and going missing in action for months, because they cannot throw the resources at it. I think that there needs to be some scope for working parties and industry bodies taking on some of the actual work that ASIC would otherwise do. If we could work with ASIC on a committee or working group basis on particular issues, that would lead to a speedier and more effective resolution in some of the tricky technical areas.

Prof. Harding—I probably should add that they just did get some extra money in the latest budget to assist them with this task.

Senator COONEY—How would you see these working parties operating? Would they operate outside ASIC and give ASIC or Treasury advice, or would they work in with the people from ASIC and from Treasury?

Mr MacDonald—I think the industry bodies, such as ASFA and IFSA, that represent some of the subindustries of financial services would be able to call on their members, which include accounting firms and law firms as well as the financial service providers, to provide commercial and legal expertise to work on, say, working groups or committees with representatives of ASIC—the effect of which is to outsource from ASIC a lot of the work, but yet they will still obviously control the end product.

Prof. Harding—Could I just comment on that? Within ASIC, they have all that considerable expertise under Pauline Vamos. The situation was basically that ASIC was given the legislation; they put in submissions much as we may have done. They then had to try to make it all work. One could argue that ASIC has not really been able to open its mouth and say, 'This is how it should really be'—even though industry would certainly have some views on that.

Senator COONEY—Professor, you mentioned that you worked with Senator Rae in the seventies. Where do you think the regulation that has taken place over the decades has now taken us? Do you think things are much better in the industry now?

Prof. Harding—I have no doubt. Some of the things that went on in the early seventies were just appalling. Broadly speaking, that is not the case now at all. There is a great deal more efficiency, honesty and, in particular, disclosure to the markets. You can see Australian investors—people in the street—are investing their money in shares in the market. In effect, they need to. Short of buying houses, how do you look after your retirement? I think they now have confidence in the markets.

It was Keynes who said that when the stock markets of the country are the by-product of a gambling casino, how could you have confidence in the markets? We have managed to overcome those sorts of academic arguments from the Chicago school to the effect that all of this is unnecessary and the market will sort it out. It obviously did not. You need regulatory intervention, and there has been regulatory intervention. I think things have vastly improved since the days of the Poseidon boom.

Mr CIOBO—Thanks for appearing today. I note that you said you were making comments on behalf of Freehills on the basis of client feedback. Would you have a retail bias in terms of your client base?

Prof. Harding—Really not. Probably we are more institutionally weighted. Perhaps I should clarify that in the sense that of course we have to advise clients on how to approach the retail market. We are not financial advisers so we are not giving financial advice to retail clients. Occasionally we may have a retail client who might walk in the door with a problem who wants to litigate or something but, broadly speaking, we tend to advise the intermediaries or the companies that are approaching the market.

Mr CIOBO—I am interested in a couple of comments. You may or may not be able to comment because it has more to do with the objectives and operations of FSR. I am interested in particular in your comments about regulation and the complexity of it—and that is concerning to me given that you are a practitioner—and what it might mean for the lay person. Given the amount of effort that has been expended thus far already by industry, in your view would it be worth while perhaps to try to capture more aspirational provisions rather than strictly regulated market conduct, and what do you think the trade-offs of that might be?

Prof. Harding—That was tried with the Trade Practices Act, in fact, under John Howard, I think, when he was Minister for Business and Consumer Affairs. That can work, but obviously ASIC would still have a substantial job of putting out policy statements to make it all work. That is a possible approach.

Mr CIOBO—Would it be one that in your view would have merit?

Prof. Harding—In this area I am a bit pro-regulation, frankly, in some sense, in that I saw so many bad things happening. Also I think certainty is enormously important. You would not want, in relation to superannuation, to have a few general strokes of the brush and people in effect not really knowing what the precise requirement is. And there are compliance issues then. So I am not really a sort of broad-brush man, frankly, but on the other hand it is almost going too far the other way.

Mr CIOBO—In terms of the compliance burden, though, it is a case of damned if you do and damned if you do not, from what you have just said.

Prof. Harding—I think clients try to comply because the consequences of not complying now are terribly serious. It just means that they have to put a lot more effort into compliance, which some would say is a good thing. Frankly, I think my main concern—and I suppose I am speaking personally rather than on behalf of the firm here—is that ultimately someone has to pay or the industry becomes very inefficient and business slows off. For example, I am a bit concerned that lots of people who could advise retail customers are going to say, 'There is too much compliance; it is too hard. I will only deal with institutions.' We have lots of clients like that. That would be unfortunate in that you need good financial advisers who work at the retail end. I do not think their task should be made intolerable.

Mr CIOBO—That actually leads to my next question. Do you think that the regulatory burden will limit or have an impact on product innovation?

Prof. Harding—Historically the market is always innovative. I just do not believe it will stop innovating. We have seen lots of innovative products come out. But there are aspects to that. For example, there have been developments of reset preference shares in recent times. That is

done by prospectus. That goes to lots of retail investors. That is all fine. But then you get these situations where you have a requirement for both a prospectus and a product disclosure statement where there is a stapled security. That is quite a useful idea. It is innovative as a product. You have two regimes which are different in some respects that you have to comply with. You have two documents, and it gets quite expensive.

Mr CIOBO—With respect to training, you spoke of feedback that you have had. I am interested to know what you foresee, given its current context—so if that were introduced as is—as being the impact on the marketplace. Do you see a premature exit of long-term financial planners and industry representatives?

Prof. Harding—I, myself, have not observed it, and I do advise a lot of brokers and financial advisers and, of course, it is in; it is a requirement. I have been to meetings with people working in the industry, and some of them are starting to realise just how serious all this is and what they have to do. But I have not actually heard anybody—even someone who is over 50—say: 'I give up. It's too hard. I'm going home.'

Mr MacDonald—My feedback is that some people will not bother with keeping up to date, but that might just accelerate their move out of the industry. Generally, it will be a cost to service providers which will be passed on to clients.

Mr CIOBO—Does it serve as a barrier to entry for new people?

Mr MacDonald—I do not have enough feedback to comment on that.

Mr CIOBO—Do you see any position that can be adopted to make the legislation more manageable? What would that be?

Prof. Harding—In a sense—after a period—a review to try to make it less complex would be desirable, given what the experience is. But I think in a sense Treasury has reacted by dealing with problems as they have arisen, and that has been a piecemeal approach to some extent—for example, in relation to insider trading in derivatives. Those things are very important because industry raises them and they are serious problems for industry. Quite frankly, I would not want that process to stop.

Mr CIOBO—So you are satisfied with the process so far?

Prof. Harding—I would not say we are totally satisfied with it; we keeping finding anomalies.

Mr MacDonald—That act itself was subject to a two- to three-year period in which we were familiar with the outline of the bill and there was a lot of industry consultation. But, as I mentioned before, the act is an inch thick and the regulations are six inches thick. The ability to consult on the regulations was provided to the industry but relatively short periods were provided. The purpose of this inquiry is welcomed by the industry, but not the same number of submissions have been received as those on the act itself. I think that, recognising the busy schedules of a lot of the participants in the industry, they have not had time to focus on a complete and proper submission on the regulations and therefore have not put one in at all. So I really think

that the regulations are where the detail is and where the real law is, and I think that perhaps a much more powerful review of the detail is required.

Ms McAlister—I can add to that with regard to superannuation. In the attempts to respond to people's submissions in that flurry of activity between December and March, changes were made which would solve one problem but then those would be inconsistent with something else. Just that very inconsistency then creates a new problem. So I think at some point obviously there needs to be a review of that at that detailed level.

Mr CIOBO—With regard to super, there was some commentary on the ongoing management charge. Do you have any comments on that in terms of its operation and clarity to consumers?

Ms McAlister—Yes, I do. The idea of the ongoing management charge is certainly a big step forward because it will now extend to all superannuation funds, whereas previously a similar concept only really applied to public offer funds. The question is, though, whether it will actually produce any meaningful information for the member of the fund, because potentially the management charge has two components—it has an investment component and an administration component—and then, if there are investment strategies within a fund, the charge has to be given for each strategy. So with some funds that offer, let us say, 20 investment choices, the multiplicity of figures that will be produced could be absolutely dazzling and quite mind boggling.

I notice that ASFA appeared before the committee before, and ASFA has suggested that really it is the bottom line figure that counts from the consumer's point of view. If there was some way to provide that more meaningful figure without a lot of unnecessary complexity, I suppose that is really what the legislation should ultimately be aiming for. To the consumer, it is 'What am I going to get at the end of the day after they have taken off all these charges?' that really counts.

Mr McARTHUR—Professor Harding, you raised an interesting issue of the 1970s that investors were not well protected. Could I ask you for a broad comment as to how you compare that with the state of the legislation as it now stands in protecting investors and having them well informed? Would you care to compare that with international regimes as well?

Prof. Harding—In a sense, one of the most important areas, or perhaps the most important area, is continuing disclosure to the stock exchange. There is no doubt that Australia has been quite in the forefront of trying to sort all that out and make it much better. The introduction some years back now of the ASX listing rule 3.1 and other listing rules and the introduction in the Corporations Act of sections 1001A and 1001B and other aspects have certainly strengthened disclosure and in effect the efficiency with which the stock exchange has chased those who have been late in disclosing. ASIC has been involved in terms of dealing with issues about analyst briefings and private briefings through a paper 'Heard it on the grapevine' and later papers. Then more recently there is the work of the chairman, David Knott, to increase continuing disclosure and make it more effective. These things have given us a much better informed market and make companies, particularly listed companies, much more conscious of their need to keep the market very well informed. That is all really outside the area of the FSR; that is a general Corporations Act and other types of regulations area. I think that is one of the things that we have now. Of course, relevant to all of that are accounting standards, but that is another very complex issue.

CHAIRMAN—I have no questions. I think the questions have covered the issues fairly well. As there are no further questions, I thank you as representatives of Freehills for attending the committee and for your answers to questions this morning.

Prof. Harding—It is a pleasure, and thank you for the opportunity of attending.

[11.23 a.m.]

LAWLER, Mr Luke, Senior Adviser, Policy and Public Affairs, Credit Union Services Corporation (Australia) Limited

LOVNEY, Mr Adrian, General Manager, Public Affairs and Compliance, Credit Union Services Corporation (Australia) Limited

CHAIRMAN—Welcome. The committee prefers that all evidence be given in public but should you at any stage wish to give any part of your evidence in private you may ask to do so and the committee will consider your request. The committee has before it the written submission from the Credit Union Services Corporation, which we have numbered 9. Are there any alterations or additions you apply to make to the submission at this stage?

Mr Lovney—No, thank you.

CHAIRMAN—I now invite you to make a brief opening statement and then we will proceed to questions.

Mr Lawler—Thank you for the opportunity to talk about the FSR regulations and policy statements. Generally speaking, we have been and continue to be supporters of the financial services reform legislation and of the objective of better information and better protection for consumers of financial services. It is a very large and broad-reaching piece of legislation. The chairman of ASIC recently described it as the single most important piece of law reform for the financial services sector of the last 50 years, and we would tend to agree with that.

There were quite a number of initial concerns and there are some continuing concerns about the effect of the legislation and some of the regulations. Treasury have responded to concerns about some of those aspects of the legislation which commenced immediately on 11 March and were not subject to the transition period—for example, the confirmation of transactions requirements and how they affected deposit accounts. Deposit accounts are already subject to a disclosure regime under various codes, and the regulations have brought those confirmation of transactions requirements into line with the codes, so that has helped a lot. Treasury have also foreshadowed a continuation of the formal consultation process that they have had, and we certainly welcome that.

We have established a regular dialogue with ASIC about its implementation of the regime, and we want to put on the record how much we appreciate and recognise ASIC's willingness to listen to industry. The main gripe that credit unions have with the FSR regime is with ASIC's policy statement 146, the policy statement on training. That policy statement sets out the training requirements for financial product advisers and it divides financial products into two bands. In one band, which is known as tier 2, are basic deposit products, non-cash payment facilities and general insurance products. In the other band, known as tier 1, is everything else—all other kinds of investment products, including deposit products, particularly term deposit products, which do not meet the definition of basic deposit products. Tier 1 product advisers

have to be trained to a diploma equivalent level. Advisers on products within tier 2—which is lower than tier 1—have to be trained to a certificate 3 equivalent level.

In short, our position is that there is no need for external benchmarks—for example, certificate 3—for assessing the competency of people who advise on basic deposit products and payment facilities. In our view, advisers on deposit products other than basic deposits should not have to meet the highest tier 1 level; they should simply have to meet the tier 2 level. So essentially we are looking for three tiers rather than two, and we want deposits which are not basic to be in tier 2, not tier 1.

The treatment of basic deposit products is unique in the legislation. This committee is quite familiar with the debate here. In fact, it recommended twice to take deposits out. Deposits are in, but they have quite a different treatment from any other products, particularly in terms of the disclosure rules. But in our view, policy statement 146 does not recognise that quite unique treatment of basic deposits compared to all other financial products. We think that other kinds of deposit products which do not meet the basic definition—which are essentially at-call deposits—such as term deposit products, should not be grouped with more complex and risky investment products in that higher tier 1 level; they should be back in tier 2.

Just to give you an indication of the practical impact of the training requirements, something in the order of 6,000 credit union staff will have to be trained or assessed to be competent against the benchmark. That will cost, at a minimum, something in the order of $3 million. The training and competency requirements are not just a matter for customer service officers but are obviously also an issue for credit union managers in terms of obtaining a licence. That issue was touched on by the previous witnesses. The ASIC policy statement 164 sets out the regulator's expectations in terms of the competencies of people running an organisation. There are four options open to licensees to make sure that their nominated responsible officers have the knowledge necessary for their roles.

Our criticism is that these options do not give any weight to industry experience in terms of knowledge. There is some weight given in terms of skills but not in terms of knowledge. There are a significant number of credit union managers who are quite experienced and who run successful credit unions but who do not have the formal qualifications that ASIC requires as stated in its policy statement. They would have to undertake a diploma course or be assessed at a diploma level, which we think is not necessary, and in fact it might be quite difficult to find the right course. Again, we make the point that these are experienced managers of prudentially supervised, authorised deposit taking institutions.

The last issue I will raise in our opening statement is one concerning credit union member shares. When you open an account at a credit union, you become a member of that credit union; you are an owner of the credit union. You pay $2 or $10 for a member share. This is a security, recognised in the Corporations Act, but it is a security that you cannot transfer, that does not increase in value and its real meaning is not something akin to an investment; it is really akin to a ticket of entry to obtain the financial services of the credit union. To make a deposit or get a loan or any other kind of financial service you have to be a member, and to be a member you become an owner of a credit union member share. Unfortunately, because it is a security, it gets caught up with a raft of FSR requirements in terms of licensing, disclosure and conduct for people who are advising on these securities, which we think are completely out of proportion

and unnecessary. We have sought relief from ASIC in relation to this particular security, and we are awaiting ASIC's judgment on that. But I think it is a good example of an unforeseen consequence of a large piece of legislation that has some 'one size fits all' qualities which you have to then spend time and resources to fix. That is all I would like to say in my opening statement.

CHAIRMAN—Thank you for that statement. Again, I will hand over to Senator Cooney to chair the questions.

Mr CIOBO—My question is with regard to what you are saying about there not being enough carve out of basic deposit products. To the extent to which you have outlined the three tiers you are seeking and the discussions you have already had with ASIC, where do you see that headed at the moment? Is it a case of you just do not know?

Mr Lawler—ASIC have said that the policy statement stands for the time being. They have not given us any indication that there is likely to be any change in the near term. One of the factors to be taken into account is that the clock is ticking on the transition period. Decisions have to be made about how you are going to train your people, what sorts of products they are going to sell, and how they are going to sell them, so there is a timing factor to take into account.

Mr Lovney—CUSCAL have certainly raised the issue in their comments on the draft interim policy statement before it was developed. One of the observations that we made about that is that the basic deposit product carve out, as it is described, came into being after the interim policy statement 146 was released in its first draft form. There was no change to that policy statement after that legislative carve out was inserted into the act. As we stated earlier, there appears to be very little recognition of this quite significant shift to the operation of the legislation in policy statement 146.

Mr CIOBO—Prior to this, what was the operation of the legislation? Essentially you were exempt prior to the introduction of the FSR?

Mr Lovney—In some respects the regime mirrors the arrangements which are currently in place for credit unions. Quite clearly, credit unions, whilst they are diversifying their business, tend to sit at the lower end of the risk spectrum in terms of the products that they offer. They are generally basic in nature and smaller credit unions in particular have a less sophisticated product suite that usually consists of what we now understand to be basic deposit products and non-cash payment facilities as well as some general insurance. They are certainly in that lower tier.

The disclosure regime that the FSR regime will include in some respects matches the existing level of disclosure that is already associated with those deposit products. The dispute resolution scheme that credit unions currently use will largely be the dispute resolution that they will use in the new regime. So the FSR regime, while it does impose additional obligations to some of the more risky products, in some respects mirrors in many degrees the existing regulatory arrangements that credit unions operate under. The one that is different is the training regime. Our concern about the training regime as it currently operates is that credit unions are forced to expend funds to essentially retrain their staff to do jobs that they are currently doing. It is one of the classic dilemmas in a piece of legislation that applies across a range of different products. It

was mentioned earlier today that in trying to create uniformity it actually becomes more complex, because the more you delve down into the regime, the more you observe some of the problems that arise in implementation.

Mr CIOBO—Were there instances of market failure before—for lack of a better term—that you think would have warranted ASIC's attention? Do you think that it was an oversight or that it was intended to cast a net so widely?

Mr Lovney—We have argued from the very beginning that there was no evidence of market failure or a lack of depositor confidence in those basic deposit products and, for those reasons, that they should be subject to a less intense regulation. We are not suggesting for a second that anything from probably a term deposit up should not be included in the regime. We support that consumers are better informed. There was certainly no evidence of market failure or a lack of depositor confidence. Depositors are well informed. Credit unions have been offering these products for a number of years. That was the reason why we argued—and indeed this committee supported—that those deposit products be carved out. What we find now is that, in the implementation of the regime, ASIC has not fully recognised that those deposit products were intended to be treated differently by the legislature.

Senator COONEY—Let us look at the issue of the training requirements. I suppose financial advice is becoming more and more important. As you say, there are different areas across a range. The ability to give advice is different and therefore the training ought to be different. But if it is becoming so important, does it not fit into the same category as lawyers? Some lawyers give very basic advice but they have to have training. Doctors might give basic advice about colds but, nevertheless, they must be qualified. If we want good plumbers or electricians they must be trained. It is certainly feasible but do you think it is safe to say, 'We will have different levels of training'? Why should we not say in regard to superannuation, with financial services becoming so important and with the public getting more interested in this area and being encouraged to do so, that we have to have a professional body? If you are going to give advice in that area, some of you will reach the heights of advice and others will be more content to give fairly basic advice. Nevertheless, that is your choice.

Mr Lawler—I think you have to look at the actual products. If you are talking about at-call deposit accounts and associated payment facilities, that really is something completely different from making a big investment, whether it is in a term deposit or something more risky higher up the scale. There has been some recognition of that in the legislation. We think that it does not make sense to have an external benchmark training requirement for someone advising on an at-call deposit account, and an associated payment facility, compared with someone giving a wide range of advice on financial planning or superannuation or the stock market. We think that is quite different. We are not saying we do not think training is a good idea. We think training is a good idea, but the training should be proportionate to the nature of the advice. It is whether you are talking about financial advice generally or someone giving financial product advice where the financial product is an at-call deposit account and a payment facility. That is quite different from making a significant investment or from a retirement planning situation.

Senator COONEY—I can follow that, but look at other professions. If you want to do law and all you are going to do is give advice on traffic law, they do not say, 'All right, you need different training from somebody who is going to advise in fairly complex areas,' such as the

area Professor Harding was talking about; you have to have the training. It is the same with doctors: some doctors might say, 'All I want to do is prescribe for colds. I'm not going to do heart surgery.' Nevertheless, they have to have the training. You seem to be saying that what is going to determine this is the area in which you give advice. That is not the sort of approach that is taken in most professions, is it—or even in apprenticeships?

Mr Lovney—Even within the legal system, though, the system reflects differing degrees of specialisation: people can see a junior solicitor, a senior partner, senior counsel or Queen's Counsel. Conversely, the legislatures are increasingly recognising that, if somebody needs their house to be conveyed, they do not necessarily need to see a solicitor. The legislative regime reflects the fact that less simple transactions do not necessarily require the same levels of training. So, as I said, while we certainly support the concept that people who engage in risky business and who want advice on complex and complicated financial products should receive that advice at the high end of the scale, we also think that the regime should be flexible enough to recognise that people who sell and advise on deposit products, which are essentially capital guaranteed and well understood by the community, can be trained in-house. I am suggesting not that training does not occur but that the training is at a different level of intensity. We think that policy statement 146 should recognise that.

Senator COONEY—Do you want to say something more about the credit union shares you were talking about or have you covered that sufficiently?

Mr Lawler—I would like to expand on two points. One is that there is an unintended consequence, and I think we will continue to see examples of unintended consequences. So the question that arises is: how quickly and effectively can they be identified and dealt with? I mentioned earlier an example of what appeared to be a disproportionate impact of the confirmation of transactions requirements on deposit accounts. That was fixed by regulation before the regime took effect. In this case, we have sought relief through an application to ASIC, so it will be interesting to see how that unfolds and how quickly and efficiently those sorts of things unfold. We are waiting to see how the system will work in that respect. ASIC has undertaken to give a prompt response.

Mr Lovney—ASIC has certainly been responsive in getting back to us when we have raised issues. We offer it as an example of how the regime can sometimes produce perverse results and the considerable amount of effort that industry has to put in to identify, advocate and then get these issues isolated and fixed. It is an example of what happens when you apply a uniform regime across products which range from passbook accounts right up to shares and derivatives.

Senator COONEY—You are saying that there has to be a distinction determined by the product you are looking at rather than determined by just wanting a consistent system right across the board?

Mr Lovney—We are saying that sometimes what appears simple can produce perverse results and that industry—and, indeed, the regulator—needs to put energy into resolving those issues. Time that is spent complying in areas where compliance may not be necessary or where this attention might not be necessary diverts our attention from areas into which we should be putting energy.

CHAIRMAN—Thank you for appearing before the committee this morning. We have appreciated your evidence and response to questions.

Proceedings suspended from 11.45 a.m. to 1.21 p.m.

MITCHELL, Mr Dugald Scott, Consultant, Association of Financial Advisers

NOWAK, Mr Joseph, National President, Association of Financial Advisers

MURPHY, Mr Michael Francis (Private capacity)

ACTING CHAIR (Senator Cooney)—Welcome. The committee prefers all evidence to be given in public, but should you at any stage wish to give any part of your evidence in private you may ask to do so and the committee will consider your request. The committee has before it a written submission from the Association of Financial Advisers. Are there any alterations or additions you would like to make to the submission at this stage?

Mr Mitchell—I assume you have received our submission 14A?

ACTING CHAIR—Yes. The committee also has a written submission from Mr Murphy. Are there any alterations or additions you would like to make to this submission?

Mr Murphy—No.

ACTING CHAIR—Would you like to make a brief opening statement?

Mr Murphy—Although I am a member of the Association of Financial Advisers, my submission and my appearance here today is as an individual. I believe you received my submission, and I apologise for any typos because it was rushed. I will get to the point and articulate as simply as and as best I can the dilemmas faced by many practitioners in our industry. Although this is a personal submission, I believe I speak for many.

Ownership of clients, satisfactory compensation and right to work are still real issues. Our current agency agreement has a buyback clause, and if we roll into the Financial Services Reform Act the asset becomes the property of the dealer. There would appear to be now no option for obtaining our own licence, as it is becoming extremely difficult to get professional indemnity insurance. Once with the dealer, I am at their mercy—and so are many others—to keep my proper authority, and with no right of redress. They impose their interpretations or requirements. Some of them are IPS 146 minimum; others require a full diploma. I have currently failed to meet minimum standards by one module, I hate to admit, but my two junior staff have obtained minimum requirements, which means I cannot practice in my own business of 16 years post-30 June this year. By the way, I can lend money without any prerequisite qualification—just accreditation from the lending institution, and they do not seem to be subjected to the same antihawking provisions. Many dealer groups are owned by the source of the money.

Structure and tax is an issue. Currently, agreements are held by a corporate entity. Payments to the entity are made and then distributed accordingly. I currently have five full-time staff and would have more if not for the inefficiency of our product providers, which we have touched on before. New structure agreements are held directly—that is, as a holder of a proper authority of a licensed dealer—although I have not seen one yet because no-one that has approached me has

applied for a licence. All income potentially is treated as personal services income and then suffers the relevant taxation consequences. Recently ASIC personnel espoused us maintaining agency agreements for insurance and having proper authority for securities business with a licensed dealer. This does not appear to be an option, due to the liability issues created by cross-endorsement. In any case, renewal of our professional indemnity insurance now is very questionable, so I doubt whether we can even trade after the end of May when my insurance runs out.

The whole thing really is about distribution control. The legislation is consumer driven, and the outcome for the consumer is questionable. All proposals for agreements with major dealer groups, who I believe will be the only sustainable entities, give a direct bias towards use of their product by favourable or unfavourable remuneration terms. That is, they are offering agreements where we will get a buyback option of four times on their product, and if we use product from external manufacturers the buyback option falls to three. Also, with the remuneration ongoing we receive 100 per cent commission from those whose product we sell, that own the licensed dealers. We get 85 to 90 per cent from using external products. In our case we are faced with the transfer of a major block of business due to lack of support from our product provider but are being compromised and therefore the consumer is being compromised because of the 25 per cent devaluation of my business. There is also the issue that I brought up previously, that new business risk is getting harder to put on board. The treatment of claims is abysmal and super administration is just absolutely abhorrent. Also, new products being supported are securities based and cannot be dealt with under our old agreements, which is forcing advisers into the new arrangements. This is just press-ganging.

I have headed my notes 'Bullying for profit'. Under the old agreements or arrangements we have a cost structure under which we can operate. Now we are being offered, or pressed into, new arrangements which involve increased payments to dealers based on increased costs of the FSRA—or that is the perception of the representations. Failure to comply is resulting in terminations of agreements, and the time frame for that is 30 June 2002. I thought the transition period was to 11 March 2004. Also, as a result of the position that I have taken, I have been threatened with termination of my agreement and being sent broke. I have been advised not to mount a legal challenge as they will outlast me in the legal system.

Through my association I met with APRA personnel regarding administration—or should I say maladministration?—of superannuation. The reason given was that ASIC neither had the personnel nor the financial resources to deal with the issues. I discovered an anomaly that needs addressing. That is, the client complaints to the administrator either direct from the client or from the adviser do not have to be logged or reported. This process is only required when complaints are made to the trustees. There is a Chinese Wall to protect the big end of town which must be dealt with by an appropriate body. The issues discussed with APRA were of gross incompetence by the providers—allocation of funds not being made, incorrect taxing of contributions, insurance not being put in place, insurance not being removed on request, funds not being transferred in the required manner and as a result insurance benefits being lost, and, finally, rollover cheques unassigned to members which could result in misappropriation of funds.

Compliance is being abused by some dealers. Their audit procedures for inspecting files is flawed. We have instances where advisers have perfect files and have taken 100 per cent in

commission—not four per cent; 100 per cent. The system employed by them will not catch the class of people who will be outside the law. It is not until they are found out that there is an issue. I am not sure of one case where the dealer has raised the alarm.

The current lack of clear interpretation of the legislation is seeing good citizens with sound businesses being forced out of business by the bullying tactics of others. The adviser has no protection under the legislation and, as I said at the time of the passage of the bill, we are the class of people the legislation forgot. We have already seen issues I raised in my submission prior to the presentation of the bill coming to pass. I, for one, am not prepared to stand by and let it happen. I have too much at stake still with my wife and six children. Thank you.

Mr Nowak—I am going on to the presentation which we made. Basically, the concern of the AFA is the protection of the small business. I am just going over what Michael said. We have come out from the Insurance Agents and Brokers Act. In 1985 I dealt with Kevin Hockter and the ATO and set up a system of ownership of trails in our businesses. That has all been eroded by this whole new transition. That has not been recognised and we have a problem as far as going forward, whether our business becomes PSI or PSB. At the moment we have no protection at all in that area—that is, going back on the ownership of our trails et cetera.

We have also present and future liability for capital gains. We do not know about on the transition. We have written to Senator Campbell and Treasury. We have not had a reply for four months. What has happened is that we have three departments—Treasury, ATO and ASIC—who have not spoken about the transition. We have asked for a meeting with those three sections so that we can say, 'This is about small business. How can you three get together and work out what we are doing and go forward?' I have asked for that and I need that to be supported, because at the moment none of the three knows what the others are doing. That is the tragedy of it all. When they have worked through this, we could have a disaster with the ATO if we do not get it right.

On the use of special licence, we were told originally that in the transition, under the agents and brokers act, we could get a special licence. We are now told that after 11 March 2004 it is not on. So we have no protection there. We have a problem with the PI insurance. We were told we could go joint and several—we could go limited licence and be a representative through another situation, but no-one with the present situation with PI insurance will take us on. It is going to all collapse. There are real big problems there.

I think the antihawking provisions are about 10 years out of date. I was told by a memo the other day that if I go and have a drink at my local tavern I have to walk in and tell everybody that I am a financial adviser before I have my first drink. That is very embarrassing. That is the last thing I want to do.

Mr Murphy—What—have a drink?

Mr Nowak—No—but that is how far it has gone.

Senator CONROY—Just wear a sign on your head!

Mr Nowak—The other tragedy about that is this: we came across advisers in regional Australia, and they cannot ring after seven or eight o'clock. Most of the people on the land do not get in until seven or eight and they like to do their after-hours work at that time. If we do not speak to our clients, we get into trouble for not contacting our clients and doing the business planning for them. So we are on a hiding to nothing. As I said, the whole antihawking legislation is driven by some people who are about 10 years out of date. Secondly, we were not on the consulting committee. I asked who was on the committee, and we were never informed of the process. That seems to be a bit of a worry with us. There are a lot of things happening, but we are not sitting in on those meetings and going through the process—which we are quite happy to do. There are rules being made without consultation.

The last thing I want to talk about is disclosure of commissions. Our association is totally behind disclosure on investment business, because that has an effect on the end benefit. If a person rolls $100,000 in a super fund out and you charge three per cent, they know exactly that it is going to be $3,000. We are very clear on that. In the risk business we are against disclosure on trauma or income protection and those issues because they have no effect on the end benefit. If you insure a person for half a million dollars worth of life cover and the premium is $100 a month, the half a million dollars would be paid out anyway. It does not matter whether you get $100 commission or $300 commission, because the legislation, as it was previously worded, was that the big end of town had what they called back-office expenses. The premium was the same. If you worked for a bank or insurance company as an employee, you said you got $50 commission and if you happened to be an agent you may have got $500 commission but the premium was the same. They were able to hide the backroom expenses away from the client—and we got that stopped. That is how stupid it is, but everyone plays the game and the big end of town had that advantage.

Last night I went to a situation involving a couple: the male partner is 57 years old and he has left the company. He was in a group life plan and an income protection plan with the company. He has got cancer. From now on, he cannot get insurance anywhere because he is in his fourth year in remission. But under the group life plan he can get $630,000 cover without any medicals, and he can get an income protection plan for $90,000, with a three-month waiting period and a benefit until 65. I implemented that because I know what to do, and I know that after 60 he cannot get that insurance anymore when he comes out. The work is very technical. At no stage did he ask me what commission I am getting. He did not care, because he could not get that policy anywhere else. So the work we are doing is very technical, and with the advisory business that we look after—the clients—what we are asking is that we get protected in the transition period.

Mr Mitchell—I want to touch on two subjects. The first is commission disclosure. We have been trying to find the regulations on commission disclosure. We could not find them, and eventually we asked ASIC where they were, and they said, 'Use our email system,' and so I did that. I sent them an email and asked them to refer me to where these regulations are on the web site. I got acknowledgment of that letter, and then 19 days later I got a rather technical email back, making a number of suggestions about where to look.

In the commission disclosure regulations we are interested to know what the word 'influence' means, because Treasury have said to us that they think influence is the payment of any commission. There are some people who do not think that. There is also the matter of backroom ex-

penses, which is important insofar as the expenses paid out of the commission are concerned. When I got the stuff back, I had a look and it seemed to me that the references they gave did not supply me with information about where to look. I say that because I think we cannot really comment unless we know where these things are and what they are.

I also want to say something about the right of the adviser to work. I refer you to supplementary submission 14A. In that, there is a copy of a letter to me terminating my proper authority. It says right at the bottom of the page:

> Pursuant to clause 9 of your proper authority agreement and the Corporations Law, CFS does not pay trailing commissions to terminated representatives.

Obviously, I will be moving my proper authority elsewhere, but while I am doing that I am not being paid. In all this process, the AFA have lived with the new concept of turning advisers into authorised representatives, but the dealer does not really know the clients or know anything about them. The adviser knows that. You will notice in the letter that there is no mention of clients. Those clients are going to be without advice, and there certainly isn't anybody, as far as I know, who is going to take them over. I make that point because that is what we are here for: we are here to advise people about their financial arrangements, and if you cancel a proper authority those clients lose that right to advice.

The other thing is that it was mentioned how in the Insurance (Agents and Brokers) Act some 10 years ago the 1985 arrangements were made. But in about 1990 there was a case in Sydney where an irate state manager cancelled quite an important contract adviser or agent in Sydney and the outcome of that situation was that, through good legal advice, the adviser was paid a large sum of money for that cancellation. Since that time, no agent's authority or contract has been cancelled. That common law arrangement does not seem to have been transferred across to the new arrangements; I think we have probably got to go through all of that again. It is really about the relationship between the agent and the principal. So I make the point again that this letter does not say anything about how those clients of mine are going to be looked after in the future.

Senator CONROY—Thank you for those submissions. I guess, Mr Murphy, it is time for you to say, 'I told you so.'

Mr Murphy—I am quite happy that you have said that, Senator Conroy. I think you are right. If you look at my original submission—which was a submission that I made purely after the first reading—you can see that I looked at my business and how the act would impact on that business. It has happened; yes, it has come to pass. It is almost biblical.

Senator CONROY—As you know, the committee was concerned about your position and we tried to get advice from the government and advice from Attorney-General's as to whether your interpretation was correct. I know that Senator Chapman worked hard, along with the other members of the committee, to try to get an amendment to the original draft. When I first saw your submission I spoke to Senator Chapman—and if he was on the phone he would concur—and we were concerned that the intent of the amendment, which was to protect you from this, does not appear to have worked.

Mr Murphy—I think the difficulty is that, in the real world, the control or the might is with the big end of town. That is the problem. Traditionally in this industry, that is where most of the practitioners have received their advice, their counsel and their support. As a result of the enactment of this bill, it is separated: now they can do without the adviser, although they say that they cannot. In my last meeting I did not know if it was rhetoric or just platitudes, was my final comment to the gentleman who was a senior executive. The difficulty is that we are faced with a situation—and we can go through those two issues that we were talking about, and I have had further discussions on those—that is unconstitutional.

I am losing value in my business and the minute I walk through the door and roll my agency business in with my licensed dealer I have just lost somewhere near $1 million. That has to be addressed. What is even worse is the situation of one of the guys that works with me—because what has happened is that I have become a source of advice for a number of people as a result of getting involved in this. He runs a rural insurance agency with a life insurance agency. He is the second generation of that family to have done so. A financial planner bought into that business 18 months ago. He has his full diploma and is fully qualified. The principal of the business—whose company owns that business—has the agency agreements with Colonial First State and others.

On 30 June, the principal of the business has not been able to get up to speed with what is required of his general insurance requirements, being a country practice, and his financial service IPS 146. So he has said, 'What I will do is let my new partner, who is a minority shareholder, take over that whole business.' He does not have any agency agreements. What he has is a proper authority through a licensed dealer, so the whole asset value of something like 35 years of business sits there with no-one that can deal with it until 2004. The guy that is the financial planner does not have sufficient income to support his agreement, which requires him to have a minimum $30,000 worth of income, but if he should roll that asset of the insurance practice into the licensed dealer it could probably achieve that result. It is a real dilemma because the licensed dealer has walked up and, as I said in my submission, has said, 'Well, it used to cost you a percentage of the business you wrote last year; now it costs you $12,000 plus a percentage,' due to the FSRA—or that is the perception. The act was never meant for the companies to profit. We are trying to negotiate to bring that whole agency into my portfolio because they have worked with me for a long time, but I have to have an employer-employee agreement with them for the licensed dealer to accept that they can work within my portfolio. Then again, the problem is that we have not got the PI yet.

Senator CONROY—If you got PI, would that speed the journey?

Mr Murphy—It would speed the journey, but the difficulty is that I still have not been able to ascertain from ASIC or anybody the cost of me having my own licence—not the cost of purchasing a licence; the operating costs of that licence. What is my PI as a sole licensee? What other costs are going to be incurred for future compliance, future research and all the other resources we need to hold a licence? My educational qualification does not allow me to have one anyhow—I am a failure. If someone could tell me, I could measure a dealer saying to me, 'You are going to pay me $12,000 a year for these services and we are going to take five, 10 or 15 per cent of this business you write,' and then I can work out pretty simply how much that is going to cost. I do not know what a licence is going to cost me, but now, with what has happened in the last month, that opportunity to get a licence has gone away because I do not

believe that I would be able to buy the PI—which makes the legislation close to being unworkable, disadvantaging and therefore a loss.

Senator CONROY—The PI issue is much bigger than just the issues we are taking on in this room.

Mr Murphy—Absolutely. Do you know who controls the PI business now? The banks. They are coming into my office saying, 'You can lend money to your clients and we will pay you to do that.' I am not qualified to lend money—you can get that in 20 minutes. I say, 'No, we don't do that. We are very good at what we do, but we don't want to do that.' So they say, 'But look at all the money you can make,' and I say, 'Hang on, my clients are not cannon fodder for your shareholders.' They get upset about that, but I value my clients. I am not there to make money; they are for me to advise them.

Senator CONROY—I do not want to hold out false hope, because the PI issue has been around for a good six months now and there are no easy answers. But there is a meeting on 30 May between all the state ministers and treasuries and the federal ministers and treasurers that will hopefully go some way to getting a solution, if not solving it. I would not want to get your hopes up by saying it is going to be solved. I am sure it will be a great photo opportunity, but what we need is an actual solution.

Mr Murphy—I can obtain PI in my current business arrangement; I just cannot change that business arrangement and still get it. And I do not know the cost.

Senator CONROY—Could you expand why they are saying, under the new arrangement, that you cannot get PI as opposed to what you have got now, or is it simply that you have an existing contract and they are just not offering PI in this new area?

Mr Murphy—The difficulty is that, until I cross the line and go into that new arrangement, I cannot apply for it. Having done that, I have just sold my soul. I cannot go back. It is like having babies: you cannot get back.

Senator CONROY—You look like an adventurous type, though. You do not mind jumping off a cliff!

Mr Murphy—I am not prepared to take the gamble at this stage that I get left out in the cold. I have no track record as a licensed dealer. I am a life insurance agent that is a proper authority holder for a licensed dealer with probably five per cent of my business. What is alarming about that, too—and I know you, Senator Cooney, are interested in this—is that the new product being brought to the market is what we used to know as securities business. The product we can sell is being diminished. Like all new superannuation offerings, it cannot be sold unless you have a proper authority. The companies that are introducing those are the companies that hold the superannuation moneys, and they want to transition that money into the new regime as well. That is one of the reasons we, as the association I was representing, went to APRA—because I was not sure whether the balances being transferred were correct. I have supporting letters from clients that could guarantee that position.

Senator CONROY—Obviously, even if we are able to solve PI, we do not solve the other problem of loss of value.

Mr Murphy—No.

Senator CONROY—Do you have a suggestion?

Mr Murphy—I do have a solution, and it is a very simple solution. I believe that all licensed dealers should pay out the agency agreements on transition and allow the proper authority holders to continue practising. It is as simple as that. As I say, none of them has applied for a licence yet under the FSRA. They are walking around trying to work out who is going to join them before they make a move. It is quite simple: if they pay out my agreement on reasonable commercial terms, transfer my business and still give me my guarantee when I leave the business, I would be quite happy to go over there. But the difficulty is that we then become employees of the licensed dealer. I run a practice with six employees, and I could employ three more tomorrow if I could get the support from the fund managers. They are hopeless. I have so many people because I have to try to make up for what they are not doing. But we cannot help it. As I said to Senator Cooney, and it is not a boast, we are in an industry which is a licence to print money if it is run properly, and that is recognised by the people who make the money—the big end of town. It is very sad, and I do not think ASIC would find too many practitioners which they could suspend for a while. They have done a great job, by the way, in South Australia in getting rid of some people we really wanted out.

Senator CONROY—Who can put pressure on them to negotiate commercially with you? Is it ASIC who goes and says, 'Look, you are not going to get your licence?' I do not think ASIC has the powers to do that.

Mr Murphy—No, they do not.

Senator CONROY—I am trying to work out what the mechanism is to make them bargain with you in good faith.

Mr Murphy—I have no answer to that. They are omnipotent.

Senator CONROY—Any suggestions?

Mr Nowak—We have been to Senator Campbell's office and we have spoken to Treasury. I think in Treasury there are new people: Nigel Ray is in a different department and I have spoken to Melissa there and she is not aware of the history. A new person in the situation is not aware historically of what is going on; they have no idea. I have asked that in July we sit down in a room like this and go through the process and get some sort of an outcome, because there are going to be a lot of people hurt and a lot of clients without advice. That is where we come from, and we are hoping that we can get that with your support. Something has to be triggered so that the big end of town back off a bit, because at the moment they are giving Michael a hard time and they have just given Dugald the chop—it is just a matter of time. They have been waiting for 11 March 2004. They do not know where they are going.

We have had so many amalgamations in the industry: Legal and General, Prudential and the Colonial. We have a new type of management who are all under 40 and they are not aware of the history; they are just driven by the shareholder dollar. They want to reform everything and clean everything up; they do not care about relationships. They are driven by that shareholder situation; they are not driven by customer satisfaction. You get that every day by the banks. They just put their fees up; they do not seem to care. That is the way they are treating us the clients, and they have the big stick and they can belt us.

Senator CONROY—Is there an ACCC issue? I am just trying to think.

Mr Murphy—I have been to the ACCC, sir.

Senator CONROY—As always, you are ahead of me.

Mr Murphy—I went to them because the day the bill was presented for the second reading I had a discussion with a solicitor from Treasury, Grant, Nigel Ray and somebody else. We had a telephone discussion. There was a suggestion that our issue would then fade away from being an issue under the new act; it would be a consumer issue, and so we should go to the ACCC.

So, having been given that indication, I decided to write to them and send them the same submission, saying, 'Is this an area where you can get involved?' Like you, they watched it very closely. I had a further discussion with them in February this year, when we reached a bit of a crisis point, and they said, 'We looked at it very closely: you are a lot of incorporated bodies, and we cannot act on your behalf because this is not a consumer issue.'

Again I suppose this is an extension of the so-called Chinese Wall: the consumer is our client and, if our client lodges a complaint within the superannuation regime, they go to the life company or to the fund manager. That complaint does not have to be recorded, because that complaint is going to the administrator of the fund; they are not going to the trustees. I only found this out in February, but it is not until they lodge a complaint to the trustee that there is any process of bringing the administrator to order. The trustee has to do that. When you look at annual reports, you find invariably that the trustees and the administrators are the same people. It is funny, I see these things all the time. So there is a real flawed issue there. We have clients whose funds have not been allocated. It is in the submission, as I say, and it is an absolute mess—they will not respond to me, the adviser, and they will not respond to the client, until the client goes to the trustee.

Senator CONROY—We have worked our way through Treasury, ACCC—

Mr Murphy—I have not been through Treasury.

Senator CONROY—What about APRA?

Mr Murphy—Yes.

Senator CONROY—What about ASIC?

Mr Murphy—No, I think to say that we are a class of people that the legislation forgot is fairly apt. There is no-one to deal with it, and where I have tried to rationally discuss things with my product providers all my dealings have ended up as personal issues, where they say, 'You had better not cause us trouble.' It is just disgraceful. I have come here in a fairly rational manner, and I think we have put some pretty good issues onto the table, but when we go to speak to them we just encounter straight-out bullying. I do not respond to that very well: I was brought up in the western suburbs in the fifties.

Mr Mitchell—In this area of professional indemnity, as we have said in our submission, there is a problem with the way it is supposed to work, and that is that the dealer is responsible for the advice. What happens, therefore, is that the dealer is contacted by the consumer, and if the consumer is going to sue he sues the dealer. The proof of whether the advice is good or not is not with the dealer. The dealer does not have the files; the adviser has the files. We have been told that, if the adviser gives those files, which are necessary to defend the action, to the dealer, the adviser's PI becomes null and void. So there is a real problem there. In this letter of mine, I have been told that I have to keep my PI up.

Mr Murphy—We have not been colluding on this, and I can prove it, but I am ahead again. A memo I wrote to my principals on 8 May 2002 says:

I have a query under the proposed new licensing arrangements relating to PI as I have just received my professional Indemnity renewal.

I would like a response from your legal department or somebody who can speak with some authority regarding the professional indemnity process.

I don't see any reason why I should carry Professional Indemnity Insurance when the Dealer is responsible as in event of a claim, this could only cause a dispute between my PI insurer and the Dealer PI insurer.

I would love the opportunity to discuss this matter with somebody but I will need to have something in writing before end of May when my current PI cover expires.

I anxiously await the outcome of your discussion.

No response. I think what Mr Mitchell says is right. If they are responsible for my behaviour, I do not need PI. I am an employee.

Mr Nowak—But if you do not have PI you cannot operate.

Mr Murphy—That is a good point, Dugald.

ACTING CHAIR—You sound like the voices crying in the wilderness.

Mr Murphy—You are right.

ACTING CHAIR—Who is going to make the pathway straight?

Senator CONROY—I am just trying to think: the unconscionable conduct provisions in the ACCC are the only thing that comes to my mind. You say you are not a consumer—

Mr Murphy—No.

Senator CONROY—so the consumer provisions of ASIC or even ACCC do not seem to be ones you can access. The unconscionable conduct provision is perhaps the only suggestion I can make to straighten the road.

Mr Murphy—The difficulty there—and I have been threatened—is that as soon I seek advice I will be told immediately, 'You are out of business.' That is the deal: I would get my agency cancelled. I have suffered this before because I stood up to them. I practised for six months while I did not have proper authority. That is not something I am proud of, but it is a fact of life—I have to feed my kids. It was for no reason other than I stood up to my licensed dealer. They did not want to answer the questions I put to them, so their only response was, 'We'll cancel your authority.'

Senator CONROY—Common law?

Mr Murphy—Again, it is the cost—

Senator CONROY—They are bigger than you and would wait you out.

Mr Murphy—It is the cost. Someone has to stand up somewhere within this regulatory system. I do not know whether the solution is political; I do not know what it is. We do not have any recourse at all.

Senator CONROY—Can the ACCC take class actions on your behalf?

Mr Murphy—I am doubtful because if they look into my business they will find it is held in a corporate entity.

Mr Mitchell—I have a view about that, too. I think legislation should be sound. I do not think he should have to go into a class action to get them to—

Senator CONROY—I understand. That is a fair point.

Mr Nowak—We were promised that under the legislation we would have a transition without loss or influence on our businesses.

Senator CONROY—At some point it will get to the pointy end of the discussion where they will pay you out—whether it is 2002 or 2004, there will be a point.

Mr MURPHY—Sadly, I do not want to get paid out. I love my clients; I have a great relationship with them. Yesterday, before I came here, before I said anything stupid, I had my submission read by my lawyer. I asked him, 'Is there anything here that I need to know?' He said, 'This is making us a lot of money. It is fantastic, but it is unworkable.' He said, 'Don't quote me. I'm a great believer in: if it ain't broke don't fix it. And that's been done, so that's a fait accompli. This is like buying probably the second best house in one of the best streets and

knocking it over and building it all over again.' He said, 'We act for a bank; I'm seeing it from the other end.'

ACTING CHAIR—I am interested in that. When he sees it from the other end—from the bank's point of view—what does he say? I am not asking about the actual agreements, but what does he say?

Mr Murphy—I think he was talking about the expense that is being incurred by his client in meeting the compliance standards and readjusting. I think the guys here from the credit union were dealing a little with that. They were dealing with this very limited commodity and having to fall into line with these educational standards. The lawyers are saying that it is a windfall. One barrister said to me last night, when he spoke to me about my submission because he was worried about what I was saying too, 'One door slams, 10 windows open—it's a great time.' I think we saw that from Freehills this morning. I could not hear but I think they were suggesting that it is quite a boon for them. Sadly, we have a piece of legislation here, I believe, that is going to cause a lot of pain and the consumer will end up paying for it. To solve my problem, there is no-one to whom we can turn to take issue with these people with whom we are dealing. That is as a result of the legislation.

Mr Nowak—And, in hindsight, we have got Stan Wallis and the Wallis report, which came out of ASC, and out of it they took no notice of the agents' and brokers' side, the ISC, and the ASC won the day on the situation of the model, and Stan Wallis ends up as chairman of AMP. Give me a break! If you were cynical, you would say it was a set-up.

Senator CONROY—That is vindictive.

Mr Nowak—I am under protection.

Senator CONROY—You have privilege, that is right.

Mr Nowak—If you look at it in hindsight, it is simple. We have to get through this. As president of the association and with 32 years as an adviser—next year will be my 38th year coming straight out of school into the insurance industry—let me say that we will get through this with your help and everyone else's, but we are not going to go away. There are too many small businesses out there that cannot provide a service now, especially in the country and regional areas where the banks are moving out, and these people out there are doing the right thing—but they will be halved. We went through that at the last meeting, didn't we? It is still the case. They will be taken out not because of competition; they will be taken out because the companies could take them out. That is my fear. Someone could be sitting out at Roma and someone says, 'Oh well, he's just not complying,' so he gets taken out without even operating out of there at the moment. And there is Dalby and now Charleville. The sad part is that competition will not take him out; it will be the banks.

Mr Mitchell—You do not know how hard it was talking with somebody in Armidale the day before yesterday, who is not compliant with 146, who was wondering what he could do about it. The fact is that he will be out of business on 30 June. One of the problems that has been created is the fact that most superannuation is now, as Michael said, under proper authority. It used not to be. Really there is no need for that to happen, but it is. Most of the new products are under

proper authority and securities. I think it is very important as far as rural Australia is concerned that these people are not lost. It is all very well to say that they are not producing much business or they are small producers or whatever, but I think the consumers need advice. It is getting more and more complicated. It seems to me that this whole thing has gone overboard in that the government is trying to protect the consumer but in effect the consumer is losing out because he will lose his adviser, and that is crazy.

Senator CONROY—I have only one final potential suggestion. Most of these major insurance companies that we are referring to very much value their good name, so standing up and shouting about how you are being extorted—to use a potentially unkind word but I have privilege as well—may be a way of drawing it to the attention of the broader community. You have begun the process today.

Mr Murphy—We are not sure what sells papers, so I do not know whether the story will be told. That is the problem. I have been given approval by the association to speak to the press, and I have consulted a client of mine who is a financial journalist who runs a company that does lots of business journalism, but it is very difficult to chart the course to make sure that the story is told correctly. Again, there is a lot of influence that can be brought to bear. I think it is fair to say that journalists write stories that sell papers.

Senator CONROY—In my experience a story that says that a small business is being extorted by a large insurance company is usually a winner.

Mr Murphy—Yes. How long do you want to be around, Senator?

Senator CONROY—Even Stan Wallis hates seeing his name in print.

Mr Murphy—Oh, he loves it.

Senator CONROY—I said Stan Wallis; not Allan Fels.

Mr Murphy—I think you are right. That is a bold step to have to take, and it is really not a step I personally would like to take, and have it on my shoulders.

Senator CONROY—I am clutching at straws for you here.

ACTING CHAIR—Are you saying the forces of darkness are just too great?

Mr Murphy—That is getting very philosophical—almost theological!

ACTING CHAIR—That is what it is. It seems to have reached that point. That is all that is left to us, I think—theology and philosophy.

Mr Murphy—Yes. It will take someone, I believe, with a far greater intellect than I to mount—

ACTING CHAIR—Probably no-one, in those circumstances.

Mr Murphy—Flattery will get you everywhere.

Senator CONROY—This Irish connection—Cooney; Murphy—has gone too far!

Mr Murphy—I am not intimidated by much, but that does make me think before I step off the edge. Sorry we have taken so long.

Senator CONROY—No, thanks. These are obviously issues which are very much of interest to the committee. One of the reasons we are holding this hearing is to see how the implementation and interpretation are going. We do have ASIC coming before us today.

Mr Murphy—ASIC have been fantastic in my communications with them, and I commended them in Adelaide. Some practitioners have been suspended and I think it is terrific to see that happening. Joe alluded to the fact that ASIC fought so that the provisions would allow us to do that. We were going along that way and suddenly there was a change—I do not what caused that change—that that was not going to work, and so it stopped going in that direction. There is clarity and that is another thing. On some of the issues, we really need clarification. The meeting Joe is suggesting needs to happen. I suppose it should be a summit or a forum. We need to get the people involved together and say, 'Are you aware of the implications of going down this track? There are tax consequences. There are legal consequences for the valuation of businesses.' It is only people like yourselves who can assist in getting those bodies together. The issue has to be dealt with.

Mr Nowak—We will let you know what happens. We intend to have that meeting. We are moving forward with that.

Senator CONROY—Thank you.

[2.13 p.m.]

DUNNIN, Mr Alex, Director of Research, Rainmaker Information Pty Ltd

ACTING CHAIR—Welcome. Would you like to make an opening statement?

Mr Dunnin—A very brief one, yes. Rainmaker became interested in the issue of looking at fees and charges several years ago. We are in the business of looking at the superannuation investment industry across the country. As you can imagine, it is fairly exciting and complex. Our interest in fees came along because we used to look at—we still do—performance across all the sectors. It is pretty hard to get that definitive information. When you start looking at performance, invariably you have to start looking at the way fees are calculated, disclosed and described. Lots of people in the industry get confused about fees, let alone poor old consumers. Even I get confused and I look at these things every day.

Fees are always the hardest thing to be coherent about. When I used to be the research director at APRA's forebear, the Insurance and Superannuation Commission, it was really confusing then. Even over the last few years since I left ISC to work with Rainmaker, when journalists and other inquirers would ask me about fees it was something we could never actually talk about in any way that made sense. That has changed a lot since we have changed the way we look at it. It also brings up a couple of other issues which I think have slipped between the cracks somewhere.

The thing that I am getting a bit excited about now is the question of fees versus costs. I might go to a fund and they may say, 'We've got really low fees.' In fact, when I used to work for the Insurance and Superannuation Commission I had a pretty feverish argument with a master trust provider. They were saying they had no fees at all. I said, 'That's fantastic. How can I join that fund?' They said, 'We have no fees because we take all our costs out of the contribution.' I thought, 'I should have joined that fund, plus I should have thought of that idea in the first place.' Then he got pretty excited, saying I did not have any constitutional right to ask these questions anyway and all that sort of stuff and we left it there. It really brings up the issue of the way you look at these things. Depending on your point of view, it can be quite different.

When you look at a lot of the regulation of disclosure regarding fees, it is all about fees; it is not about costs. We are getting into the issue of accounting standards. I might have a super fund which might have earned 15 per cent but might only give me 13 per cent because a two per cent cost has been taken out. Then it might say, 'Hang on, we've got some operation costs, I'll take out another one per cent,' and it will give me 12 per cent or whatever the calculations turn out to be. A lot of the fees in the industry and the costs in the industry are implicit. They are taken out in background. It is an issue for not-for-profit funds just as much as it is an issue for retail funds. It is an issue for retail funds in the sense that I might look at a fund that is unitised, their asset pool might be a billion dollars and they might take out $100 million in their costs—which means there is $900 million which they divide amongst the unit holders. And then they hit you for the fees. So what is this $100 million stuff? How is that broken out? There is a lot of disclosure about fees, but if you are trying to break that out it is pretty difficult. For me, just a

consumer living in Canberra and going shopping in Tuggeranong on the weekend or wherever it happens to be, I do not really care if it is a fee or a cost—I am still paying it.

It is a similar but different issue for an industry fund. As we know, an industry fund used to say, 'We charge a dollar a week.' A lot of industry funds now do not like doing that because it is not really true. You are paying a dollar a week plus an investment charge—a very low investment charge; nonetheless, you are paying it. In the interests of fairness, they are realising you have to compare apples with apples; you have to change the way you look at it. It is really all those sorts of issues which have brought to the fore the fact that we need some sort of framework to look at fees and charges.

To cut a long story short: the Financial Services Reform Act through the regulations is talking about the ongoing management charge and trying to come up with a universal metric, which is a really important thing to do. But because we are not actually looking at contribution charges—I leave aside the fees versus costs issue—we are missing a big part of the debate. If I am starting out as a young person, my account is growing because of all the money I am pumping in. It is not really growing because of my investment performance; that does not happen until I get momentum. So my contribution charges are where it is at. If we are not going to look at that, then we are missing the ball game. That is really the point that we are trying to make. That is why when Rainmaker looks at these things—we are asked about these things all the time, and I mean literally all the time—we are really happy to talk about these issues but we have to incorporate contribution charges, because if we do not the information we provide is meaningless. That is the essence of what we are trying to say.

ACTING CHAIR—I was about to call Senator Conroy, but I have got to acknowledge the person who gives him guidance and direction, Diane Brown. I am going to embarrass her by putting her on the record. I think I ought to acknowledge her in these circumstances because she is brilliant in this area. Do you want to say something, Senator Conroy?

Senator CONROY—I can only agree with you, Senator Cooney—I was hoping the facade of 'it was all my own work' would last a bit longer but you have blown it away! Mr Dunnin, thank you for your submission, because this goes to a very important part of the intent of the legislation. Whenever disclosure of fees and commissions and everything else is mentioned to most people in the financial markets, it is like a stake to a vampire. It is really pleasing to see someone with the knowledge that Rainmaker has coming forward and actually trying to make a positive contribution.

Mr Dunnin—We also found, on that theme, that when we used to start talking about fees—say, two years ago—we would have people who would say they really hated what we were doing, but no-one ever came along and said what we were doing was wrong. But as we are probably getting better at looking at this issue I think we are being a lot more intelligent about it—and all credit to the industry, to all sides of the industry, because we are starting to realise that charging fees or not charging fees is not so much the point but what you get for it. What we are doing now is a really big part of that, but the next point is saying, 'If I am going to charge someone 10 per cent versus my competitor who is charging one per cent, I have to make sure I am 10 times better.' That is the thing we have got to try and get to, but this is the first building block. It is good to play around with these issues, but I think that is why the industry used to

panic about this stuff before. It does not need to be a negative. The smart players are turning it into a positive.

Senator CONROY—If we can help create that price signal and driver, then we will have done something parliament rarely does, and that is get it right. But at the moment I agree with your general premise that what is being suggested is not good enough. I think you missed some of the earlier testimonies this morning which took us through some of the time pressures that Treasury and others were under to try and just put something out, so there is a combination of time pressures and inexperience. Were you involved, or have you had a chance to put a submission to Treasury-ASIC with your model?

Mr Dunnin—No. Because I used to work for the Insurance and Superannuation Commission I probably OD'd on regulatory issues, so I have taken a step back and I actually think it is probably a lot more important just to get on with it. I had a meeting with some people in Treasury about a month ago—I met them at a ASFA lunch in Canberra. I think a lot of the officials in Canberra are doing some really good stuff. What they are missing is to actually try and get a sense of what the industry really looks like, even though there are four or five really switched on super funds in Canberra—and because I live in Canberra I am totally unbiased, as you would appreciate. They really should be talking to those funds a bit more to understand some of these issues. When I talked about fees versus costs they sort of looked at me as if I was a bit crazy—and, okay, maybe I am. But there is also the feedback you get from even senior journalists. Alan Kohler, whom we talk to a lot, raised this issue with us in a pretty strong way when he was trying to work out, from some of the accounts that funds were presenting, where the administration charge was going. He could not figure it out. It is a really big issue.

But, no, I have not lodged submissions. We talk to people. I have found getting involved with a lot of the associations and this sort of regulatory process takes too long. We are just better off working out our models and going forward, dealing with the funds and they can use our information as they see fit.

Senator CONROY—In the legislation we were trying to capture the sense of 'total cost to consumer'. A phrase like that has got to have a legal meaning at the end of the day, and I was hoping it would be as comprehensive as your total expense ratio. Do you think the words 'total cost to consumer' would capture everything? As someone who has been a regulator, you know how things can get—

Mr Dunnin—I think it can go a long way towards it. Just as background, I understand that this total expense ratio concept is used in parts of the US market. We all have heard stories about lots of areas of the financial industry where Australia is charging really cheap, world competitive rates; there are other parts where we are unbelievably expensive. The feedback you have from fund managers in the US is that some parts of our retail market are very overpriced, and they would love to be able to charge those prices back home. But they say when they started doing these comparisons they used that total cost to the consumer, as you put it—that is actually a good term, I might pinch that—

Senator CONROY—Feel free.

Mr Dunnin—They started using the total expense ratio concept. I really favoured this concept because I personally do not like the term MER—management expense ratio. As I explained in the submission, for a lot of the new multioptioned retail products, when you talk about the MER you tend to talk about just the investment management cost but, because the investment management cost is separated from everything else, that might only be a quarter of the cost that you are paying. That is why we often say to lobbyists and journalists, 'When you are going to complain about fees, stop picking on the fund managers all the time, because in lots of ways you are picking on the wrong people. They are being squeezed by everyone as well, which is why they are all trying to buy master trusts and wrap services and planning groups and so on.'

Senator CONROY—Do you think your total expense ratio could just be lifted and used right now? Are you satisfied it covers everything you think should be included from a consumer's perspective?

Mr Dunnin—I think so, yes. The trick is really to recognise that there are three main types of fees. There are flat dollar fees, and there are actually about four or five ways to refer to those fees, which is a problem in itself but that can be easily addressed just by understanding what the chunks are. You have what we call the ongoing fees, and they are fees that are charged as a percentage of the account balance and, just looking at the range of prospectuses that we have been looking at frequently over the last couple of weeks, there are at least eight terms that refer to those sorts of costs in different ways. You then have up-front fees that are applied to the contribution—which nine times out of ten in superannuation is a function of your salary due to the SG levy—and there are about five or six ways of looking at that, leaving aside the three of four ways of talking about exit fees.

The main thing is to say that you have all the terms out there but they apply to either the contribution—they are a flat dollar fee—or an account balance, and that is the essence. When you start getting into IDPS and similar distribution platforms, you sometimes have more subtle issues such as if the cash investments have a lower ongoing management fee than non-cash investments and those sorts of subtleties, but we are really talking about people at the premium end of the retail investing market. I think that goes way beyond the scope of what the ongoing management charge is trying to do anyway—it is trying to be indicative.

The feedback we have had from some super funds, though, is that, because they are trying to talk about the ongoing management charge and are still trying to talk about all the other fee measures, some of their members and consumers are getting a little bit confused about some fees being included in the ongoing management charges and some not, and they are not quite sure which are and which are not. We are getting to the point where we are disclosing so many things that we do not want to get back to where we were, in the sense that there is so much information out there we still do not know what to do with it. So we need something that basically says, 'This is it, lock, stock and barrel.'

Senator CONROY—A lot of people in the industry that we have spoken with tell us how hard it is to calculate a dollar figure—that it is nigh on impossible, in fact—although I have not always understood how they do their own company or personal tax returns. They try to argue that it is just too hard to actually come up with a figure. Is that the case in your experience?

Mr Dunnin—It is probably very hard to come up with a precise, absolute figure that you could defend in the High Court—I would totally agree with that—but it would not be that hard to actually de-compose your own fee regime.

Senator CONROY—You wouldn't think so, given you have introduced it.

Mr Dunnin—If you cannot do that, then we have a problem here. It is really just a matter of going through and looking at the fee schedule they have described. Jumping back a bit, I used to be a high school teacher and I would get my year 8 students in Temora, near Wagga, to do calculations that were much more complicated than this. Calculating fees is controversial, but I do not think it is hard. There is so much detail, and the issue is which bits do you bunch and which bits do you separate. It is that sort of conceptual framework question which is hard, but once you have set up the right approach—and I think we are just about there anyway—I do not think it is really that difficult, especially if they can do monthly company accounts.

Senator CONROY—Given that the debate is fundamentally about money going from one pocket into another pocket, do you think it is a coincidence that there are so many different descriptions and it is so complex?

Mr Dunnin—Obviously the answer to that is that it is not coincidental at all. It also comes down to the fact that if I am trying to market anything—two football teams, two super funds or two cars—my job as the marketing manager is to differentiate me from my competitor. I do that through different terminology, different structures and subtly different features. That is not a negative; that is just a statement of reality. Again, we come down to the point that the terminology for all these different types of fees applies at three main levels. To borrow a quote from the Aussie Home Loans ads: it is not rocket science.

Senator CONROY—To follow on from your analogy, there is some rocket science involved in the way that, say, Wizard versus Aussie presents their fees. I think you regularly see Wizard saying that they are half a per cent cheaper than Aussie because Wizard outsource their legal fees and a couple of other fees. They then say, 'They are not really our fees; they are fees we are charged.'

Mr Dunnin—That smells like a fees versus cost question.

Senator CONROY—Yes, so you capture those things in your—

Mr Dunnin—Trying to de-compose the costs is something that is very difficult to do. The answer is no, we don't because we—

Senator CONROY—So can they get around this if they suddenly start outsourcing and then say, 'They are not our fees; they are fees we get charged and we are just passing them on to you'?

Mr Dunnin—That comes back to the issue of, if you have your gross asset pool, what costs are they taking off before they start saying to the members, 'This is your money that the fees apply to'? What is happening in this sector? It is one of those questions. I think it probably goes beyond what the FSR is trying to do, as far as I understand it. I think you are really getting into

how this information is described in the accounting standards for some superannuation funds. I know this is a bit of an issue for company directors and whatever, because the level of detail some very large super funds provide in some of their accounts is probably not as thorough as it is in much smaller companies.

Senator CONROY—I always admire the ingenuity of this sector in particular, which is why I probably favour the phrase 'total cost to consumer', because it does not matter whether the cost is charged by a third party or not, it has to be incorporated as part of that amount. So you could outsource the entire business and it would just be one person saying, 'This is what I can do for you,' and then you just put together a package of outsourced things. That is still going to be 'total cost to consumer'.

Mr Dunnin—If we get into the issue of charges and fees and things, we are talking about where it actually says, 'Look, Alex, this is going to cost you a dollar,' or, 'This is going to cost you 0.2 per cent.' We have to go beyond that because we are getting bogged down in the terminology.

Senator CONROY—Yes. But if we were to say, 'Look, we think your method is fantastic. Here, ASIC, this is your new OMC'—but call it something else—it still would not quite capture the total cost to consumer at the moment.

Mr Dunnin—At the moment, no. What we have presented in the submission is a broad generic calculation. You would probably have to add one or two extra levels to it. As I said earlier, every time we have a discussion about these extra levels, it still means that you include an extra expense ratio or something. The hardest thing that this comes into, though, is when you start having volume discounts. A good example is some of the corporate master trusts. We are reading lots of stories in the financial press at the moment about companies which are finding that running their super fund is getting too hard, so they are just ringing up a consultant to advise them on two or three master trusts that they should roll the fund into. They may say on their prospectus that the fee is one per cent, but if companies have $100 million to roll into this fund, because they are throwing so much money into the fund, they may pay only 0.5 of a per cent.

I do not think capturing that discount is that difficult to do, because you can look at a worst-case versus a best-case scenario for those sorts of things. The industry will often talk about the rack rates versus the real fee rates and then negotiate it on an individual basis. A lot of retail corporate master trusts can be very cost competitive because they can take advantage of the fee discounting, but you are still talking about the same model. Instead of throwing eight types of fees into the ongoing fee calculation, you might have nine or 10, but it is still being thrown in because it comes down to: is it being applied to the account balance, to the contribution or to the dollar amount?

ACTING CHAIR—Mr Dunnin, having listened to the various submissions during the day, you begin to wonder whether there is anybody who is in control of this area at all. For example, you say the fund managers are not the group that ought to be blamed, even though they are. Is that right? Is that what you are saying?

Mr Dunnin—Every time I take a question from the press about the fee issue, there is a general sense of, 'Oh, it's the fund managers; they're ripping us off.' That may or may not have been true a few years ago. It is a real opinionated question, but when you really analyse what is going on the fund managers are simply not drawing that fee revenue. A good example is that a corporate master trust might have 100 investment options and the investment management charge, which goes to the fund manager, is only 0.4 or 0.5 per cent. The consumer is still paying two or three per cent. The difference between 0.5 per cent and the two or three per cent is going to the master trust operator, the planners and everyone involved in the distribution.

ACTING CHAIR—So the whole thing gets diffused among a group of people?

Mr Dunnin—Yes.

ACTING CHAIR—Do you think that issue has been addressed? This is a very dynamic area: things are changing all the time with superannuation. As you say, fund managers' positions change and so do others. Where do you think it is at now? Where does the money go, other than to the person who ultimately hopes to get something at retirement? I am thinking very seriously about retirement now and I am very interested in this.

Mr Dunnin—In the financial industry we often talk about the question of manufacturing versus distribution, but that applies equally to every industry you can think of. It is a little bit like the telecommunications industry. There is a lot of commentary about whether Telstra is going to try to buy Channel 9 so it can start to control the content that is going down its bandwidth pipes. That is similar to funds management. Fund managers who are used to managing the money are finding that the people who are bringing the money to them, being the dealer groups or the master trusts, because they control the money that is feeding to the fund managers, can therefore screw down the fund manager fees. So the fund managers are saying, 'What are we going to do here? Perhaps we'd better start up our own master trusts or distribution outlets, buy out a dealer group or establish something.'

As these things go on, it is really important to understand that the value chain is changing. There is a much stronger recognition that the fund managers are managing the money and that the people bringing in the money are providing a very different set of skills and level of service. We are simply breaking up the industry so that we can recognise who is doing which specialisation. The way we are looking at it now and the way these products are developing has probably only become so widespread over the last few years.

Another example is that when we looked at the master trust industry in a lot of detail, about this time last year, the typical master trust had 30 investment options. When we look at that same thing now, the typical master trust has 60 options. When you say there are about 300 different master trusts and wrap services out there, it turns out to be more than 15,000 options. I am not saying that one person has to choose from 15,000, but if I want to get involved with AMP Balanced Fund I can go to AMP or I can go to probably 298 other people to get there as well. Depending on the way I access AMP, the gateway I use, I can almost choose my level of fee. Again, the fee structure has nothing to do with its goodness or badness. It comes down to a statement of reality: the more people between AMP and me, the more fees I must pay.

ACTING CHAIR—Thank you very much for coming and giving us your contribution.

[2.47 p.m.]

WOLTHUIZEN, Ms Catherine Nicole, Senior Policy Officer, Financial Services, Australian Consumers Association

ACTING CHAIR—Welcome. Would you like to make an opening statement?

Ms Wolthuizen—I will make some fairly brief introductory comments about the position that ACA wishes to put to the committee today. First of all, I thank the committee for the invitation to appear. ACA hoped there would be a process of ongoing review of the FSRA regime, and we are very happy to see it commence so swiftly after the implementation of the act. For those of you who do not know, the ACA is an independent, not-for-profit and non-party political organisation based in Sydney. It publishes *Choice* and Choice Online, and also advocates on behalf of consumers.

At the outset, I have to state that, owing to some time and resource constraints, I will only be focusing on the issue of disclosure of fees and charges in my submission to you today, but of course I am happy to take questions on notice and offer some comments on other areas relating to FSRA.

Looking at the ambit of this committee's inquiry, and particularly referring back to the aims of the legislation, it is the view of ACA that getting the issue of disclosure right from the outset is critical to meeting those aims, particularly that of promoting confident and informed decision making by consumers in relation to financial services. Certainly, the explanatory memorandum with regard to the FSRB stated that the aim of such new measures as the product disclosure statement would be to 'provide consumers with sufficient information to make informed decisions in relation to the acquisition of financial products, including the ability to compare a range of products'.

In the view of ACA, this means an advance on the current position and a lot of the confusion which many consumers report to our organisation when they negotiate the financial services market, but unfortunately it does not appear that this has been met with some of the measures that have been introduced post FSRA, in particular the ongoing management charge.

I will go through in detail some of the shortcomings that we perceive with that new measure. I am sure you would have heard this morning from the superannuation funds association about the literacy testing that they have conducted in the past, revealing some of the concerns with regard to how much consumers understand when they are presented with financial services information and product information, particularly when it comes to calculating fees and charges that are presented to them in a percentage format as opposed to dollar based disclosure. That certainly underlined the very strong position ACA has taken throughout this reform process in favour of dollar based disclosure wherever possible.

It is interesting to note—and this is a point made in the submission provided to the committee—that, even in areas of financial services where consumers have perhaps a daily dealing with a product such as a bank account, or even when making a mortgage application

where they understand the nature of the product quite well, they still report quite strong confusion over the different fees and charges and the different features of different products and have difficulty comparing products from different providers and across different classes. Indeed, we have recently seen moves in the mortgage area to introduce measures to streamline the presentation of charges in the form of interest rates in order to simplify that process.

That is for a product that is relatively well understood. When we come to the area of managed investments we are dealing with an entirely different class of investments, which are often much less well understood by consumers. Looking at the ongoing management charge, the OMC, and how it is being formulated and presented with respect to FSRA, we do perceive some quite concerning shortcomings. We hope to present a strong case for a different formulation based on a table, which I hope you have all received, that has been formulated by the ACA in consultation with industry.

The first concern we have about the OMC is that it is presented as a percentage based formula which, as I have said, can make it very difficult for consumers to calculate the real costs that they will incur with regard to the product. It excludes entry and exit fees. From our perspective, these are important not only given their potential impact on the rate of return and thereby the cost of the product that the consumer might be looking to purchase but also because of the very nature of those fees, given that entry fees can be rebated in certain circumstances and exit fees will apply at different points and at different levels across different forms of products. They may even form a basis for comparison when a consumer is looking at different products, and should certainly be included in any calculation of eventual cost. I will touch briefly as well on the means by which the OMC is calculated, as a percentage cost on average account size, which is also potentially misleading. I am happy to elaborate on that further but I am sure that point has already been raised.

ACA have developed a preferred model, which you all have in front of you with the accompanying campaign material from our web site. The key features of that model are that information is presented in a dollar amount and as a percentage and, as you will see, there is information presented just prior to a table that sets out forward projections of the impact of the fee on the expected return. The time period is shown in dollar amounts over five and 10 years and then there are three possible retirement ages, so a consumer can make some quite considerable forward projections about how much they are likely to pay. That introductory material has the commencing salary and the contributions and then has a table that separates the different charges and fees that are likely to apply. Hopefully, that would address some of the concerns raised with the previous witness with regard to capturing all the fees, charges and costs that would apply. We have administration fees, fund manager fees, trustee fees and other fees. If it were presented in the context of total cost to consumers, we would certainly anticipate that the 'other fees' category in particular would capture any remaining costs or charges that the consumer would incur.

We believe that it is important to separate the administration and investment expenses, especially where a consumer can assess investment management costs against returns as that is often presented as a justification for higher investment management fees. Again I am referring to that point of comparison. We believe that prescription is vital to ensuring the industry wide take-up of standardised formats such as this. Without that, you will not have the standardised

terms and the easy comparability that consumers tell us they need in order to negotiate financial services products.

We would also like to see fee calculators on fund web sites where possible, so that consumers can play around with the information that would be input on a table like this and explore different scenarios as regards costs and returns. As always, testing of comprehension and education programs would of course be critical to any implementation of whatever model of disclosure is eventually decided upon, to ensure that we know consumers understand it and to assist them in using it. I am happy to take questions on the model I have presented or on any other issue I have raised.

ACTING CHAIR—Thanks very much for that.

Senator CONROY—You heard the evidence from our last witness. Are there issues that he raised that could be incorporated in your model or do you think your model is broader than the one that Rainmaker were talking about?

Ms Wolthuizen—If you look at the first page of the model I have given you, the separation of all the different types of fees is a very useful addition to what was being described earlier. We have the table of different projections. I should also point out a no-fee column that would show consumers a ready point of comparison of what their anticipated returns would be if no fees or charges were being levied. Certainly, that initial breakdown into dollar figures and percentage of contributions of all the different charges that would apply would be a very useful addition.

Senator CONROY—I am not sure if you were here earlier when ASFA gave their evidence. They described the process with which they dealt with Treasury and the speed with which Treasury needed to get something out in the end. Are you familiar with the sorts of difficulties they encountered?

Ms Wolthuizen—I think ACA was probably quarantined from that process, due to a changeover between my predecessor and me. I can understand the need to get something out there but the unfortunate reality is that, given the shake-up that is taking place with the introduction of the act and the new regime, it is critical to get the reform right the first time around because otherwise it will be a process of constant revision and change. While that should not preclude review and change where absolutely necessary, every effort should be made to make sure we get it right. Already there are various attempts by different industry groups to come up with a meaningful model of disclosure. I gather ASIC is finalising a process of investigation as to what that might look like. Hopefully, we will see results from that in the immediate future as well. I think there is an appreciation to varying degrees of the need to get it right and to get some form of meaningful disclosure. From our perspective, that means it should be as comprehensive as possible.

Senator CONROY—Were you aware of real estate agents being exempted from FSR?

Ms Wolthuizen—Yes, I have heard of that and of the concerns raised around that. I am not sure whether ACA has made specific comments with regard to that.

Senator CONROY—Was it ASIC, or was it a Treasury regulation or legislation? What was the mechanism used?

Ms Wolthuizen—I would have to take that on notice and check that for you.

Senator CONROY—I was hoping you could tell me.

Ms Wolthuizen—No, I am afraid not.

Senator CONROY—I have not worked it out either. Our next witnesses might be able to help us. Would you have concerns about exempting real estate agents from financial disclosure to their clients?

Ms Wolthuizen—Given the mania at the moment for investment in property, it would perhaps be a concern. I am certainly happy to look into it further.

Senator CONROY—A couple of court cases in Queensland involve banks and types of agents—

Ms Wolthuizen—Two-tier investment schemes.

Senator CONROY—They are the words I was looking for, thank you. They do not seem to have a good record in this area, if that is any indication.

Ms Wolthuizen—No. While there is a property bubble, there is obvious incentive for unscrupulous practice.

Senator CONROY—I am not sure if you heard me refer to Senator Sherry's famous Burnie pub test.

Ms Wolthuizen—No.

Senator CONROY—You missed that? It is familiar to a lot of people in the room. Can you please take me through the second page of your table so that I can get an understanding. There are so many figures there, I am beginning to worry. Take me through how that table works and what that is telling me.

Ms Wolthuizen—You can see there are two scenarios of investment return, one set at six per cent and the other at eight per cent. Obviously we are about to enter a period of returns that are likely to be well below that. The table could be amended accordingly. The time frame, as you can see, is set out over five years and 10 years and then it takes a big jump to projected age at retirement of 55, 60 and 65. The salary is estimated to increase at a three per cent rate per annum. There are a number of assumptions underlining this sort of table. The third column you see across after 'Salary' is if no fees had been levied, with an expected return of six per cent per annum.

Senator CONROY—This is just on basic contributions?

Ms Wolthuizen—Contributions increasing by three per cent per annum, so contributions and salaries are assumed to increase at that rate. Then you have the whole fees that have been separated on the previous page applicable and showing the impact and the expected account balance as a consequence.

Senator CONROY—So the way I work out how much in fees that I have been charged from the previous column is to look at the difference between the no-fee position and the—

Ms Wolthuizen—'XXX Fund' fees.

Senator CONROY—So in the case of the first one that would be $600-odd.

Ms Wolthuizen—Yes.

Senator CONROY—In the second one, it is a couple of thousand dollars and so on. So I actually derive what it has cost me to be in this fund by subtracting those two numbers?

Ms Wolthuizen—Yes, that is correct.

Senator CONROY—At the first line, where it says 'Years 5', is that an annual figure? Is that $600 or is that $600 over the life of the five years?

Ms Wolthuizen—My understanding was that it would be over the life of the five years. I might have to check that for you. My understanding was that it would be over the life of the five years, but that would appear to be a very low fee being charge.

Senator CONROY—The balances are probably pretty low at the beginning so it is possible they are very small. Like you, I looked at that and I thought that was a bit low and wondered if that was just your annual fee.

Ms Wolthuizen—I will check that and get back to you.

Senator CONROY—I am hoping that by the time they get to age 65, if it is the annual fee in the first year, they are not getting 30,000-odd a year—in that last bit. I just wanted to make sure in my head whether it was an annual or cumulative figure over that period.

I appreciate your being able to get here, and I am aware of your resourcing constraints. Today's hearing is at short notice and I appreciate all the witnesses' efforts to get here at such short notice. In the many thousands of pages of corporate simplification that is known as FSRA, are there any other areas that you have had a chance to have a look at and that you have specific concerns about?

Ms Wolthuizen—They are not to the same degree as the concerns expressed with particular regard to this, because we see some action that can be taken quite readily to fix the problems that are arising here. I suppose the other areas that I would raise would be in relation to a reiteration of our position on, for example, the alternative dispute resolution measures, our preference for fewer rather than more alternative dispute resolution bodies being recognised by

ASIC so that we do not see a confusing proliferation of bodies over which consumers have to try to work out where they have to go and any sort of arbitrage between the different bodies. Beyond that, we are happy to see more resources go to ASIC so it can do its job, and I am sure we will not get too much argument from those in the room.

Senator CONROY—Hopefully we had a win on that—I am not sure. I have heard a rumour that most of the funds that went to them were tied, but I am hoping that, if that is the case, at least some of them were tied to FSRA implementation. We will find that out next. I am sure Mr Johnston is looking forward to giving us that answer.

ACTING CHAIR—Do you have any idea of what sorts of overheads the people that look after this industry have? I know they earn big fees, but I am just wondering what they could take out of those. Do you have any concept of what is involved in running a business that deals with investments?

Ms Wolthuizen—Do you mean a business of a large managed fund?

ACTING CHAIR—I am asking about at any level at all. I want to get an idea of how much money is going out of the contributions and to what extent that is justified. Have you any thoughts on that?

Ms Wolthuizen—I could probably give you a better answer if I go away, look more closely into it from our perspective, and get back to you. There are some legitimate costs and some costs we would regard as possibly not quite so legitimate, particularly with regard to some soft dollar commissions that we are starting to see emerge in the industry, that are causing us particular concern. I imagine those would not necessarily be disclosed by the particular funds or advisers in blatant form by choice, but it is certainly our view they should be.

ACTING CHAIR—It might be difficult—if that is so, do not worry—but perhaps you could get some idea of just what is involved. On your sample scenario, that is the salary. How much has been taken out of the salary each year to get to the fund?

Ms Wolthuizen—Sorry; how much has been taken out?

ACTING CHAIR—The salary is $39,600, the gross investment return—

Ms Wolthuizen—Presumably it would be the ordinary superannuation guarantee levy perhaps with additional contributions on top of that. That would be the assumption to my mind.

ACTING CHAIR—So if you took out of the $39,600, the normal superannuation contribution—

Ms Wolthuizen—Yes.

ACTING CHAIR—that is what you would get from the six per cent and the eight per cent?

Ms Wolthuizen—Yes.

ACTING CHAIR—Have you any impression as to the sorts of services you get from different sections of the industry? If you have been in here today, you will have heard people saying, 'What about the service that you get?' That is a factor in addition to the amount of money you would earn. Have you been able to factor that into the system?

Ms Wolthuizen—I suppose a lot of the impressions ACA receives are that the complaints from consumers are based on the service they receive. They tend not to ring us to congratulate various providers on the excellent service they have received. But certainly there is that sense of being very much at arm's length. I think there is a real manifestation of a trend of funds building relationships with advisers and planners rather than with the consumers. Consumers have reported that, if they tried to raise issues with the fund, they have been redirected back to their planner or adviser. They report that it is difficult sometimes to pursue matters and to get information out of funds. When it comes down to the financial planner, when consumers are grumbling or complaining about paying these ongoing fees and getting very little information or service in return, there is very little sense that they are being actively managed by their financial planner. As I said, we get the complaints. There is no doubt that there are the good practitioners out there but there is also this growing sense that the consumers are the ones who have put the money in—or the money is going in from their superannuation guarantee—and that everyone is getting their cut and eventually they will take out what is left at the end.

ACTING CHAIR—If you are the person who is paying this money in, you are finding it difficult at times to realise what is going on with the funds you have contributed.

Ms Wolthuizen—It depends also on the level of sophistication of the investor. There are investors who are in a position to, for example, negotiate away entry fees on managed funds with their financial planner and who can take an active interest and keep a close eye on what is happening with their investment. But for a lot of consumers the very reason they go and seek financial advice is that they do not have the time to take that kind of active role with their investments, and they are quite reliant on the advice that they receive. One of the most frequent requests we receive in the area of financial services is: how do I choose a good financial planner? It is a difficult question to answer and is certainly one where we give out advice to consumers to seek that assistance. We are now engaged in a survey with ASIC to test the quality of advice that is out there because we do not have a great deal of confidence.

ACTING CHAIR—But the impression is that there is a significant concern about the advice—not necessarily about the quality of the advice but the way that it is given, in the sense that people brush off an inquirer?

Ms Wolthuizen—Yes, certainly the sense that they are being brushed off, either by the fund or, in some cases, by their adviser as well. For example, I received a complaint quite recently—and the individual is quite happy for me to forward the complaint to you as an example—where a man had sought to have a look at how his investments were going. The correspondence he had received from the fund had a particular name for his fund, yet when he actually looked through the fund's documentation he could find no evidence of any investment of that name. He is having great difficulty in reconciling the different information and getting any clarification from the fund. He obviously feels very frustrated that he cannot even find out how his money is going because the information he is receiving is just so inadequate.

ACTING CHAIR—Thank you very much and thank you for coming at such short notice. We will see you again, no doubt.

[3.12 p.m.]

ADAMS, Mr Mark, Director, Regulatory Policy, Australian Securities and Investments Commission

HUGHES, Mr Sean, Director, FSR Regulatory Operations, Australian Securities and Investments Commission

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

RODGERS, Mr Malcolm, Executive Director, Policy and Markets Regulation, Australian Securities and Investments Commission

VAMOS, Ms Pauline, Director, FSR Licensing and Business Operations, Australian Securities and Investments Commission

ACTING CHAIR—Mr Johnston, you are going to tell us the answers to all the problems that have been raised today!

Mr Johnston—We will certainly do our best.

Senator CONROY—Hasn't Mr Larcos given you a briefing yet?

Mr Johnston—Not yet.

CHAIRMAN—Senator Cooney, I am back online now.

Senator COONEY—Mr Johnston was about to tell us the answers to all our problems!

CHAIRMAN—I look forward to that.

Mr Johnston—I would just like to make a brief opening statement. As the committee is aware, FSRA is the most wide-ranging piece of financial services reform the country has seen for some time, and the implementation of the act is certainly the largest and most complex logistical task undertaken by ASIC. We are charged with the responsibility of providing general policy guidance to industry, consulting with industry and consumers on that guidance, implementing a new licensing regime and supervising compliance with the conduct, disclosure and consumer protection provisions of the law. We have undertaken this task at a time when the demands placed on the agency's resources, in terms of the number of other matters referred to us and their complexity, have never been higher. We are pleased to have received substantially increased funding from government to meet our obligations under the Financial Services Reform Act and, indeed, for the wider sphere of ASIC activity.

We have set out in our submission to the committee the process that we followed in setting our policy position on various matters, determined on a prioritised basis by consultation with industry and consumer groups. I do not propose to cover that ground again in this statement. There are, however, some additional points that I would like to make today. First in relation to the transition period, parliament wisely set a two-year period for market participants to come to grips with and embrace the most material provisions of the act. This allows issues to emerge during this period, allows regulatory experience to be gained and responses to be developed where necessary.

ASIC made it clear in its policy development process that early guidance would be given—day one guidance, if you like—on the most important issues faced by industry. We also stated and reiterated in our policy documents that we would use the transition period and our experience of it to develop further guidance. It would not be reasonable to expect ASIC to be able to provide guidance or answers on every issue prior to or on the day that the legislation took effect. In this regard we are currently working on several matters which will be the subject of further guidance. For example, we are developing a position on the application of the anti-hawking provisions. This issue has been raised by several industry groups as being urgent and will be the subject of a release soon. We are also preparing guidance on the application of FSRA to accountants and considering the need to issue further guidance on financial product advice.

There are other issues that will be dealt with in the medium term and no doubt there are further issues yet to be discovered but which will emerge during the transition period. I want to point out, however, that it is not ASIC's task to rewrite the legislation nor to change the intent of the act. We do detect from time to time pressure from some quarters for ASIC to come to a position on a matter which, while it might suit certain market participants, departs from the provisions of the act. We will resist that pressure. The proper course in such cases is for aggrieved parties to seek law reform or in appropriate circumstances to lodge with ASIC an application for relief from the law, which would be determined by us on well established principles.

I turn to what guidance ASIC can give. We do not view our role to be that of a legal adviser to individual participants. While we do provide overall guidance on policy, it is not the role of the regulator to give detailed legal advice. We are neither mandated nor resourced to do so. Further, it would place individual staff at ASIC in an unacceptable position. We are receiving a large number of specific questions for advice as to the applicability of the law to individual entities and as to how some should structure their businesses. Apart from the fact that it cannot be the role of the regulator to perform this task, one can imagine the thousands upon thousands of requests that we would receive if we were to engage in specific advice.

We do, however, try to help. We have been in frequent dialogue with industry associations and we meet regularly with them. This allows us to gain insight into emerging issues and also to pass messages to such bodies for dissemination to their members. We have also established a comprehensive question and answer section on our web site which is updated as important issues emerge. However, even taking into account the considerable policy statements which we have issued, our meetings with industry, seminar speeches, web site information et cetera, there will still be some who believe that our efforts to assist them fall short. ASIC is adopting a facilitative approach to FSRA implementation and we will continue to do so. The staff at the table are happy to answer any questions you may have.

Senator CONROY—I will start with that resourcing question. I saw in the budget, thankfully, finally, what looked like a reasonable increase in your funds. Are you able to indicate whether any of that is specifically tied to any particular program, and in particular was there any specifically allocated for your FSRA implementation?

Mr Johnston—The application for funding we made was as part of the output pricing review process and in our funding bid we identified what resources we thought we needed to implement FSRA. That went to policy formation, to employing staff to carry out the licensing task, the resources we thought we would need to carry out surveillance in the marketplace, the resources that we would need to consider applications for relief from the law from market participants and indeed what resources we might need in terms of enforcing the law. We wrapped all of that into a bid. We added to that a shortfall that we thought we had in terms of enforcement resources generally, going wider than FSRA. The money that we received was largely in line with the bid that we had made. Off the top of my head, I cannot remember what percentage went specifically to FSRA, but I think in the first year it was around $13 million.

Senator CONROY—Was that $13 million or $30 million?

Mr Johnston—Thirteen. That will allow us to employ in excess of 100 additional staff to help to implement this piece of legislation across those areas that I have just mentioned. That was in the first year. Certainly, I could provide better information at Senate estimates.

Senator CONROY—I am sure I will be asking similar types of questions. So you say up to 100 new staff, at least in the first year. How long will that last?

Mr Johnston—The peak in staff will come during the transition period. We will not need as many staff in four years time, say, as we might need in the next two years as we bring the number of licensees in during the transition period. So if we were to issue around, say, 10,000 licences—either new or reissued—we would need a large number of additional staff to do that. Once we get through the transitional period, that demand will drop off to some extent.

Senator CONROY—I am sure that will be a relief to a lot of people who know that you are understaffed.

Mr Johnston—Yes, we have been encouraged by messages of support from various quarters.

Senator CONROY—So that I can get this in my head: what force do your policy statements have? I understand a law; I understand a regulation, which is a disallowable instrument of the parliament. What is the status of a policy statement? Does it have to go through the parliament?

Mr Johnston—No, a policy statement is guidance that ASIC issues. It gives an indication to the marketplace as to how ASIC will interpret the law and how we will apply the law—but it does not have the force of law.

Senator CONROY—So, in a real sense, someone could completely ignore it and just do whatever they wanted? You could say, 'No, we think you should do it this way,' and they could say, 'Well, I don't care!'

Mr Johnston—We put them to the test.

Senator CONROY—You put them to the test of a court.

Mr Johnston—We have our director of policy here, who might say a little bit more on this.

Mr Adams—No, I would agree with that. I think of it in two ways. The policies quite often give an indication of how we might exercise our discretions in relation to specific discretionary powers we have. Another element of them is, as Ian indicated, the guidance element—the interpretative consistency that they provide.

Senator CONROY—Mr Johnston, I think you mentioned exemptions from the law. You said they were well established. If it can be done quickly, can you tell me the circumstances in which that is able to take place?

Mr Johnston—We have actually issued guidance on the circumstances in which we would grant relief from the law. That is where a market participant comes to us and says, 'The law in fact does not work in my circumstances. It would be overburdensome for me to have to comply with this provision of the law.' We are entitled in such cases to grant relief in relation to specific applicants, depending on the circumstances of that application.

Mr Rodgers—I might just add that there are two other limbs to that. There is the impact on the person who is seeking some kind of relief, but I think there are two other things that we would have in mind—and this is an approach embodied in a couple of the policy statements that we have provided to the committee. We would want to be confident that the customers or consumers who buy products or use services provided by people we give relief to are not disadvantaged by the grant of relief and still effectively have the protection that the law intended them to have. We would ask ourselves whether, in all the circumstances, it was actually necessary.

So it is really that three-stage test of saying, 'Does this look like something that is really unduly burdensome? Is it impossible for someone to comply?' You do occasionally find examples of that. Is it really unduly burdensome because it is so far on the fringe of what the legislation looked like it intended to capture that it is really very difficult? An overriding factor is whether our giving relief would do any damage to the protective regime which the law is there to provide.

Senator CONROY—Have you granted any exemptions to FSR yet?

Mr Adams—We have one form of relief dealing with one of the issues raised on secondary sales. We have an interim form of relief to accommodate some of the concerns that were raised in terms of the practicality of the application of those provisions.

Senator CONROY—Secondary sales of?

Mr Adams—Securities.

Senator CONROY—Does this involve the witness at the beginning of the day—secondary markets?

Mr Rodgers—I think you heard from Professor Harding, who may well have mentioned section 707, which is the provision that we are talking about.

Senator CONROY—So the SFE have been granted—

Mr Rodgers—No. We are at cross purposes here, Senator.

Senator CONROY—Could you take me through the details?

Mr Rodgers—The example that we are talking about is this: with the commencement of FSR, there was a change to that part of the law that really is designed to make sure that it is not easy to avoid the prospectus provisions. It is that part of the law that says if I am a wholesale participant, an offer of securities to me does not require a prospectus. It should be open to me to then on-sell them to the retail market, because the effect of that would be that the purchasers at a retail level would not have the benefit of a prospectus.

The law was changed in the FSR legislation in a couple of important respects, to deal with what we and the government had identified as a loophole in the pre-existing legislation. There are some problems, we think, and certainly industry has put very strong propositions to us that there are some problems with the operation of the amended provisions. We have granted some very narrow interim relief, at the same time saying we will look at this issue in a more detailed way. The answer may not be for ASIC to do anything else, because it may be a law reform issue. We may need to go back to the parliament and say, 'Industry thinks this doesn't work the way that it ought to work and we agree with that,' or 'We disagree with that,' or 'We are neutral about it.' But we have said we would not want the effect of the new provision in exactly that form to bring the placements market to a complete halt, which is at least what some industry participants were saying. We thought we could provide some form of interim relief without doing any damage to the antiavoidance mechanism built in to the law. In the meantime we would act as a sort of catalyst in producing a sensible debate that will go forward for action by us or it will go to the government.

Senator CONROY—What mechanisms do you have to publish or advise that you have granted a waiver or relief? What is the formal process? You have made the decision that there should be relief; what do you do to let people in the broader community know?

Mr Rodgers—Normally, with relief that we do as a result of a policy, we will issue a final policy that says, 'We have granted relief,' and then we will name an instrument number. That instrument number is itself part of the public record. The instrument has to appear in the gazette; a copy of it is accessible from our web site.

Senator CONROY—If you click onto your web site, you might surf around and find the list of waivers.

Mr Rodgers—I should clarify one aspect: the process that I am talking about is where we have given general relief by way of a class order; in other words, it applies to a broad popula-

tion. Where we give individual relief, in individual instances, that process is not subject to those full public announcements, although it is not a secret. There are a very large number of those given routinely by ASIC under our policy every day—for takeovers, for prospectus provisions and so on. So there is not, as it were, the same demand to understand, and all of those are given within the framework of an existing policy.

We do publish in that area what we call pro formas—which is to say that we have a policy and, if you bring yourself within that policy, although it is not a class order, we will grant you relief, and the pro forma tells you exactly what that relief will be and the conditions that will attach to it. That pro forma itself is a public document.

Mr Adams—Might I just add one thing, if that is all right? Just on the kinds of relief that Mr Rodgers indicated earlier, I have referred to the secondary sales relief which related to a new issue coming out of the act. Policies 167 and 169 indicate the status of all the existing relief we had in place before the new legislation, and much of that has been carried over into the new post-FSR regime where there are basically the same issues. There are quite a lot of class orders of that nature.

Senator CONROY—I hope we would have solved them for you in the new, all-encompassing bill.

Mr Adams—Some of them have been.

Senator CONROY—You would be familiar with the Taxation Office's binding rulings situations, where they have private binding rulings. Exemption from the law is a fairly serious thing to be put in charge of. The tax office got themselves into quite a mess over the question of private binding rulings—which led to a full inquiry. They have had to put in place some processes but now, most fundamentally, they have to put them up on the Web as public; there is no longer such a thing as a private binding ruling.

I raise this because this is such an all-encompassing bill that covers everything and I think you are going to be getting many thousands of people knocking on your door with many thousands of requests: some fair, some unfair. You will knock some back and you will keep some. I suspect you are going to be, like the tax office, drawn into a situation where people are going to be aware that you have given one ruling for one situation, but another ruling where there are similar circumstances. Have you given any thought to the public policy process of how you are going to cope with that? More importantly, have you thought about them being, as you say, not a secret? By putting them on the Web, if people want an exemption from the law, everybody has to know who and what it is for.

Mr Rodgers—Yes, we have. Indeed, we have a long history of using our exemption powers and our modification powers in a very transparent way. That is one of the main purposes of the policies that we issue: if you come to us asking for this kind of exemption or a modification of the law, these are the things that we will have in mind when we are thinking about that application; these are the circumstances where we have decided that we will be prepared to grant some kind of exemptive relief; these are the conditions that we will apply to that; and so on. So it is public in the sense that the work we have done over the past 10 years, on articulating policy and making sure that the policy communicates, is designed to give people some real

confidence, not only when they themselves are the applicant but also when other people are in the same position or when there are other stakeholders in our work: to give them a clear idea of how we think about these things and of where we will use those powers and where we will not.

Mr Johnston—The other thing that we do in our liaison with industry is to make sure that we pass through to industry the examples of which Mr Rodgers is talking, so that people well understand what ASIC's position would be on those issues.

Senator CONROY—I appreciate that and I do not think anyone has raised any issues at any stage. I have no hidden agenda here that there is an issue I am going to ambush you with. I am just concerned that this bill, for the first time, hands enormous powers to you. The bill really is a skeleton. It delegates enormous powers to ASIC. If I had any qualms about the bill at all, they would be about the amount of legislative power that was being passed over either to a Treasury reg—which still at least has a parliamentary aspect to it—or, more importantly, to you guys and ladies.

My concern is that, from this point forth—from 11 February forward—you are faced with a different world. You have enormous power, and if you do not have a process in place that is probably an advance on where you have been. You are eventually going to be dragged into the same sort of debacle the tax office got themselves into. You may already have a central register. You cannot go to your offices in Canberra, Sydney or Newcastle as happened for tax, where favourable rulings could be got from the Newcastle office that could not be got from the Melbourne office—there is all sorts of evidence about that. I am not putting anything, other than different interpretations. You may already have that central process.

Mr Johnston—There are a couple of comments that I would like to make. One is that we do have a very formalised and central process for granting relief. There is a body within ASIC which is known as the Regulatory Policy Group, and any novel applications for relief must go before that body so there is a commonality about the decisions that are made. I take your point about the powers that we have under FSRA, but we have had significant powers under the Corporations Law, generally, and we are used to exercising these types of powers. For that reason, several years ago we instituted this central body whereby it determines these things on a consistent basis. I am comfortable with our processes, but I do take the point that we have significant discretions available to us.

Senator CONROY—The reason I am raising these issues is that I am probably coming to the view that you may need to do what the tax office does now, and it is a personal opinion. You may need to basically start publishing your exemptions on the web—what they are and who they are for. You are covering a much broader range of people now than you may have previously. My friends down the back from the financial association, whom you may not have had to cover before—you probably have, but not in the same way you cover them now—are entitled to the same information as the big end of town who have smart lawyers who knock on your door every day, who probably work on ten cases with you. So you not going to get dragged into this—this is an issue of resourcing—by the people who come to see you. The big end of town know what they can get away with and know what is acceptable to you, but the small independents and individuals are caught in a position where they really are lost. They are not able to access the information, albeit they can look at your web site and your general themes, but not in terms of what an exemption was for. You heard me mention real estate agents

before—I want to see something in writing as to why they were exempted. I do not believe that was part of any discussion on the floor of parliament or that there were any discussions, before the bill was passed, about real estate agents being exempted. I am trying to work out what happened. Maybe it was not you guys that did it, maybe it was a Treasury reg that I have not disallowed yet! Or it was some amendment that snuck through while I was dosing on the floor of the Senate.

Mr Johnston—I think I can comfortably say that there would have been no indication that we would have given that anybody should have been exempted from this.

Senator CONROY—You concur that the real estate agents appear to have been exempted?

Mr Johnston—Yes, I do. I think there is an issue here—I believe it is a constitutional law issue, and it is not something that I or the people at this table can opine on. We were given the people who we regulate—the hook, I think, was people who give financial product advice. Real estate is not a financial product, according to the act. My understanding is that property law generally, and real estate—

Senator CONROY—It is a state issue, I understand that.

Mr Johnston—I think there is a constitutional issue. If they were brought into the ambit of this, we would happily regulate them.

Senator CONROY—They certainly thought they were. They were organising seminars, they were marching in the streets, so to speak. They really thought they were going to be caught by FSR, so I am trying to understand why, suddenly, all those very smart people were just so badly misguided.

Mr Johnston—I do think it is a question for Treasury.

Senator CONROY—I am happy to harass them; I look forward to that discussion. Coming back to the substantive issue of variations to the law and how you implement that, this is something you could take on notice—it is something for you to take away and think about; it is probably something I am going to niggle you about for at least another 2½ years: what process is there and can it become more transparent? I appreciate that it is transparent in a sense, but it is not what I would call fully transparent.

Mr Johnston—I am happy to take that on board and give that more thought. One of the things we would need to investigate are the administrative law implications for people who ask for very specific relief applicable to their circumstances. As Mr Rodgers said, the class order relief that we give, the wider relief, is set out there for all to see.

Senator CONROY—Class orders I do not have a problem with.

Mr Johnston—We will take on notice the other matter and come back to you.

Senator CONROY—Thanks. As I said, Treasury are coming to a later hearing, so some of these questions you may happily want to handpass and say, 'They are Treasury, Senator.' But are you able to give us any information about the way in which fees and charges are to be disclosed in the various disclosure statements and in relation to various products as required by FSR and the relevant regulations? Have you been involved in those discussions?

Mr Johnston—We had input I guess in the same way that other market participants had to the legislation. Our starting point as the regulator is that we believe that there should be full disclosure of fees, charges, commissions. We certainly did not draft any of the provisions that are there. I cannot recall what our comments were on specific provisions at the draft bill stage. I am not sure if Mr Adams has a better recollection.

Mr Adams—Our comments related to clarity in making the intent of what they were putting together work. Forgive me if I am going over things that are quite familiar to you, but my understanding is that there are three key documents. One is the financial services guide, which is provided to retail clients where they, for the first time, may take up financial services. That guide includes broad information, including about remuneration arrangements and any conflicts of association that there may be in place. If that individual obtains personal advice from an adviser—being one class of financial service provider—they are to receive a statement of advice, and that is the second document. That statement of advice is to contain more specific information relating to that piece of advice, including more specific details about remuneration, fees and charges and any conflicts in relation to that advice.

The third document is the product document, called the product disclosure statement. If the advice is recommending a particular product there is an obligation on that adviser to make sure that that individual has a product disclosure statement. Likewise, product issuers can make available their product disclosure statement. That includes information more particular to the product and the costs and fees associated with the product itself. And unless the fees and charges associated with the adviser affect the return in relation to the product, the product disclosure statement will not reveal that; it is not obliged to do that. That is on the assumption that the financial services guide and the statement of advice perform that role.

Senator CONROY—Mr Johnston, you and I briefly discussed this when, if you remember, you caught me by surprise the last time we met, when I was discussing disclosure of fees and charges in a generic context and you indicated to me that, no, it was in fact only required for super.

Mr Johnston—In terms of prescription.

Senator CONROY—Can you clear up for me what caused you to delineate that?

Mr Johnston—We did not delineate that; that is in the act and/or the regulations. That was not an ASIC decision.

Senator CONROY—Can you point me to the section of the act? I genuinely do not remember delineating super out of managed investments. I am happy for you to point me to the reg, and I do not mind if it was a reg, but I just do not remember the legislation saying that. I could be wrong.

Mr Johnston—I could not tell you the section number.

Mr Adams—I might be able to give some information. The provisions which deal with the content requirements of the product disclosure statement are quite general, applying to all financial products, and there is an item heading there and one of the list items is about costs associated with the acquisition of that financial product. That does not differentiate. The regulations differentiate. They differentiate in the level of detail which is required to comply with that headline provision in the act.

Senator CONROY—So it is a reg?

Mr Adams—Exactly.

Senator CONROY—It is Treasury. You are safe.

Mr Rodgers—For superannuation, on this question the regulations themselves carry forward a lot of the old superannuation industry supervision legislation.

Senator CONROY—I just thought we were trying to get one rule for the whole financial services sector and I was surprised to suddenly find that certain sectors were exempted. But, if it is a reg and you are just applying it—

Mr Adams—The regulation does not quite exempt the other products. There is still an obligation on fees, but the regulations are more prescriptive in the context of superannuation.

Senator CONROY—I appreciate how they have split the hair—how they have, not how you have. That will be a matter for me to take up with Treasury. But I presume they just gave out the reg and said, 'Here, go and implement that'?

Mr Adams—Yes.

Senator CONROY—In policy statement 168, *Disclosure: product disclosure statements (and other disclosure obligations)*, you refer to good disclosure principles: could you just expand on those five principles. Could I get a brief outline from your perspective of principle No. 2, that disclosure should be relevant and complete. Would there be a blank if you had no information to comply with relevant and complete?

Mr Adams—These principles have been developed to assist product issuers in the production of their documents in compliance with the act, so the act and its obligations are the overriding things. Against that backdrop, we picked these principles—about disclosure being timely, relevant and complete, promoting product understanding and comparison, highlighting important information and having regard to the needs of the consumers—really to emphasise that we encourage issuers to think about these items and to develop good practices to fulfil the outcomes that these purport to indicate. When I provide presentations at our ASIC Speaks seminars, I normally boil these down to say, 'Think of the consumer and their needs when devising your document.'

Senator CONROY—And what do you do when they finish laughing?

Mr Rodgers—I will add a little bit to that though, because this was an area where during the policy making process we got two very strong but diametrically opposed sets of arguments about what we should say in our policy and how we should approach the administration of these disclosure provisions. One argument was that the law sets out what is required to be done and that can be done and will be complied with by industry without any further assistance from ASIC. Another set of arguments, which came not only from consumer stakeholders but also from some parts of the industry, said that ASIC could be helpful here in articulating what it expects to see in good disclosure documents and indeed in some cases explaining what ought to be done to comply with the law.

In what we set out in that policy, we tried to steer a reasonable middle ground while also making it clear that we do think the intent of the legislation and what it should be seen as trying to do is to produce quality consumer directed disclosures in a form that is useful to people who are going to make their decisions on the basis of those disclosures. Although this is a policy and does not have the force of law, we still want people to be very clear that ASIC does think that there is room for improvement in the disclosures that consumers get and that ASIC has taken and will go on taking an active interest in this area.

Mr Johnston—We foreshadowed that we might say more about it when we saw how the market behaved.

Senator CONROY—But for those in the former category—the on your bike category—basically, if they follow through with that approach, there is nothing you can do about it?

Mr Johnston—We have indicated in that policy what we think are good disclosure principles that give effect to the intent of the legislation, so if we came to the view that the intent of the legislation was being frustrated in some way then we would take them on, frankly. We have also—and this might be where Mr Rodgers is going next—instituted a project of looking at how industry might frame its response to its obligations and how it might behave. There is a piece of work that we have started under the guidance of Professor Ian Ramsay to have a look at some of the options for better disclosure.

Senator CONROY—How far away from the release of Professor Ramsay's report? He is a busy man.

Mr Rodgers—We are to receive shortly, I understand, a final version of the work that has been done jointly by Professor Ramsay and ASIC staff. I think I am due to receive that in the next couple of weeks.

Senator CONROY—Do you think it will be public before estimates, so I can ask you about it at estimates?

Mr Rodgers—I am not sure that it will be public before estimates, because I do not yet have the document in my hand. There has been a bit of a delay in it coming to me. I am expecting to get it in the next week or so.

Senator CONROY—I am looking to save time—for myself but also for yourselves—in terms of dragging you to another afternoon like this. We can try to find a way to cover it at estimates or if you come—and I think you are coming—to visit this committee again as part of your annual report.

Mr Rodgers—Yes, we are—shortly afterwards.

Senator CONROY—I am hoping to not drag you out to another meeting if it is publicly available. Do you envisage releasing it immediately or studying it?

Mr Rodgers—I would not want to commit to that before seeing it, but I hear also your implied invitation that we might need to talk to you about it separately unless we take an early opportunity—and I will certainly bear that in mind.

Senator CONROY—I am really just trying to save time for all of us.

Mr Johnston—It is certainly not our intent that that report would be something that we would keep.

Senator CONROY—No, I am sure you do not want to come and meet me any more times than I want to keep catching up with you guys.

Mr Rodgers—I will make one final point on the point that you raised. It would be wrong, I think, to see us without remedies for poor disclosure. The law provides us with tools. For example, the law says the disclosure must be clear, concise and effective. If we came across disclosure that did not meet that description, we could act against it as non-complying disclosure. Similarly, the policy statement that you are referring to has a list of things that we think might stimulate some kind of enforcement or enforcement like action on our part—so it is not just about exhortation here. The law gives us tools to deal with defective disclosure.

Senator CONROY—My problem—so that you are conscious of it—is that the parliamentary clock is ticking for me. You are implementing regulations and my capacity to influence those regulations runs out soon, and if I do not have it before 15 parliamentary sitting days from the tabling of some regulations so I know how you intend to apply it, I will be in a difficult position to make a judgment. I am not for a moment suggesting that you have any intent there, I am simply saying that my problem is that I have a deadline in terms of parliamentary timetable.

While I can say the case is building to disallow the regulations, I would like to know how you guys are going to be implementing it, particularly—as I said earlier, and I do not think you were here then—as IFSA and representatives of IFSA have very strongly articulated their opposition to these disclosures and do not believe that they are of any value whatsoever. In fact, the speech that I was present at was quite strident. I think, Mr Johnston, you were at Parliament House as well that day. Frankly I was amazed that there was such a position being articulated, and it did not give me a lot of confidence that you were going to have much success in convincing those with those strident views to comply with at least the intent and if not the letter. My only capacity to influence the regulation runs out soon.

Mr Johnston—I understand that. I would reiterate Mr Rodgers's comments that, regardless of what people may think of the guidance that we have given, if we see examples of disclosure that we do not think comply with the law then we would act against them, as we do at the moment.

Senator CONROY—That gives me no confidence. I was about to offer you an opportunity to reassure me and you shattered my hopes. On that interpretation, current disclosure is fine as far as you are concerned because you do not have every single company in court right now.

Mr Rodgers—Yes.

Senator CONROY—Clearly, the parliament thinks that the level of disclosure at the moment is unsatisfactory, hence we are going down this path. My concern is: if you currently have the same power as you are going to end up with at the end of the process, there is therefore going to be no change in behaviour.

Mr Johnston—No. I am saying that at the moment we have certain powers to act in respect of disclosure, as the law stands, and we exercise those powers in a large number of cases. We are moving into a disclosure regime which will apply to financial services licensees as they become licensed or as they opt in, and that operates to a slightly different standard.

Senator CONROY—So you think there is a slight change?

Mr Johnston—We think that one of the purposes of this piece of legislation is to improve disclosure to consumers—and in respect of a wider number of products it certainly does that—and also to promote comparability between products. That is one of the things that we look at in terms of good disclosure principles.

Senator CONROY—We had evidence earlier today from Rainmaker Information. They highlighted, as did the Consumers Association, the six different ways that companies describe their fees, charges, management costs and those sorts of things. Mr Murphy described it as: 'If you do it right, it is a licence to print money.' That is the exact quote you used, Mr Murphy. There is a lot of money involved. It appears that it is the most confusing area in terms of the various descriptions such as 'no fees'.

If I see one more eChoice television ad saying that they are going to give you a free mortgage, I am going to go spare. That has got to be a breach of either the ACCC's false and misleading provisions or your new powers under FSR about disclosure of commission. The mortgage brokers do not offer a free service and they should stop advertising they offer a free service. Can you help me? I know I have asked this question of you before, but eChoice is the one that I think is most notably in the advertising on telly. I am sorry to divert. Does this come under you now? It is a financial product. It is a mortgage. People are shaking their heads, so I am back to Professor Fels for false and misleading.

Mr Johnston—On the earlier example you were giving, in terms of the various forms that disclosure is taking, that is precisely why we have commissioned the work from Professor Ramsay: to see what we can do to try to marshal that in some way.

Senator CONROY—But this is not a question of those criteria you described. This is a direct falsehood. These people are remunerated.

Mr Johnston—I was referring to the more general examples you were giving about the various forms of disclosure that people were making.

Senator CONROY—But I am saying this is the reverse of any disclosure. This is telling people that they are getting a free lunch when they are not. They are paying a trail commission or a commission of some sort or some remuneration is going from whichever bank gets the work back to eChoice. So who is responsible for regulating this?

Mr Johnston—We would need to look at that specific case. I am not familiar with it.

Senator CONROY—As I said, they are actually advertising on telly most nights.

Mr Johnston—I have not seen it.

Mr Rodgers—People must have more fortunate nights than you.

Senator CONROY—Three o'clock in the morning is about the only time I get to see TV! No, it is not that late. It is on during *The West Wing* usually. I have watched the ad and I have thought to myself, 'Right. It is a financial product. It has got to be under FSR now.'

Mr Rodgers—I would need to actually look at the ad and the exact services. It is true that under the new legislation we have larger responsibilities for credit provision than we had before, but we do not regulate the provision of credit in the same way that we regulate the issue of other financial products.

Senator CONROY—Is a mortgage credit?

Mr Rodgers—It is the provision of credit by way of a loan.

Senator CONROY—It is a loan. To me, a loan is a financial product. It is not a provision of credit. It is a financial product. I accept that there is some obvious definition here that I am not totally across.

Mr Rodgers—It may be that we do have powers in respect of that. I do not want to talk about specific instances but, if there was misleading and deceptive conduct in relation to the provision of credit, we would have jurisdiction to deal with that. It is not a requirement that a PDS be provided for the home loan.

Senator CONROY—I understand that aspect. It is just that the whole point of this bill was to force disclosure. I appreciate that there is a two-year transition, but it does not seem to have affected eChoice and the mortgage providers who continue to advocate that they are providing a free service to customers. It is usually half a per cent and goes on for the rest of their natural lives. Their children and grandchildren inherit it and someone gets very rich from it. I have digressed and I have almost forgotten what I was asking you about. Bear with me for a moment.

Are you satisfied the OMC comes off sufficiently? We have heard a fair bit of criticism today, but in no way are we critical of you or Treasury. We appreciate the time constraints. Are you satisfied that it meets your principles for disclosure?

Mr Johnston—The OMC is not something that was mandated by us or something that we in fact suggested should be there. I think it is probably too early to say how effective it is going to be. We have not been through a product disclosure cycle at this stage. Any criticisms that I have heard of the OMC at this stage have been there from the beginning, because there are people who think that it does not work. It may not work in the way that people would wish, but I think that is really something that should go back to the original decision that was made to implement it—and that is a Treasury matter. We would be interested to see how it is actually going to play out in the marketplace. Once we see a few examples of it being used, we will see whether in fact it is doing something useful. That would be what we would look at.

Senator CONROY—Do you think it would be useful if it was market tested, like most other products are market tested in some way? Senator Sherry is fond of describing the Burnie pub test. You walk into the Burnie pub and put the PDS or the key FS on the table and say, 'Do you understand what is written there?'

Mr Johnston—We have certainly said, in the guidance that we have given on disclosure documents generally, that it would be useful to have some comprehension testing done on various forms of disclosure. We would support that.

Senator CONROY—Has Treasury done that at this stage, to your knowledge?

Mr Johnston—I do not know, Senator.

Senator CONROY—I have raised with you on many occasions this question of dollar versus percentage. Rainmaker—who are a well-established, well-known financial market participant—seem to believe that, while you may not be able to get the exact dollars and cents right, there really is no good reason why these experts in the financial services industry could not give a reasonable indication in dollar terms.

Mr Johnston—I think we have made it clear that we prefer dollar disclosure. Where it is possible to do that, that is certainly what we would expect and wish to see.

Senator CONROY—It would be nice if some day a judge said that something that is understandable to the consumer has to be in dollar terms. You could run a test case for us if you liked.

Mr Rodgers—Leaving aside the specific provisions that apply to superannuation, we have not said that the only way you can comply with the law is dollar disclosure, because we think that would be taking the law beyond where it naturally goes. But we have said, in the policy that we have issued on the area, that we think a good practice that would certainly help you comply with the law would be to disclose dollar amounts.

Senator CONROY—What would your response be if the industry said, 'No. Percentage is all we are going to cop'? Would you think that was a satisfactory outcome from this legislation?

Mr Rodgers—As I said, we have expressed a preference and said that, in our view, that aids the intention of giving consumers the information that they really need. Are we in a position to assert that if you did not do that you would be breaching the law?

Senator CONROY—No, I was asking whether you thought that was a satisfactory outcome—if they just say no.

Mr Rodgers—It is still to be tested.

Senator CONROY—If you are saying your preference is for the dollar, then that is the only answer.

Mr Johnston—And we have made that clear in our statement.

Senator CONROY—Diane was surfing the Net one day and noticed that the FSA in the UK provides comparative tables of costs et cetera across a wide range of products within a product class. I can get you the pages if you are interested. Are you familiar with that site and service at all?

Mr Johnston—I am aware that that is what the FSA does, yes.

Senator CONROY—They obviously must come up with some common metric for determining costs. There has got to be some way of plugging it in.

Mr Johnston—I would imagine so, Senator, but I am not privy to what that is.

Senator CONROY—ASFA has put up a sort of metric—is it ASFA?

Mr Adams—ISFA does have a standard on managing its—

Senator CONROY—Dracula is in charge of the blood bank, too!

Mr Adams—My understanding is that in the UK a similar sort of formula was used for the disclosure of fees and charges.

Senator CONROY—I think it might have been ASFA that recently announced on their web site that you can plug in, to your super fund, a calculator. Have you considered providing such a service as the FSA provides—borrowing any of the models? I can recommend a couple of reasonable ones to you. We have got Rainmaker's, we have got ACA's.

Mr Johnston—We have not at this stage, Senator. It is one of the things that from time to time we have raised in discussions because it is certainly something that we have been aware of. As we said before, while it is not specifically something that I know that Mr Ramsay would address in his report, we are using that as our starting point for what might be the best way of going forward. So while I am not saying that he would specifically refer to it, because we have not seen his report yet, in the work that we are doing with him we are looking at what is the best

way of encouraging the right sort of disclosure, and that might be one of the tools that we would consider.

Mr Rodgers—What we do know is that Professor Ramsay, for example, has the benefit of what the ACA has discussed with you this afternoon.

Senator CONROY—While I think it would be a great initiative if you were going down that path, it would not be a substitute for the companies actually telling their individual clients what they are charging them, at the end of the day. But it may be a way of encouraging the debate.

Mr Adams—I can confirm he is aware of the major international developments in many jurisdictions as to how they deal with fees and charges.

Senator CONROY—On areas other than disclosure, a number of submissions make reference to policy statement 146, which concerns training requirements. Can you take me through the requirements in the policy statement and tell me how it satisfies the requirements for the FSRA? I know some people in the room are very interested in the training requirements. It might help them pass the next one.

Mr Johnston—The first point to make is that the work we were doing in respect of policy statement 146 was independent of FSRA. Even if the legislation had not got up, we were going ahead with policy statement 146. That is on the basis that we believe that anyone who is involved in advising retail clients in respect of financial services ought to meet some minimum—not minimal—competency and training standards. So that was our premise, and that was independent of the legislation. We did, on the way through, realise that there was a timing coincidence. There were some in the industry who believed it was linked to FSRA, but we tried to disabuse them of that view.

Essentially, we believe that anyone who gives financial product advice to retail clients ought to have a level of competence and a level of training. As you would be aware, the interim policy statement was around for quite some time. We consulted widely with industry and with consumer groups on just what it should be. I would not pretend that we had a universally consistent view. Clearly, it was going to raise the bar for some sections of the industry from where they were before. That automatically, if you like, creates some friction, but we held firm to the view that there should be minimum standards in place.

We eventually arrived at a two-tier standard and said—and I will paraphrase here—that people who are advising in respect of investment type products should have a higher standard to meet than people who are dealing in less complex products, which perhaps have less of an impact on the consumer. Those who are dealing at the second level, the lower level—for basic deposit products, for most general insurance products—can meet a lower level of competency and training. The act then requires that people who—

Senator CONROY—So it is an investment versus risk test, if I can put it that way.

Mr Johnston—Investment versus non-investment. The act then came along. The act provides that people who do this do have to meet certain requirements, but it is for ASIC to say what the requirements are. We do that through policy statement 146.

Senator CONROY—A number of submissions asked about training in relation to basic deposit products. Where are we at with that? What are we expecting?

Mr Johnston—What are we expecting?

Senator CONROY—Yes, in relation to basic deposit products.

Ms Vamos—As in whether it is tier 1 or tier 2?

Senator CONROY—Yes. I am presuming it falls into that lower category.

Ms Vamos—It does, yes.

Senator CONROY—I am talking about bank tellers. Do we have agreed training processes? The banks I presume are pumping hundreds of people through at this point. Are you supervising it? Is there an outsourced company that is doing the training? What is the process?

Ms Vamos—Basically what policy statement 146 says is that in order to meet the requirements you need certain knowledge. The knowledge, particularly for tier 1, needs to be generic about the industry and products generally. It also needs to be product specific. You also need to have the skills to provide advice, as in do the needs analysis and all of that type of thing. With tier 2, with some of the basic deposit products, that level of skill and knowledge is not required and that is why it is a lower level.

There are a number of courses on the register that have been approved or accredited by registered training organisations, which have applied to put them on our register, that meet the skills and knowledge required at level 1 or level 2. There are some courses specifically for certain products. I know there are some courses being developed for basic banking products, to cater for the specific needs of your smaller ADIs. But you should also be aware that under 146 the basic premise has always been that anybody providing retail advice needs to meet the requirements. However, there is, if you like, another tier: if you do have a large number of service personnel, they do basically follow a script and they are supervised by somebody who is 146 compliant, that organisation has met 146.

Senator CONROY—That is a new one, I have to say. So this would happen in an organisation where employees, like bank tellers, work off a computer screen. So, in other words, bank tellers are receiving no extra training to comply with the legislation. In essence, they are reading off a script, which you have ticked off.

Ms Vamos—But that script has been vetted to ensure that it complies with any of the requirements under 146.

Mr Johnston—But not by us.

Ms Vamos—But not by us, of course.

Senator CONROY—When was that decision reached?

Mr Johnston—That is in the policy that has been there. Maybe I can give an example as to how I think it might work. As Ms Vamos said, if someone is working from a script and does not depart from that, then, provided the script was properly prepared and provided they are supervised, that individual does not need to be 146 compliant.

Senator CONROY—What is your definition of 'supervised' for a bank teller—someone standing there looking over their shoulder?

Mr Johnston—No, there needs to be someone to whom they are accountable in their line management, who actually makes sure that yes, they are sticking to the script and yes, they are dealing with the right sort of customer. What I think is more likely to happen in practice and why I am not sure that it is quite as onerous as some might say is that—

Senator CONROY—No, I am worried it is not onerous at all, Mr Johnston. I think you have got the wrong end of the stick.

Mr Johnston—Well, the industry certainly thinks it is. I would imagine that you might have one or two people within a branch who have to meet the requirements. If someone comes in and deals with a counter staff member just to open an account or by saying, 'This is the type of account I would like', clearly the staff member does not need to be compliant for that. But if the customer strays into actually wanting some advice, we would expect that the staff member would then say, 'I'll just have to refer you to this person here.' That is how we believe it would work.

Senator CONROY—Does that or does that not cover the two-year term deposit, which is where we got to? I am looking to know whether the script on the screen covers two-year deposits or there is training involved for the two-year deposit—for the individual, as opposed to the script.

Ms Vamos—That level of compliance could apply to the two-year deposit, but the entity would need to have in place monitoring, supervision and checking systems to ensure people were not straying outside that script.

Senator CONROY—What would you consider satisfactory monitoring and supervision? I am thinking about bank branches where there are 10 or 12 tellers—and there is no bank manager anymore in most branches so there is a supervisor who is doing a hundred other things. What is the level of supervision?

Ms Vamos—One method is mystery shopping—and I know some banks are engaging in this—where you test clients, whether it is by phone or by going in. Again, if the supervisor is doing the hundred other things, that would not meet what we consider to be basic supervision and monitoring.

Senator CONROY—Okay. Let us think of the casino model where you have four blackjack tables and you have one supervisor sitting and watching the four blackjack tables. That is supervision. Take me through the gradients of supervision down from there.

Mr Johnston—I am not sure that is the example we would want to use.

Senator CONROY—Unfortunately it is beginning to sound like it.

Ms Vamos—Part of the supervision and monitoring is also to have some minimum training in place. People providing this type of service need to understand why these limitations are put on them and why they have to do certain things. So it is a holistic approach as far as supervision and monitoring is concerned. For example, there are some call centres where calls are recorded and they are checked that way; there is random checking, which is a good level of supervision.

Senator CONROY—But fundamentally, from all that you have said to me today, bank tellers will do nothing different from what they did before the act was introduced other than potentially read a different script.

Ms Vamos—No, they will be limited in what they can say in that script.

Senator CONROY—I know but I am saying that they have just got to follow the script. They do not have to understand why they are following the script; they have just got to be—

Ms Vamos—But they do.

Mr Johnston—The script is one thing, but if they do in fact stray into giving advice then they need to have been trained to give that advice.

Senator CONROY—Sure. But I am thinking about someone who walks in and talks about opening an account, making a withdrawal or a deposit and says, 'Look, I am interested in one of those two-year term deposit things'—which is the majority of people who go into a bank. There is no extra training that has evolved from this wonderful consumer protection bill that we have all lauded?

Mr Johnston—I think that the script would be more relevant in the call centre example—really there were two examples that were being used. In the-dealing-with-someone-over-the-counter example I think the supervision model is going to be the more appropriate model.

Senator CONROY—I am one of these idiots that still go into bank branches; I am not sure if you have made the leap onto the Internet yet, Mr Johnston. I just do not remember ever seeing—and maybe it is because the queue is too long and I just cannot see among all the people—somebody hovering in the background keeping an eye on people.

Mr Johnston—But this is a requirement going forward from now. We would not expect to have seen this in place yet.

Mr Rodgers—In practice, of course, many of the banks are actually ensuring that people who do that kind of counter service are in fact trained, so it is making a difference.

Senator CONROY—I am looking to find out what level of extra training bank tellers have so that they know to comply with your bill. I am getting very afraid that there is basically nothing.

Ms Vamos—The feedback we are getting from banking and other types of deposit-taking institutions is that, because they want to provide that value-adding to their customers, they do not want their counter staff to follow a script. So they are having to comply with the tier 2 requirements in PS 146. It is only where those counter staff provide a very limited dialogue with the customers that they will follow that part of it. But in the end I think most ADIs will be following tier 2.

Senator CONROY—I hope you are right and I think that would be fantastic. Are you monitoring the level of people that will become registered? Are we able to say there are 20,000 bank tellers in Australia and seven per cent of them are tier 2 now and in a year's time I will be able to ask you and you will be able to say, 'No, 28 per cent are, and next year there are is going to be 52 per cent'? Are you in a position where you are going to be able to give me that sort of analysis if I am silly enough to ask?

Ms Vamos—We are not required to keep those records. The entity is required to keep those records and we have powers to obtain that information.

Senator CONROY—I cannot see why they would not want to put one extra line on the information that they supply to you. Are you able to ask for that information on a regular basis? Say, 'Blame Conroy, you know he hates you anyway and he is going to ask me, so I have to have an answer, so you can just supply it to me now.'

Mr Johnston—One would expect that it is the sort of thing that in our supervisory role we would ask for after a period of time once this is through. That would be the sort of information in which we would be interested.

Senator CONROY—Yes, but I am hoping to come back and you can say to me, 'They are rolling their staff through these training courses.' I will not go to what is in the training courses yet; we will leave that for a little while.

Mr Johnston—That is one of the things that Mr Hughes, who is my director of regulatory operations and therefore is responsible for the team that carries out surveillance and supervision for us, would have on his plate.

Mr Hughes—Indeed, one of the reasons that we have ended up with this policy statement is reflected in the fact that we had a high number of complaints from consumers about poorly trained and poorly educated staff giving inappropriate advice to consumers in relation to financial products. It is in response to that concern that we end up with the policies that we now have. Mr Johnston is absolutely right, that we will be testing the ability of those institutions to comply with those new standards when we go out and monitor their compliance.

Senator CONROY—I am trying to ensure that Mr Murphy, who is sitting behind you, is on a level playing field with people who are trying to sell similar products. It is not fair that Mr Murphy has to struggle his way through the qualifications when bank tellers basically just have to follow a script that qualifies. I saw Mr Murphy looking eager before when you mentioned an approved script. I dread to think what is in his mind, but there was certainly a twinkle in his eye about coming to you with a script. I am assuming that that would not pass your test for level 2.

Mr Johnston—The script is there to ensure that they do not stray into giving the advice, but when they do they have to meet the requirements.

Senator CONROY—Okay. So I will be able to ask you in a year's time roughly what percentage of tellers are going to be able to have passed—are we talking tier 1 or tier 2, Ms Vamos? From what they are telling you, they are going to roll them through tier 1 and tier 2, or just tier 1?

Ms Vamos—The types of services that can be provided via the script supervisory would not be the tier 1 services. It is more akin to the fairly simple, basic tier 2.

Mr Johnston—Tier 2 is the lower level.

Senator CONROY—I had got them around the wrong way in my head. So you would think from what they are telling you that they want to upgrade the skills of their tellers and they want to get the highest possible qualifications so that they can compete with Mr Murphy.

Ms Vamos—There will be certainly some people available in branches that will be to tier 1—

Senator CONROY—That was a simple model. I never understood why they wanted to draw this distinction, but that was a simple model. Other submissions referred to the alternative requirement in PS 146 for five years experience in the last eight. What is the basis of that level being chosen?

Mr Adams—That policy again has some history, so that goes back some time. There are various methods by which someone can demonstrate that they meet the skills and qualifications bases. There are a couple there that deal with three years experience in five years, three in five and then there is the five years in eight if someone is going to go down the individual assessment route of demonstrating that they have skills in compliance. In the end I think there is no doubt that the numbers have a level of arbitrariness about them. No matter where you pick numbers, there is going to be some line. I think it was just an assessment that there needed to be some sort of graduation between people who had some qualifications, and in that context we picked three years experience in five years, and those who did not have qualifications, and we suggested five years out of eight.

Mr Rodgers—As we have said, this policy had its origins in the mid-1990s, when we were looking at the provision of advice generally—long before the FSR process. Generally, the policy says that the default setting is that you demonstrate competence by having appropriate qualifications as well as a little bit of experience. But we recognised at that time that there are people who have been in some parts of the industry—we had in mind the stockbroking industry, for instance—for very long periods of time, indeed long before qualifications were an industry entry requirement. Most new people joining a stockbroking firm at the moment will have done formal tertiary qualifications of the kind that the policy contemplates. But we had an alternative mechanism for those people who had been in the industry for longer, and that was that they could subject themselves to some kind of individual assessment. But we would want to be confident in that circumstance that there was no lessening of the standard, so that, as well as the individual assessment, we would look for a longer period of experience in the industry. We

thought at the time that five years was an acceptable minimum to meet those needs, and that is the approach that we have carried forward into the revised policy under FSR.

Mr Johnston—And there is the eight-year requirement to give it some currency.

Mr Rodgers—Yes. The five in eight means that there is no point having five years experience 20 years ago and saying, 'I have my five years experience.' It has to be five of the most recent eight years that you have actually spent actively doing this work in the industry.

Senator COONEY—This is all based on the policy statement, is it not? But that sounds very much like legislation—subordinate legislation, but it sounds very much like legislation to me—particularly when it affects the sorts of things that somebody like Mr Murphy can do. That is doing stuff that regulations, or even the act, ought to be doing. Yet you told us before that it has no force of law.

Mr Johnston—The act requires that people be qualified and competent to do the work, and asks ASIC to set some standards. In setting any standard, it is very difficult for us to do so without prescribing in some way.

Senator COONEY—That is the point, though. I am happy with what I have been hearing in the examinations here today; everybody is happy with that. What they are not happy with is that those statements can be made without any parliamentary review.

Mr Johnston—I am not sure that that is something I can address, because the act asked us to do it and so we did it.

Senator COONEY—I understand that. I am not expecting you to; I am just thinking aloud and telling you that to give you an indication of how I am thinking. It obviously makes a difference to the sorts of activities that people like Mr Murphy can go round. Yet he has no chance, as far as I can see, of going to parliament and saying, as Senator Conroy said, 'Can you vote against this?'—as you can against a regulation. Yet it has just the same effect.

Mr Rodgers—In that context, it is important—and we have drawn attention to this fact—that this policy has been around for some time. The legislation was enacted with that policy as a background. I appreciate the point you are making, Senator.

Senator COONEY—That just seems to me to be another indication of why it ought to have a bit of parliamentary supervision: because it has been around for a long time and is likely to be around for a long time. I can understand the exercise of a discretion, as you put it, where somebody comes and says, 'What is Ms Vamos going to do? Should we let her do this? Yes.' You exercise a discretion; I understand that, that being something that ASIC exercises its mind about. What I cannot quite understand is that there is, in effect, a policy and an execution of that policy which affects a very wide range of people and which will be ongoing, yet that is not subject to parliamentary scrutiny, as far as I can tell.

Mr Johnston—I guess it was open to the parliament to prescribe it itself, but parliament in fact gave us that power so we simply exercised it.

Senator COONEY—You are not to blame.

Senator CONROY—Senator Cooney is a bit of an old traditionalist, like me.

Senator COONEY—I am just thinking that perhaps parliament ought to have a look at it.

Mr Johnston—I will just go for a minute to how we arrived at the policy, without going over the ground that Mr Rodgers and Mr Adams covered, because there is an arbitrariness about any number we pick. We really had three options. We could go back to the days when no-one required any training, and I do not think any of us would like to go back to those days.

Senator COONEY—I am sorry; I should not have interrupted you. I might not be making my point well. I am not cavilling about the training; of course there ought to be training. What I am cavilling about is who makes the decision about that and what standards they set. There are two things. They make a decision that training is right and that standards ought to be set, and I agree with all that. But who should be making the decision? That is the issue.

Mr Johnston—I understand that. I was just going into why we chose the model we did. The other option that we might have, apart from having low standards, would be to require everyone to sit an exam. That happens in some jurisdictions. We chose to recognise the fact that there are people with qualifications in the industry that could be recognised and go down a qualifications route rather than an examination route at this stage.

Senator COONEY—Sorry, Senator Conroy.

Senator CONROY—That is all right. You will be sadly missed, with views like that. Some submissions refer to the new standard to disclose if any ethical, environmental, social or labour standards were considered in an investment decision. Are you planning to issue guidelines in relation to how that is disclosed?

Mr Johnston—Yes. We are in a consultation period at the moment, taking various views into account. We have had round table meetings as well as individual meetings with a range of stakeholders who have an interest in that. So we are likely to put out some guidance but I think we are still some time away from doing so.

Senator CONROY—Have you any thoughts yet as to how you will monitor compliance with the provision?

Mr Johnston—The short answer is no.

Senator CONROY—I am just aware that there are some people in the industry who are scratching their heads about exactly how they are going to comply with this and, as always, everyone looks to you.

Mr Johnston—I think that will be part of the guidance that we issue so, at this stage, no.

Mr Adams—The legislation and the regulations do provide some detail to those provisions. There was some immediate concern about how people will comply with that obligation, and those regulations basically say, 'You either do or don't have standards that you keep yourself as a product issuer and, if you do, you need to indicate what they are.' So there is a minimum sort of requirement in the regulations and it is against that backdrop that our further consideration of the issue is going on.

Senator CONROY—I mentioned real estate agents earlier, but you indicated that that was a regulation Treasury issue rather than your own. Did you examine the issue of real estate agents and did you make any recommendations about their inclusion or not?

Mr Johnston—Not directly on the point of FSRA, but we did issue a report two years ago to the federal and state governments saying that we were concerned about the number of, for want of a better term, get-rich-quick seminars and advice that may be given by people who are outside our regulatory ambit. We produced a report that said, 'These people are outside our regulatory ambit. We think there is mischief that is being done but we cannot do anything about it. Perhaps governments need to consider collectively how that should be addressed.' So we issued a report to the federal government and to state governments just pointing out what the issues were.

Senator CONROY—Was there any response? While it appears for the moment that they have got an exemption from FSR, have any of the state governments acted in response to your report?

Mr Johnston—I cannot speak with great authority. I believe there was some legislation in Queensland over the past 12 months that regulated the two-tier type activity in some way, but I cannot speak with authority.

Senator CONROY—Are you conducting the two-tier case, or is that the state jurisdiction?

Mr Johnston—It is the state jurisdiction. I can say that it is an area that we are going to look at again. Within my directorate—the financial services directorate—we have an activity planned for the first quarter of the new business year to see what we can do about some of the seminars that are around, to see whether we can take action against some of them if they are behaving in a misleading or deceptive way. If we cannot, we would produce another report which says, 'These are the jurisdictional issues that we face. We can't do anything about them, but someone needs to.' Again, that will be under Mr Hughes's direction.

Mr Hughes—One area where we may be able to take direct action would be in the negative advice context, for instance, where a real estate agent said, 'I wouldn't recommend buying this property. You'd be better off getting into a managed fund.' There is clear financial advice there and they would be caught.

Senator CONROY—I guess they had better practise their script.

Mr Johnston—We are concerned about the issue. We will do what we can, but we are not sure what we can do.

Senator CONROY—I appreciate that. The FPA also raised the issue of having 'financial planner' as a restricted term. Are you aware of unqualified people using that, too?

Mr Johnston—I do not know that the issue goes to unqualified. My understanding of the concern of the FPA is that there are people who can use that term who are not members of the Financial Planning Association because it is not a restricted term under the legislation.

Senator COONEY—They could also use the term outside the act.

Mr Rodgers—They certainly cannot carry on a financial planning activity without holding the appropriate licence.

Senator COONEY—But the point is they can hold the name; can't they?

Mr Johnston—Yes. Someone could call themselves a financial planner and providing they were not unlicensed and giving financial product advice—

Mr Hughes—There is no prohibition on having the name, provided they did not do any financial planning.

Senator CONROY—Do you mean they could be a lawyer?

Senator COONEY—If they sold property, it would be all right.

Mr Rodgers—If it was not a financial product, that is probably right, although it risks stepping into the territory of misleading and deceptive conduct.

Senator COONEY—A person who lends money on a mortgage, from what you said before, is not caught by this but could say he is a financial planner by simply saying, 'Look, this property would be a better investment than that one.'

Mr Rodgers—If they said that, they may be in breach of laws that we administer because it may be misleading to say to someone, 'I am a financial planner and I am recommending that you buy this property,' which, under the ordinary Australian law and ordinary understanding, is not a financial product. I am splitting hairs to illustrate that these things are not totally beyond our reach.

Senator COONEY—This is where it gets to be farcical. Putting money out on mortgage is a very traditional form of investment and getting money on mortgage is a very traditional form of loan. When I was a boy of Senator Conroy's age, that is what we used to think of money.

Mr Rodgers—I want to remind you that our area of responsibility is bound by the four corners of the act.

Mr Johnston—As I understand it, the position the Financial Planning Association is concerned about is more people who meet the legal requirements and call themselves financial

planners, even though they are not members of the association. They might still be operating squarely within the law and quite properly.

Senator CONROY—Is it you or Treasury who would determine this?

Mr Johnston—It is Treasury.

Senator CONROY—Busy little beavers, aren't they?

Mr Rodgers—That is because the act envisages regulations that create restrictive terms.

Senator CONROY—I noticed last week—was it you who issued a class order on recognised accountants?

Mr Rodgers—We did—not me personally.

Senator CONROY—What is the difference between a class order and a regulation?

Mr Johnston—Mr Rodgers is the expert.

Mr Rodgers—In that case, the act expressly empowers us to make declarations of that kind.

Senator CONROY—I thought it declared professional bodies out.

Mr Rodgers—No. It creates regulation that attaches to people called 'recognised accountants'. How do you know a recognised accountant? The act says—and I am paraphrasing—that a person is a recognised accountant if they are—

Senator CONROY—I do not remember the act—maybe you are talking about a reg—but I do not remember anywhere in the act that refers to 'recognised accountant'.

Mr Adams—There is a provision in section 88B of the act.

Senator CONROY—I have some bedtime reading.

Mr Adams—I think it is 88B. It is the one which deals with what is a recognised accountant. As Mr Rodgers indicates, it states that ASIC may declare who is a recognised accountant. That provision only relates to one regulation. Contrast that with the concept of a financial planner or a stockbroker: they are restricted terms in a different provision which are set out in the legislation and there is a regulation making power specific to that section which enables government, through Treasury, to issue further terms for that purpose.

Senator CONROY—What is the impact of this class order about recognised accountants? Are they exempted from anything because they are called a recognised accountant? Other than hanging a sign on the wall saying, 'I am now an ASIC recognised accountant,' how will I recognise them?

Mr Adams—As Mr Johnston said, we are thinking about issuing some further guidance for accountants on how the financial services legislation applies to them. One of the relevant provisions is regulation No. 7.1.29 which provides for an exemption for certain kinds of conduct by accountants from the concept of 'what is financial product advice?'

Senator CONROY—Could you say that again, please?

Mr Adams—That regulation, and its first subregulation, lists kinds of conduct which may be exempt from the provision of financial product advice. There is a further qualifying regulation to it which states that you cannot rely on that exemption where someone provides a recommendation, an opinion or report, regarding a financial product—which basically mirrors the definition of 'financial product advice'.

Senator CONROY—What is the purpose of issuing a statement if it does not provide any difference?

Mr Adams—What is the purpose of the regulation? I think you might have to ask Treasury that one to know the background to it.

Senator CONROY—It occurs to me that a back door then opened to exempt accountants from some of the provisions that were not specifically written into the legislation.

Mr Johnston—But, Senator, it may be helpful—

Senator CONROY—No, Mr Johnston; this was a very specific debate.

Mr Johnston—It may be helpful if Mr Adams outlines the type of activity that was exempted, because my understanding is that that was not the purpose of the regulation.

Senator CONROY—It might be the impact but not the purpose?

Mr Adams—As I said earlier, the scope of the exemption is limited by a provision which states that if you provide financial product advice you cannot rely on this exemption; so the effect of the exemption is limited. I have given various presentations and in describing it I have generally said that the first part of it tries to give an indication of typical conduct which, depending on their circumstances, may not be advice. But it is subject to an overriding qualifier saying that, notwithstanding that, if you do give advice that conduct is still caught.

Mr Rodgers—The issue of being a recognised accountant does not affect that scheme. To get the benefit of that limited set of exemptions that are listed in that regulation, you have to be a recognised accountant in the first place in that limited way.

Senator CONROY—Do they have to come to you to be recognised, or do they have to go to somebody else to be recognised?

Mr Rodgers—Our declaration says—and it really carries forward a position we have actually maintained for some years—that members of the Institute of Chartered Accountants in Australia and the CPA are recognised accountants and the National Institute—

Senator CONROY—I am speaking to the National Institute of Accountants tomorrow and I was very concerned I would be stoned if it did not apply to them as well. Please guarantee me that I will be safe tomorrow.

Mr Rodgers—I think you can be comforted by the fact that they are named on the declaration that we made last week or the week before.

Senator CONROY—I will not pursue this any further. I will go away and have a read of 88B and 7.1.29 and the exemption list, but I am sure I will be coming back to you on this one. I appreciate that earlier in the day Mr Larcos was here but you were not. There was one issue in particular that I wanted to raise that Mr Michael Board from Derivatives.com.au Pty Ltd raised this morning. You might have seen the submission already. He asserts that in his view, your policy statement overturns the amendment the Senate put in place.

Just to give you a little background, technology has changed at the SFE and they have moved from the pit to electronic screens, and so it is a relatively new phenomenon. There are transactions which are not listed on the screen. This would be a problem because of the changing technology, irrespective of FSR. He believed that FSR would cover off on ensuring disclosure of some transactions—and you might want to have a look at his evidence this morning. Essentially, he believed that the first draft of the bill which we put before parliament allowed, if you like, a trade-off between fair, efficient and transparent.

Mr Rodgers—Fair, orderly and transparent.

Senator CONROY—Yes; orderly and transparent, thank you. But the Senate amended the situation so that there was not the trade-off. Certainly from my recollection—and I think it was my amendment—that was the intent. But he believes that your policy statement, by using the word 'composite', reintroduces that element of balance between the three. My reason for being concerned about this is just that I wanted to make sure that the intent of the amendment that was carried by the parliament has not been subverted; but his concern was that he believed the bill that was finally passed would force all of the transactions to basically be disclosed on the screen, so to speak, and that by going back to the composite balance that requirement would no longer be there. So there is the macro, in that I am looking for an explanation of what looks like a policy statement returning back to the unamended bill. Then specifically, he has raised what I think is a legitimate concern. It sounds odd to me—although I do not know enough about this particular market—where some transactions are taking place which are not actually disclosed in a timely manner to the market.

Mr Rodgers—Let me take the first point first. It is true that our policy statement says that 'fair, orderly and transparent' we take to be a composite statement. We do that not on the basis of overturning. As you will recall, the original bill said to do all things necessary to ensure that the market operates in a way that promotes the objectives of fairness, orderly and transparency; that was the text of the first bill. Also, it did say to do that to the extent that it is reasonably

practicable to do so and, in particular, to the extent that those objectives are consistent with one another. That was the bill that was amended.

Senator CONROY—'Consistent with one another' was where we had the problem.

Mr Rodgers—Yes; that was amended. But the notion of 'to the extent that it is reasonably practicable to do so' continues and is part of the amended legislation. What we say in the policy statement is in recognition of there being limits to the practicalities which the legislation recognises on 'fair, orderly and transparent'. The fact is that we said and say in the policy statement that this is composite and needs to be looked at as a whole—and that is the same language we use in our policy dealings with other licensees' obligations to operate 'efficiently, honestly and fairly'. We say that you have to view it as a whole, and we have taken the same approach to that. I do not think, with all due respect to Mr Board, that it is fair to characterise us as having, by policy, tried to reinstate the position that was in the bill. Indeed, we expressed in the debate that went with that some problems with the language, and we had most problems with the difficulty of 'promotes the objective of'. We argue that there should be an obligation to do these things rather than to simply promote them.

Senator CONROY—We might revisit that one.

Mr Rodgers—There has been a longstanding debate in the regulation of financial markets about the issue of transparency. Let me give you a concrete example. In some situations there is a strong argument that being fully transparent operates unfairly, and economists, lawyers and regulators have all opined on this. The example that I have in mind is that I am about to do a very major transaction on the market. If I am obliged by the rules of the market to signal my intention to do a transaction of that size—

Senator CONROY—You will move the market.

Mr Rodgers—in parts of the market I will be savaged because everyone will jump on the other side. If I am a buyer, the price will go up disproportionately. There is academic evidence that suggests that kind of price volatility is very short run. It lasts for as long as the transaction is in the market and, when the market disappears, the price falls back to a level. The argument is that that degree of transparency operates unfairly to the participant whose trade that is. In what we have said in the policy, we have tried to recognise that there are balancing considerations in approaching this. It has been a feature of Australian markets. While the ASX market has a general rule to the effect that most trade should take place off market, it has had an exception to that rule for large transactions and for international transactions that take place outside normal trading hours. The proposition that somehow or other this is new to the Australian marketplace is, with all respect, not quite correct.

The SFE have, over some years, been experimenting with ways of solving what they have identified as a problem—short-run, adverse market reactions. Their argument has been that if the market rules do not permit those kinds of transactions to take place then they will simply take place outside the market framework altogether. It is not as if they will not happen, they just will not happen anywhere near the market. It is to the advantage of the market and market users generally that they do, because the transaction might occur other than in the normal process of, say, electronic matching of orders but reporting that transaction, if it takes place within the

overall framework of the market, is instant and made known to the market. In other words, the price at which that transaction gets done gets fed out into the market.

Senator CONROY—From what you have said, I think that may cover off on Mr Board's concerns. I do not know enough about it to ask you questions, but would you have a look at his testimony—and hopefully I got him to explain it sufficiently—and come back to us before estimates so I can take up any issues from there? I think that covers off on all of my questions for the moment. Thank you all very much.

CHAIRMAN—My question follows on from some of the questions that have been asked regarding the requirements for licensing and education. What is the situation where a bank teller in a bank asks a customer to give permission for someone to contact them regarding another bank product, for example insurance? That bank teller might say, 'Look, I'll get someone to contact you because I think the bank's associated service company can provide a better deal than the one you're getting,' and the person might be in there making a deposit in their bank account. Does the teller have to be appropriately licensed to do that or can they come under the umbrella we were talking about earlier?

Mr Rodgers—I will give a response and then call on Mr Adams and Mr Johnston. As I understand it, there are actually two separate parts to that question. The first is: do I as a bank teller need to have the training that an adviser has, merely to refer somebody to somebody else? The answer is no, the law does not require that.

CHAIRMAN—That is certainly what we were trying to avoid: requiring the bank teller to be educated in that, because of the country branch situation and so on. Providing that they were providing a referral, we regarded that as acceptable, when we were dealing with the original legislation.

Mr Rodgers—The second part of the question relates, as I heard it, to the antihawking provisions.

CHAIRMAN—That is right.

Mr Rodgers—Can I just confirm the question, to have a clearer understanding? If a teller says, 'Would you be interested in having someone from the bank contact you about your insurance needs?' and subsequently there is a meeting with that person, would that meeting be in breach of the antihawking provisions?

CHAIRMAN—Yes.

Mr Adams—That issue is related to the guidance that Mr Johnston indicated that we are hoping to issue shortly. There is an issue there about whether the initial contact between the teller and the client was unsolicited in the context of the reference to the insurance product. That will depend on the circumstances, as to the relationship there. If it were given quite cold, there might be an issue that that was unsolicited. However, that is a technical reading. There is another aspect of it, and that is: would we administratively be concerned about that—where it is quite clear that there is no pressure selling involved here but it is more a case of an individual,

upon being informed of something, then taking up an election that they wish to see someone about that. So they are the kinds of things that we are planning to give some guidance on.

Senator CONROY—It is about the reversal of onus: whether they say, 'Oh yes; get someone to ring me' or the teller says, 'I'll get someone to ring you.'

Mr Rodgers—In the approach that we have been taking—and I want to stress that we have not finalised what we are going to say publicly here—we have concentrated on the work that the antihawking provisions are supposed to do, as we understand the work that they are intended to do, which is to remove the risk of pressure selling in circumstances where, either on the phone or face to face, that kind of contact has not been asked for by the customer. In the example you have given—and again, I would not want to be seen to be giving legal advice here or even committing us to a position on that—if that is an ordinary conversation that takes place in a bank that does not involve anything much else, it does look, at least to me, as though that does not involve the pressure selling that the provisions are directed towards.

Senator CONROY—There is probably a prior existing relationship.

Mr Rodgers—But you can work that scenario out in a number of ways. You could say that, well, in certain circumstances, it just might be.

CHAIRMAN—It was not a hypothetical circumstance that I raised. It has actually happened to a member of my staff on more than one occasion. Also, when he has been in line at the bank, he has heard other customers spoken to in the same way by the tellers.

Senator CONROY—Perhaps I can agree with Grant: it is what is happening at the moment, because the squibs on the screens put pressure on tellers to try and—

CHAIRMAN—Are they trying to circumvent the antihawking laws in this way? Also, if the tellers receive a fee for any successful referral, should they disclose that to the customer at the time they are offering this referral?

Mr Adams—There are provisions dealing with referrals. It is in the regulations. Where the referral involves an employee-employer relationship, that employee does not need to disclose that. It is based on the assumption that the financial services guide that the client will receive will outline the remuneration arrangements.

Mr Johnston—I would reiterate that it is a matter that is under our consideration in terms of the guidance that we will issue, but we have not yet come to a view on all of those matters.

CHAIRMAN—The other question I have relates to the general issue of education. Can you outline for me what education programs you have in place or plan to have in place, firstly, for consumers and, secondly, for those who are required to comply with the new regime? Again, I refer in particular to hawking, for example, so that consumers are aware of the new provisions in relation to antihawking and so that, equally, those who are engaged in selling are aware of that.

Ms Vamos—Certainly, consumer education is something that ASIC sees as being important for it to deliver. One of the first things we did immediately prior to 11 March was to introduce some clear consumer messages on our web site. They did cover some of the provisions of FSRA that were starting from day one, and one of those was antihawking. So the alert is there. When we finish guidance in relation to areas like antihawking, that guidance will be distributed through consumer bodies and on our web site, so that we do get that consumer awareness up.

Mr Rodgers—Let me add to that. I think the huge effort that we have described in our submission to provide guidance to people in a whole variety of mechanisms has been directed towards what I understood to be the second part of your question, as to what we are doing to make sure that industry participants who are affected by the new regime know about their obligations, and we will continue to put a very considerable effort into making sure that the message gets out.

CHAIRMAN—Do you have a process in place for consumers who might want to call ASIC—for instance, to complain about that example I gave involving the bank teller?

Mr Johnston—In terms of complaining?

CHAIRMAN—Yes. If they want to ring up and say—

Mr Johnston—Yes. ASIC has an open—

CHAIRMAN—'I'm not sure that this should happen to me,' or 'The bank should be doing this.'

Senator CONROY—I think they said they have got a hotline, Grant.

Mr Johnston—There is a complaints line that people are able to come through on. We receive 5,000 to 7,000 complaints of misconduct per annum. But there is a 1300 number that people can come through on with those sorts of matters.

CHAIRMAN—I have no further questions. Are there any others?

Senator CONROY—No.

CHAIRMAN—If there are no further questions, I thank all the officers from ASIC for their attendance at the committee hearing this afternoon, and particularly for their patience in answering the questions. It has been quite an extensive session and we have gone well over time. So thank you for your patience in that regard.

Committee adjourned at 5.04 p.m.