

# RECA

**Real Estate**

**Consumer Association Inc**

**SUMMARY OF SUBMISSION**

## **SENATE JOINT COMMITTEE CORPORATIONS AND FINANCIAL SERVICES**

**INQUIRY INTO REGULATION OF:**

## **PROPERTY INVESTMENT ADVICE**

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## **Inquiry into regulation of property investment advice**

On 8 December 2004, the Parliamentary Joint Committee on Corporations and Financial Services resolved to inquire into the regulation of property investment advice by the Commonwealth.

RECA would like to thank the Parliamentary Joint Committee for the opportunity to respond to its inquiry into the Regulation of Property Investment Advice

RECA is a not for profit consumer association established in 1997, to inform, educate and protect consumers of real estate products including property trusts, mortgage trusts and development portfolios.

RECA's founder and director has been nominated for a number of consumer protection awards and has been over a number of years responsible for the bringing to justice those who mislead consumers about the value and return of property investments.

These investment scams have left many, many people, at or near retirement age, destitute. Because Centrelink insists "investors" carry the loss for five years before they can "write it off", these victims are denied immediate Centrelink assistance. They are forced to face the humiliation not only of their loss but also of relying on the good will and charity of family and friends during this critical time.

### **A plea from a consumer:**

*.....We have lost, our home, our business, our income, our industrial shed, our investment property, our pride, our dignity, and our health. We are only one of many in this situation, but nobody, in authority wants to know us.....*

### ***Maurice***

RECA contests that the 'twin peaks' model of regulatory supervision has failed the public, industry stakeholders and the market-place.

Moving forward, and in the interests of all consumers, present and future, RECA believes that a bi-partisan acceptance that a new model of regulatory control needs to be placed on the discussion table.

RECA argues that Australia needs a properly constituted consumer protection agency, totally independent of any "dual role" system.

In this response RECA proposes a completely new model of national consumer protection, It seeks to combine the talents of top drawer experienced fraud investigators with a team of highly qualified forensic accounting specialists, law enforcement officers and consumer protection analysts, to form a permanent and dedicated **National Consumer Protection Agency**, independent of ASIC and APRA and the ACCC.

RECA wishes to acknowledge that the ACCC were placed in an invidious position in this matter and have at least tried to deal with a situation, which was clearly taken from their hands in 1998, when responsibility for Consumer Protection in the area of financial services, was passed on to ASIC.

The model proposed is similar to the concept of enforcement of law against white-collar criminal activities, taken on by Mr Eliot Spitzer & the office of the Attorney General of New York and Mayor Giuliani, which provided a constituent friendly environment and a strong regulatory approach to servicing properly constructed consumer protection policies.

Warnings from several experts in the business community and those of consumer groups have brought about at last, a welcome inquiry into the Property Investment Advice industry.

It is RECA's intention, on behalf of consumers across Australia that have relied upon our services in the past, to bring these issues before the Senate Joint Committee and hopefully to stimulate debate in that area.

Following is RECA's response as per the Committee's Terms of Reference:

## **RECOMMENDATIONS:**

RECA recommends that in order to achieve effective regulation in the Property And Financial Investment Advice ("PAFIA") sector that a **National Consumer Protection Agency** and **National Consumer Taskforce Unit** be established immediately to best serve the interest of consumers, the financial market and the honest industry traders.

### **Recommendation 1**

Legislative provisions are made to form a permanent National Consumer Protection Agency ("NCPA"), to prevent the conflict of interest barriers in agency handling of complaints.

- a. All consumer complaint files relating to the PAFIA industry be immediately removed from ASIC offices and vaults, ACCC office and all other agencies who received these files, as a matter of urgency.
- b. The referred to above files, be immediately placed in storage, in the care of an independent guardian, as custodian representatives of consumers.
- c. A National Consumers Taskforce Unit is created to give consumers independent representation of their interests in the PAFIA sector.
- d. All consumer complaints against PAFIA traders received since 1998, be properly re-examined and re-assessed by an independent consumer dedicated taskforce.
- e. Parliamentarians, in good conscience, acknowledge the identification of the PAFIA traders' activities.
- f. Funding allocations for a National Consumer Taskforce Unit, independent of existing industry influences.
- g. Funding allocations for preparation of cases in relation to existing compensation provisions of Corporations Law.
- h. Funding for counselling of the aggrieved.

### **Recommendation 2**

A Royal Commission be conducted into the regulatory failure to deal with specific consumer complaints in the PAFIA industry.

### **Recommendation 3**

Mechanisms are put in place to minimise industry influence in the handling of consumer complaints for the specific purpose of protecting the interests of honest and efficient industry stakeholders.

### **Recommendation 4**

Abolishment of the practice of industry supervisory bodies handling consumer complaints, other than minor disputes that can be easily and quickly responded to.

### **Recommendation 5**

Open and accountability to be the driving force affecting all areas of legislative reforms in the Financial Services industry and in the creation of the new Consumer Protection regime.

### **Recommendation 6**

The formation of a specific taskforce to scrutinise, question and legally challenge all Prospectuses, Information Memorandums and other instruments of capital raising activities.

### **Recommendation 7**

The current exemptions for solicitors, accountants and "sophisticated" investors are abolished. Rather that these groups are classified as being under active scrutiny by the Taskforce as a temporary measure. Provisions could then be considered for discretionary powers being utilised, as opposed to blanket exemptions.

### **Recommendation 8**

Super Choice to be placed on hold until the above mechanisms are in place, to ensure proper complaint handling procedures as suggested by the Wallis Committee of 1997.

# SUMMARY of ISSUES

## RECA SUBMISSION February 2005:

### Senate Inquiry into regulation of Property Investment Advice

1. CONSUMER PROTECTION: Current Consumer Protection legislative provisions ought to have protected the very class of people who have suffered the most losses – vulnerable unsophisticated investors. Failure to correctly identify the activities of property investment advisers and their links with members of the financial planning industry has been the root cause of an escalation in property and finance investment advice scams.
2. PROPERTY INVESTMENT ADVICE: Investment strategies, wrapped in a financial advice package, created a monster industry resulting in significant consumer losses, culminating in hundreds of complaints from all over the nation. Consumers expected regulatory control. Property Investment Advice has become a growth industry causing all consumer agencies to consider remedies, creating logistical headaches for departmental chiefs.
3. LEGISLATIVE EFFECTS: Regulatory responsibilities of the administration and enforcement of Financial Services licensing and compliance should not have been bundled with consumer protection responsibilities and given to one agency. It is the potential for regulatory conflict of interest that places consumers in the gravest of danger of not having their complaints properly dealt with.
4. PLAYERS IDENTIFIED: Property, investment, finance and advice are inextricably intertwined within a complex array of financial products, corporate structures and commission driven sales executives. No reputable financial planner would have ever chosen to place all of their client's funds into one asset class and particularly into high-risk ventures and financial products, dressed up as 'low-risk'. Yet, financial planners, valuers, accountants, solicitors used existing industry integrity as a key platform to market undesirable financial products firmly linked into the property market. The product was ADVICE and financial strategies.
5. COLLUSIVE CORPORATE STRUCTURES: Property is used as a facility to generate business in the financial markets by unscrupulous professionals, in a collusive network of licensed and unlicensed operators to entice unsophisticated vulnerable consumers into using all their major assets for investment purposes, by concealing the risk.
6. PRODUCTS SOLD AS STRATEGIES: Strategies on property and securities were simultaneously used to lure consumers into high-risk ventures, using both home equity and their superannuation funds via DIY packages. Planners and their legal advisers developed Education Courses, teaching management of financial risk strategies to produce *sophisticated* investors. The intention to deceive is clear: control of punters' assets. Consumers were given material to suggest that all of the products on offer by the licensed players in the network were safe and secure: risk-free. Lender-Consumer complaint files delivered to ASIC show that securities on offer relating to property, were in fact non-existent. There is an alarming amount of evidence to suggest that Buyer- Consumers thought they were purchasing a strategy to better their financial future. Those we interviewed never expected to be forced into the settlement of a property, and consequently thrown into the process of losing their home.
7. INVESTMENT ADVICE ADVERTISING: Advertisements are a crime scene.
8. SPRUIKERS: The PAFIA introducers/spruikers are the key component of a scam designed to lure unsophisticated investors into the hands of linked associates of the Financial and Investment Advice profession. Spruikers are sometimes former real estate agents with current licenses. I would argue that former careers are irrelevant to these arguments. None of the players we have identified were using a real estate licence in any way that suggested the normal course of activity which falls under state-based laws. Similarly, solicitors involved in these activities are

acting as financial advisers using “exemptions” of Corporations Law to avoid scrutiny of their business dealings linked to the spruikers and developers.

9. CONSUMERS: It is men who suffer the most from the consequences of white-collar crime. Our RECA volunteers and myself speak to the widows of those who suicided. We speak to the ordinary folk who suffered the financial loss. We understand the upheaval, the stress, but we speak to them in their homes and we read all of their documents and seek competent legal advice. There is no counselling available for these people. Communities who have assisted us are disappointed with the apparent lack of consumer protection in the area of financial investment advice.
10. CONDUCT AT POINT OF SALE: Property/Finance Advice scams deceived the regulators as well as consumers, yet consumers have had to pay the highest possible price for this folly.
11. LICENSING ISSUES: Consumers believe the interests of the licensed or unlicensed villains were being served ahead of their interests as taxpayers. Victims have experienced, first hand the ill-conceived consumer protection service and the lack of enforcement of law. In 1997, the Wallis Committee warned that if a regulator assisted both licensee and consumer, a conflict of interest could develop. The committee suggested a review be undertaken. This occurred in 2000 and the results failed to identify the overall problem.
12. HISTORIC ISSUES: Two-Tiered Marketing of the mid nineties is slightly different in format to today's model. The resultant financial loss is the same. Historically these scams have been prevalent in various forms for the past three decades.
13. IDENTIFICATION OF SCAM MODELS: Risk-taking strategies developed for the express purpose of cheating ordinary citizens out of their homes and retirement funds, has become a growth industry due to its label. I argue that the incorrect identification and proper assessment by ASIC of these activities, has become the lynchpin of why these corporate businesses flourished and why the magnitude of the losses has already escalated into the billions of dollars as we continue to discover funds at risk. Correct identification of the model in 1999, ought to have led to immediate regulatory action to close down PAFIA corporations, together with all subsidiaries and linked providers. (*attachment H: The Model of Deceit*)
14. ASIC'S POWER AS REGULATOR OF FINANCIAL SERVICES: ASIC as corporate regulator of securities and investment advice, financial services, financial products, financial advice, and credit providers has been unable to provide the necessary activities for legitimate consumer protection. The reasons for this apparent and overall regulatory inertia are varied and given the magnitude of the losses, the proliferation of these known and often discussed, shallow business practices in the finance, banking and property sector, consumer protection has reached crisis point where regulatory control of any description is now sailing rudderless through muddy waters. Market Integrity and Consumer Protection in the area of financial advice and services, fall directly under the responsibility of ASIC.
15. LEGAL ISSUES: Consumers given *misleading information* in relation to high-risk investments, whilst being assured they were “low-risk.” Consumers were misled that Education Courses or Information Memorandums and Prospectuses were ASIC approved. *False and misleading* advertisements identified the selling of financial ADVICE, the use of financial strategies as a link to the use of property strategies. *Unconscionable conduct* has become the norm as people are targeted in order for advisers to gain control of superannuation dollars and home equity. Planners engaged spruikers to bring the clients to the financial planning profession for financial services and strategies. *Day-to-Day control* of the funds lay with the trustees of the trusts that lead to 100% losses. The product being marketed has been ADVICE on *management of financial risk strategies*. Evidence of intention to defraud abounds in the consumer complaint files. Whether someone is a former real estate agent or former policeman is irrelevant. Property was merely used as a facility to obtain maximum control and use of other people's money, by engaging in *misleading and deceptive conduct*. These scam activities were specifically designed to deceive vulnerable members of the public, by deeming people to be *sophisticated investors* when clearly they are *unsophisticated vulnerable*

consumers. The PONZI has reached the fifth level where billions of dollars have been stolen and now the stakes are higher. Lawyers are involved in supplying legal advice to enable a collusive network of fraudulent traders to continue with these activities. Unconscionable contracts have been used as the tool of trade. Lawyers and accountants abused the *exemptions* offered by ASIC. The collusive nature of these scams identifies the magnitude of the problem. ASIC had a duty to pursue *compensation* on behalf of consumers. These provisions have clearly been ignored.

16. ACCC: Failure to identify the damaging consequences of these identifiable corporate links has created an overlay of responsibilities, rather than the suggested "gap." Consumers have had to suffer inappropriate "jurisdictional" juggling, whilst being passed back and forth to the sister regulators. ACCC resources were continually being called upon to contact confused consumers stating "*it is ASIC's jurisdiction.*" In turn RECA had to deal with inquiries at this level. My view is that consumer protection should have remained the responsibility of the ACCC in 1998. The wide powers given and the broad interpretation policies spoken of in 1996, ought to have been vested in the ACCC. Consumer protection is more likely to be effective in a fair, honest and competitive market-place.
17. APRA should have been advised by ASIC of the involvement of the non-banking institutions and insurance companies regarding the use of fake deposit bonds. Consumers have no information as to the secrecy surrounding these advisory activities and intended "swapping" of information in the consumers' best interests.
18. COMPETITION: Market competition has been placed at risk due to the uncompetitive behaviour of these spruiker/financial planning/advisory networks and their solicitor partners. Regulation in the PAFIA sector depended upon all operators acting efficiently, honestly and fairly.
19. CONSUMER COMPLAINTS: Consumer complaint files reveal the truth of our assertions. Consumers sought professional advice specifically relating to the management of financial risk, from those whom they believed were licensed. The "*ASIC Approved*" promotions from several spruikers, led people to an agency whom they had not heard of prior to their signing for the education courses. The courses were the "bait" to lure people into revealing their personal financial net worth. From there, consumers were channelled to "experts" for professional and personal risk management strategies. These files lay dormant in ASIC offices in each state. If investigations are now underway we would challenge why it has taken five years to receive an appropriate interpretation of jurisdictional issues, knowing the grave danger that vulnerable consumers faced when attending these seminars and replying to "financial strategies" advertisements.
20. INDUSTRY DISPUTE RESOLUTIONS: In my experience, complaints to FICS and the FPA have addressed none of these issues in a manner likely to produce warnings of shortcomings within their own ranks. Nor have we seen these industry based groups raise the issues that we are raising. Serious consumer complaints alleging fraudulent activities should not be considered as a "dispute" between two parties. ADR's suggest a mild disagreement between consumer and trader, a softening of irreconcilable difficulties. The types of issues RECA has been raising for a number of years are far removed from the capabilities of those industry groups to respond.
21. FEDERAL GOVERNMENT AND IOSCO: I have sought information as to whether other nations have been given information relating to the PAFIA Traders here in Australia and their global activities and movements.
22. CONSULTATION – INDUSTRY AND CONSUMER GROUPS: A clear lack of statistical analysis from the regulator responsible for the complaint files has created a new wave of misinformation from industry groups, as to the actual cause of these activities. From a grass roots perspective, there has been a distinct lack of consumer home consultation in all areas of governmental processes whose role is consumer protection.
23. MARKET INTEGRITY: Of even greater concern is the overall neglect of the issue of market integrity. There can be no effective consumer protection, if market

integrity is compromised. Both of these issues fall directly under the responsibility of ASIC.

24. STATISTICS: We are disturbed at the lack of statistical data or correct acknowledgment of the magnitude of the losses currently known or for the potential for future loss. There are no formal assessments of the likelihood of ongoing capital raising activities by known offenders.
25. LAW ENFORCEMENT AND FRAUD: Property advice is freely available from real estate offices. Consumers paid for lessons on investment advice, specifically personal financial advice in relation to management of financial risk. I believe I am able to provide the Senate, if required, evidence of what I believe to be fraudulent activity: the intention to deceive and conspiracy to defraud consumers.
26. NATIONAL APPROACH to Consumer Protection: The written advice given to consumers by the Australian Securities and Investment Commission ("ASIC") during the past seven years, has not only proven disastrous for consumers' financial well-being, but created a dream ride for the villains responsible for the activities which have become the subject of this inquiry. The dilemma presented in the PAFIA sector should be dealt with as a bi-partisan approach to consumer protection. It is on the Parliamentary agenda because the mechanism for safety of advice to consumers in matters relating to finance, financial products, financial services, whether in property, investments and all forms of financial securities, has inextricably broken down.
27. COMPENSATION: As a nation, we cannot turn back the clock. However, we can undo some of the damage. We can as a nation, compensate the victims, as should have occurred under the provisions set down in the ASIC Act 2001.
28. SUPER CHOICE: If ASIC officers are stating publicly that they are nervous about Super Choice on 1 July 2005, then we should be all listening. The Wallis Report suggested that de-regulation in the superannuation market should only occur if consumer protection mechanisms are working well and we have strong enforcement of law policies.



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**Consumer Association Inc**

**SUBMISSION**

**SENATE JOINT COMMITTEE  
CORPORATIONS AND FINANCIAL  
SERVICES**

INQUIRY INTO REGULATION OF:

**PROPERTY INVESTMENT ADVICE**

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**FEBRUARY 26<sup>th</sup>, 2005**

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## ACRONYMS:

|       |                                                 |
|-------|-------------------------------------------------|
| ACCC  | Australian Competition and Consumer Commission  |
| ADR   | Alternative Dispute Resolution                  |
| APRA  | Australian Prudential Regulation Authority      |
| ASIC  | Australian Securities and Investment Commission |
| ATO   | Australian Taxation Office                      |
| CCAAC | Commonwealth Consumer Affairs Advisory Council  |
| IM's  | Information Memorandums                         |
| LVR   | Loan to Value Ratio                             |
| PAFIA | Property And Finance Investment Advice          |
| SRE   | Single Responsible Entity                       |

## **INTRODUCTION:**

Proof of the effectiveness of any legislation ought to be measured in terms of the consequences born by those whom the provisions intended to protect: ie, the consumer.

To separate property from finance is inconsistent with the interpretation of existing law.

For this reason, RECA felt compelled to obtain three Legal Opinions as to ASIC's jurisdictional powers over property and finance investment advice cases.

Opinions were given freely in the interests of consumer protection. The law firms contributed on the basis of a community effort to clarify these issues for consumers.

RECA has identified numerous incidences, across all States and Territories, where spruikers or introducers, licensed or unlicensed, linked to AFS licence holders, are using property as a facility to promote financial products.

I have personally conducted extensive investigations during the past seven years, into the activities of PAFIA traders. I have worked closely with author Neil Jenman, during the past three years, on his detailed research into the "Spruiker" phenomenon in Australia.

Our combined efforts have been centred upon consumer files, dealing with these activities from a grass-roots perspective. Jenman understands the model from the consumer perspective, better than any other person in Australia. In particular he understands the impact these scams have had upon other people's lives.

Jenman assisted Four Corners with vital information in April 2003, enabling the ABC to completely expose the nature of the education courses. The subsequent programme named "Tall Stories," holds considerable historical significance.

Suspect traders have raised billions of dollars of retails funds from unsuspecting consumers, creating a fifth level PONZI.

Our research shows that financial traders deliberately and maliciously target unsophisticated 'mum and dad' investors, urged on by "introducers," to seek "professional" advice from licensed planners. Joining the corporate dots easily identifies conflicts of interests between the linked providers of these financial services and products.

## **RECA findings include but are not limited to:-**

### **1. Preliminary findings:-**

- 1.1 Enticement of consumers into sham education courses as an introduction to financial investment markets.
- 1.2 Property and Finance Investment Advice ("PAFIA") traders gain pre-access to banking and asset details from potential client/victims.
- 1.3 Consumers pay fees of \$3000 - \$10,000 to licensed financial planners for "expert" advice specifically relating to *management of financial advice strategies*.
- 1.4 Consumers are advised to purchase multi - properties as part of that investment advice package, amid claims that *profits will pay for the course and advice fees*.
- 1.5 Debt-generated funding strategies and intertwined financial products create the platform for linked companies to raise capital for commercial ventures.
- 1.6 Consumers are specifically advised the risks are minimal and the beneficiary companies offer protection by way of 'guarantee.'
- 1.7 No guarantees or warranties or insurances are honoured. Broker commissions are not disclosed
- 1.8 Property is merely used as a "facility" to generate interest in seeking financial planning strategies for the express purpose of producing additional income without the associated risks.
- 1.9 Investment advice is more than a key component; rather it has become the catalyst.
- 1.10 Licensed Planners use these strategies to generate billion dollar fund raising activities without risking any of their own offshore holdings.
- 1.11 Unsophisticated investors who harbour a 'yearn to learn' and are prepared to pay for an upmarket education, those with assets, are the prime target of the promoters.
- 1.12 The collusive nature of the PONZI scams is evidenced via links to the beneficiaries of these identifiable racketeering activities.

### **2 consumers relied upon:-**

- 2.1 The integrity of the AFS licence holder who developed the personalised strategies
- 2.2 Network use of ASIC "approved" products, strategies and educational courses.
- 2.3 Risk management and regulatory control as fundamental to the decision-making process, as regularly being assessed by ASIC.
- 2.4 The integrity of the legal profession and the contractual arrangements relating to the offer.

- 2.5 Guarantees and insurances offered by the licence holders.
- 2.6 Deposit Bond strategies; as a method of 'affordability' of the courses and fees.
- 2.7 Credibility of "big name" traders endorsing the facilities on offer and the registration of the financial products on offer.
- 2.8 A false impression of strong regulatory control by ASIC, promoted by PAFIA traders.
- 2.9 ADVICE regarding strategies and products being endorsed by ASIC; as promoted by AFS licensees conducting course lectures.

Consumer protection issues and inappropriate handling of consumer complaints has been reduced to jurisdictional squabbles, flawed regulatory advice, and narrow interpretations of existing statutory powers.

ASIC is the agency out of step with consumers. For these reasons and more, the legal opinions sought by ASIC in 2000, should be made public in the name of open and accountable government.

Fully cognisant of the risk to consumers with regard to all advice delivered to potential investors and the blurring of financial products in terms of definition, ASIC continues to hand out licenses to those who were known to be *unfit* traders.

We allege that ASIC ignored existing legislative provisions contained in the Acts under ASIC's jurisdiction, with regard to consumer protection and market integrity policy.

**ASIC provided exemptions to traders:**

Despite its role as consumer protector, ASIC provided exemptions to traders, which were not as a result of consumer lobbying. Rather they were the result of consistent industry lobbying by PAFIA industry participants.

RECA alleges that ASIC directly or indirectly contributed to activities that are the subject of this Joint Parliamentary Inquiry.

The Parliament, in forming the extensive and powerful provisions in 1998, expected consumer protection to be of world standard, specifically in the area of the PAFIA sector.

ASIC claimed to consumers it had a *lack of resources*, yet contradicted their own position in Parliament on 2<sup>nd</sup> June 2004.

As to whether there are existing legislative "gaps" or regulatory "overlays" has contributed significantly to the alarming increase of consumer complaints regarding licensed and unlicensed entrants into the PAFIA sector, creating an unwelcome growth industry.

The PAFIA industry has become riddled with misleading and deceptive conduct. Directors who engage in these collusive business houses could not reasonably be described as acting efficiently, honestly and fairly.

## In response to the questions asked in the terms of reference:

### (a) LEGISLATION ISSUES

**the effectiveness of current regulation (including the *Trade Practices Act 1974*, the *ASIC Act* and the *Corporations Act 2001*) of the property investment advice industry in protecting consumers;**

#### (a) 1. RECA argues that:

- a) The current statutes: The ASIC Act 2001, Corporations Act 2001 and the Trade Practices Act 1974, all provided specific consumer protection mechanisms that ought to have brought the licensed security dealers and their authorised and unauthorised introducers to justice.
- b) In terms of jurisdiction and consumer interest, ASIC has continually argued in the negative. Our opinions have brought forward the alternative positive arguments, that ASIC did have powers in these circumstances and that they failed to use those powers by taking a narrow interpretation of the Acts referred to: [www.reca.com.au](http://www.reca.com.au).
- c) Existing Regulatory Powers specifically designed for consumer protection in the area of property and investment advice, have yet to be properly tested. I argue that for regulatory effectiveness to be properly tested, hundreds of cases must be adequately assessed, processed and presented to the courts for judgement.
- d) Federal Court judiciary are the appropriate people to examine and determine the effectiveness of legislation. However, the system is dependent upon qualitative investigative work accompanied by expert briefing of cases to be presented.
- e) ASIC cannot be trusted to achieve these aims in a proper manner, due to historical indifference.
- f) ASIC has activated too few cases in response to consumer complaints against licensed members of the financial planning industry and their unlicensed introducers.
- g) RECA has discovered hundreds of complaint response letters from ASIC to consumers during the past five years, relating to PAFIA scams, stating: "*no resources*," or "*not our jurisdiction*." These letters are testimony of the rubber stamp approach to corporate policing, on the part of our Federal regulator.
- h) ASIC has demonstrated a distinct lack of consumer consultation on these issues and an obstructive approach to consumer complaint assessments.
- i) Incorrect identification at assessment level, of the activities carried out by the PAFIA industry and the interlinked financial markets, has been and continues to be, a direct cause of the proliferation of these schemes.
- j) Consumer complaint files show that traders are promoting financial products delivering personal financial advice and life-changing investment strategies.
- k) Real Estate agents involved in the PAFIA industry are in the minority, are mostly operating outside the "norm" of real estate business activities as former agents, and are not identified as the "ringleaders" of the PAFIA circuit.
- l) Financial Planners, solicitors and accountants are the main prime movers of the PAFIA industry, using introducers who are from all walks of life and careers: former bankers, teachers, police officers, real estate agents, domestic engineers.
  - a. The former occupation of the planners and introducers, as company directors of 'empires of evil', is irrelevant for the purpose of this Inquiry.

- m) ASIC had an identifiable potential for conflict of interest, as identified in the 1997 Wallis Report, due to a dual role in looking after the interests of industry vs consumers in conflict.
- n) RECA alleges that the content of the 1999 ASIC Review of FSR was self-effacing and untruthful as to the non-identification of PAFIA practitioners, placing future consumers in the path of significant risk of loss and financial well-being.
- o) To separate property from finance in PAFIA activities is inconsistent with the original intention of the current legislation: consumer protection and market integrity in the financial products and services industry.
- p) The collusive nature of these PONZI scams have revealed a common thread: financial planners, solicitors, lawyers, accountants, valuers, brokers, credit providers and non-banking institutions have all contributed to the formation of the PAFIA activities to the detriment of consumers.
- q) RECA argues that the PAFIA Traders, behave in a predatory fashion towards unsophisticated investors by advising them to channel home equity and superannuation savings into risky financial investment products and services.
- r) ASIC, cognisant of these occurrences, continually demonstrated little regard for consumer's financial safety over a long and sustained period of time. Regulatory behaviour produced the poor assessment syndrome, ignoring the following legislative provisions currently available to the agency: -
- s) Licensed security dealers assisted the advancement of the scams, by providing "*management of financial risk strategies*" to vulnerable consumers.
- t) Consumers were left with no *day-to-day control* of their investments.
- u) *False and misleading statements* were made both in the spruiker seminars, at point of sign-up, and in material and brochures provided as inducements.
- v) Evidence of *misleading and deceptive conduct* and *unconscionable conduct*, by all interlinked licensed providers, has been gathered by ASIC since 1995.
- w) Evidence of *linked credit providers* being used as part of the process of the PONZI scams, as revealed in 1997.
- x) Evidence of property and financial products being used in *money laundering* operations in the late 1980's.
- y) Due to the complexities of some of the world-wide PONZI activities, legislators viewed the creative mind of the PAFIA operators as foreseeable and provided legislative wording to suggest: "*and or any thing.*"

**(a) 2. If, as ASIC has argued for seven years, they do not have powers to prosecute these cases, then as consumer protector, they had a specific duty to:-**

- a. Advise Parliament via the Minister, to amend the Act by changing a definition, (since the "specific exemptions" did not include property), if that was their honest belief.
- b. Bring the activities to the attention of the public with large advertisements and issuing widespread public warnings of the known consequences in dealing with the PAFIA industry.
- c. Do all manner of things to effectively protect consumer interests.
- d. Advise all other relevant agencies and inter-related industry bodies of all pernicious practices contained in the consumer complaint files, in order to preserve market integrity.
- e. Recommend that the banking Ombudsman examine the complaint files regarding the inter-related banking activities in these areas.



- f. Recommend that APRA examine all consumer complaint files the insurance and deposit bond activities related to the PONZI activities
- g. Recommend that ACCC examine all consumer complaint files regarding all advertisements that contained false and misleading statements.
- h. Recommend that ATO examine all consumer complaint files regarding all activities of the identified companies.
- i. Recommend that the AFP examine all consumer complaint files regarding alleged fraudulent nature and the money-laundering aspects of the scams.
- j. Hold the accounting profession accountable for their member activities with regard to audits and trust accounts.
- k. Warn the Prime Minister and the Treasurer of the effect of these PONZI's regarding known overseas business activities of the main offenders.
- l. Notify IOSCO and relevant member agencies, of the problems associated with regulatory control of the PAFIA industry and identification of the main suspects who regularly travel overseas, as part of a Global monitoring process.
- m. Explain to Parliament, through the Minister, all matters that are considered to be of extreme importance to consumer protection and market integrity.

All of the above ought to have been executed in a timely and appropriate manner with a high degree of urgency. Had ASIC either used current powers as we have suggested, or conversely, taken the above steps; we as a nation, would not be facing the escalation in complaints, the escalation in inappropriate DIY superannuation activities and the magnitude of reported losses that perhaps as many as one hundred thousand ordinary citizens are now facing.

If ASIC had taken the above steps, an estimated 100,000 citizens of other nations, perhaps could have been spared the same fate.

Inappropriate handling of consumer complaints has led to the PAFIA industry becoming a growth industry, inhabited by those who could not reasonably be expected to pass the *fit and proper* test.

**(a) 3. ASIC in effect, has compounded investor losses by its continued refusal to:-**

- I. Provide consumers with the legal opinions sought by ASIC in 2000, on the issue of property and investment advice traders
- II. Consult with "grass-root" consumer groups on the same level of service as given to industry bodies.
- III. Validate warnings from consumer and industry bodies, and MPs.
- IV. Properly brief the Minister on the true nature of the PONZI scams.

Support group activity is a key indicator of regulatory failure. During the past eight years, RECA has been engaged in gathering evidence against not only the villains in the PAFIA industry, but also dealing with regulatory tolerance of these practices to the point of taking on the task of the regulator.

This situation cannot sustain. The traders are the only beneficiaries of this regulatory impasse.

All states are affected by this problem, hence the inquiry. Legislative change, without acknowledgment of the fundamental breakdown in corporate law enforcement, will only add to the current consumer crisis.

(a) 4. **Our arguments are based upon the evidence gathered from consumers; that ASIC's determination to separate property from finance, whether directly or indirectly, caused :-**

- 1) Failure in their duty to fully protect consumer clients
- 2) Failure to place the interests of consumers ahead of PAFIA traders.
- 3) Failure to correctly identify the linked activities of PAFIA traders.
- 4) Failure to uncover the inter-linked activities of the security dealer licensed providers.
- 5) Failure to fully investigate the linked activities of the professionals who entered into the PAFIA sector, as authorised representatives.
- 6) Failure to use available powers to close down these identifiable businesses.
- 7) Failure to control the advice delivered by the members of the PAFIA consortiums.
- 8) Failure to challenge the directorships of those who traded in the PAFIA industry.
- 9) Failure to bring charges against/prosecute, the worst offenders, despite legislative provisions currently available.
- 10) Failure to stop the problem escalating and to do all things possible to stop the conduct, in terms of the selling of risky financial products to unsophisticated vulnerable consumers.
- 11) Failure to identify the risk and warn consumers in a timely manner.
- 12) Failure to recommend effective legislative change where they believed a weakening in remedy may apply.
- 13) Failure to seek remedies of compensation for affected consumers under existing law.
- 14) Failure to assist consumers in grouping together in terms of providing a user-friendly consumer service.
- 15) Failure to conduct appropriate interviews of consumer complainants
- 16) Failure to reign in the conduct of traders in the PAFIA.
- 17) Failure to recognise the consequences of regulatory neglect, in terms of future consumers who would most likely be enticed into the identifiable market.
- 18) Failure to bring to the Parliament's attention the existence of internal reports suggesting identifiable and known breaches of all of the relevant Acts under ASIC's jurisdiction.
- 19) Failure to supervise audits and the conduct of the SRE's.

(a) 5. **RECA maintains that the current legislation can only be properly tested if:**

- I. The assessment of complaints is of a high standard.
- II. The potential for manipulation and interference is diminished.
- III. All serious cases are placed before the judiciary.
- IV. The potential for conflict of interest within the regulatory agency is removed.

The Federal Regulator, despite its seven years of claims to the contrary, has failed its duty in the area of consumer protection and the corresponding area of market integrity.

**(a) 6. We further argue that: -**

- A. ASIC has wrongly claimed: "*constitutional*" reasons for inaction.
- B. The current regulations have never been properly tested in a court of law, given the number of key traders who entered the PAFIA industry: -
- C. Consumer Compensation legislative provisions remain relatively untested.
- D. Misinformation sent to the consumer complainants suggesting: "*no jurisdiction,*" "*no resources,*" and "*no investigations at this stage.*"
- E. Obstructive regulatory conduct in failing to assist consumers with basic information.
- F. Providing statistical advice to MCCA, which is inconsistent with our own research.
- G. Providing exemptions to current laws, likely to cause grief to consumers.
- H. Consumers paid the highest price for these alleged regulatory failures.
- I. ASIC generally behaved in a secretive fashion using "*confidentiality*" in a manner likely to cause further loss.

Losses could climb towards \$5 billion over the next two years as the doubling effect takes hold, as further evidence of all of the above.

**(a) 7. Legislators did not expect:-**

- a. Lobbying by industry groups to bring about exemptions to the very class of people who were the prime movers of these scams.
- b. Legislative changes by definition, flawed interpretations, or exemptions, which contradicted the original intention of these, Acts, demonstrating little regard for consumer protection issues. *Eg: "exemptions for sophisticated investors."*
- c. The federal regulator to ignore, intentionally or by default, the fundamental principle of market integrity relationship to consumer protection issues.

Consumers feel significantly let down by regulators, evidenced by their letters of mistrust of the regulatory system to various Parliamentarians. Consumers view ASIC's assessment of claims, as a process to search for legislative "loopholes."

RECA holds grave concerns that due to the fact that the PONZI has now reached its *fifth level* of operation and failure to acknowledge these activities and to prosecute under existing law, or provide tighter legislative controls for the future, will cause even greater financial loss to consumers.

ASIC's lack of delivery of a competent consumer service left RECA with no choice but to seek advice from solicitor firms who would assist us with appropriate clarification of ASIC's considerable powers in this area. RECA has provided those opinions for the benefit of the Senate Inquiry. (*attachment D: Legal Opinions*)

## **CONDUCT**

### **(b) Allegations that property investment advisers engage in behaviour including:-**

#### ***i. Characterisation of their activities (for instance, as "education seminars") in order to avoid regulation;***

As an overall analysis of the PAFIA activities, it is clearly the case that Financial Planners and their legal advisers used spruikers and introducers to gather people together in city based Spruiker Seminars.

### **(b) 1. Key elements of conduct and behaviour**

- a. Initially, the PONZI starts with a complex corporate structure. A series of at least 20 companies are registered with ASIC. The words *finance, investment, financial advisers* or *financial services* are generally used in the names of the key advice companies.
- b. We have found registered financial services company names being intentionally registered and subsequently used to deceive consumers, without the benefit of and AFS licence or authority.
- c. ASIC permits words like *"finance, financial services, investment or mortgages"* to be registered by company directors who were not holders of AFS licences, yet whose sole purpose was to deal in the financial services market as key advisory companies.
- d. Several of the companies we identified, operated under an AFS licence and appropriate authorisation, whilst others did not.
- e. Spruikers often use the word *institution* in their registered company names, again used as credibility tools to wrongly imply that education courses would provide credits for University and TAFE.
- f. The "Group" structure involves a number of professionals: security dealers, financial planners, solicitors, accountants, spruikers and introducers. The intention is for all PAFIA directors to feed from the databases gained at the seminars, as a major source of their businesses.

### **(b) 2. Characterisation of the CONDUCT of the PAFIA traders:-**

**Spruiker Seminars:** are used as a tool to lure unsuspecting consumers to a *free information night*. The use of expensive *free* tickets is a usual trademark.

**Databases:** Massive databases link companies in the group structure and contain personal asset details of potential "clientele" targets.

**Misleading methods of persuasion:** *"our professionals can teach you how to set up companies, tax minimisation, share trading, investment strategies, how to use other people's money, how to buy property with no money down, use of options to pay for the course, the course will cost you nothing, etc, expert financial advice, products and services, guarantees and insurances, government watchdog protection, a one stop shop."*

**Tax and Financial Advice:** Licensed AFS holders provide advice on how to use tax effective planning strategies, multiple purchase strategies, mezzanine finance and multiple income stream strategies.

**ASIC:** Liberal use of the word "ASIC" is prevalent by all members of the PAFIA group.

**Targeting Unsophisticated Investors:** Wealth strategies promoted to entice those who are prepared to pay for expensive education, regarding investment, money and finance.

**Risks:** Investment advice on high-risk securities promoted as low risk.

**Fear tactics:** Traders suggest that equity in your home is a *dead money strategy, as a road to poverty*. DIY strategies, superannuation plans are all used to entice consumers to invest their home in off-the-plan apartments as temporary buyers, mezzanine lending and joint venture pooled mortgage funds.

**Banks and Brokers:** Consumers enticed to use Group credit facilities, or linked credit providers, to pay exorbitant fees for "tuition."

**High-pressure tactics:** Consumers are urged to sign up immediately - reduced pricing for investments packages.

**Worthless guarantees and warranties:** Fear tactics and high-pressure techniques are the norm along with worthless investment and rental guarantees.

**Group related Lecturers:** Financial Planners and accountants and lawyers become the inter-linked lecturers at the courses, to add credibility to the business.

**Secret commissions:** Evidence of secret corporate links and commissions would be obvious to a trained investigator.

**Credit Cards** for course fees and deposit bonds: Clients are given personalised strategies to entice attendees into using credit cards, creating further debt for those who were employed or unemployed.

**False Market Predictions:** that profits from recommended security investments would cover the cost of the course within short period of time if the advised financial strategies are adopted.

**Deposit Bonds scams:** Linked insurance companies provided further twists to the arrangement of purchasing 5-6 properties on options, as per the consumer funded financial advice ON the management of financial risk strategies.

**Relationships of Trust:** The AFS licence holders are on hand to ensure the client suspects nothing from the original courses. Relationships are built into the program. Consumers believe they are actually purchasing a financial strategy and are being shown high-tech risk management techniques by "experts" licensed with ASIC.

**Network:** The group network is structured to ensure that conflicts of interests are difficult to identify, until after the consumer funds have disappeared.

**Financial products and services links:** Financial Advisers arrange all relevant documentation for lenders and buyers and joint venture victims.

**Information Memorandums:** Everyone in the "Group" is feeding from the consumer carcass. Consumers, who have assets to invest, are channelled into Information Memorandum and Mezzanine Mortgage scams, touted as "securities."

**Options To Purchase:** Those who have home equity assets are channelled into "options" to purchase as a temporary strategy, using interlinked loans to immediately raise 20% deposits. Those funds then disappear.

**False promises:** that the “options” or “purchases” will be purchased by genuine buyers prior to settlement.

**Unconscionable Contracts:** Contracts drawn up by the PAFIA legal advisers, state that the asset cannot be on-sold and secrecy is paramount via confidentiality clauses. These clauses and conditions demonstrate *unconscionable conduct* on the part of the financial and legal advisers.

**Solicitors:** Lawyers prepare the contracts in a manner that fits in with the overall operation of the PAFIA traders. Some law firms are co-directors of the actual development projects and/or are beneficiaries of loan monies.

**Developers:** Developers are linked to the rest of the group and at times the planner is found to be the undisclosed beneficiary of the development loan monies.

**Disclosure issues:** Consumers are unaware of any of the above until it is too late to recover funds.

**Credit Providers:** have been profiteering from the PAFIA industry, via dishonest brokers who are not known to consumers.

**The Sting:** The security on offer, often turns out to be non-existent, the financial planner has moved, existing phone lines are terminated and the group structure has collapsed.

**Collapse and re-boot:** The PAFIA traders regroup and re-invent the process using variations of the above and a new front line of company structures.

**The PONZI effect:** Monies are channelled from one investor and used for the servicing of debt to another, via a variety of projects as the PONZI increases.

**The Players:** The introducers come from all walks of life. Former, policemen, bankers, brokers were engaged as introducers or partners. A person's previous career had no bearing on the actual transactions that took place other than knowledge of an industry.

**Consumer Victims:** come from all walks of life, including agents, policemen, teachers, directors etc.

**Valuations:** Traders had to have known the over-valuation of the properties – ie the nature of the PONZI, to suggest a “discount” purchase and profit and pay fees for education strategy.

**Collusion:** Case files contain evidence to show that licensed and unlicensed commission-driven traders worked as a collusive unit to deceive consumers.

**Conspiracy to defraud:** by the recommendation of placing all available funds into one asset class: specifically financial products attached to property.

**“ASIC” Approved:** Licensed PAFIA traders compounded the spruiker misleading statements by advising consumers that these products and services were approved by ASIC.

On occasions, consumers were advised to become a lender, a buyer and a joint venture partner on the same development. These were classic files for ASIC to pursue. As several victims have stated: *“we trusted the experts. How can we walk down to the shopping centre and lose our home?”*

Consumers trusted the licensing system. Understandably consumers expressed feelings of being deceived by both the advisers and ASIC. We understand those frustrations.

Cleverly constructed 'empires of evil', were designed to steal people's homes and superannuation funds causing endemic losses for vulnerable consumers.

The conduct is covered by the relevant legislation listed in the introduction. ASIC is the designated consumer protector and failed to properly identify this conduct in the financial services industry and the obvious linking of property investment advice strategies, financial products and services, management of financial risks, promoted in sham education courses.

**(b) ii *habitual use of high pressure selling techniques in order to induce investment decisions;***

Considerable evidence exists in consumer files of the high pressure tactics used in the initial seminars, and again in the courses. Further courses and linked financial products, are promoted on the 'one-on-one' counselling provided by financial planning subsidiary companies.

Decisions are made on the basis of "fear" techniques, including sleep deprivation camps in some cases. Financial Planners provided specific advice, again using similar fear-driven techniques with regard to retirement, planning and superannuation.

PAFIA Traders bombard consumers with their knowledge of money and finance. The Spruiker campaigns are specifically geared to convince consumers to seek advice from linked licensed financial planners. An elaborate structure of secret commissions created the environment for the PONZI scams to gain momentum.

The Treasurer's warnings regarding "responsible saving for retirement" is used as a convenient selling tool at the education courses. The retirement strategies are in fact the product on offer.

**(b) iii *failure to disclose interests they may have in properties they are selling;***

Our investigations revealed wide instances of "options to purchase" on multiple properties from linked developers. Failure to disclose conflicts of interest in development properties between spruikers, introducers, financial planners, lawyers and accountants, is rife.

Consumers are told: "*our lawyers have gone over these contracts and you (the client) benefit from all of our "due diligence."*" The Group related companies were not made known to consumers.

Companies are often structured to collapse within a three-year period. Consumers, who are coaxed into anything below the first ranking, unknowingly risk 100% capital loss, plus anticipated, and budgeted for, income. It is a cruel fate.

**(b) iv *failure to disclose commissions and fees associated with their services; and***

Evidence of secret commissions has emerged as the case file stories gain media exposure. The links are easy for investigators to follow. Most of the links are exposed by a quick search of ASIC's databases.

Often former Spruiker and Planner staff members are the best source of information as to the flow of funds and activities.

All of the activities we have examined are based upon deceit.

These activities are not simply a case of "inappropriate disclosure." The recommendations supplied to consumers as a specific financial strategy attract fees ranging from \$3000-\$10,000, payable to the Financial Adviser. Consumers think they are hiring experienced and expensive ADVICE. Advisers' fees are charged in addition to those paid for the courses. Course fees range from \$5000 to \$50,000.

***(b) v failure to provide appropriate disclosure of downside risk associated with the property or financial products they recommend;***

Deception is required in order to convince consumers to place their funds into high-risk financial strategies, promoted as "low-risk." The Traders will say: *"Yes, of course we guarantee them low risk investments - it's the only way it works. If you told consumers the strategies/packages were high risk they would never say yes. The same applies to the valuations"*

Consumer files that we have researched show a complete failure to provide consumers with adequate and accurate information regarding the downside of risks. PAFIA traders offered worthless guarantees on pooled mortgage investments, joint ventures, commercial projects; "Martian landing pads", wine investments, car investments, share trading, tax advice, property: CBD Units, house and land packages, mezzanine financial products, promissory notes, unregistered caveats and unsecured notes.

We have found instances whereby consumers were promised first mortgage security and received only a receipt as "documentation."

Allegations most common: fake valuations, fake asset and liability statements, fake pre-sale registers and fake security documentation. We have even uncovered the use of fake stamp duty stamps and fake loan applications presented to non-banking institutions.

We have also witnessed people under pressure from conversion fo registered securities into worthless shares, as recommended by the financial planner. Fear of loss is used as the main tool of persuasion.

As the PONZI climbs to the fifth level, the scammers have become more desperate. ASIC Annual reports show an annual average of ten prosecutions or less, per state from an average of 10,000 overall consumer complaints.

PAFIA traders have therefore developed a cavalier attitude to law and order.



## SELLING STRATEGIES: property and finance mix

- (c) **Whether it is appropriate for property investment advisers to simultaneously sell an interest in property and financial products enabling such purchases;**

PAFIA Traders often have multiple licenses.

**(c) 1. Correct identification of the product on offer is a key factor in understanding consumer interests.**

**The product on sale is defined as follows:-**

- a. The products on offer were "*management of financial risk*," incorporating retirement strategies and use of superannuation funds in terms of investment advice.
- b. Strategies included advice from accountants regarding DIY strategies resulting in a 45% increase in the use of these plans.
- c. Consumers who paid \$20,000 for educational material, particularly for earlier spruiker driven courses, signed contracts to learn about financial strategies to increase retirement funds. Such was the nature of the promotions.
- d. The Treasurer often spoke of a need for citizens to adopt a more responsible approach in planning for retirement from an early age. This point was widely used by the spruikers and the PAFIA traders who delivered the lectures.
- e. Responsible consumers, many were families, took time away from work to attend courses and went into serious debt in order to pay for the education on offer.
- f. The lectures are delivered by professional lawyers, accountants planners who deliver materials and personal advice on shares, the stock exchange, various securities and insurance products, tax advice and commercial ventures using family funds.
- g. Consumers believed they were acting as responsible citizens paying for additional courses to learn about a variety of strategies. Their aim was to improve their own financial well-being and security. Many of the people, I have personally met, were families who had already purchased property and knew that property advice was free of charge.
- h. Fear of not knowing enough about money and finance, fear of financial illiteracy were the key drivers of selling these type of courses.
- i. Education courses rely upon professional speakers. Their target is specifically people who have equity in their homes and/or superannuation and savings.
- j. The product on sale is financial literacy schooling, as delivered by the licensed financial "experts."
- k. Spruiking occurs during course classes, after assets are revealed and personal advice sought.
- l. Continual subliminal messages delivered by the PAFIA advisers, seal the fate of the consumer/victims.

**(C) 2. "Property Investment Advisers" is a recent regulatory creation.**

- a. ASIC, for whatever the reason, has consistently attempted to separate property from finance in these particular cases as though the victims were people purchasing property.
- b. That is entirely a misrepresentation of the facts. To create a picture of "property advice" as if it can be separated and stand alone, is clearly wrong. Our legal opinions explain the correct determination and identification of the products offered for sale.

- c. Prior to sign up, some attendees rang ASIC and NTIS to verify the validity of these courses. ASIC appeared to endorse the process by its failure to warn consumers who bothered to make inquiries. This point has angered many of the victims.
- d. PONZI scams rely upon financial products as an integral part of the overall strategy. Securities and Investment products can involve property, finance, insurance, deposit bonds, promissory notes, debentures and various other hybrids of investment offers. ASIC was clearly aware of the model.
- e. Property sold in this manner cannot be compared with the normal activity of real estate agents selling real estate. Consumers know that advice on purchasing property is freely available at local real estate agency business offices.
- f. Correct identification of the scam model is therefore crucial for reasonable discussion of these issues to be presented to the Senate Inquiry.

**(C) 3. Enforcement of Law issues regarding selling of PAFIA strategies.**

**Simply changing a law to ban all planners** from giving financial advice relating to property will, in my view, only serve to trivialise the systemic areas of chaos in the finance sector and to separate the major issues.

- a. Traders who recklessly snub the law, due to the millions of dollars involved, will continue to do so, and will most likely increase their activities unless they are brought to justice.
- b. Financial planner's who are engaging in these pernicious practices, ought to be permanently banned from working in the banking, property and finance industries.
- c. Banning licensees is not enough. "Rent-a-licence" is the natural remedy for banned traders. Custodial sentences are the only remedy to curb these activities.
- d. PAFIA traders /company directors involved in these practices, have no regard for rules and regulations.
- e. A \$300 million loan book is worth risking a comparatively small fine. Traders fear incarceration and the pain of loss of freedom.

In characterising a person by their profession, we run the risk of ignoring the fundamentals.

Our Consumer Protection laws provided a *fit and proper* test for licence issue, yet ASIC continued to licence those who had entered the industry for a second time.

Consequentially, the licensing system has lost any integrity it may have hoped for.

Consideration should be given to the 30% of the financial advisory industry members who are hopefully honest.

White-collar-crime in Australia is rarely prosecuted, enabling traders to move freely about the financial markets.

Our minimalist approach to corporate law and order has created a thieves' paradise for the traders whom we have spent years researching.

Legislative remedies can be re-assessed as cases are put before the judiciary. Tokenism cases are a waste of time and money and can be set up to fail.

With little or no enforcement of law, the activities become "the norm."

ASIC as regulator has managed to decriminalise that which our laws determine to be criminal activity. Fraud is destructive presence in every part of our community.

Even Al Capone had an attorney, yet his colourful career came to an abrupt end on a simple charge of tax evasion.

Somehow we have lost the art of understanding how to deal with these problems.

## **MODELS**

### **(d) Advantages and disadvantages of possible models for reform of the property investment advice industry including:**

- i. national coverage through uniform state and territory legislation;
- ii. Commonwealth legislation; and
- iii. a scheme of self-regulation of property investment advisers on a national basis; and

#### **i. National Coverage through uniform State and Territory legislation.**

The RECA submission highlights the difficulties faced by consumers when having to deal with several agencies across eight jurisdictions.

Fundamental to the overall efficiency of regulation is the strength of enforcement of law. White-collar crime is on the increase and the PAFIA scams have re-opened debates on how as a nation, we can protect consumers from the activities of rogue traders.

We argue that consumers fall through the cracks of this particular model, particularly when the activities cross all jurisdictional boundaries. There are also valid concerns that jurisdictional arguments could arise as to the model of process and the sharing of responsibilities towards consumer interests.

RECA Members believe that a National issue, such as the consumer crisis in the PAFIA sector, requires a National approach to regulatory control by way of Commonwealth legislation.

#### **ii. Commonwealth legislation.**

### **The RECA Model:**

RECA members sincerely believe that the task of consumer protection should be transferred to a proper consumer orientated, independent, **National Consumer Taskforce Unit** ("NCTU"), made up of professional white-collar criminologists, forensic accounting and legal professionals and grass-roots consumer representatives who have experience in dealing with fraudulent activities.

Independence from industry persuasion is imperative. We envisage the model will be similar to that of the Spitzer/Giuliani model in New York, with hopefully a hard-line approach to white-collar-crime.

We suggest the NCTU as an immediate initiative, to be followed up with a properly constituted **National Consumer Protection Agency** to oversee the day to day handling of consumer complaints and issues.

**ASIC's Role:** The RECA Model suggests that ASIC would remain the licensing regime with responsibility for compliance issues relating to normal course of business transactions and the registration requirements of the corporate sector and general corporate surveillance.

**Funding:** ASIC currently collects an average of \$400 million per annum in fees from the corporate sector. Treasury appropriates approximately \$200 million per annum back to the seven ASIC offices.

Funding suggestions could include a consumer based transactional levy on property, finance and banking products connected to the PAFIA industry.

One national office would be preferable as a central intelligence agency, dedicated to white-collar-crime.

RECA suggests that some of those funds can be utilised in a more productive fashion by an allocation of funds to a **National Consumer Protection Agency** and a **National Consumer Taskforce Unit** regarding criminal investigations.

**The 1997 Wallis Report** warned the nation of a potential for conflict of interest if the corporate regulator was asked to serve two masters: Financial Planning Industry members vs consumer interests.

The major policy change, affecting consumers in 1998, came from the FSI Wallis Committee recommendations in taking the responsibility of the financial services sector from the ACCC and delivering the task to ASIC. In Phil Hanratty's critique of the Wallis Report, 1997, he noted:

*"it could be argued that this (ACCC to ASIC) policy change will create disparities in consumer protection with the rest of the economy, because the tendency for the industry-specific CSFC(ASIC) to come under 'undue' influence from the finance sector."* <sup>20,4</sup>

Certainly we have been inundated with letters from consumers who have been most disappointed with the lack of service from ASIC. Often the letters imply there appears to be a greater emphasis on the concern for the industry players than for consumers.

#### **ASIC's inappropriate attitude towards consumers;**

The FPA has recommended that if ASIC claims are validated regarding the definition of the Corporations Act be amended immediately to accommodate the distinction of property investment and security advice: -

*"The Corporations Law should be amended so that it applies to all distributors of property investment advice and not just those who provide advice on securities."* <sup>19,40</sup>

ASIC has demonstrated time and again, that the agency has no will to tackle these problems. Consumers have lost faith in the regulator to effectively serve their interests.

By way of example: The Parliament did not contemplate that ASIC would hand out exemptions for sophisticated investors, when clearly no consumers had lobbied for such a thing to occur.

#### **CLEB condemned any situation which would exempt major players from the law:-**

*"There is no justification for a regulatory stance which would result in the participants in Australia's financial system being conferred with a special status which exempts them from the normal rigours of the law."* <sup>13,13</sup>

These exemptions became the golden key for suspect PAFIA traders to use *'Information Memorandums'* instead of registered Prospectuses, free of ASIC's responsibilities and duties towards consumers. ASIC permitted Prospectuses to be divided into a Part I and Part II, effectively leaving consumers to believe both Part I and II were 'registered.'

Consumers believed that ASIC monitors each and every prospectus. Another myth promoted by AFS licence holders.

Parliament also contemplated that ASIC would use its considerable powers to pursue compensation on the part of consumers. This power was rarely in use, again to the detriment of consumer interests.

For all of the above reasons, consumer criticisms currently levelled at ASIC are justifiable. We therefore cannot endorse the idea that ASIC is the appropriate agency to continue in its role as consumer protector and that of market integrity.

Market integrity is dependent upon consumer protection being of a high standard.

Consumers are desperately in need of protection from these specific activities and RECA welcomes an urgently required National Approach to the issue.

iii. **a scheme of self-regulation of property investment advisers on a national basis**

Of particular note is the warning given in the CLEB Report in relation to Industry Supervisory Boards ("ISBs"):-

*"The Financial System Inquiry should acknowledge the contribution of effective law enforcement, and in so doing:-*

- (i) *Recognise the benefits of a 'whole of government' approach to law enforcement in the financial sector.*
- (ii) *Recognise the limitations of self-regulatory organisations; and*
- (iii) *Recognise the necessity for effective surveillance of compliance."*

13,17

Existing national self-regulation of the PAFIA industry has been unable to stop the escalation of the instance of fraudulent activities and consumer losses. The concept of industry taking care of their own is often given a positive argument in that it does have cost benefits enjoyed by Governments.

However, the PAFIA traders' activities cross a number of industries: solicitor driven financial advice, non-institutional banking, credit providers, and financial strategies involving property investment advice.

If regulatory authorities have shown surveillance or enforcement difficulties in dealing with fraud in the PAFIA sector, then ISB's are certainly ill-equipped to provide an effective solution due to the inherent conflicts of interest, that could arise when dealing with consumer complaints.

Consumer users of the current system argue that industry bodies tend to deliver self-interested industry results, as is the case with Law Societies and FICS.

ISB's enjoyed consultation processes and considerations when dealing with ASIC, yet none of those discussions and decision-making processes are assisting consumers as end users of the PAFIA industry generated products.

ISB's are geared for minor disputes between industry and consumers rather than the activities described as the subject of this Parliamentary Inquiry.

Despite the level of good will on the part of some of the participants, self-regulation of the PAFIA industry is fraught with danger for consumers. The argument of cost efficiency is rendered impotent in light of the escalation of consumer complaints and the magnitude of the losses, estimated to be around \$3 billion.

Consumers pay the highest possible price for this model. Cost to the industry can be measured in terms of the fallout from scandalous fund raising activities developed by licensed security dealers. Cost to the Federal Government can be measured in terms of welfare based pension funding for self-funded retirees.

The Federal Government needs to take into account, the cost of market failures and the possible impact on the economy as suggested by several key economists during the past three years of the property boom.

Consumers, who saved for retirement, have complained of losing their superannuation funds to the PAFIA industry, soon after receiving those monies. Seeking professional advice from AFS licence holders, retirees and pre-retirement consumers have suffered the agony of having those hard-earned savings stolen.

They have reported further stress in dealing with ISB's.

## **Super Choice**

RECA holds grave concerns that unless legitimate allegations of regulatory deficiencies in dealing with consumer complaints are addressed and a newly created National framework is set up to accommodate those complaints, Super Choice will become a magnetic playground for all of the "unknown" unlicensed cowboys who are currently riding the regulatory range unchallenged.

## LEGAL PROCESS - JUSTICE - DISPUTES

**(e) Whether current legal processes provide effective and easily accessible remedies to consumers in dispute with property investment advisers.**

Despite the 1998/1999 robust debates and the recommendations from the industry bodies for national uniformity, little has been achieved by way of successful outcomes.

We are dealing with Professional dishonesty. Parliament has been advised of these issues in the past and needs to respond in a manner that can truly deliver consumer protection in the property and finance sector.

It is the apparent "highly adverse consequences" that have been born by the consumers, whilst those responsible move millions of dollars offshore. This condition hardly presents itself as a fair and equitable market place.

Hanratty warned of the consequences of distress in one market place can impact on another and provide a general lack of consumer confidence:

*Consumers cannot reliably assess risk "particularly the creditworthiness of the financial promisor." <sup>20,4</sup>*

It then falls upon Governments to restore stability.

Many of those who have suffered losses through fraud, will no longer be able to afford retirement. White-collar criminals have not only stolen retirement dreams from consumers, they have presented current and future Governments with the tremendous cost of paying long term welfare payments to those who never contemplated fending for themselves or indeed being shunned by the regulators in such a situation.

RECA members believe for the sake of consumer protection in the Property and Finance Investment Advice industry there needs to be a Royal Commission as to why all of the above has taken place, and for a clear determination of what is required of regulators in the future.

*Definition of Racketeer: "a person who operates a dishonest business."*

## **In Conclusion:**

Enforcement of Law is fundamental to the idea of consumer protection. Consumer support groups form when regulatory control has broken down.

Our efforts to secure freely given legal opinions to test ASIC's jurisdictional assertions, would not have been necessary but for the fact that we discovered obvious and systematic malfunctions in the area of complaint handling and consumer protection issues.

PONZI scams have invaded the PAFIA sector in a most significant way. The ultimate target is and will obviously continue to be retirement funds and pre-retirement funds. These activities, driven by members of the financial planning sector, are a licence to steal billions of dollars of hard earned funds.

Consumers were in urgent need of protection in 1996. All of the good intentions expressed in the 1997 speeches and the Wallis Report, have evaporated. Instead, rogue traders have been given easy access to licences effectively permitting the PONZI to continue.

Bandits in suits are robbing those who can least afford to lose their retirement funds and then chose to live extravagant lifestyles on other people's money.

How can our decent citizens wander down to the local shopping centre lose their homes? At present we cannot legitimately claim that Consumer Protection in Australia is at a reasonably high standard of delivery. To do so would be dishonest.

RECA's intention is to alert the Federal Parliament of the true nature of these PONZI scams, but more importantly report the apparent lack of regulatory will to take action against the offenders.

ASIC is currently assessing "consumer behaviour," blaming poor decision-making skills for the epidemic rather than non-effective policing the corporate sector. The regulatory "blame the consumer" approach is a modern day smoke screen, rather than serious discussion on the looming consumer crisis. This is most unhelpful. The regulators should firstly examine their own behaviour.

What is lacking at present is an understanding of the magnitude of the current losses, the risk of "the doubling effect" of future PONZI scams and, how these PAFIA activities can alter the face of the property markets and perhaps impact upon the economy, if permitted to escalate. However, we leave those forecasts to the economists.

Personal financial planning ADVICE has reached a dangerously low level of integrity to the point we would consider it fool-hardy for consumers to trust any member of the profession, whilst the PONZI continues onto the fifth level.

For these reasons, and amid ample evidence to validate all of our claims and assertions RECA members believe, that the formation of a National Consumer Task Force to deal with white-collar-crime is the only fair and reasonable way to restore law and order in the corporate sector.

As a nation we have permitted an unhealthy invasion of our finance and property markets, by plunderers whose one motive is the gratification of their own avarice.

A new consumer based policing regime, is perhaps one solution that can give every stakeholder a fresh start and a confidence to enhance and restore market integrity.



## SECTION 1. CONSUMER PROTECTION

### 1.1 To recommend legislative change – too simplistic.

Regulators failed to identify the links between property and financial strategies in the Property And Finance Investment Advice (“PAFIA”) scams. ASIC’s role has been specifically one of consumer protector during the past seven years. A failure to use their existing powers at an early detection period has contributed to the losses experienced by consumers today.

ASIC had a dual role of looking after the interests of financial planners, advisers, financial services and the licensing of those persons recommending risk-prone products. This dual role could have led to an over-emphasis being placed on licensee interests ahead of consumer interests. Whatever the argument, consumer paid the highest possible price for believing in the integrity of a system that clearly harboured deep-seated flaws in its application processes.

To simply recommend legislative change as a correctional measure is to demonstrate too simplistic a view on an issue that has already reached crisis point. In addition, it would ignore the under-lying factors that could, if properly canvassed, give rise to greater wisdom in dealing with the problem of “property advice vandals.”

Consumer protection issues seemed to take a back-seat to the interests of the industry players. Consumers have lost an estimated \$2 billion in these property advice scams, whether, as a result of pressure driven advice, investing as buyers or lenders or joint venture partners.

Without a specific application of consumer protection provisions, there is no market integrity. Integrity is all about trust and confidence in the system.

Consumer Protection would therefore have relied upon the following key factors: -

1. Effective legislation: powerful enough to close all PONZI scams on discovery.
2. Adequate resources: to ensure strong corporate policing
3. Policies consistent with fairness: unbiased to industry or consumer
4. First-class consumer complaint handling processes.
5. Industry right of reply: as a guide to overall patterns of behaviour
6. Broad interpretation of all evidence gathered.
7. Active Enforcement of Law
8. Public disclosure of activities and findings.
9. Strong penalties: fines are a woefully inadequate deterrent.
10. Skilled and independent regulators – consumer dedicated
11. Statistical analysis prepared regularly and for its accuracy to be tested by out-sourcing complex investigative work.
12. Periodical Reports produced with progress of files to be made available for public scrutiny.

What is missing is a watchdog watching the watchdog, hence the lack of adequate policing in the area of white collar crime. Report recommendations alluded to these problems during the past 30 years of discussion on the same types of scams in the property and financial investment advice sector.

Consumer protection can only be relied upon if all of these regulatory mechanical parts are in working order. Consumers need to be armed with a full understanding of risks in relation to licensed financial and legal advice, and in terms of security of investment funds.

### 1.2 Burden of Paying Pensions to retirees suffering loss

People on pensions today, are likely to be yesterday’s scam victims. Several of those citizens have told me of their 40 years of hard work and frugality in savings, yet have

missed out on a fully funded retirement due to seeking "advice" from crooked "licensed" financial planners and their rogue solicitors.

As a nation, we taxpayers now have the added burden of paying pensions to people who were secure enough to provide for their own self-funded retirement. Billions of dollars in losses have disappeared amid speculation that these funds have been squirreled off-shore. We as a society, inevitably share in those losses.

*Definition of "consumer": a purchaser of goods and services.*

Consumers are people who may have funds to spend or even small amounts of equity or income to service a debt. If those funds are systematically stolen, honest traders miss out on the value of that potential for trade. Consequences of white collar crime involving the PAFIA model of fraud can be viewed as parallel with the Savings of Loans scandal of the eighties in America.

### **1.3 Fifth level of the PONZI**

In Australia, we have reached the fifth level of the PONZI (*see section 2.4*). Consumers have innocently and unwittingly been dragged into a Property Investment Advice scam of monstrous proportions and consumer protection needs to be placed high on the Parliamentary agenda.

If regulatory complaint handling mechanisms were working properly as Parliament intended after the Estate Mortgages fiasco, consumers would not be experiencing the losses and heartbreak that is now occurring across the nation. There is mounting resentment amongst consumers that the federal regulatory authorities were aware of these activities, yet failed to come to the rescue of consumers.

Forewarned is forearmed, yet Australian consumers were left with little warning of the reoccurrence of these crimes.

It is fair to say that the current process has abandoned the idea of consumer protection.

### **1.4 Spruiker/Planner Racketeering**

Consortiums have developed massive databases gained from the original seminars, hooked into wealth creation magazines. The databases are then on-sold to overseas interests, exposing Australian consumers to further unsolicited contacts relating to financial advice.

My own experience with these files suggests strongly that Federal agencies have unwittingly or otherwise, misled sister agencies with flawed assessments of cases as to real estate agency activity in the PAFIA scams (*see 2.2*). Regulators have blamed government policy for their own inadequate and flawed assessments of consumer complaint files. They have blamed consumers and industry groups but never their own inadequacies. Playing the "blame game" has led to wholesale theft in the financial advice sector, with rehearsed racketeers using property as a well-worn vehicle, along with tax advice and accounting strategies. The true nature of these frauds and money-laundering activities has yet to be properly investigated by trained specialists in the area of forensic accounting.

A distinct lack of accountability on the part of the regulators, in terms of consumer complaints has led to an alarming escalation in white collar crime involving significant loss.

## SECTION 2. INVESTMENT ADVICE – A Growth Industry

### 2.1 Property and Finance intertwined.

For centuries “men of property” were considered successful. The word “property” conjured up thoughts of wealth, financial security, coupled with the promoted expectation of responsible safety, and security, in retirement.

In 1993, interest rates dropped, causing many retirees to leave the banking sector and seek professional advice on managing funds. Consumers most vulnerable have been identified as those who retired a decade previously on \$200,000 or less and depended upon a critical 10% return to survive on funds only marginally greater than the pension.

Predictably, those who attempted to seek advice were steered into unsafe investment, dressed as “low risk.” I have viewed many files where consumers were led into mortgages and property ventures, along with various debentures, promissory notes and other financial products.

Few consumers buy property without the need for a financial product. In recent times, finance and property have been intertwined as raw material used in a number of “manufactured” financial products and packages.

Of particular note is the increase in DIY schemes, as a prime indicator of methods used to have consumers part with their assets, without significant scrutiny.

In order to comment on the effectiveness of current regulation, a thorough examination of the details of existing property investment scams would be required to enable all participants and stakeholders to properly discuss the issue of Property Investment Advice.

Property investment Advice has become a growth industry in Australia, particularly during the past six years. Sophisticated professional advisers are targeting today’s consumers either by phone, advertisements or at “property and finance expo shows.” People living in a capitalistic society, generally have a natural curiosity about money and finance. Quality of advice is therefore central to the process of informed decision-making, particularly in terms of financial planning.

### 2.2 Real Estate Agents unfairly blamed

Consumer files reveal that “property” is used by a number of licensed and unlicensed professionals as a facility. Consumers are lured into courses to learn “management of financial risk strategies.” No-one needs to pay \$6000 plus to learn how to buy property. Consumers knew they simply walk to the local real estate office and obtain general information given freely.

Consumers have a natural ‘yearn to learn’ about money, banking, finance and property markets. A great number of careers are professionals in mechanics, trades, educational services, but large numbers of consumers have little skills in the area of management of money and more importantly management of financial risks.

I did discover rogue real estate agents involved in the PAFIA scams but that factor was incidental to the activities they were engaging in. Real estate agents who were linked to the PONZI scams were acting as introducers to the financial service industry.

### 2.3 Financial Planners and Accountants - the architects:

Members of the financial planning centres, wishing to profit from the sale of financial products and financial services, are the architects of these pernicious practices. Professional thieves have created a market worth billions dollars, evidenced by the sheer numbers of consumers being “advised” to place their home equity and superannuation funds into “high risk” investment, touted as “low risk.”

Choice Magazine, in conjunction with ASIC, conducted **three surveys** into the financial planning industry during 1995 – 2003. The first of these surveys in **April 1995** explained that: “*less than 10% of the financial plans we examined could be classed as good.*”<sup>9,1</sup>

Most of the surveyed plans were described in 1995 as “downright frightening.” In the nineties, linked syndicates were using similar tactics, described by authorities as unconscionable conduct, to entice consumers into first and second mortgage lending which

proved to be tainted with over-valued property scams. The failure of federal regulatory agencies to deal with these problems resulted in a reported **\$350 million dollars in losses**, suffered mostly by retirees during the late nineties. These figures did not include over \$200 million of losses in other states, nor were subsequent statistics released as to the continuation of the scams.

Our research, based on size of loan books and liquidators' reports on the ratio of known 'bad loans' in 1999, suggested the losses had reached \$1 billion.

RECA statistics indicate losses have increased to three times that figure, due to the number and size of the loan books involved. Today, those figures would conservatively indicate a potential of \$3 billion in lost funds where a reported 90% of loans were bad loans. All scams uncovered involved property, financial products, advice, over valuations on property and fraudulent activity amounting to grand theft of superannuation and retirement funds. Key indicators were obvious to diligent investigators.

#### **2.4 PONZI scams**

Regulatory neglect of the problem, by design or failure to identify the model early enough, resulted in the PONZI gathering momentum as occurred in the US in mid 1980's.

These activities include two-tiered marketing scams. In the 70's and 90's consumers were enticed by free-flight seminars to purchase over-valued land and housing packages. Consumers would be driven initially by curiosity and state: "I cannot afford to buy property." On arrival, consumers would be shown to the property by real estate agents, yet the key introducers were linked to the financial advisers, valuers, solicitors and planners.

Bankers were waiting to sign up the loans, solicitors prepare the documentation, yet it is the financial advisers that ultimately convince the consumer to sign up under pressure. Without the signature at this point, all the other parties stood to lose commissions and financial gain. Buyers were sold a strategy/personal plan, by the advice giver.

Simultaneously, solicitors devised a plan for education courses, run by spruikers to feed urgently needed clientele into mezzanine lending financial products. Prior to this scam model, "mezzanine" was a traditionally respectable name for lending facilities in the commercial construction markets. Lenders and buyers are required to complete the "profit" cycles.

There were obvious links between the rogue companies. Early detection was possible had proper investigations been carried out in the early stages. Collusive practices in the late nineties had generated into a full-blown 30 company corporate structure, registered as a "Group of Companies" all inter-related by directors, shareholders and business transactions between the linked providers. The same names of offenders continually re-appear.

Consumer attendees of "ASIC Approved" courses are asked to divulge their personal finance details including assets and liabilities. This personal information, assessed by financial planning experts linked to other companies in the scam trail, determine whether consumers will be channelled into becoming a BUYER or a LENDER into the same projects, without any regard to exposure of risk or wholesale theft of funds.

If consumer attendees admitted to equity in their homes, AFS licence holders advised them to become an investment BUYER and passed them to the "property sourcing" area. Conversely, if the attendee admitted to cash reserves and equity, clients are then channelled by linked advisers into the property market as investment LENDER's, in similar activities to the solicitor mortgage scandals of the nineties.

#### **Levels of the Ponzi**

The first level of the PONZI scam is first mortgage security, the second level is second mortgage "security", the third level is mezzanine "securities," the fourth level is promissory notes, unsecured notes, caveats etc. The fifth level is capital guaranteed scams and all levels above first level are grand theft: ie there is no intention to return funds to the consumer. All security holders after the first ranking generally lose 100% capital.

First mortgagees will lose approximately 20% - 80% of capital. The fifth level means the operators simply promise security, steal the funds and leave clients with little or no paperwork. Each level is paid with money from the previous level.

Dishonest Valuers are also part of the network providing over-valued property information to the borrowers to facilitate high lending practices. Valuers, knowing the nature of the scam, would claim no liability owed to the end user – the consumer. The planner generated valuations were then used as a selling tool by the linked introducers and advisers to deceive both lender and buyer victims.

In the US, these easily recognisable scams are called “doubling.” Each year the scams continue the potential for overall loss of capital doubles. Here in Australia, the PONZI has reached the fifth level. The advent of Mezzanine scams, Promissory Note scams and Unsecured Notes, dressed as capital guaranteed in 1999, insured the continuation of the PONZI to the next level.

The majority of “investors” in the Australian PONZI have predictably lost most of their invested capital. I condemn the regulatory practice of assisting villains with arrangements to pay back the stolen funds using fresh capital gleaned from future investors, using the same dishonest techniques. Such activity only serves to perpetuate further losses and is unhelpful.

Consumers unwittingly become the receivers of stolen funds, unaware their own capital has been passed on to others. Late payments lead to discovery that the security on offer is either worthless or on levels three to five, non-existent.

Our research shows the “theft of funds” occurs on the first day of the scam, yet the victims may not fully understand the loss for two to five years. Monthly payments give the overall picture of “healthy investment advice,” when the opposite is true.

#### **2.4 Financial Advice as the core vehicle**

Property is merely incidental to the core vehicle: Financial Advice. It's a perfect product for activities based on theft. None of the above can occur without the assistance of dishonest members of the legal profession, accounting profession, financial planning profession, mortgage brokers and valuers. All the professions grouped together are an integral part of the credibility machine. Commission driven members of the financial planning industry or unlicensed members of the mortgage broking industry, drive the entire PONZI. Spruikers and introducers are paid to lead intended victims to an “advisory” section of the package.

From there, consumers are separated into whether “suitable” for the property market as a buyer, enticed by “strategies designed to relieve income strains,” or the mortgage lending market, using debt as a key component of the cleverly worded enticement package on offer. Investors are advised to become an investor in both options.

Consumers are encouraged to borrow funds to even attend the bogus and fraudulent “education” courses. Those channelled into “LENDER” driven scams had assets of either super funds or equity in their homes. Those channelled into BUYER driven scams were people who could not afford the deposits for ‘off-the-plan’ purchase of property and were told they would never have to settle. Credit Cards are encouraged to secure an option to purchase using property strategies whereby settlement is impossible. Guarantees are issued in a liberal manner. These guarantees later prove to be fraudulent.

Buyers are promised that “real buyers” would be provided nearer to settlement and the contracts drawn up by participating lawyers, prohibiting ‘client-buyers’ from selling their ‘asset’ to anyone else. The secrecy of the operation contained in the legal documentation is perhaps the proof of the intention to deceive, and deserving of close and experienced scrutiny. Confidentiality clauses are a common feature of the deceptive contracts.

#### **2.5 Lessons in Money Laundering techniques**

Paid professional financial planners, tax accountants, lawyers, former agents, former policemen and brokers deliver course lectures, declaring warnings of the use of dishonest

operators who used “fake valuations, fake assets and liability statements, fake pre-sale registers, etc.”

All of the above is evidenced by the consumer comments in the course notebooks, including “advice on shares, overseas markets, and corporate structures using Nauru, Vanuatu and Virgin Islands as ‘safe havens’.” Large doses of information on money-laundering techniques were delivered in some of the more exuberant lessons by hyped up speakers, noted as “lecturers” in the course manuals.

Attendees, hoping to learn the secrets of ‘big business’, would innocently write down these foreign terms in their arch-file course manuals, not realising the significance in the early stages. Gradual awareness developed, leading to a significant number of complaints filtering to ASIC offices across the nation. Consumers would ask: “*How can ASIC approve such a thing?*” and “*How long has this been going on?*”

ASIC investigators simply needed to interview consumers and read the course manuals to realise what was going on in 2001.

Highly charged motivating speeches by the major players (holders of AFS licences), gave consumers the impression that all of this information was cleared with ASIC. Some consumers were faster than others to understand the gravity of the sham courses and demanded their money back. Most consumers were unable to get in touch with each other and were unable to group together, in their dilemma.

RECA formally accused ASIC of using a “divide and conquer approach” in relation to consumer victims in 2001. Others believed that the major credit providers and other big name companies would not be putting their name to these courses unless it was indeed registered with ASIC. Slick marketing became a key factor. Consumers told the financial planners that they “*do not trust these spruikers,*” and planners agreed as they signed up the business without disclosing their own links to the spruiker.

## **2.6 Loan Book Growth**

Today’s loan books have risen to an average \$500 million per book, from a noted \$60 million in 2001. The average investment has grown from a suggested \$20,000 in the mid nineties to today’s takings of \$300,000 per person. All the evidence is there in the regulatory vaults. The advent of DIY superannuation, increasing by 45% in the past 12 months, should have rung huge alarm bells. The public has been blissfully aware of the knowledge gleaned by the regulatory authorities during the past six years.

Regulators would question the high rates on offer, but did little to stop the advertising. Amid claims they were “monitoring” the events, few prosecutions took place.

Key indicators have been ignored. The appropriate method available to protect consumers is by court ordered *stop orders* placed on capital raising activities and monies in trust accounts frozen until regulators are satisfied that consumers have not been deceived.

Consumers are told that prospectuses are registered with ASIC. Consumers currently believe that ASIC staffers are employed to read these documents with some expertise and knowledge of scams. We understand that this task became redundant a few years ago. However, Part II of the Prospectus is not required to be registered as a matter of policy. Consumers have little understanding of the ramifications of these processes.

Consumer Protection is all about preventative measures as well as compliance related matters or indeed prosecutions once the investigations are completed. An average of eight prosecutions per state per year contribute to a cavalier attitude to law enforcement by regulators and a direct incentive for industry rogues to double the loan books as quickly as possible.

## **2.7 Supply and Demand**

Supply and demand of consumer clientele, as with any business, is the driving force of the financial planning industry. Supply of genuine low-risk borrowers is slim, yet lenders are in strong supply, due to Spruiker activities. Buyer/investors can be coaxed into strategies if given certain ‘information.’ Proof of this can be found in the use of the same network

of limited 'borrowers,' who do not pay payments. The payments are 'padded in' to the projects and instigated by the planner and solicitor.

Consumers have a natural need to seek advice about money and finance. Members of the financial planning and financial services industry have a greater supply of spruiker-generated clients than ever before. Consumers do not necessarily trust the spruiker. The initial spruiker seminars are regarded as entertaining at best.

However, people do trust the AFS licence of the "expert" advisers and pay a further \$6000 to learn the next pieces of information promised and heavily promoted by the planners.

Consumers trust the system; namely that ASIC acted as watchdogs and would closely examine the substance of all claims.

The sting occurs in the second section of the education course scam. ASIC admitted in a written report in 2003, it did not have funds to send officers on these four-day courses. The spruikers task is to supply a constant stream of pre-conditioned new recruits, dressed up as "investment lenders or buyers" to the offices of the financial planners and advisers. By this stage, unsophisticated clients have already given their financial details and listed their available assets (mostly home equity) to the loan sharks.

## **2.8 "Empires of Evil"**

Demand for more projects to be "started" with no possibility of completion in many cases, has planner/developer corporate structures creating a constant shortage of worthy borrowers. Therefore a false method of borrowing is set up with the same borrowers raising hundreds of millions of dollars as part of the PONZI. Demand for funds come from "serial borrower companies" (in the US they are named as "straw borrower" companies). These companies are linked to the spruiker/introducer firms, via a network of corporations, unbeknown to consumers. I have dubbed these firms: "empires of evil."

Over 120 law firms on the east coast were involved in the mortgage lending industry driven by property projects, 80% of which collapsed according to liquidator reports, resulting in the \$1 billion dollar losses in the nineties. It appears that as a society, we have learned nothing from the devastating and financial consequences of Estate Mortgages in the eighties and similar scams in the sixties and seventies, including the Russell Island and Moreton Bay land scams.

The PAFIA business has nothing to do with market participation with participants acting "efficiently, honestly and fairly," for the common good. The players I refer to, based on eight years research, have spawned businesses where false and misleading advice, misleading and deceptive conduct and unconscionable conduct, is the norm, rather than the exception.

Our markets are advice driven. To separate property and finance is detrimental to consumer interests and can only benefit the inhabitants of the empire of evil. I refer to the old adage: *"evil flourishes when good men (and women) do nothing."*

## **2.9 Qualitative Investment Advice**

The devastating effects of suffering the loss of one's retirement within days of receiving a superannuation payout, is hard to imagine. To work 40 years and have all of those savings stolen, brings on unimaginable strain and hardship. Security is all about saving for one's retirement. Those who did so, have a right to seek experienced and proper financial investment advice, whether in property, shares or other forms of investment.

To simplify the process of understanding the difficulties faced by consumers when seeking competent advice, I have attached a briefing of the general structure of differing models of activities known as 'property' scams. (*attachment A: 'Scam Models'*)

More importantly, I would argue that for the sake of consumer confidence in the market place, qualitative investment advice is fundamental to market integrity, in the finance, banking and property sectors.

## SECTION 3. LEGISLATIVE EFFECTS

### 3.1 1997 WALLIS REPORT – Financial Strategies and Advice

The 1997 Wallis Report discussed the financing of real estate packages, involving “*real property*” and the promotion of negatively geared investment packages, in terms of the provisions available to control quality of advice under Corporations Law. The idea was canvassed that when a retail investor purchases property through a series of finance strategies or borrowed money to fund the strategy, the temporary purchase of ‘off-the-plan’ property, the investor had indeed, placed heavy reliance upon that financial advice.

#### 3.1.1 The Issue of Tax Advice – Financial Strategies

In 1999, ASIC conducted a Review: “*ASIC does not have the jurisdiction to deal with these issues at present.*” It suggests, that should no remedy be forthcoming, there should be a national co-ordinated approach. The report acknowledged an “*emerging problem with the provision of taxation advice,*” noting that financial strategy was a key element of the transaction, specific to the *buyer’s* taxation position. The MCCA, in looking into these matters, suggested that a national approach to the issue was preferable.

*Licensing Requirements – for providing advice*

Recommendation 16 of the Financial System Inquiry (the Wallis report 1997)

*“Real Estate agents providing investment advice should be required to hold a financial advisory licence unless the review clearly establishes the adequacy of existing legislation.”<sup>27</sup>*

#### 3.1.2 Reliance Upon Financial Advice

ASIC highlighted the real risk to consumers, that as investors, they were being : “*misled or confused about the implications of investments, including investments in real estate.*”

*“The existing law, both at Commonwealth and State level, contains prohibitions against misleading or deceptive conduct which can be applied to cases where, misleading taxation and financial advice is given about investing in real property.”<sup>27,1</sup>*

The Government’s response to the 1999 FSI Report that existing regulation covering financial investment advice will be reviewed and that real estate agents engaging in financial advice activities should be subject to current licensing requirements.

*“Some advisory activities of real estate agents are already subject to regulation under Corporations Law. For example; where they give investment advice relating to property syndicates and services strata schemes within the definition of managed investment schemes.”<sup>4,10</sup>*

#### 3.1.3 State Real Estate Acts

The ASIC Media release on 14<sup>th</sup> February 2000 in which ASIC Chairman, Alan Cameron stated:

*“The key findings were that while investors were clearly looking to real estate as an investment, the regulatory regime for real estate agents was not designed with financial advising activities in mind, especially individually tailored financial advice.”<sup>6,1</sup>*

*“ASIC believes that real estate agents who appear to give recommendations about the suitability of particular real estate investments for a particular investor should comply with similar regulatory requirements as investment advisers...this can be imposed either through state based regulation or a co-ordinated national approach.”<sup>6,1</sup>*

According to internal papers, ASIC investigators and their legal advisers admitted that if financial **advice** was given relating to **financial products and strategies**, then action



could have been taken against the spruikers, including using provisions of the TPA. These documents clearly identify breaches of the Corporations Act, ASIC Act and the TPA.

**3.1.4 Phil Hanratty's critique:** The major policy change, affecting consumers in 1998 came from the FSI Wallis Committee recommendations in taking the responsibility of the financial services sector from the ACCC and delivering the task to ASIC. In Phil Hanratty's critique of the Wallis Report, 1997, he noted:

*"it could be argued that this (ACCC to ASIC) policy change will create disparities in consumer protection with the rest of the economy, because the tendency for the industry-specific CSFC(ASIC) to come under 'undue' influence from the finance sector."* <sup>10,4</sup>

Certainly we have been inundated with letters from consumers who have been most disappointed with the lack of service from ASIC. Often the letters imply a perception that regulators placed a greater emphasis on the concern for the industry players than for consumers. I must stress that this may not be entirely justified and no doubt, ASIC would argue from a different point of view, yet the instance of these complaints are showing a worrying pattern of consumers of investment advice, financial advice, securities and financial products, continually being told: *"this is not ASIC's jurisdiction."*

It is the apparent highly adverse consequences that have been born by the consumers that cause valid concerns for RECA, whilst those responsible for these activities are suspected of moving millions of dollars offshore. This condition hardly presents itself as a fair, honest and equitable market place. Hanratty warned of the consequences of distress in one market place can impact on another and provide a general lack of consumer confidence. *Consumers cannot reliably assess risk "particularly the creditworthiness of the financial promisor."* <sup>10,4</sup>

ADVICE is the prime factor that drives the financial service market, and as a consequence of the financial advisers' activities, the property market. Faced with mounting occurrence of financial loss, the issue now falls upon the Federal Government to restore stability in relation to investment advice.

### **3.2 The ASIC Review (1999)**

#### **To separate property and finance is dangerous for consumers**

False and misleading advertising is a common factor, giving investigators an opportunity to achieve early detection. Misleading and deceptive conduct and unconscionable conduct are evident at each level of the scams and easily identifiable.

Property is used as a core vehicle, a facility for mezzanine scams, debenture scams, promissory note scams, placing consumer funds in high risk ventures, intentionally dressed up as low risk.

I have witnessed a number of examples involving shares, franchises (in wine and coffee), tree growing ventures and numerous tax-effective scams, resulting in massive loss of financial security to tens of thousands of investors.

The Australian Media has brought many examples of these activities to light during the past decade. I will therefore offer news clips and other substantive material to be called upon by the Senate, if required.

I would argue that large numbers of consumers have been left unprotected from the activities of white-collar criminals due to a lack of proper identification of, and attention to, these models. (*attachment H: 'Models of deceit.'*)

For any regulator to suggest that consumers had protection for these specific activities under State –based legislation is clearly wrong. To leave consumers exposed to these scams by denying jurisdictional powers is, to my mind, unconscionable conduct on the part of those sworn to protect consumer interests.

The ASIC review, started from the position that real estate agents were exempt from Corporations Law due to the fact they had a state licence to simply act for a vendor in

selling their home. Property marketers were not engaging in normal real estate duties. In fact, the marketers set up complex corporate structures and, as directors, their activities fell within ASIC's jurisdiction. The product on offer was clearly identifiable as: *"management of financial risk strategies."*

Whether a scam player is a real estate agent, solicitor, accountant, valuer, finance broker, financial planner, adviser, mortgage broker, is irrelevant. The career path chosen by the major players involves bringing disgrace to their respective professions and industry colleagues, by embarking on business careers that involve the stealing of people's homes and superannuation savings.

The entire report could be viewed as a poor identification of the major issues of property investment advice, and a lost opportunity for regulators to rectify the problem of tainted financial advice, thereby protecting consumer interests.

Despite this very serious issue being on the Government's agenda, evidenced by the calling for the Review by the Minister in 1999, no examples or models of what was actually occurring at the point of sale of the financial investment products involving property were forthcoming. The only instance of this appeared in the document I referred to as the 'Latimer Report.' (*attachment J: 'the Latimer Report'*)

### **3.2 Solicitor's Run-Out Program**

Lawyers and accountants were granted relief by ASIC, from the provisions set down in the Corporations Act, by way of exemptions. These exemptions were granted conditional upon the activities being incidental to the normal functions of solicitor based businesses.

Yet certain members of the legal profession are the worst offenders in the mortgage scandals.

Over 100 Solicitor firms, running similar defaulting mortgage loan businesses as part of a wider networking process were examined by ASIC during the end of the late nineties. Over 50,000 ordinary 'Mums and Dads' investors lost a reported \$550 million in savings scams across the country. That figure grew to \$1.5 billion in 2001. (*attachment G: Solicitor Run-Out Mortgage Loans*)

### **3.4 Tasmanian Law Society**

In all the scams researched by RECA, lawyers were involved in some way. An over-representation of law firms was found to be the main organisers of these businesses, all of which involved the property and finance industry.

Queensland and Tasmania were the hardest hit and resulted in the Senate Inquiry into the Tasmanian Law Society in 2000. Many of those victims have yet to recover any of the monies lost in the mid to late nineties. Only a handful of those lawyers have been charged under the criminal code.

Lawyers involved in defaulting loan businesses, are currently threatening bankruptcy. Some of the law firms were exposed in 2002 by Paul Steindl's report on the Sunday program *A Law Unto Themselves*.

In the Tasmanian cases, we found financial planners gathering clients via advertisements offering "safe and secure" investments. The Planners would recommend the solicitor mortgage loan investments to the consumer/clients without bothering to conduct a due diligence test. Solicitors running the mortgage loans, acted for the borrowers.

In at least one case we found six "first ranking mortgages" on the one title. Each of the victims was told they had "first mortgage security." The last group of clients to be registered (on the same day) found they were sixth in ranking. The deception lasted two years until the loan finally fell into default.

The valuations were so high that only the first group of six mortgagees were able to recover partial monies by taking possession of the properties. All other contributors lost 100 cents in the dollar.

Most of the clients were retirees dependent upon the investment for income. Some of the people, to whom I personally spoke and kept contact with, are now welfare recipients and are still battling to recover funds. Others have given up and some are deceased.

There is a consistent pattern of behaviour prevalent in all of these professions, that is unacceptable in today's market place.

### **The Kettle Drum Brigade**

A well organised local protest group invited RECA to gather a large number of people together in 1999 in the streets of Hobart, to protest on these activities. The march known as 'the kettle drum brigade' protested outside the offices of the lawyers, the Tasmanian Law Society and the offices of ASIC. We then had a meeting with ASIC officials.

None of this would have been necessary had ASIC been consumer friendly. These people had been battling for two years previously with just the usual round of excuses.

### **3.5 Senate Inquiry into Tasmanian Law Society**

The activists did achieve a Senate Inquiry into mortgage scams run by Tasmanian law firms the following year. We managed to band together 66 people who had been kept apart through the 'divide and conquer' approach used by ASIC against consumers.

RECA challenged ASIC in 2001, on the use of this approach being detrimental to consumer interests. Correspondence exists on this matter.

The victims of those scams are still begging for relief, despite a few wins in court of recent times. All relied upon the advice given by the advisers: *competent financial advice in relation to investing in property mortgages*.

In most cases there was no security delivered and a great number of people were placed on second mortgages (and higher) suffering a predictable 100% loss of capital. Once again, the LVR's were the fraudulent nature of the initial proposals on offer.

Solicitor firms involved, made use of licensed financial planners as a ready source of new clientele.

Consumers reported losing their homes. Several lost approximately eight years income or more. Few recovered their capital. Consumers of these products were predominantly retirees who never expected to rely on the Government for financial support. Victims reported having to apply to Centrelink for the pension. RECA had to follow up on these issues in 1999. (*Attachment K: Hansard July 1999 Centrelink Issues*)

The Law Firms involved were placed on the infamous 'Solicitor Mortgage Run Out' program. (*attachment G: Solicitor Run-Out Mortgage Loans*)

### **3.6 Run Out of the country with the funds**

The Run Out scheme involved permitting rogue lawyers, who were already the subject of consumer complaints to ASIC, to run out defaulting loans, prohibiting those firms from setting up further loans in that manner. This program effectively left consumers to deal with the very people, who had placed their savings at risk. The mortgage 'securities' were in the names of the solicitors who had day-to-day control of the loan books. This particular initiative was a recipe for further disaster.

Some of the firms who were the subject of complaints were eventually deemed "qualified" for a security dealer's licence. RECA identified the worst of these firms in 1999. I would argue that this example of regulatory control is 'soft approach' regulation at its worst.

Many retirees caught in those defaulting loan mortgage scams, are yet to collect 10 cents in the dollar of lost capital from their 1998 investments. Documentation shows that defaults occurred within the first month of investment. All of these financial investment products involved retirement monies channelled into property as a strategy package promoted by law firms acting as financial advisers in financial services businesses.

Despite the fact that ASIC had powers to recover losses from compensation claims, these powers under Corporations Law were not used. (*attach: D "Legal Opinion on Spruikers*).

Instead, victims were asked to fund all the liquidation processes as the lawyers and brokers declared bankruptcy. Recoverable assets had been sold long before, in anticipation of the obvious collapse of the Ponzi scam. Some of the liquidators' bills quickly ran into millions of dollars, as the truth bubbled to the surface.

Traders involved in these scams can easily collapse one Ponzi to set up another. Day to day control of the trust funds allow the operators to chose their own timing. One part of a \$500 million Ponzi collapsed and the operators were able to transfer other loans into new Ponzi scams. Investors did not realise that their funds were being channelled into previous debts, rather than the intended purpose of new construction ventures via mortgages.

### **3.7 The South Australian Experience**

In 1996-97 ASC effectively stopped further compensation avenues in South Australia after defaulting loans were discovered, promoted as safe and secure investments by finance brokers and their lawyers. Over \$20 million in compensation funds were paid out, but the activities continued due to lack of prosecutions against major players involved. The action taken was clearly a token effort. All future consumers were denied compensation, yet were not made aware of the dangers. ASC handed over regulatory responsibility to the Finance Broking Industry. Later members of this committee were found to be responsible for some of the defaulting loan activities.

Once again consumers were left in the dark and the villains ran free.

### **3.8 Milking of Trust Account Monies**

The trust accounts were bare. I recall sitting in a courtroom in Western Australia, listening to Justice Neville Owen (HIH Commissioner) who said: *"I would have thought that a trust account in the red, was a contradiction in terms?"*

One trust account was reported in the liquidator's report as being \$5 million over-drawn for two years and at one point, for 86 consecutive days. No authority wanted to claim jurisdiction.

As a nation, to say we have no laws to protect consumers in these types of cases, beggars belief. To suggest we are still "in discussion" over the matter is tragic, after a decade of consumer abuse.

If, as ASIC claims, it had no jurisdiction, yet held a genuine concern about the magnitude of losses in the Spruiker/Broker/Lawyer/Accountant/Valuer related activities, the volume of complaints in all of the above areas and the overall proliferation of these same type of scams in every state, why did they not use their amazingly tough powers to alter the definitions in the Act to protect consumers?

At the very least the matter became so grave that ASIC as national consumer protector, ought to have recommended to the Minister that these serious issues be brought back to the Parliament for further scrutiny. RECA's call for a National Inquiry into these scams in 1999, were ignored.

We are not being advised as to whether any changes in legal definitions were applied for. To date and as far as we know, the definitions referred to in hundreds of ASIC response letters to consumers, remain unaltered.

### 3.9 ASIC's failure – real estate agents providing financial advice

The Finance Services Inquiry ("FSI" 1996-1997), known as the Wallis Committee produced a Report in 1997, demonstrating the fact that members had no difficulty in understanding the necessary marriage between property, finance and investment advice. A 1997 'FSI Report critique' by Philip Hanratty noted the recommendations that CFSC (ASIC) develop:

*"A single set of rules and advice concerning minimum standards of competency and ethical behaviour and rules in handling client property and money. In particular, **real estate agents providing investment advice** should be required to hold a financial advisory licence unless a review clearly indicates otherwise."*  
20.12

The above observation is crucial to a point of reference that I deal with further on in this report. "*Unless a review clearly indicates otherwise*" became a future weapon of misuse. I argue that real estate agency legislation covers agents' commissions to ensure they are paid for work completed. No state provisions were made in terms of financial advice.

Real Estate was a previous career of mine, hence the formation of RECA. We were instructed in the eighties that we were not given a licence to give personal tax or property investment strategy advice and that to do so would be in breach of federal legislation. As real estate representatives, we understood this point from the TAFE course lecturers.

## SECTION 4 PROFILE OF THE MAJOR PLAYERS

### 4.1 Financial Planners And Advisers

A concerned and honest financial adviser told me: *"No ethical financial adviser would ever have recommended that the client place all existing funds, equity cash, into one asset class."*

### 4.2 The Legal Profession

*"even Al Capone had an Attorney."*

Author Neil Jenman who has become a national consumer champion in the area of real estate, describing in simple terms, the plight of *"how Errol and Wendy lost their home."* Neil detailed several a-typical PAFIA scams in his third book *"Don't Sign Anything," 2002.*

*"Hard working citizens...they trusted the men in suits: the financial consultant, the lawyers are all in cahoots with these salespersons who call themselves experts..."*  
*"Compared with the sudden shock of a violent crime, white-collar crime, especially in real estate, may take years to reveal itself."*<sup>21,224</sup>

Author Terry Ryder referred to his own research on real estate agents who earned a living from referrals of clients to members of the legal profession: *"they also earn rewards from solicitors, mortgage brokers, lenders (planners), valuers, by referring buyers..."*<sup>26,31</sup>

Properties could not be sold without the express assistance and credibility of lawyers and accountant/advisers as "experts." Consumers trusted the system, that all of these players could not put forward these schemes without government approval, or at the very least, that authorities were monitoring their activities.

Law firms were clearly identified as running financial planning businesses, selling risky financial products and giving financial planning advice. Those firms were clearly deceiving and cheating on their own colleagues, yet again, there were few prosecutions. Meanwhile, regulators appeared to develop a minimalist approach to white collar crime.

### 4.3 The Loan To Value Ratio Factor

RECA found evidence of 2<sup>nd</sup>, 3<sup>rd</sup> and 4<sup>th</sup> mortgage investments in high-risk unworthy loan vehicles, despite written assurances to consumers in all states, that the loan investments were 'safe and secure 65% Loan to Value Ratio ("LVR"). Later we revealed LVR's to be as high as 500%, in direct contrast to the material and advice given to consumers.

We contend that these frauds were obvious to investigators that understood the model and knew of the fraudulent LVR factor.

### 4.4 Accountants

Accountants were using client databases to feed future business. Without accountancy strategies and reported audits, it is fair to say the financial products and related property scams would have become less credible and therefore less effective.

### 4.5 Enforcement Of Law

Enforcement of Law in the white-collar sector, has become a major issue on a national basis. It is my honest belief, after a decade of research, and consistent lobbying, achieving seven inquiries into this sector, that the entire framework was based upon a "conspiracy to defraud."

For fraud to exist there must be intent. A close look at all of these files would leave professional investigators in no doubt that fraud was evident in many of these cases. Consumers have expressed disappointment or stronger that stealing someone's retirement or home only attracts a few years punishment and at times a fine. These soft measures are inconsistent with the seriousness of the crimes or the placement of people's savings into risky and undisclosed linked ventures.

A \$10,000 fine for stealing millions of dollars may be to some villains: "worth the risk." There was little or no risk of punishment.

Consumers in all states have continually expressed concern that the blatant stealing of millions of dollars and then declaring bankruptcy, is unacceptable.

Operators set up off-shore accounts, rented large homes and lived lavish lifestyles with little regard for the financial security of others in the community. Trust accounts were raided and trust in the market-place, violated. Yet the biggest deception is perceived as the continual betrayal of consumer protection.

#### **4.6 Justice Issues**

I found when criminal charges were laid by various DPP's, only "one case" would be put forward before the judge. The defendant could then claim "this is my first offence after 20 years in business (due to the previous lack of enforcement)."

Judges would not be privy to the raft of evidence that the average operator had set up 400 loans of which 90% or higher were "bad loans." No mention of millions of dollars of lost funds by the defendant would be presented.

To date, RECA has assisted with information, which has brought about at least 10 custodial sentences for a range of time between 6-10 years. I feel confident that without the inquiries and media assistance in reporting the facts as newsworthy, all of these cases would have received little judicial attention.

An estimated 200 traders have been or are currently involved in these scandals. It is hard to quantify the number emerging during the past 12 months.

For simplicity, I have created three classic examples of lawyers in loan businesses and the entry of ex real estate agents, accountants, valuers and financial planner recruits into the mix. (*attachment B: 'Loan examples involving property'*)

#### **4.7 Real Estate Agents**

Former real estate agents turned developers, no longer sold and received commission from residential sales covered under state-based laws. These operators specifically became joint partners, or commissioned developer hacks, used to entice vulnerable retail consumers into investment 'packages' prescribed by financial planners. Former real estate agents acted as introducers to the financier.

Consumers generally, did not necessarily trust real estate agents or even ex real estate agents. The irony that agents were being paid by the financial planners became known at a later date. The planners and solicitor-prepared documents became a critical component of the process to entice a signature from the consumer. Well-constructed edification processes would ensure large numbers of consumers fell into the trap. Each player would edify each other to conclude a sale.

#### **4.8 Professional Gangs at work.**

- Introducers are required for the marketing of the property and as a conduit for the consumer to be passed on to the financial planners/legal advisers.
- Solicitors are required for the contracts and accompanying documentation.
- Valuers are required to over-value the asset.
- Accountants are needed for credibility, by way of inadequate audits and advice on "tax minimisation schemes."
- Brokers are needed to become the intermediary for the banking sector. Finance contracts are used in sign-ups by introducers.
- "Expert" Financial Planners and advisers are employed to deliver the financial advice in the actual courses.
- Finance Brokers are often used as the middlemen between the lawyers and the spruikers.

- Spruikers are needed as the charismatic front men/women to deliver the gateway ceremony to all of the above.

The collusive nature of the schemes in question, the unacceptable conduct of players bankrolled by professional licensees, the magnitude of the losses and consequences suffered by tens of thousands of consumers, demonstrate clearly that a replacement policy is urgently needed.

Our members advocate that a national approach to this issue is long overdue.



## SECTION 5 COLLUSION - Collusive Corporate Structure

One clear pattern has emerged during the past decade. For property investment scams to deceive the public on such a wide scale, criss-crossing all state boundaries, there has to be present the element of collusion.

### 5.1 Conversion of Mortgages to Shares

Players in the finance and property sector as described in section 4 of this submission are known to oscillate between markets. At present there are players advising clients to convert "secure" mortgage holdings to shares in suspect linked companies. Consumers are threatened with the idea that to insist on return of capital from the secured loans would result in a total corporate demise.

### 5.2 Triple Scams on the same property

Fear is promoted as a bullying technique, to encourage consumers to convert their mortgage investments to the stock markets. I have read parliamentary reports, which suggest these same techniques were used in the late sixties. During the investment period, further capital raisings of one million dollars occurred.

Ten months later, the listed company would collapse and previous and current funds were lost forever. Yet the same property could be re-set for another round of new investors, who are blissfully unaware of the previous activities of the advisers and the previous history of losses. RECA uncovered examples of triple scams on the one property all involving offers of security in various forms.

In an industry riddled with kickbacks and incentives, traders will be under pressure to consider bank-rolling another round of "lucrative" deals. This point needs to be thoroughly canvassed when selecting appropriate penalties and sanctions. Professional traders of this calibre are constantly challenging market integrity.

### 5.3 Collusion leading to International activity

I have personally interviewed hundreds of consumers in six states in Australia, as well as those overseas, who have been caught in these investment advice scams. Where security did exist, albeit, grossly over-valued, the more recent scams leave consumers with none of the promised security, either property titles, mortgage investments, unit trust certificates, debentures, promissory notes or shares etc.

Furthermore, the collusive nature of the scams clearly demonstrates to even the novice officer that these activities are the work of professionals working as consortiums in suspected money-laundering rackets. Overseas trips are frequent. Consumers are then advised: "funds are due in from our international activities."

### 5.4 Persuasive Language

According to consumer/victims of these scams, general language of professional promoters revealed a pattern of dishonest conduct. By way of sample:

*"Our solicitors have gone over every word of this document. We would not be permitted to promote these products if the content were non-compliant with Corporations Law. Everything is registered/approved with ASIC. ASIC is a tough enforcer, they go over everything we produce and would prosecute us, if we stepped out of line."*

### 5.5 Linked Credit Providers

As the spruiker scams flourished, consumers were being advised by licensed advisers to take funds from the equity in their homes, turning the debt into investment capital and placing those funds into recommended mortgage lending facilities and in some cases using part of those funds into off-the-plan unit developments.

At times consumers were urged to become both lenders and buyers as a strategy to secure future financial security, using deposit-bonds and/or credit cards. Strategies were debt-driven. Fake insurances were used in the deception process.

Consumers were asked personal questions at the close of the seminars, via questionnaire forms, regarding existing assets, liquidity and income regarding capacity to afford loan repayments.

Questions were again asked of the consumers at following day personal advice sessions to enable the information to be analysed by "experts" in finance.

These experts were licensed financial planners holding an AFS licence, or unlicensed mortgage/finance brokers. Two-tiered marketing depended upon "loan approvals," based on tainted information that was likely to deceive the consumer. Clients were churned from one non-bank institution to another in the process. Newly formed companies in the banking system therefore, became a major key link in the creation of these businesses and a proliferation in such practices.

## **5.6 Links exposed by former staff members**

We found non-bank institutions that were providing loan facilities for the "ASIC Approved" investment education courses and other products linked to the Spruiker activities, via the brokers. Staff eventually came forward to explain the mechanics of the model when they failed to receive payment for work done and when complaints from consumers reached crisis point.

Consumer complaints were also received by the Australian Taxation Office as to tax avoidance issues.

There is no doubt on the part of those who have viewed the results of investigations into these files, (ie, where personal interviews of the victims took place) that consumers were being profoundly misled as to the level of risk and the likelihood of 100% loss of capital invested. Consumers who had liquid assets were channelled into lending facilities and those who were unable to purchase or settle on a purchase of property were plunged heavily into debt on high-risk strategy programs.

Linked credit providers benefited from these scams. Students paid \$6000 for this advice to the planners and up to \$15,000 for each course. They were guaranteed profits from those strategies which would cover the outrageous costs of the "government" sanctioned courses. Lawyers running mezzanine and promissory note financial products prepared the contracts. Accountants provided the tax advice. All were commission driven from the same source and passed clients to and from the various outlets. Initially consumers thought they were being well looked after and were willing to pay further funds for "more assistance."

Consumers eventually realised the valuations were a sham, their funds were at risk, the payments on investment ceased, guarantees were not honoured, advertising material had been false and that many of the supposedly independent companies, were in fact inter-linked by way of activity and directorship. Only when the information was properly researched, did the extent of the collusive activities become public knowledge.

As one consumer pointed out: "why would we check the adviser's due diligence, after paying \$6000 for his advice? The due diligence is what we paid for. It would be like buying a dog and barking yourself. Had we known these scams were the norm, we would have stayed away – definitely."

## SECTION 6 FINANCIAL PRODUCTS – STRATEGIES

**DEFINITION of security:** *“secure condition or feeling.”*

### 6.1 Investments regarded as securities by the public

All of the financial “products” I have reviewed are sold as investment **strategies** and as **securities** in the context of ‘safe and secure investment’ registered/approved with ASIC and/or the Taxation Department. The method of selling in terms of conduct can at best be described as unethical and at worst unconscionable.

CHOICE Magazine expressed concern over unlicensed agents selling financial products and offering investment strategies and described the industry as a “mish-mash” in terms of regulatory control. The Deputy Chairman of the ASC stated: -

*“we receive thousands of calls each year... a valuable source of information.....the ASC had no systems for analysing this data...if the industry doesn't lift the standards in the next few years, then we will.”<sup>9,13</sup>*

### 6.2 A Matter of Trust

Our files reveal the level of trust placed in promoters by scam victims due mainly to the use of industry integrity promotions. Consumer letters are testimony to the information given at point of sale. Clearly, financial security appears to have been of primary concern to consumers as they sought financial planning advice from those whom they believed and trusted to be the experienced advisers in these recommended products. Letters, interviews, journals, notes, reported phone calls and false assurances, later verified consumer complaints regarding betrayal of trust.

### 6.3 Financial Security Issues

Consumers sought security advice and in most cases considered a number of options. They purchased a strategy to enhance financial security. Two Tiered marketing victims were told that they needed to embrace a complete investment strategy and purchase an investment “package.” Buyers were guaranteed that “genuine buyers” would be introduced for a fee.

It is clear from the evidence at hand that large numbers of consumers could have been saved the financial trauma that so many victims are experiencing today. It is my firm belief that had regulatory officers, interviewed all consumer complainants as a follow up to valid complaints in the late nineties, these activities ought to have been stopped at an earlier date. Had proper complaint assessments taken place, these PONZI's could have been stamped out.

## SECTION 7 INVESTMENT ADVICE ADVERTISING

### 7.1 False And Misleading Information for Sale

Irrespective of whether clientele were steered into property investment strategies as a buyer, or 'a variety of mortgage loan investment products' as a lender, or 'tax effective scams,' their ultimate losses depended upon which advertisement consumers replied to.

In October 1998, ASIC again asked **Choice Magazine** to survey those charged with giving investment-planning advice. Choice warned of investor confusion and delivered this incredibly simple logic: *"investors don't know what they don't know. That's why they seek professional advice."*<sup>10,22</sup>

Advertisements would falsely declare: "ASIC approved" or "approved for superannuation investment." Consumers undoubtedly felt safe in this market and trusted the licensing system. As one consumer stated: *"we didn't give our hard earned funds to the milkman!"*

### 7.2 Legal Remedies available in 1998

Corporations Law provided consumer protection remedies for corporate misbehaviour and conduct relating to management of financial risk activities. The TPA provisions covered material produced at sale: eg: brochures containing false and misleading statements. Adequate consumer protection laws were put in place in 1991. The relevant legislation was rarely tested by the judiciary. The statute there became merely a general road map rather than an instrument of worth. Laws are written expressly for the villains of the industry, not for the majority who would conduct themselves in an honest fashion.

Decent professional advisers are appalled at the lack of enforcement of law.

### 7.3 Disclosure Issues

Designing legislative requirements involving 80 page disclosure documents for consumers can best be described as utter stupidity. Not only will the cost of such monstrous documents be born ultimately by the consumer, it is a regulatory ambush for consumers to be left deciding what the ultimate omissions are or could be. Ensuring full disclosure is akin to describing whether a glass is half full or empty. Consumers are often ill-equipped to understand the legal trickery used in contracts.

Those whose ethnic background place English as a second language are left utterly vulnerable. Consumers, whose literacy skills are poor, are prime targets for dishonest activity and yet need to lace the greatest amount of faith in the advice given at the time.

Enforcement of law and exposure of criminal activity is the only effective deterrent and what white collar criminals fear the most. Other democracies came to this conclusion long ago.

Professional bandits with AFS licences will only laugh at the ease with which they can fully disclose the scam in 80 pages of complicated nonsense. RECA members that I have spoken to on this issue, consider the suggestion to be of poor judgement and ill conceived.

Consumers will then be left in a position of being told by their accountant, advisers: "No need to read the fine print, our lawyers have gone over every detail in your interest. Trust me." When more losses surface, the argument will be "buyer beware."

What is required is that consumers need two pages of explanatory material and a large notification and warning: "we suggest on the information we have given that you consult with your own independent lawyers, accountants etc, prior to any decision you may choose to make."

Consumers need to be advised which planners are the ones who are the constant subject of consumer complaints and responsible for the largest losses. The current system is of no benefit to consumers in any honest assessment of the end user.

## SECTION 8 SPRUIKERS

### 8.1 Information Memorandums

During 1999 we witnessed the proliferation of unlicensed Spruikers holding seminars, using untrained introducers as the 'frontline,' to channel unsophisticated consumers into Mezzanine products, also known as managed investment schemes. Throughout the nineties, solicitors using Law Society premises as a fast track method of gathering new clientele, conducted spruiker type seminars.

The emergence of the Information Memorandums as a selling aid, clearly identified a linking of all industries and players who inhabited the property, finance, investment and banking sectors.

The new model of spruiking via Information Memorandums to unsophisticated investors drew a few recruits from the real estate industry into the finance sector, yet introducers came from all walks of life. The introducer's job was to infiltrate centres of influence; community, clubs, churches, charities and lead future clientele to the financial planners.

Financial Planners promoted the Information Memorandums in regular newspaper advertisements suggesting higher rates of return with low risk products were possible for those willing to pay for "professional advice."

Consumers who were seeking investment advice from "professional advisers" expected trustworthy financial advice. Instead they received risky strategies that would ultimately lead to the loss of their financial security and in many cases the loss of their major asset: their home.

#### Use of "Experts."

ASIC vs The Austral Timber Finance Pty Ltd [1999] VSC 351, No 6480/6481, Supreme Court of Victoria, Byrne J, 8 October 1999.

*"an expert legal opinion; a taxation opinion...the Information Memorandums."*

All of these strategies were embodied in the glossy brochures laden with professional logos, entitled: "**Information Memorandums.**" These brochures were being passed off by the advisers as prospectuses registered with ASIC. Intention to deceive can be found in a significant number of consumer complaint files.

### 8.2 Class Exemptions for "Sophisticated Investors."

ASIC again delivered a class exemption for investors who earned more than \$250,000 net per annum and chose to invest amounts of money greater than \$500,000, into one asset class. It is important to note that these were granted as a result of industry lobbying, not consumer pressure.

ASIC felt that investors who could take their own risks without the need for regulatory protection or scrutiny were deemed to be "sophisticated investors."

Exemptions became "loopholes" in the system; to the detriment of consumers. Industry players lobbied for these exemptions, yet no-one examined why this occurred and who was to benefit.

The exemptions for "sophisticated" investors came as a result of using a "wealthy investor" model by way of example. ASIC informed us that the ceiling was set at \$1 million during the initial discussions at regional director level.

Later that year, under pressure, ASIC lowered the bar to \$500,000. Rogue traders then channelled consumers into "pooled mortgage" arrangements of less than 20 people. Those funds are lost or currently at a high-risk level, yet were marketed by the advisers as "low-risk," using Information Memorandums and "exemptions" as a major tool of trade.

### **8.3 Warnings from RECA regarding Mezzanine Products**

In 2000, I travelled to several states speaking with Regional Directors of ASIC. I voiced concerns that "unsophisticated" investors were being spruiked via seminars and encouraged by dishonest and licensed planners, to place their major assets into high-risk mezzanine mortgage lending products. I further explained that Information Memorandums were being misused in this way to the detriment of consumers.

The response I received in 2000 from ASIC chiefs was a welcome one, admitting knowledge of these practices and a determined approach to stamp out these practices. I was assured that ASIC chiefs were seeking further legal advice. I again raised this issue in 2001, believing that hundreds of millions of dollars could disappear very quickly unless these practices were immediately brought under control.

### **8.4 RECA Website regarding PONZI scams (and others)**

I provided written models of the scams in 2001 and placed them on the RECA website. ASIC responded by placing similar warnings on the FIDO website. Yet little else was done and the spruikers continued to market these products to vulnerable consumers.

### **8.5 ASIC Legal Opinions**

In 2002 I again raised the subject at ASIC Public Forums. In 2003, I again warned ASIC in a radio broadcast and via print media. ASIC announced, "*we are seeking legal advice.*"

To date, ASIC have resisted all requests to produce these legal opinions and identify which law firms were asked to provide those opinions. Consumers were again left out of the discussion by way of consultation, or even being kept informed. Instead, we received response letters: "*we are advised.....*" The nature and author of this advice remained top secret, yet the ASIC "*not our jurisdiction*" letters seemed to stem from this period in time.

### **8.6 PART I and PART II Prospectuses**

In 2001, I also noted that consumers did not fully understand that prospectuses had been split into two parts, with again, devastating consequences for consumers. Part One of the Prospectus became a glorified brochure with only general details regarding the corporation.

This part was registered with ASIC. Part Two which contained all the details of the investment relating to the borrower and the subject property, including forecasting profits, funding details and statistical analysis, was exempt from registration with ASIC.

Spruikers were using these brochures as credibility for their own recommended strategies and again these materials were being misused to trick consumers into accepting the advisers' recommendations for safe and secure investment proposals.

Consumers have been and continue to be clearly misled by rogue advisers into believing that both Part I and Part II of the Prospectus on offer was scrutinised and registered by ASIC.

Monies were being channelled from the spruikers to the financial planners to support the business structure according to the bookkeepers and other staff members. I would argue that correct identification of the activities in 1999, and the use of enforcement processes, ought to have stopped these practices. Consumer Protection was considered possible given the material at hand in 1999, including that supplied to ASIC by RECA.

Spruikers used high-pressure tactics to sign people into these courses expressly designed to deceive consumers by offering management of financial risk strategies. The initial intent had been to tap into the retirement fund market. Development of these activities altered to include pre-retirement funds by assisting new investors into DIY packaged products.

### **8.7 Joint Venture Packages as strategies**

Using the above method the advisers could channel superannuation funds into high-risk joint venture packages and/or mezzanine lending, where day-to-day control of these investment funds fell into the hands of the developer related companies.

Only 25% of consumers who attended seminars actually signed up for courses. Yet all registered personal details with Spruikers. Promoters and introducers specifically gathered huge email databases.

Weeks later, consumers reported a series of similar phone calls aimed at phone canvassing potential buyers for the over supply of CBD apartments, as developers continued to set up new projects.

The caller persuasively entices the consumer to make appointment with local financial planners, for a \$200 fee. The advisers would then demonstrate the best way to increase income by as much as \$1000 per month. Consumers are assured that these are licensed "experts." The CBD Units are not mentioned on this initial contact. Consumers who made appointments were able to provide us with the offers being made including the brochures.

### **8.8 Fear of Retirement Strategies**

Property Investment Advice market is riddled with slick marketing techniques. Once again the suggestion was made to use existing equity in residential homes and the usual "fear of retirement model." There is no doubt that all of these links prove the collusive nature of the spruiker / financial planner activities.

There is no doubt that the intention is to place ill-gotten consumer funds into previously launched, distressed and over-valued projects. All of the above fell within ASIC's jurisdiction.

No studies have been conducted to ascertain flow on effects on consumers, markets and industry. Consequentially there is little public data to be properly examined and analysed and/or statistics provided. Whilst seminar scams were the scourge of the 70's and 80's, these new hybrids sent consumer danger indicators into flash point mode.

Few regulators are asking the big question: "**Where have all the hundreds of millions of dollars gone to?**" This question became the theme for the RECA Tours in 2000 to Queensland, Victoria and Tasmania. It was our small attempt to warn future consumers of these dangers. I believe we did manage to save a number of people, using this method of communication.

When we asked ASIC to assist us with the postage stamps to contact many of the victims, those requests were denied. We challenged ASIC on this matter in the name of Consumer Protection that resulted in written acknowledgement that ASIC could do more to assist consumers. Yet, one year later the same letters of denial of assistance were being sent to new complainants.

Consumers were being denied the basic right of grouping together and basic assistance in seeking group advice.

### **8.9 RECA Tour in Eastern States in 2000**

I found victims in Tasmania and SA who had invested with Queensland lawyers, with borrowers in NSW, and properties in WA and Victoria. ASIC continued to respond to these consumers, telling them to seek civil remedy. Their funds had been stolen. There was little or no remedy according to the regulators and the villains were protected by this obstructionist behaviour. ASIC ignored its duty to pursue compensation on behalf of the victims. Such an initiative could have delivered a powerful message to corporate villains, instead the reverse applied.

I was aware that ASIC had powers of remedy, due to the fact that the postage stamps method had been utilised by one of Regional Directors, in 1999. He told me then: "it's the least we can do."

We found the original spruiker seminars had been held in the premises of the various Law Societies. Consumers had been left to rot in a sea of debt and despair.

By 2003, these activities had reached epidemic proportions. Intelligence gleaned from the files suggests that hundreds of millions of dollars have been moved offshore, yet there seems to be a complete lack of will by federal regulatory authorities, to chase these funds.





## SECTION 9 CONSUMER PROFILE: a victim of fraud

### 9.1 Seeking Professional Advice

'Property' was merely a word used as a comparatively small part of the overall finance and property scams. After meeting hundreds of these consumer/victims I concluded that they were not illiterate, in fact some were highly educated people who had simply retired and needed some good sensible, honest, reliable, trustworthy investment advice.

### 9.2 Responding to Teaser Tickets

Victims found "teaser tickets" in their letterbox and, driven by the curiosity factor, saw no danger in attending "free information nights." People caught up in these pernicious practices were looking for ways to increase their current or future retirement income.

Well-spoken, smartly dressed "introducers" were trained to individually lead the potential victims to the desk of the licensed financial planner. Evidence suggests it was not unusual for both introducer and planner to be present at the point of signing. Contracts prepared by the interlinked solicitor, completed the circuit of respectability and credibility.

### 9.3 Property Purchase a sham

Consumers that I have made contact with freely admitted that prior to the enticement, they had never intended buying property. They did not believe it was possible because they could never afford to settle.

Most of those I consulted with agreed that their knowledge of finance and money was extremely limited and therefore insisted on "professional advice." Those who did purchase off-the-plan investments purchased "an investment strategy." Few could afford to settle and therefore forfeited an average \$40,000 each in deposit bond monies. Those who had been coaxed into financing bonds on five units were left with no alternative but to lose their family home. (*attachment C: 'strategies in selling'*).

### 9.4 Consumer Awareness

Consumers tell us: *"had they known what was occurring, we would never have entered into property investment market. We were not made aware of the risks. On the contrary we were told the investment plan was "safe and secure." We made it known to the 'adviser' that we could not afford risk and that our property, or superannuation was our only asset."*

### 9.5 Consumers And The Regulators

Consumers are now angry that the regulators were aware of all of these activities for many years prior to their own involvement. Some believe that regulators have behaved in a reckless fashion in permitting these businesses to flourish. Their letters to the regulators reflect this sentiment. They express grave concern that their own financial well being has been compromised by the inaction and lack of enforcement of law. As taxpayers, they realised that the consumer protection mechanisms, which they believed to be in place, were either ineffective or, the issue of the conduct on the part the regulators in failing to provide adequate consumer protection needs to be examined in a public hearing.

With continual reports of mounting losses, that anger will more than likely escalate.

We have every reason to believe that the current crop of spruikers (there have been 80 in the past 12 months) is using identical methods of delivery. I have personally attended many of the advertised "free nights," and spoken to countless consumers who have paid for those packages.

Neil Jenman is currently writing a detailed analysis on each of the 80 spruikers and their linked providers.

## SECTION 10 CONDUCT at point of sale

### 10.1 One on One Meetings

In the 'one-on-one' meetings, the licensed advisers asked students of the 'ASIC approved' training courses: *"write down your assets, home equity, superannuation, cash at bank."* The forms were the driving factor in the giving of personal investment advice.

### 10.2 Inability for regulatory attendance to courses

Hansard records the response to a question as to whether ASIC had attended the courses or read the course manuals to ascertain whether or not this matter fell within their jurisdiction: "I believe officers went to the Spruiker seminars, but we could not afford to go to the courses."

For this reason we assume that ASIC has been unable to comment on what really occurred at the point of sale. The consumer complaint files do however give a detailed account of the false and misleading statements used by promoters at the point of sale and then further misleading and deceptive conduct on the part of the AFS licence holders and their authorised representatives and unconscionable conduct in relation to the finance arrangements and brokering activities.

### 10.3 Trained Counsellors deliver unlicensed advice

Not all of the course participants paid for the personal investment advice and did not become part in the subsequent investment strategies. However, some of those people did apply the same strategies and were given personal advice via meetings with their "trained counsellors," who consulted with the planner experts." These courses ran for twelve months. People signed amid written assurances that they would receive hands-on "step by step" financial advice on each segment of the course.

### 10.4 False claims of University accreditation

Consumers who did not invest funds in finance based property deals, were still left with debts for courses that could not be completed, where classes did not eventuate and where the accreditation for University and other educational credits were exposed as a sham.

From inception, misleading and deceptive conduct occurred on all levels of spruiker generated courses and accompanying activities.

### 10.5 Grass roots examination of conduct

The biggest problem facing consumers, apart from the financial loss, has been the lack of assistance in being able to group consumer together. Those who spoke out publicly could be forgiven for believing that no one was listening. No one of authority it seems, were available to sit in the lounge-rooms of the aggrieved in order to conduct a thorough examination of the documents and hopefully assist them. No-one wanted the grass-roots job of collating the material and understanding the long term consequences.

CHOICE Magazine survey considered that consumers were exposed to a game of "russian roulette," when dealing with financial planners. The Report described the conduct of "ill-motivated, unethical, unprofessional people" who have entered the financial advisory markets. To demonstrate the seriousness of these industry alarm bells:-

*"In some cases we have found the project does not even exist." 9.1*

### 10.6 The Voice of Consumers in each state:-

*"We went to a licensed financial planner to arrange finance, at the recommendation of the developer/real estate agent. We signed the papers in front of the solicitor. We told all of these people we could not afford to risk one dollar of our investment funds. We are not risk takers – never have been. We would not have been able to save for our retirement if we had made impulsive foolish decisions. We thought these people were licensed. They said they were."*

*We trusted that the entire industry was regulated by ASIC. That's what they told us. We flew across to look at the properties. The valuers were big name people. The banks the same and we trusted their valuations. The authorities simply said: "we cannot regulate against greed."*

*We are not the greedy ones, never have been. Yet these crooks are professional players, pillars of the community, or so they told us. They are the greedy ones. They not only stole our home, our dreams, they stole our retirement. Forty years of hard work, doing the right thing. How can that happen in a place like Australia?*

*Our intention for 40 years was never to be a burden on the next generation. We only had the super dollars for ten days after 40 years hard work. How can that happen? Who is minding the shop? We were advised to put some money into property as security and other funds into mortgage investment. Those funds were our security. Now its all gone. ASIC needs a caning over this one. We rang ASIC prior to investment and they told us nothing.*

*We wrote to ASIC and they wrote back and said: 'not our jurisdiction.' No help there.*

*The worst part of all of this was the lack of counselling. Had we lost our home in a bush-fire, all departmental doors would have opened up to assist us. Yet, we lose our home by dealing with these conmen dressed in suits, and no-one comes to our aid."<sup>24</sup>*

Despite the negative content, the Anzac spirit eventually came shining through:

*"We have had to move into a caravan, and accept a pension. That day at Centrelink was the worst day. But we have come through all of that and we look around and see people worse off than we are. The thing, which gets us, is that those culprits are still walking the streets and presumably doing the same thing to other innocent people. These crooks in suits keep flying off to other parts of the world on our money. It would make you weep."<sup>24</sup>*

**10.7** Once again it is RECA that has to come to the rescue of these consumers via donations from real estate agents in the Jenman Group who recognised these problems and were willing to have Neil Jenman and myself bring these matters to the attention of the general public. Other institutions have also assisted RECA in continuing its efforts in the area of consumerism.

I have delivered numerous speeches across the country on fraud during the past four years attempting to bring the plight of consumers to the attention of the federal licensing authorities.

My consumers have been saying:

*"How can we be prosecuted and jailed for walking into a bank and 'attempting' to steal \$5000 and these bandits in suits (financial planners and their lawyers and their spruiker partners) walk into our lives and steal the house, the car, the marriage and all of our superannuation funds and then walk away? How can that happen? How can each state be infected with this problem? Instead, we the consumers are copping the blame for being stupid. We were being told it was ASIC Approved and then find out all of those brochures, registered with ASIC, were a lie. Why is there one law for blue collar crime and then white collar criminals are behaving as if they are a law unto themselves? Why can't we fix this problem? The advertisements are bigger than ever. Who is minding the shop?"*

Similar consumer related speeches in regard to quality of advice and enforcement of law, were made in the eighties after Estate Mortgages. In a speech made by the Treasurer and ASIC Chairman during 1996 – 1999 to the "International Organization for Securities Commissions ("IOSCO").

*"we would use the broadest interpretation of the law. We will set up the best Consumer Protection mechanisms...."*

I mention this in the context that there comes a time to admit the villains are winning and consumers are losing their life savings and their homes. The aftermath is yet to peak in terms of the revelation of the magnitude of the losses.

## SECTION 11 LICENSING ISSUES

### 11.1 ASIC's view on Unlicensed Traders

ASIC stated regulatory objectives: *"to protect consumers and promote fairness, honesty and professionalism among those who provide financial services."* <sup>14,17</sup>

### 11.2 Unlicensed Advisers - Enforcement of Law issues

ASIC appear to have adopted a recent view that their responsibilities to consumer protection are only in relation to "licensed" operators in the financial services sector and that they have no control over the "unlicensed." In some cases prosecutions have taken place for "unlicensed" activities, yet those cases seem to be spasmodic. Consumers need to see a much heavier approach to enforcement of law.

Consumers ask: *"why do we have a licensing system when the licence means nothing?"*

For the purpose of the ASIC Review 2003, ASIC officers freely admitted that they did not concern themselves with "unlicensed" promoters of property investment advice. <sup>19,10</sup>

Submissions from REIQ, QLS, UDIA and the Property Council of Australia agreed that *any* persons providing property investment advice and *introducing* the buyer to the purchase of real property as part of the process: *"should be licensed or be a proper authority holder under the Corporations Law."* <sup>19,39</sup>

In 1999, the FPA's view considered that current state-based real estate legislation was inadequate to cover unlicensed financial advice relating to property investments.

I argue that a responsive and determined regulatory crack-down on licensed and unlicensed advisers is the only way to provide market integrity and consumer protection, otherwise the licensing regime is meaningless.

In 1998, ASIC warned: *"a growing industry that needs to be carefully regulated,"* <sup>23,24</sup> and recorded "1800 licensed planners who employ a further 26,000 authorised representatives." No mention was made of the number of complaints relating to "unlicensed" operators and the links between the major players.

### 11.3 ASIC Report 2003

In an ASIC report dated May 2003, on the subject of "Get Rich Quick Schemes" the focus in Section 4 refers to "Unlicensed Real Estate Investment Activity (per Corporations Act). I believe this report to be one referred to by ASIC officers in the Economic Estimates committee on 2<sup>nd</sup> June 2004:

*"In February 2000, ASIC released its key findings on completing a review of the financial advising activities of licensed real estate agents [per media release]."* <sup>6</sup>

*00/64]...The review however did not extend to the activities of unlicensed persons or 'property marketers' in relation to whom ASIC merely noted that the matter was at that time being addressed by the states and territories through the Ministerial Council on Consumer Affairs."* <sup>8,11</sup>

### 11.4 ASIC'S Existing Powers

ASIC had powers under the ASIC ACT 2001, Corporations Act 2001 and TPA, and should have taken action within those parameters. What is not clear is whether discussions took place with the various Ministers regarding widening powers in the interests of consumer protection. In addition discussions over the fact that market integrity could be compromised by the proliferation of these fraudulent activities.

Real Estate agents were used as a major discussion point to hand all relevant material to the MCCA. **Yet very few real estate agents were involved** in the PAFIA activities described in this submission. The agents we discovered were in fact "former agents." By this I mean they have not relinquished their licences, but the same situation has occurred as with solicitors jumping into the financial services market.

We found examples of banned real estate agents (banned by state agencies) applying for security dealers licences or becoming "authorised representatives" (under Federal laws) in a commission driven financial advice market.

### **11.5 Company Directors breach Corporations Act 2001**

In reality, all had become company directors and as such their conduct and responsibilities were governable under the provisions set down under Corporations Act and the ASIC Act.

Once again the problem of delinquent licensed and non-licensed company directors, giving financial investment advice, has become a major topic of national discussion.

Once again it is consumers paying the highest possible price for this overlap being misused.

Financial Planning licence applications increased dramatically after 1998 and many of the applicants came from either a property or banking background. Whatever their previous "profession," consumers were left to assume that licensees fitted the *fit and proper person* criteria as a minimum requirement.

### **11.6 Group Companies registered with ASIC**

The corresponding problem of former property, finance and banking people becoming company directors, by registering a "group" of companies with ASIC and then hiring licensee holders, started a trend of impropriety: placing consumers at greater risk and confusion than ever before.

Directors boasted to clients of being an ex agency manager, operating within a partnership of security dealers, registered with ASIC. From there sprang the spurious claims that *"we are ASIC Approved."*

### **11.7 CBD Units in an overheated market**

Commissions on \$100,000 - \$1 million investment advice plans involving developing CBD units and lending on mortgages, became a new found source of wealth for operators within the finance sector.

When banks stopped lending in an over-heated market, the new source became private lending from the residential home equity funds and DIY superannuation funds, and other non-bank sources.

These alarming trends became obvious to economists and the Reserve Bank of Australia in September 2002.

### **11.8 Family and Friends approached**

Consumers were being asked to involve family and friends in pooled mortgages and managed investment schemes. The Spruikers became bolder in their assertions believing their own legal advice that if they gave "general advice" and handed clientele over to the waiting "experts," ASIC could not act upon their activities.

We have found a number of people who followed advice given by spruikers and planners and have asked parents and family members to place all their collective funds into pooled mortgages only to find the investment monies had disappeared to places unknown. Those responsible for these crimes are still operating in the market place. We have evidence to suggest the money is overseas. Again, the victims received the usual ASIC letter: "not our jurisdiction."

Had ASIC attended the spruiker seminars and courses in 1999, and conduct proper investigations into the emerging consumer complaints, none of the above would need an Inquiry today. At the time ASIC was dealing with the Solicitor Run-Out program and knew the Model of Deceit, involving property, pooled mortgages and financial investment advice.

By the time ASIC officers attended seminars in May 2003, millions of dollars had already been bilked from unsuspecting consumers.

ASIC also knew the decade-long consequences of the two-tiered marketing scams which involved mortgage brokers, real estate agents, valuers, lawyers and planners with tax effective personal advice.

Consumers believed the consumer provisions of the newly formed ASIC regime and the regulatory provisions of the FSR gave the public confidence that this particular market place could be trusted.

*"Supervisory and prudential regulation alone is not sufficient to deal with financial activity; such regulation must be supplemented by effective punishment and deterrence."* <sup>18</sup>

### **11.9 CHOICE Warning**

The 2003 CHOICE report displayed the frustrations of the agencies to deal with the specific problem of planners, some who held dual real estate licences. CHOICE Magazine surveys, commissioned by ASIC, highlighted the fact that approximately 50-60% of planners' advice and services could not be relied upon by consumers. They found planners recommending investments without justification: -

*"The results are particularly worrying considering company principals (who may employ other planners) are currently applying for licences under the new Financial Reform Act (FSRA). The Act promises enhanced consumer protection, but a large proportion of the advice in our survey would fail to meet some of its basic requirements."* <sup>12.2</sup>

and this:

*"The quality of advice given by some financial planners in our recent survey is frighteningly poor. We have put the industry to the test three times in the past eight years and found serious problems each time – this ongoing failure to lift standards is disgraceful."* <sup>12.1</sup>

It matters not whether someone is a butcher, baker, teacher or ex-policeman. If you are giving financial advice to unsophisticated investors without the benefit of an AFS licence, then the financial services authority ASIC, ought to have taken widespread action against the perpetrators.

## SECTION 12: HISTORICAL EVIDENCE

### – New hybrids, old tricks.

#### 12.1 The Western Australian Connection

My research reveals that these practices first surfaced in Australia, during the sixties and were known as 'real estate scams' due to the connection between property and finance. In 1975 the West Australian Government brought in the Finance Brokers Control Act, in an attempt to stop unlicensed financial planning advice being given by real estate licensees to entice retirees into mortgage lending investments involving dubious property activities.

Dual licences came into play and scams escalated when key players linked into those in key watchdog positions.

The irony now becomes obvious. This small State-based Act of Parliament came in prior to collective revisions of state-based Land Agents' legislation. Investment strategies promoted by multi state operators steered funds from Western Australian retirees to risky Eastern States development projects. My point is that these scams are not new inventions.

#### 12.2 Land Grabs in the 1920's – through to the Sixties.

Spruikers and property scams have been around since the land grabs in the 1920's. Shonky valuations were used to cheat returned servicemen from their land holdings. Spruiker seminars seemed to have started in the late sixties and early seventies, using negative gearing strategies to excite commission-driven businesses.

Spruikers criss-crossed borders with ease, with authorities suggesting it was national problem, decades ago. New land frontiers in Queensland and Western Australia, made these states the obvious target for operators who started operations from Melbourne and Sydney. I may note that the Northern Territory is the only State/Territory that may have avoided these problems.

#### 12.3 Loan Defaults in the Eighties

Referring to the loan defaults of the eighties, Philip Hanratty's 1997 critique of the Wallis Report focused upon overall consumer protection in the financial system:

*"The greater range and complexity of financial products and, in some areas, concerns about more aggressive selling practices, have also led to an increased focus on consumer protection."* <sup>20,19</sup>

#### 12.4 WA and Eastern States Gangsters

In 1998 and 1999 RECA provided ASIC Regional Directors, in WA, Qld and Tasmania, with ample evidence of investment advice being given by former bank managers and former real estate agents and others, some licensed as WA finance brokers, resulting in millions of dollars in losses in property and mortgage lending racketeering businesses. The WA Parliamentary Hansard records the now state Attorney-General as stating that these practices as being conducted by the "dirty dozen," describing their activities as those of "gangsters."

*Definition of racketeers: "a person who operates a dishonest business."*

Whilst the finance brokers, regulated under state law, promoted mortgages as security investments, the borrowers and promoters held multiple licences and the operators and activities had reached all states.

#### 12.5 "Fit and Proper Persons" – Millions of Dollars lost

Those we had reported to ASIC as being part of the overall mortgage scams, were some of the first companies to register prior to 15<sup>th</sup> December 1999, as holders of AFS licences with ASIC. In the interests of consumer protection, Parliament needs to inquire as to how and why these directors were ever considered "fit and proper" people to hold these licences, given the track record of the players.



Predictably, further businesses are collapsing after intense capital raising across state borders, leaving authorities recording further additional losses in the millions of dollars.

The collusive nature of these businesses reveal complex corporate structures whose main line of profit is generated from the promotion of property investment strategies using financial planners as the required "expert advisers." None of these businesses could even remotely be described as "normal" real estate practices.

All states were infected with this 200 year old problem as "professional players" aided by members of the legal profession, criss-cross the country targeting unsophisticated consumers, enticing the vulnerable to become investors in the property market, as lenders in financial products, and/or buyers of real property.

## SECTION 13 IDENTIFICATION OF THE SCAM MODELS

### 13.1 Initial grouping of the players:

Funding is required to set up "spruikers" for much the same purpose as occurs in showground activities: to bring in the crowds and hope attendees are converted into customers.

In the property development and finance sectors, charismatic, hyper masters of spin are required for the "frontline" and are of paramount importance for the success of the entire operation.

Key funding providers of the inter-linked consortiums are rarely discovered. A number of licensed professionals are approached to become part of the Ponzi, which will be called: "the Group." Several we have traced as being part of the initial levels of the PONZI.

In earlier models, real estate agents were used to sell the properties. Even then the activities were collusive by nature with players in league with a consortium of brokers, planners, lawyers and valuers. These activities were entitled: "two-tiered marketing scams," and designed to cheat investor **buyers**.

At the same time solicitor mortgage scandals were cheating investor **lenders** and further scams involved scurrilous joint venture scams.

Overtime, and in light of little evidence of enforcement of law, hundreds of other young hopeful players entered the arena, eager for a quick sting.

A new PONZI has evolved from all of the above into a master scam, combining the talents and models of all of the above, via the use of talented "spruikers" and "introducers."

Property is merely a facility and as the buyer is being used to "hold a property" to on-sell to future clients, consumers will sign on the basis of professional advice and strategies delivered in the spruiker courses by the professional and licensed racketeers.

Consumers believe they are firstly purchasing an education course on money and investment strategies, how to manage risk, how to use stock market strategies AND, on how profits from the first year of the activity will pay for the extravagant course fees. People flock to learn how this is done under the mistaken belief promoted by the Group, that this is all Government Approved. Fear tactics are used to entice people to sign for a *"on-the-night only discount offer, sweetened by a money back guarantee."*

The whole structure is a con. At times we have found the constructions are merely "martian landing pads." The group may purchase a property, pads are laid down one year later, and then the property changes hands, leaving investors with zero recovery chances. This ploy is used to provide a possible defence of "intention to construct" rather than an obvious intention to de-fraud.

Other times the initial property does not even belong to the person stated in the documentation. Villains have made a mockery of our consumer protection system, the construction industry, the titles offices, the twin peak agencies, the mortgage industry, the non-banking sector and insurance groups. White collar criminals have developed the word "property" as if to mean a prime scam market.

As a nation, to admit we did not understand the model is a sad state of affairs. What is most tragic aspect of these cases is the magnitude of the losses suffered by over 100,000 Australians who need not have carried this burden.

Ultimate losses are difficult to quantify due to the fact that a qualified team of specialists were not called for and, as a result, no proper investigation has taken place. These cases were treated as a misdemeanour as if a little shoplifting was taking place.

A quick reckoning of the size of the loan books, the numbers of "investors" and the security on offer, multiplied by the average investments, reveal that the PONZI of 2000, where \$1.5 billion was lost from a \$5 billion dollar market, would have doubled in the past five years.

By way of example, the WA loans were averaged at \$20,000 per person and the losses in 1992 began with three companies in debt for \$5 million. By 1998, the multiplying effect had blown out in excess of \$100 million in losses.

In the US it is called a PONZI, but others refer to the activities as "doubling" scams.

With Super Choice almost ready to make its debut on the Australian financial markets, consumers will be incredibly vulnerable to a greater number of complex sophisticated scams without a properly constituted consumer protection agency ready to do whatever it takes to protect consumer interests.

The main players have now multiplied in a frenzy of greed, spurred on by promises of easy money and lack of enforcement. Spruikers are still in business, channelling victims towards financial planners. AFS licences have escalated alarmingly. Super Choice is the prize way to steal funds in the current "buyer beware" environment.

United Kingdom residents paid a heavy price for trusting that British Government assurances transferred into notions of preparedness for consumer protection in the area of superannuation churning. No-one it seems was prepared for the superannuation and financial carnage that took place.

Local and overseas players know the Australian authorities are unprepared. Now spruikers from overseas are heading down-under. The Global aspects of this phenomenon should place all security and investment commissioners on full alert.

Perhaps the most shocking aspect of this sorry event in our economic history, is ASIC's recent attempt to demonise consumers. Parliament viewed ASIC as the appropriate protector of consumer interests, in 1998.

ASIC are currently suggesting that taxpayer funds be spent on a "behavioural study" to find out why consumers behave in this way. I would like to personally recommend that ASIC revisits its "Good Advice" program from 1996/97 era.

Taxpayers money would be better spent on a Royal Commission to specifically examine ASIC's failure (and behavioural problems) in its specific duty owed to all consumers of advice and financial products and services.

ASIC's policies have proven to be industry biased due to a distinct lack of grass roots consultation processes and as such consumer end-users no longer trust the current regulatory system.

*(attachment H: Model of Deceit)*

## SECTION 14 ASIC'S POWERS AS FEDERAL REGULATOR

### 14.1 The Little Black Book of Scams

In July 1998 with enthusiasm of becoming a new super regulator from the ASC to the ASIC, regulators across all states joined forces to produce the NSW Fair Trading concept of consumer protection: "The Little Black Book of Scams," dated August 1998, highlighting the dangers of 'get-rich-quick' scams:-

*"Scam operators dress for success....and often try to sell poorly understood financial products...deal only with registered financial planners."*<sup>22,29</sup>

Sadly, this initiative fell far short of the information consumers needed to be fully informed and was not widely distributed. Consumers needed to be empowered with risk conscious material in order to make an informed decision.

### 14.2 Jurisdictional Issues

I am often asked:

*"Just what is ASIC's jurisdiction? We were told by the licensed financial planner, the real estate agent and the developer that this was indeed "ASIC Approved...it was in the advertisements, along with "approved for superannuation investment. Now millions of dollars have gone missing and no-one wants to know."*

Regulation in order to protect market integrity, has prescribed standards and quality of service in the financial markets. Quality of investment advice and consumer protection are recognised by the governing Parliamentary Statutes as the supreme focus of regulatory duties, for the financial well-being of all stakeholders. Hanratty noted concerns over risks attached to financial promises:

*"As a general principle, financial regulation for safety purposes will be required where promises are judged to be difficult to honour, difficult to assess, and likely to produce highly adverse consequences if breached."*<sup>20,19</sup>

The key factor in all of these discussions is that consumers are tricked into investment plans when they rely upon the bona fide of the adviser, to explain all known relevant risks at the point of sale.

*"Management of Financial Risk"* was a key component of the protective mechanisms in legislating for effective consumer protection regulation and enforcement of those laws. When consumers were faced with obvious losses through unconscionable advice in relation to risk management, they were sent letters from ASIC that stated either: *"No resources"* or *"no jurisdiction,"* or *"we will not be investigating at this time."*

I argue these activities were adequately captured under ASIC's existing laws and therefore the consumer complaints did fall under Federal jurisdiction.

If, as ASIC claims they did not have jurisdiction over these practices, then I question why two reports by ASIC staffers conducted in May 2003 and Jun 2003, came to the conclusion that several 'Get Rich Quick Spruikers' were breaching specified provisions of Corporations Law.

These reports came about as a direct result of exposure of spruiker activities by real estate author Neil Jenman and the ABC Four Corners Team in early May 2003.

### 14.3 Investigations

The test of efficiency of regulation can only take place if cases are brought to court. One judge has clearly stated: *"insufficient evidence has been placed before me."* This is not an isolated incident.

ASIC investigators should have attended the education courses due to the obvious misleading deceptive conduct and even the misuse of the ASIC logo and "ASIC Approved,"

statements. All spruiker seminars attended by me, including overseas spruikers, used ASIC's name in some part of their spiel, as a tool of credibility.

Had ASIC read the course notes written in hand-writing by the attendees, the breaches of Corporations Law would have, in my view, been obvious and sufficient to cause immediate closure of these businesses. The Planners would have then been thoroughly exposed and hopefully prosecuted.

The apparent lack of quality of investigations witnessed further substantial growth in spruiker/planner activities in the property investment advice sector. It is evident that the instance of complaints escalated. Chief Bureaucrats had a duty to advise the Minister and apply for further resources. This may have occurred, yet the public perception is that no such recommendations were made by the chief bureaucrats. In any case, the public have not been informed of the outcomes of investigations and are denied any rights to ask questions. Stonewalling has become the norm.

We have not been advised if advice took place and to what extent the Commonwealth Consumer Affairs Advisory Committee ("CCAAC") advised the Minister. We received correspondence suggesting that ASIC officers were simply following "policy." That statement is yet to be tested.

#### **14.4 Letters of Undertaking – Enforceable Undertakings ("EU's")**

In the late nineties, ASIC developed an EU as a cost effective measure to deal with tardy financial planners and/or introducers who have been the subject of written consumer complaints rather than enforcement of law. However, this initiative has proven disastrous for markets and consumers. It was an inappropriate mechanism to be used on serious cases, involving complaints, which clearly demonstrated millions of dollars in losses and financial hardship.

The files also revealed that once fleeced, consumers have rarely been in a position to seek legal advice and civil remedies through the courts. Essentially, rogue traders knew that if you steal a person's castle, then there is freedom from prosecution for the villain. To suggest these people could then afford a lawyer is farcical. I came across very few people who could afford legal advice, some of whom once again suffered further abuse and betrayal of trust by inter-related lawyers to the scammers.

#### **14.5 ASIC suggests civil remedies**

ASIC understood this dilemma. I had discussed the issue on several occasions with ASIC chiefs and staffers during the past seven years. Consumers have been terribly let down in these areas. ASIC letters again stated: "we suggest you seek remedy via the civil courts."

ASIC appeared to be treating case files where fraud seemed evident, as a "civil" matter. Close examination of these files, had serious investigations taken place, would show that company directors who were likely to face "disciplinary measures," could simply sign an Enforceable Undertaking and stay in the business of taking further millions of dollars from innocent consumers.

Policies of this nature have left consumers in an untenable situation.

ASIC had a specific duty with regard to "*fit and proper person*." The dilemma for ASIC became one of inability to hand the rogue directors a licence under the *fit and proper* criteria, but considered them harmless enough to permit them to continue breaking the law. This apparent conflict of interest was no isolated incident. ASIC failed to ask where all the millions of dollars were disappearing to and failed to launch recovery action with respect to compensation for the aggrieved consumers.

Clearly, ASIC's role of consumer protector shifted to that of industry protector.

At times, ASIC made comments suggesting the consumers were greedy, without thought to the feelings of those who had lost their homes or loved ones. We heard statements such as: "*we cannot legislate against greed*."

I raised this point in Australian Story in November 2000: *"the greed was in the people who set up the deals."*

ASIC seemed to have lost its way with consumer protection and this has largely been symptomatic of being given responsibility of serving two masters: industry players and consumers.

It appeared that ASIC did not want the responsibility of handling consumer protection issues. Suggesting these are state issues, flies in the face of reason.

#### **14.6 Questions raised in Parliament**

On February 18, 2004 and June 2, 2004, questions were raised on some of these issues by Senator Conroy and put to ASIC Chairman and staff, in the Parliamentary Economic Estimates Committee. As yet, those who are accountable to Parliament for the information sought by consumers, have yet to provide Parliament with answers to those specific and vital questions.

The public are yet to be informed of the answers to those questions. Meanwhile, seven senior ASIC officers have left the regulator's employ.

Our evidence includes letters from ASIC to the consumers, over a number of years citing "insufficient resources" as a reason for not taking action. One of the questions raised in Parliament, brought an answer from the bureau chiefs: "we have plenty of resources. No we do not require further resources."

To date, no criminal charges have been filed against the most serious and known offenders. ASIC appears therefore, to have decriminalised that which Parliament deemed to be criminal behaviour.

#### **14.7 ASIC data viewed as unreliable**

I noticed in the ASIC report to the MCCA a reported "70 complaints relating to one particular spruiker during 2002-2003." This cannot be true. ASIC staff had hinted at far bigger numbers than that suggested in the report. The complaint letters I have gathered suggests a much wider number of people from six states complained. We are unable to confirm just how many complaint letters were received.

ACCC recorded a significantly higher number. I wish to bring to the Senate Committee's attention that at one stage, complaints were particularly heavy enough to send ASIC response letters from WA and Queensland officers stating: *"no jurisdiction,"* in response to Victorian consumer complaints against Melbourne traders.

I did take it upon myself to ask how and why a west coast state, would be properly able investigate an east coast complaint. I was informed by the writer, that Head Office had received hundreds of complaints and had delegated the letters to others states.

I did look into this matter in some detail after requesting in writing that some 3000 victims write to ASIC. I accept the fact that not all would have bothered to do so.

To state to the MCCA that only 70 complaints had been received would imply an approximate average of 10 per state. I find it difficult to accept these figures. I asked those who had ASIC letters to send me copies, in order to verify the answers being given to consumers and to form my own views as to systematic problems which may be occurring within the offices of the federal regulator.

I started this routine in 1998. I bring this point to the committee's attention because I view the matter as serious. We are suggesting that an audit of ASIC complaint files may be necessary to establish what transpired during the past five years.

## SECTION 15      LEGAL ISSUES

### 15.1    Taking the Narrow View

Investigations ought to have been focused upon the actual activities taking place and subsequent interpretation of laws, needed to be broad in nature rather than the current narrow view taken. Previous professions or existing licences acquired by the scam operators selling these financial products are irrelevant.

The regulator has the responsibility of providing the ultimate determination of whether the legislation governing these activities is effective enough to protect consumer interests.

#### Legal Opinions

From the dawning of the 1997 new age of consumer protectionism in Australia, consumers were consistently receiving letters from all regulatory agencies, and in particular ASIC, stating "not our jurisdiction."

Consumers also received letters from the ACCC stating "your complaint falls under ASIC's jurisdiction."

To break the regulatory impasse, I sought clarification of jurisdictional powers, from three known law firms, in two States, as one of significant community interest and importance.

After briefing the lawyers on the nature of these activities in the finance and property sector and ASIC's responses to our continual questioning, they formed the view that ASIC does have a wide range of powers, that could have seen action taken to assist consumers utilising the provisions set down in all three pieces of legislation mentioned in the Senate Committee's Terms of Reference. (*Attachment D: Legal Opinions*)

### 15.2    Barclays vs ASIC

ASIC used these same suggested powers as a defence in the Barclay case, which I made mention of, in a RECA letter to the Prime Minister, dated 1/7/03 and attached to the Solomon Opinion.

Barclays won this case against ASIC due to the fact that arguments revolved around a database, which Barclays correctly argued, did not pose a risk to consumers.

This case, I believe, proves that ASIC not only had the powers to prosecute those placing consumers at significant risk, but in fact had been advised the same, by their own legal counsel.

The fact that ASIC used the wrong case to demonstrate these powers is irrelevant to the overall argument, other than a grave misjudgement and waste of taxpayers' funds. The point is that consumers were at risk, and ASIC was very aware of those powers. ASIC knew it had been provided with significant legislative provisions and could have, and ought to have applied those same arguments in cases, where significant risk was obvious.

The activities of the professional villains we identified and presented to ASIC on many occasions, did pose a significant risk to consumers.

ASIC officers agreed at the time, that these scams were likened to playing Russian roulette with people's homes and overall financials security. Those who viewed the properly researched files were suitably horrified at the content.

Consumer's best interests were not only hampered by this clear lack of direction or enforcement of law, it could be sensibly argued that consumers were actually being placed at financial risk for a further six years. ASIC admitted it had the powers in certain circumstances, yet I argue that the regulator failed to correctly identify those activities.

I therefore view ASIC's continual procrastinations as unhelpful obstructionism.

Discussions on the quality of advice delivered by real estate agents, lawyers, accountants, valuers, mortgage brokers, financial advisers and planners, needed addressing in the mid nineties. As a nation, we appear to be still grappling with this situation.

### **15.3 Buying of Property was incidental to the financial strategy**

I argue that the buying of the property was incidental to the overall strategy. Had the strategy not been pushed onto the consumer using false and misleading material, pressure tactics, unconscionable conduct, then consumers could not have been left in such a vulnerable financial position. Any one of these activities was an offence under existing laws mentioned above and directly falling under ASIC's jurisdiction.

### **15.4 False and Misleading Information, Deceptive Conduct**

The TPA provisions intend to stop "misleading and deceptive behaviour. The ASIC Act and Corporation Act intended to stop racketeering activities in the financial advice industry by creating a licensing regime.

It is clear that the instance of fraud in the "**advice**" sector, whether property, investment, tax or banking, has escalated to the extent that these inquiries are not only necessary, but for the sake of consumer protection, long overdue.

The legislative provisions contained in the existing Acts mentioned, could easily have been used to break the back of the consortiums by prosecuting all those licensed professionals who were part of any or most of, the components of the PONZI.

### **15.5 Prescribed Interests**

Prescribed interest provisions were introduced by Parliament in 1991 to stop members of the legal and accountancy professions from running further mortgage security **loan books** without strict regulatory supervision. Members of these two professions have been the prime mover of these fraudulent scams, yet of the 127 law firms who were running an average \$60 million in loan books and noted as having defaulting loans, only two have had charges laid.

Exemptions were given to the very professions who stand accused of running these PONZI scams.



**SECTION 16 APRA**

The deposit-bond issues ought to have been fully investigated by APRA when exposed by the *Sydney Morning Herald* and *The Age*, in mid 2004. ASIC had a corresponding duty to advise APRA of the insurance links in these activities.

## SECTION 17      ACCC – Competition Compromised

### 17.1    ACCC Left Powerless

It is my considered opinion that ACCC were left with only limited powers to deal with these problems in any significant way after the 1998 hand-over of consumer interests to ASIC. Injunctions for advertisements meant little could be done to address the consumer-crisis, other than to correct previous advertising.

Staff at the ACCC have continually been frustrated in sending consumer complainant letters back to ASIC marked: "ASIC's jurisdiction." ASIC would then send letters back to the consumers stating: "*not our jurisdiction.*" Consumers were left with regulatory musical chairs, until there were no more chairs in the room and the music had stopped.

### 17.2    Spruiker Tourists Down-Under and Unlicensed.

American and UK Spruikers invaded our shores in 2004. RECA wrote specific letters to the Chairman of ASIC, asking that ASIC use its powers to close down these seminars. We provided valid arguments and proof of false and misleading information contained in advertisements, mail-outs and "free-ticket" material. In addition, we highlighted what we believed to be breaches of the TPA.

I had further concerns about the gathering of Australian resident databases should the content of the shows later prove to be as dishonest as the promotional material.

Due to the nature of intended property investment advice, I considered these seminars to be the flash point in terms of regulatory inaction on behalf of consumer interests.

There were also competition issues in relation to unfair business practices. Included in my concerns was the expectation that millions of dollars would again be lost in the system and consumers find they may be in danger of losing their homes.

It appears that the tourist spruikers do not need an AFS licences, according to ASIC, despite negative information coming from the country of origin of previous activities. I attended most of these seminars.

Once again people were being told "*equity in your home is dead money.*"

Fear tactics were used: "*not enough in retirement,*" and "*join our courses and we will give you the advice you need to be successful,*" and "*you have to have the right strategies.*" "*We love using other people's money, love it.*"

All of these expressions are shades of earlier criminal activity.

No business makes money from "free" seminars, unless accompanied by a secretive campaign to move consumers into a future cyber-lair for further contact. The products and services being offered were characteristically bound by ADVICE. Financial advice was the commodity on offer.

Financial advisers were waiting for the databases. ASIC understood the model, yet failed to attend, despite the warnings from RECA that vulnerable consumers would most likely be at risk, simply by attendance.

### 17.3    Property Investment Advice – the flagship

Property Investment Advice was again the key flagship, followed by taxation advice, share market and trading advice. Consumers were encouraged to extract monies from families and friends, and thereby network others into the same nightmare into pooled investments.

In each case, the seminars were permitted by ASIC to continue, providing that promoters announced at the beginning of each show, amid assurances that they were honest and reputable, that an ASIC directive suggests correction of at least six "*errors*" identified by ASIC.

Serious breaches of Corporations Law and the TPA were deemed by ASIC to be that of "errors of judgement." This gave the impression to the audience (intentionally) that ASIC had gone over the spruiker material and the credibility of the shows were established from that point on.

#### **17.4 Trading Tricks on Wall Street**

Consumers were asked to provide credit card details to borrow material that contained instructions on how to "safely" guide consumers into purchasing shares on Wall Street Stock Exchange. Amid claims that "an unmarried mother" has just invested the equity in her home to win \$35,000 in 10 minutes of playing with a few buttons: is an indication of the skulduggery going on. The audience was assured that "The Australian Stock Exchange is too small to make any money." The Property Investment Advice component of this particular seminar was dropped, yet I watched as 500 people raced forward to sign up.

Our members can perhaps be forgiven for noting a profitable three day trip for the promoters, with active assistance from a helpful regulator.

#### **17.5 American Property Market**

The above investment packages were registered in New Zealand. I hold grave concerns that people will be hooked into a twelve month system that will slowly and surely convince them to use the equity in their homes and superannuation funds and gamble their assets on the US stock exchange. There is no doubt that the original plan had been to entice a new group of Australian consumers to invest in American property markets, using local promoter-linked facilities for finance and advice.

We understand that New Zealand regulators were aware of these particular traders and had issued earlier warnings.

The free tickets which flooded to thousands of Australian letterboxes, posted from the US, were a quiet insidious way in which spruikers could move in a secretive manner into multiple jurisdictions and hold a series of seminars.

#### **17.6 ASIC on Standby Mode**

ASIC permitted the event to take place, knowing the risk to consumers. No AFS licences were needed to provide consumers with this advice re share trading techniques, yet I believe the ADVICE fell under ASIC's jurisdiction, despite ASIC's denials.

I remain convinced that ASIC could have acted in a stronger fashion. I rang the night before to ask if anyone from ASIC NSW had been instructed to attend. The answer was no. Obviously the promoters had assured ASIC of certain things and ASIC were satisfied that consumer protection issues have been adequately dealt with.

## **SECTION 18      COMPETITION ISSUES**

### **ACCC Left Powerless**

Since 1998, the ACCC could only deal with false and misleading advertising, by asking the courts to issue injunctions. The advertisements in the above example had already been published, the registrations gathered and the show went on regardless.

We should all brace ourselves for a down-under tourist spruiker invasion. It seems our consumers, are easy pickings. Databases of 5000 clients from 20 million people justify the expense of a reported \$40,000 per venue, no licences required.

In hindsight, ACCC was far more experienced in dealing with consumer interests than the licensing authority.

Moving forward, consumers interests are better served by the establishment of a dedicated federal consumer agency with powers to take all action necessary against the behaviour and activities described in this RECA submission.

## **SECTION 19 CONSUMER COMPLAINTS**

### **19.1 Increase in consumer complaints**

Big commissions from the finance and banking sectors, continually lure new directors and advisers into the PAFIA sector, bringing federal regulators a new wave of consumer complaints. Further spruiker seminars and activity are emerging on a daily basis.

### **19.2 Strategies for consumer protection**

The Federal Treasurer's intention was clear in his speech on Financial Services Reform on the 17<sup>th</sup> July 2003 that:

*"This regime [FSR provisions under Corporations Law] should promote consumer confidence because financial service advisers must be properly trained and must comply with high standards of advice to consumers."*<sup>15,1</sup>

He further discussed his vision for complaint handling mechanisms and compensation schemes, noting that consumers can only make informed decisions if the financial advice (strategies) given, are of the highest standard. He stated: *"the Government wants to ensure the correct balance between investor protection and commercial flexibility."*<sup>15,1</sup>

## SECTION 20      **INDUSTRY - Internal Dispute Resolutions**

### **20.1    Internal Dispute Resolutions**

In October 1999 ASIC announced in its media release that: *"Industry-based complaints schemes play a vital role in resolving consumer problems in the finance sector."*<sup>5</sup> These schemes were supposed to give independence to the process; however, this has been far removed from those original concepts. Too much responsibility was given to industry bodies in the handling of systemic industry problems.

Industry bodies have set up dispute resolution based consumer complaint bureaus. ASIC wanted to abrogate their responsibilities by passing them onto the IDR's. Serious crime has been treated by industry as being a dispute between two parties, rather than examining the fraudulent and collusive nature of the scams. I accept that the industry bodies are under-resourced and recent media statements from the FPA warn of their lack of funding. As a long standing consumer group we receive no government funding, yet manage to investigate these cases.

It is the age old problem of: *"Caesar judging Caesar."*

### **20.2    Industry Members Frustrated with the Process.**

Consumers I have spoken to and who have used these IDR services were told in writing, that there was no remedy for them.

ASIC would recommend consumers contact FICS, who demonstrated an inability to effectively deal with the problem. FICS had more of a conflict of interest than ASIC. I believe the industry bodies were limited in terms of possible outcomes.

For this reason the wider investigations of these activities were seldom exposed from these complaint sources. I am aware of individual complaints to FICS that have been going on for at least three years.

Industry members, who do not abide by the rules, merely frustrate the process. IDR's are therefore limited in their powers and appear to be useful only for compliant and honest businesses in a genuine dispute with consumers.

### **20.3    Misjudgement of magnitude of growing misconduct**

When Governments and Industry bodies misjudge the enormity of the problem of fraud and white-collar crime, it is consumers who pay the highest possible price: the complete loss of financial freedom and in some cases, stress related problems leading to early departure from this life.

## **SECTION 21      GOVERNMENT AND IOSCO**

### **21.1    IOSCO**

The aim of the Financial Stability Forum (created in Feb 99) was clearly to set an international benchmark in terms of policy strategies and transparent agency activities. However, a simple task of examining the evidence held in consumer complaint files and accurate reporting of the content would have revealed of the collusive nature of these practices across all states and all professions in the finance, property and banking sectors. RECA can be certain of this, due to the files passed on to ASIC at this time.

### **21.2    Warnings of Australian Operators Overseas.**

With regard to agreements with IOSCO, I have asked ASIC to ensure that in regard to certain files, that overseas authorities be notified. Often we become aware of overseas trips by operators that we may be tracking. At times we become aware of their intentions to tap into new markets, under the same businesses. These are traders known to be the subject of numerous consumer complaints here in Australia.

The standard regulatory response has been: *"we will be advising other authorities when our investigations are complete."* Some of these investigations have been going on for a number of years, until case-files are deemed to be "too old to pursue."

Co-operation between IOSCO members could achieve a great deal for consumers, if they were each fully informed of which networks were in operation or likely to set up in their own nation states. Australian spruikers setting up similar businesses in other countries should be of deep concern to us as a nation, in terms of corporate reputation.

Australian villains have been named in at least one overseas Parliament in recent times accompanied by five days of lead story and media attention. Such situations are an embarrassment for our regulatory regime. I reported one of these scams to ASIC in 2002. We received the standard "not our jurisdiction" response letter.

## **SECTION 22 CONSULTATION – CONSUMER GROUPS**

### **22.1 Grass roots Consultation**

It is a fact that consumers are rarely interviewed or consulted, despite the seriousness of the allegations and the obvious financial loss running into billions of dollars. Consumer representatives on the various panels and committees dealing with consumer issues are rarely experienced or engaged in, grass-roots damage control on a national basis.

Industry leaders rarely contact support groups that have formed as a result of high instances of loss amongst the community.

No-one it seems, wants ownership of the problem.

### **22.2 Over-Representation Of Industry Groups**

Consumer support groups receive none of the benefits that industry groups enjoy. There is an over-representation of industry consultation in matters relating to legislative provisions, governmental policy and consumer protection issues. On the other hand we have a glaring under-representation of grass-roots consumer consultation.

### **22.3 Informed decision-making.**

Extensive consultation with all groups would make for better decision-making. Perhaps this is an explanation of how consumers of PAFIA products have become so disenfranchised to date.



## SECTION 23 MARKET INTEGRITY

For regulators to pontificate that: *"there is no evidence suggest..."* is an indictment of the failure of the system designed to promote consumer confidence and market integrity.

These words reflect the appalling attitude that has developed, creating obvious poor assessment practices and outcomes. This situation cannot continue. To sustain this condition is to ignore key market principles of fair, ethical and honest dealings.

### 23.1 Consumer Confidence

I would argue that market integrity has been compromised. Competition for genuine honest and compliant stakeholders in the property and finance sector is tough at the best of times. Consumers and traders realise that a fair and open market place is of paramount importance for consumer confidence.

### 23.2 Unfair Trading

Looting of consumer bank accounts and assets, not only lowers the tone of desired trading conditions, it is seen as a direct threat to competition. Businesses can hardly be said to be competitive if licensed or unlicensed cowboys were out to steal the client's horse. The same client is then prevented from travelling to the next point of trade.

In today's terms the major asset is property and most consumers require finance and financial advice to achieve the first step into the investment market. Consumers need confidence and assistance in order to make an informed decision.

If the home is the only asset and those assets are stolen or lost, other businesses suffer either from lack of future trade or from debt related flow on effects.

A customer without further funds to spend is not a customer. Other businesses, particularly retail markets, miss out on profits when we allow villains to rob people of their major asset, free of any regulatory control.

Linked industries should therefore, develop an interest in the theft of multi-million dollar funds by the fringe dwellers of the financial markets.

### 23.3 Centrelink Issues

Retirees thrown onto the pension lists are hardly a newfound source of wealth. In 1999, I wrote to Ministers Joe Hockey and Senator Newman on these very issues.

In 2000 I became so concerned about consumer protection and market integrity issues, that I took it upon myself to travel to three states (funded by retirees) and spoke with regional directors of federal authorities and their staff. I also visited with Commanders of Fraud Squads at the same time in 2000. I gave first hand details of consumer concerns on Four Corners in May 2000, The Australian Magazine in August 2000, and Australian Story in November 2000.

Retirees who were denied assistance for five years have since lost interest in pursuing losses, due to the pain of the deeming provisions when dealing with Centrelink. They have gracefully accepted the pension, due to the stress of the past five years.

### 23.5 ASIC'S Role – Market Integrity

Market integrity is critical to consumer protection according to recommendations of the Wallis Committee, adopted by the Government, that the proposed Corporations and Financial Services Commission, renamed ASIC, would be responsible for a wide variety of interconnected business activities in the corporate sector including: security dealers, investment advisers and the financial services markets and specifically fund raising activities by corporations:

*"The Treasurer, the Hon. Peter Costello MP, established the Financial System Inquiry (the Wallis Inquiry) in June 1996. It was given a wide brief to stock take the results of the deregulation of the Australian Financial System."*<sup>9,2</sup>  
*"ASIC will be responsible for market integrity, consumer protection and corporations."*<sup>1,3</sup>

The Treasurer contemplated that ASIC would have the sole responsibility as protector of consumer interests and would be using the broadest interpretation of the new laws.

In reading the Council of Financial Regulators' Annual Report of 1998 and 1999,<sup>1</sup> there can be no doubt as to the intention of Government to co-ordinate response to potential threats to financial stability, by setting up a framework, clearly defining the roles of the three main agencies qualified to deal with these matters.

Council described the reasoning behind the establishment of a separate regulator (ASIC):

*"to deal with market integrity and consumer protection issues across the financial system."*<sup>7,5</sup>

The Council's ultimate objective and intention was to debate the matter of quality of advice in the financial markets and contribute to the efficiency and effectiveness of regulation.

In terms of superannuation the Council noted that *"the Treasurer can levy the industry to partially compensate members for losses due to fraud, where such compensation is judged to be in the national interest."*<sup>7,5</sup>

To date, most of these victims have been left in a no-win situation. Consequently, market integrity in the financial services industry, has not yet been accomplished during the past eight years.

## **SECTION 24 STATISTICS**

### **24.1 Grouping Together**

Statistical analysis is another area of scant information, leaving consumers with an acute feeling of neglect. At first, consumers are confused as to who is the appropriate complaint-handler. Those who have experienced loss are traumatised. After being told to complain to ASIC, and then being told "*no jurisdiction*" or "*no resources*," the matter becomes a classic argument for sociologists.

Sufferers of fraud have a need to group together, when all doors have closed victims experience the pain of disenfranchisement.

### **24.2 Lack of statistical analysis**

Frequent periodical statistics are vital if, as a nation, as a caring society, we intend to deliver open and accountable conduct within the regulatory system.

One most frequent complaints by PAFIA stakeholders is the lack of data or statistical analysis, despite the magnitude of the losses and the complaints registered in each state.

Each year over 10,000 complaints are received by ASIC, yet only 250 investigations are carried out. I am referring to the Annual Reports data. WE are told that some of these complaints are regarding minor breaches yet there is no useful breakdown publicly provided that we are aware of. Therefore, accurate assessment of trends and patterns are missing from the regulatory radar.

Consumers are disappointed at the continual stream of unhelpful letters and lack of information on case handling from ASIC.

We asked a private detective to tape answers to questions in an ASIC public information seminar where the solicitor speaker admitted assisting one of the more notorious spruikers and admitting that "*in those circumstances ASIC would have the power to act.*"

I have taken the decision to reveal these facts due to the incredible amount of secrecy that surrounds the process of investigations carried out by the Federal regulator, responsible for regulating, policing and enforcing investment advice strategies.

## **SECTION 25                      LAW ENFORCEMENT - FRAUD**

### **25.1    Estate Mortgages – the Lessons from Loss**

The intention of Governments of all political colour in 1991 ensured: "this (Estate Mortgages) should never happen again." The intention of Government was clear in 1997 re-articulated in the need for further assurances that these "new" 1998 financial services laws would specifically focus upon consumer protection issues.

Criminal sanctions provided the public with a sadly misguided belief that confidence could be placed in the PAFIA sector. Lack of enforcement of law regarding criminal activity became a key factor in the proliferation of these scams.

Few consumers that I am aware of purchased any of these sham products without first taking "advice" from one of the linked providers.

### **25.2    Enforcement – Market Integrity**

Considerable discussion surrounded ASIC being the enforcer of law, in 1998.

*"responsible for standards of financial market behaviour, for financials sector intermediaries, and for selling financial products, including investments, insurance superannuation and deposit-taking activities. These standards aim to protect markets and consumers from manipulation, deception and unfair practices and, more generally, to promote confident participation in the financial system by investors and consumers."*<sup>7,9</sup>

### **25.3    Law Enforcement**

CLEB stressed that the issues of law enforcement are integral to credible financial regulation. The submission referred to market responses conducted by ASC in 1994 and 1996, which reveals a strong consumer belief in that: -

*"Enforcement is the single most important role or function of the companies and securities regulation."*<sup>13,1</sup>

The Commonwealth Law Enforcement Board ("CLEB") acknowledged that financial transactions can and all too often do involve serious crime. They advised: -

*"It must also be stressed that many breaches in law by participants in the financial system can and do result in significant harm to individuals, who are often not in a position to pursue any recompense or recover from the harm that has been inflicted."*<sup>13,13</sup>

CLEB also referred to consequential ramifications to remedies of recovery for consumers who suffer loss through flaws in the financial system.

### **25.4    The Justice System – High Profile Cases**

Our laws are tested via the justice system. Instead of tackling the financial planning industry complaints, officers were being asked to spend valuable resources looking into 'high profile' cases, which would not overly benefit the community as whole. Significant losses to ordinary individuals were being over-looked, despite widespread non-compliance.

Consumers believe the 'high profile' factor has become a key indicator that the PAFIA sector was too widespread for regulators to tackle.

RECA members believe that inappropriate use of resources dried up the enforcement budget, by activating high profile cases that would bring the least relief to the greatest number of consumers.

### **25.5    Fraud in the Finance Sector**

In discussing fraud in the finance sector, fraud on consumers, including superannuation, securities, non-banks and financial institutions, CLEB commissioned a report from John Walker Consulting Services: -

*"crime (fraud) costs the Australian community a total of some \$10 billion to \$12 billion per annum (2.5% of the GDP)." <sup>25,4</sup>*

**25.6 NCA Statistics**

The 1991 National Crime Authority report on Money Laundering named 'real estate' as one of the top five industries engaged in organised crime. In fact property was named as a key factor in most transactions used in a variety of models of criminal dealings. <sup>27,41</sup>

## SECTION 26 NATIONAL APPROACH FOR CONSUMERS

### 26.1 State Ministries – Consumer Affairs

The State Ministries have frequently argued that their legislation did not cover financial advice. The point has been clearly made by all stakeholders that a national approach was urgently needed on the subject of consumer protection in terms of property and finance.

Consumers who used these investment strategies were not covered by state-based legislation, irrespective whether the “introducer” held a licence.

As one former trader explained: *“Unless the valuation was exaggerated, there was no profit for anyone. It’s the way it worked. We couldn’t tell the consumer those details or they would never have invested. You really are gambling on the rise in the property market. Of course you use other people’s money, not your own. If it starts to wobble you just pick up the funds in the next state. The funds are moved offshore very quickly.”*

For two decades, consumers have been, and continue to be exposed to scams run by licensed and unlicensed players in the property and finance markets.

### 26.2 Law Societies – inadequate supervision

ASIC passed on the regulatory responsibility of investigating and prosecuting villains in the legal professions, to inadequate disciplinary supervision offered by the state-based legislative provisions governing Law Societies. We found those complained against were on the various committees. Consumers stood little chance of having proper investigations conducted by these quasi-agencies. None of the traders, in the hundreds of files we have examined, would have passed a reasonable *‘fit and proper person’* test.

### 26.3 Exemptions - Lawyers and Accountants

Clearly, those particular operators could not be trusted. Due to intense lobbying by powerful industry groups, it was the legal profession and the accountancy profession that gained “exemptions” from ASIC that was never contemplated by Parliament.

The regulator has exempted the very class of people that were running the scams resulting in hundreds of millions of dollars of recorded losses.

### 26.4 Industry based IDR’s no remedy for consumers

Industry-based dispute mechanisms could never take the place of proper and adequate investigations into organised white-collar crime. IDR’s are only useful from a general compliance perspective and industry advisory issues. Too many biases prevent effective consumer representation.

Consumers once again paid the highest possible price for this ill-conceived policy, of passing regulatory responsibility for enforcement of law onto industry bodies.

Hanratty also stated that:

*“Professional advisers, such as accountants and lawyers, should not be required to hold a financial advisory licence **if** they provide investment advice only incidentally to their other business and rebate any commissions back to their clients.”<sup>20.12</sup>*

During the past four years, lawyers and accountants have again received class order exemptions from Corporations Law. The Queensland Government has had to act against the Queensland Law Society, as did the Tasmanian Government against the Tasmanian Law Society.

Many of the Law firms (127 East Coast law firms, named in the ASIC 1999 run-out list) had clearly converted their businesses to financial planning activities, which were hardly ‘incidental’ to the main part of the business of law.

With regard to financial products, Hanratty (1997) observed:

*“Broader regulation of ‘financial products’ should replace current less flexible securities and futures law.” “The ASIC should have broad enforcement powers and*

resources which are adequate for carrying out its responsibilities...and the referral of matters to the Director of Prosecutions for criminal prosecution."<sup>20,12</sup> And:

If we ever were in any doubt that these issues ought to have been widely canvassed in the interests of both consumer protection and market integrity, he added:

*"Financial safety is fundamental to the smooth operation of the economic system."*  
<sup>20,12</sup>

## SECTION 27 COMPENSATION ISSUES

### 27.1 Collectivism issues

One specific area where ASIC could have assisted victims of these pernicious practices is in the area of compensation. Investors who had suffered significant losses averaging \$50,000 - \$400,000, received response letters from the regulator that gave little assistance. RECA wrote several times to ASIC to request assistance by way of a letter sent to each of the victims in a group and suggest they contact a group spokesperson or the local support group.

ASIC's non co-operation in this area is viewed by consumers as obstructionist rather than helpful. Generally, victims were simply told to seek their own legal remedy. After being fleeced by the villains, consumers expressed an inability to afford to seek legal advice.

Once again, ASIC had powers to assist and failed to use them. The victims of these crimes come from all over Australia and due to the travelling habits of the Spruikers, grouping people together became geographically impossible. Calling a meeting in one city would prohibit 80% of the group from attending due to the fact that one scam could net victims in all states.

### 27.2 Legal Opinion on Compensation issues

RECA then approached ASIC to assist with compensation. These initiatives have also been ignored. In one particular case, ASIC had a chance to freeze accounts and recover tens of millions of dollars from the villain company, but failed to do so.

We asked Doug Solomon, of Solomon Brothers to give advice on this issue. In his legal opinion dated 21<sup>st</sup> June 2004, which ASIC has also ignored. The following paragraphs explain his interpretations of the compensation issue:-

*"Not only did ASIC have the power to put the spruikers out of business, there are strong consumer protection provisions in the ASIC Act 2001 which are for the benefit of consumers. ASIC is empowered to pursue claims by court action to recover compensation for the benefit of victims who consent to ASIC doing so."*  
28. at 18

*"The court must give priority to ordering compensation to victims, rather than imposing fines."* 28. at 18

*"Given that one of ASIC's objectives is promoting the protection of consumer interests, it has every reason to seek compensation for victims of spruikers and, if ASIC refuses to do so, the Minister could be pressed to direct ASIC to give priority to doing so."* 28. at 18

Solomon made this opinion public, as a community gesture, to assist RECA in its quest for justice for these people.

ASIC's conduct in these matters is further proof of the need to take consumer protection matters out of the hands of ASIC. All steps should be taken to avoid delegating this task to any agency that would then be placed in the same invidious position of serving two masters.

Our RECA Model of setting up a National Consumer Protection Agency is detailed in the answers to the Terms of Reference for the Property Investment Advice Inquiry.



## SECTION 28 SUPER CHOICE

### 28.1 Single Responsible Entities

Our research discovered real estate valuers, already the subject of high profile corporate complaints in the property and finance market, applying as "company directors" to become Single Responsible Entities. Known dishonest professionals are becoming part of the consumer protection process supposedly monitoring the activities of companies engaging in large capital raising activities.

Despite a committee being set up in 1998 to exchange important information of any activity, which was likely to affect the stability of the financial markets, *with due regard to the urgency of doing so,*"<sup>7,29</sup> the issue of infiltration by valuers of ill-repute invading the domain of SRE mechanisms, no admittance to this became apparent until a few months ago. ASIC then revealed a staggering 85% of SRE's were non-compliant with current regulations in the finance sector.

We would argue that the agency in control of this flow of information, ought to have looked closely at the activities of valuers, lawyers and accountants, in terms of previous links with property investment advice businesses.

### 28.2 Infiltration of Boards and Committees lobbying Government

Mr Chris Connelly, Director of Financial Services Consumer Policy Centre raised extremely serious concerns of inappropriate "consumer representatives," in a Choice article in June 2001, that:

*"The Boards and Panels of these schemes are now stacked....and the consumer movement has no confidence in the schemes' ability to conduct themselves with integrity and independence."*<sup>11,1</sup>

We advised ASIC Commissioners of this concern with respect to SRE's and Mezzanine Mortgage lending, debenture scams and inter-connected property investment advice in 2001.

### 28.2 Superannuation Churning in UK

We note that the UK experience where 'churning' occurred and lunchtime "advisory chats" became easy "sign-up sessions," thousands of innocent workers found their savings and superannuation funds completely dissipated within 12 months of re-investing.

The 45% increase in DIY funds in Australia, has been channelled on advice from professional advisers, into the risky end of the property market. We note the Government's concerns on this point, given the instance of property spruikers in the finance sector and dual dishonesty in the accountancy and legal professions: -

*In the UK, many members of generous defined benefit schemes were enticed to leave those schemes and transfer to inferior products. In order to minimise the risk of a similar experience in Australia, the government has included in the choice legislation a provision that.....employers are responsible for advising their employees of the implications of leaving that fund to join another."*

This leaves employees with the responsibility of warning their employees of the risks associated with the "churners," or their products and services. In the UK people found they were enticed to swap funds for an additional 3%, which over 30 years, projects as mega dollars on a compounding basis.

Yet, one year later, those consumers found not only were the forecasts wrong, but their capital had been completely lost in the system.

### 28.3 CHOICE Surveys

Once again consumers will need to seek advice. Quality of advice is of paramount importance for consumers to empower themselves to make an informed judgement. If CHOICE Magazine surveys are an accurate indicator of the wider financial services sector, then less than 30% of advice can even remotely be trusted.

I have no reason to doubt this deplorable situation.

Spruiker/introducers will be warning consumers not to trust their employer's "advice." Figures will be presented to confuse consumers and drive the fear home. Regulators will remain in the same dangerous "monitoring" mode.

Young people and also those about to retire will be the biggest targets. Kickbacks in terms of client databases are chronically under-policed.

#### **28.4 Warnings Needed – Super Advice**

My advice would be to warn of the dangers in this matter, describing the UK situation. Warn of the lack of regulatory control. Those who feel they need advice should speak with six advisers (no matter the cost), to understand the "super industry spiel" and gain information, to discover who is really telling the truth and who is blatantly dishonest.

#### **28.5 Superannuation and deregulation**

The Wallis Committee also recommended that consumer protection be assured prior to the advent of any deregulation of the superannuation market.

and this:

*"The Australian Government is planning to introduce Super Choice. Based on the current performance of some planners, that's a disaster waiting to happen unless consumers are fully protected."*<sup>3.2</sup>

Whilst there is continued disorder, RECA members fear that slick practitioners will simply swing on to Super Choice to promote DIY strategies via accountants, linked to other professionals who appear in our files. Whilst current legislation may make those activities difficult we have further information that new hybrids of scams are already in operation.

Consumers seeking advice will be left with Bad Choice if the wrong choice of adviser is made. I believe that our first duty is to clean up the consumer complaint handling system in the PAFIA sector, so that consumer protection can eventually and hopefully, be relied upon.

## RECA SUBMISSION TO THE SENATE INQUIRY ON PROPERTY INVESTMENT ADVICE, February 2005

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