

TO : All members of the ASIC Oversight Committee

CC : The Australian Media

FROM : Graham MacAulay, President Westpoint Investors Group
PO Box 1490 Miranda
gmac@ihugcom.au 02 9525 2396 0411 141 888

Date : 22 September, 2008

Subject : Matters arising out of the ASIC Oversight Committee's Report of August 2008

Dear ASIC Oversight Committee Member,

Perusal of the [Hansard August 2008 Report](#) only increases my dismay of achieving effective regulation of the Australian marketplace. Any vague hope I once harboured of the current ASIC administration repairing ASIC's past damage plummeted to even greater depths than my previous dismal expectation level. The report left me with the distinct impression the Oversight Committee was very dissatisfied with ASIC performance, but did not know how to approach rectifying the problem.

I possess no formal legal qualifications. However, I have had extensive systems experience. Enough to know some changes in legislation may be required, but the current laws are not the prime cause of the shambles in the current Australian Financial Regulatory System. Financial regulation is much more than the enforcing of a collection of prescribed laws (a matter in which our regulators have largely failed). ASIC's performance to date is best described as a regulatory disaster.

ASIC claims it has difficulty in judging how "heavy-handed" it should be (Para. 2.11). I contend ASIC does not, in the everyday semantic meaning of the word, regulate anything. Parliament prescribes the laws for all participants in the financial marketplace, and the market runs freely under the application of those rules. ASIC's defined role is twofold: Enforcement of the legislated financial marketplace laws, and the protection of financial consumers. I can find nothing in the legislature that infers anything about "heavy-handedness". Surely the law is the law, and if ASIC finds a marketplace participant has broken the law, then no matter how minor the breach, ASIC has a clear duty to pass the matters on to the appropriate authority. ASIC is the policeman - not the judge. That ASIC does not fully understand its role is borne out in Para 2.9, where it speaks about an external advisory panel. The only conclusion one can draw is that the current ASIC management lacks confidence it can do the job by itself. If legislation is unclear, then it has a duty to refer the matter back to Parliament for clarification.

ASIC has consistently ignored its role of financial consumer protection - a major reason the Howard Government gave for the creation of ASIC. ASIC's arbitrary judgements have been disastrous for the very people it has sworn to protect. The previous ASIC Chairman, Jeff Lucy gave as the reason for not taking earlier action on Westpoint; he didn't want to be unfair to Westpoint!

The Report clearly indicates the Committee's dissatisfaction with ASIC's ubiquitous warnings (Para. 2.7). How many times has one read in the press where ASIC ignored a warning about a company only to see the inevitable disaster unfold? ASIC's warnings are no more than hot air. One can only agree with the committee; ASIC has a duty to act on infringements - not issue warnings that no one heeds. ASIC offered the same warnings excuse after the collapses of Westpoint, Fincorp, and ACR. In doing so it failed to mention the following salient points

1. The alleged warnings were vague and of a very general nature. In no instance did they come close to referring any particular product by name.
2. The warnings appeared ASIC website. At the time of these warnings, where even with considerable computing experience it was difficult to find them. ASIC has since altered the abysmal user interface on its website with a slightly more user-friendlier one. Even today the warnings are not easy to find -

- particularly for those with little computing expertise.
3. ASIC has never warned the general public via media advertising
 4. In respect of the warnings, ASIC took no action on any of the companies until much later.

A classic instance of ASIC ignoring warnings involves the current ASIC Chairman, [Alan Kohler interviewed Tony D'Aloisio in 2005](#) when he was the ASX CEO. Kohler queried D'Aloisio at some length on insider trading. No record exists of Tony D'Aloisio making any effort to initiate action prior to the problem exploding into public view earlier this year. However, when other regulators around the world banned short selling, ASIC made its 'me too' declaration, and banned short selling. In discussion with 2UE's Mike Carlton on 22-09-2008, a senior SMH financial journalist claimed ASIC instituted an inquiry into short selling and market manipulation instead of acting. He stated that many of the problems arose in this area because ASIC had never applied the existing laws, and he went on to claim that ASIC's outright ban was the worst possible solution, as it would disrupt the market. .

ASIC possesses a deserved reputation, stretching back from its inception, of being too close to the suppliers and sellers of products and of tardiness in taking action. It has never learned that immediate severe punitive action the moment a problem surfaces would quickly teach potential wrongdoers - regardless of the nature of their intent - to consider their actions carefully. Nor have they learned that such action results in a greatly reduced workload.

In Para 2.10, ASIC claims it is very good at cleaning up, but gives no evidence of its successes in this area. What did ASIC do to clean up after the collapses of HIH, ONE.TEL, Westpoint, ACR, FINCORP, and OPES to name but a few companies. ASIC conveniently forgets to mention its failure of timely preventive action adding to investor losses on each of the above companies.

That ASIC does not possess a specialised central intelligence unit (determined under questioning from Senator Boyce) beggars belief. It is a glaring example of ASIC not knowing the benefit of information. The Report mentioned callers providing ASIC with information, only to see ASIC take no action. It mentioned ASIC upsetting callers by not ringing them back to let them know the outcome of an investigation. People who have contacted me have had exactly the same experience. They found the experience an exercise in frustration. In the overwhelming majority of cases ASIC's response left the caller most dissatisfied. ASIC does not inform the caller they cannot accept the information unless they give their name and contact details. Without the contact details, both the information and Ascii's statistics lose validity. ASIC very rarely bothers contacting a caller who has supplied contact details again to let them know the result of any investigation.

The ASX, among others, has in the past brought ASIC's attention to numerous problems. ASIC's characteristic response has been to ignore these warnings until they burst into the public domain. This reluctance to take timely action is not restricted to any particular segment of the marketplace. ASX, with its obvious conflict of interest, should never have been a co-regulator. ASIC has never complained about this matter demonstrates its lack of interest in ensuring the image of marketplace as being free of favour to any party.

Given its laxity in information gathering techniques, ASIC currently has no chance of identifying emerging problems at an early stage.

The Report discussed the failures of Westpoint, ACR, and Fincorp. In the case of both Fincorp and ACR, ASIC placed a number of stop orders on each of them. In every instance the cause of the stop order arose from inadequate disclosure in prospectuses. In one case involving Fincorp, the Court found the company had issued a "deliberately false and misleading" prospectus. As with each of the other instances of unsatisfactory prospectuses, ASIC took no punitive action. Although the court ordered repayment to the affected investors, Fincorp went on to fleece financial consumers of a further \$90 million before its collapse. How many times must an entity transgress before ASIC initiates prosecution? Investors rely on prospectus information when making critical investment decisions. It is

clearly the duty of a company to ensure a prospectus meets the necessary standards before submission to ASIC, and ASIC vets it before the product reaches the marketplace. ASIC has admitted in the press it reads only about 2% of prospectuses. In the majority of cases this happens after a company has collapsed.

ASIC's failure in the Westpoint case is somewhat unique. The well-known advocate Denise Brailey warned ASIC about the dangers of Westpoint Mezzanine products before they ever reached the marketplace; ASIC provided a document to Westpoint lawyers, Freehills in 2000 indicating ASIC would take no action on the use of promissory notes; Denise Brailey spoke with the Queensland Commissioner in 2001 (Channel Ten's *David and Kim Show* of 05-05-2007; in 2002 the West Australian Government wrote the first of its five letters to ASIC and Treasury; Keibel Investment Bank (a fictitious entity) promoted Westpoint Mezzanine products for three years without detection either ASIC or APRA; [ASIC's Mark Steward claimed ASIC "cat and moused" for months in 2003](#); in 2004 ASIC started proceeding against Westpoint on a number of counts including the use of promissory notes (they lost some and won others); in 2006 the WA Supreme Court found the Mezzanine Company test cases from the 2004 action were illegal MIS's; [Westpoint's Norm Carey wrote to Tony D'Aloisio on 30-07-2007](#) with the documents containing details of ASIC's actions on Westpoint and Westpoint's presentation to ASIC in 2003 - well before Jeff Lucy told a Senate Estimate Committee meeting ASIC first became concerned about Westpoint in 2004. In short, ASIC failed to detect the Westpoint Mezzanine companies were illegal MIS's from the outset, and took no action on the many warnings they received in the intervening years. ASIC's suppression of critical material denied Westpoint Investors making informed decisions.

At a meeting of ASIC and the Westpoint Investor Group's executive committee on [08-11-2007](#), Tony D'Aloisio refused to discuss ASIC's negligence/incompetence in not recognising the Westpoint Mezzanine Schemes as MIS's, and why ASIC should not be responsible for investor losses. He also stated he was more interested in what happened in the future, than the past. One can only assume Tony D'Aloisio believes all past ASIC responsibility ceased with his appointment. I refer the committee to my unanswered document of [12-02-2008 to Mr. D'Aloisio](#). Presumably, the reason ASIC does provide truthful answers to the questions it raises is ASIC would then have to provide answers elsewhere. I request the ASIC Oversight Committee direct ASIC to provide answers to those questions. I look forward to Mr D'Aloisio's reply.

Para 2.20 of the Report discusses personal indemnity insurance (PII). The law as it previously stood did not demand an AFSL holder have PII. Contrary to popular belief, most of the planners involved in the Westpoint collapse did possess a reasonable amount of PII. The main problem for investors was the escape clauses in the policies of the half dozen insurance companies involved. It is now mandatory all AFSL holders possess PII. However, the possibility of escape clauses in the policies remains. The only real solution is Parliament prescribes the policy contents. If that happened, there is a very high probability insurance companies would cease offering PII policies and no planner would be able to "spruik your money is safe because of our insurance policy", as they have in the past. A natural assumption from the above is ASIC considers the profits of planners and insurance companies more important than investor losses. Lost business in the marketplace is unthinkable when a new crop of investors waits patiently in line for the fleecing of their hard-earned savings. Note how the current situation passes high cost PII to the planner, and how the smaller end of the planning market subsidises the very large companies (see the [Investor Daily of 22-09-2008](#)).

ASIC claims, in Para 2.18, it has a recovery of \$300 million underway for Westpoint investors. The claim raises interesting questions. It is almost three years since the Westpoint collapse. Dissipation of the original money in a variety of ways ensures a lowering of the original available money. In addition, no one knows how much of the money was available three years ago. It is highly unlikely the Section 50's underway, and any ASIC might undertake in the future, will recover a figure anywhere near the claimed \$300 million. IMF, a company with considerable resources and a proven record of chasing money, put considerable research into this matter and launched action against only three or four

entities. If ASIC is to achieve even a third of the figure they claim they will obtain, it must possess research techniques far in excess of those of IMF. Given its poor performance in major trials, which required major research, ASIC's claim seems fanciful.

The Committee's disquiet about FICS is well founded. I respectfully refer the members of the Oversight Committee to a series of [documents exchanged between FICS and myself](#), and leave determination of whether FICS has been a credible organisation to each member.

The document written to [Senator Sherry dated 03-09-2008](#) is mandatory reading for the Oversight Committee. I have yet to receive an acknowledgement for its receipt, but I look forward to Senator Sherry's considered reply.

Daily, one reads of further collapses that have their roots in ASIC's failure to carry out its designated function. With each new such company failure, more hapless investors (ASIC victims) add to those who have already suffered the same fate and now receive the pension. Every Australian taxpayer pays for the ever-increasing costs of these pensions and their associated outlays in other areas. Having worked all of their lives, the victims pay a high price - financially and emotionally - for their trust in the Australian Government. How many more victims will ASIC's incompetence/negligence throw on the scrapheap, and why have successive Governments refused to take the necessary remedial action?

The current ASIC thinking in solving the current regulatory problem lies in improving disclosure. One cannot disagree disclosure of those offering products, and relevant events in a company's life affects investors, and is a necessity. However, despite its importance, it is not the panacea the current ASIC administration claims. The major problems in the marketplace have occurred because of ASIC's unwillingness to take the necessary preventive action the moment a problem is detected, and deal harshly with those who flout the rules of the marketplace. If the rules are inadequate, then ASIC has a clear duty to publicly approach Parliament to have the rules strengthened. That has not happened to date. It is time ASIC stopped trying to pass its duties on to others. With the undeniable evidence of ASIC failure, and no coherent detailed plan on how to repair the current problems, and ensure it does not repeat the mistakes of the past, one can have no confidence in the current ASIC management. Particularly when they have so diligently withheld the truth on so many occasions. To date, ASIC's presentation of how it intends to fix the current problems has been little more than a morass of unintegrated generalities.

The overwhelming evidence is ASIC has failed cataclysmically (if the reader disagrees, please browse [Need for Royal Commission](#) on www.wig.org.au). However, much of the website information is limited to Westpoint material. Should the reader require other entities suffering because of ASIC's negligence/incompetence, then please contact me and I will supply a list of contacts.

It may be repetitious, but the simple fact remains: had ASIC applied the current laws diligently, the current chaos in the marketplace would not exist. Appointing capable people to positions before the design of an integrated system employing generalisation, and making full use of monitoring and intelligence gathering techniques is not the correct approach. To date, either ASIC management has not recognised this simple concept, or chosen to ignore it. It is natural that a systems approach will not fix all problems, and there are some problems that demand some form of change in legislation. The majority of the regulatory are mundane, and need little more than strict application of the law. An integrated system would quickly see their demise, releasing personnel and other resources to concentrate on those of a more complex nature.

Thank you for reading this document, I hope my input is of benefit to the ASIC Oversight Committee. I also hope you join the rapidly growing number of people who not only demand the [open inquiry Senator Sherry promised](#), but demand it should be a Royal Commission.

Graham MacAulay