

1 • **SENATE ECONOMICS COMMITTEE**

2 **Budget Estimates hearings**

3 Wednesday 31 May 2006.

4 ASIC witnesses: Jeffrey Lucy; Chairman. Australian Securities and Investments Commission
5 Jeremy Cooper; Deputy Chairman. Australian Securities and Investments Commission Mark
6 Steward; Deputy Executive Director, ASIC Enforcement directorate

7 **Discussions regarding the Westpoint group**

8

9 **Senator WATSON**—My first questions concern the Westpoint scheme. If I may commence
10 with the general observation that I believe the Senate is increasingly becoming frustrated by the
11 inability of regulators to act in a timely manner to prevent consumers from unnecessary losses
12 and hardship, and the subsequent discovery of legislative gaps in regulatory powers. I remind
13 you, Mr Lucy, that the most recent case came before us yesterday, when the regulator in that
14 case, the Australian Taxation Office, sought to quickly remedy the problem. Therefore, I ask
15 you: were concerns about Westpoint's operations formally raised with ASIC as early as 2001
16 by the Real Estate Consumers Association and in 2002 by the Western Australian government,
17 in particular about an apparent gap in the Corporations Act in relation to
18 promissory notes?

19

20 **Watson clearly expresses the growing concern with ASIC's lack of action.**

21

22 **Mr Lucy**—I am very happy to answer that. Indeed, I think it is important that we again put on
23 the record the background to Westpoint, because there is some misunderstanding.

24 **Senator WATSON**—Misunderstanding by whom?

25 **Mr Lucy**—The media in particular.

26 **The media had been very critical of ASIC, and Lucy in particular.**

27

28 **CHAIR**—Senator Watson, let Mr Lucy make the preliminary remark he wants to make.

29 **Mr Lucy**—If I could remind the Senate that Jeremy Cooper does not participate in matters to
30 do with Westpoint, so to the extent that he does not respond on these issues it is simply a
31 reflection of his ongoing situation regarding a former conflict, so he is not engaged. I am
32 engaged. I have advised the Senate of that previously. I am engaged literally on a daily basis.
33 But Mark Steward is engaged on a minute-by-minute basis as far as Westpoint. With your
34 indulgence, I will ask Mark to perhaps talk about where our investigation is at the moment,
35 although we do have some constraints as to what we can talk about. Nevertheless, as fully as we
36 possibly can, he can talk about our investigation, and then trace back to 2001, the earlier date
37 that Senator Watson referred to.

38 **The ASIC Deputy Chairman barred himself from commenting on Westpoint. He did so based**
39 **on a twenty minute conversation with Westpoint many years prior. All very strange.**

40

41 **CHAIR**—I know this goes without saying, but let me just say for the record anyhow that, if
42 any questions trespass beyond what you feel you are able to answer without compromising
43 the investigation, you will indicate it at once, won't you, Mr Lucy?

44 **Mr Lucy**—Thank you, Chairman.

45 **Senator WATSON**—Mr Lucy, that may well come later, because I would like to find an
46 orderly development in terms of a calendar approach to how you have managed this scheme,
47 rather than where we are now, because where we are now is that millions of dollars have been
48 lost, homes have been broken, fortunes have been lost and there is a lot of hardship out there. I
49 would like an answer to my question, firstly, going to 2001 and concerns from the Real Estate
50 Consumers Association, and then in 2002 from the Western Australian government about an
51 apparent gap in the Corporations Act in relation to promissory notes. And then in due course, I
52 think we will come up to the current situation, which obviously we have a lot of interest in.

53 **Watson raises the matter of the effect of the Westpoint tragedy on people early in the**
54 **discussion, and then sets the pattern of the way he wants to discuss matters. In short, he lets**
55 **ASIC know who is in charge from the outset.**

56
57 **Mr Lucy**—Up to the year 2004, which of course encompasses the years 2001 and 2002, ASIC
58 received an aggregate of 12 complaints to do with Westpoint. During that period, we would
59 have typically received about 40,000 complaints. Of those 12 complaints, none related to any
60 suggestion of financial difficulty as far as the Westpoint Group. None related to its viability as
61 an operation. All of the questions related to our jurisdiction.

62 **Lucy tries to steer the argument away from the human tragedy.**

63 **RECA were not complaining about a gap in the act. In 2001 Denise Brailey, who knew at that**
64 **stage the Westpoint Mezzanine Model was an illegal MIS, spoke to the Queensland ASIC**
65 **Commissioner and his advisers. He stated ASIC knew it was an MIS and a lot of people would**
66 **lose their money. She made a statement to this effect on Channel Ten's *David and Kim* show on**
67 **05/05/2007.**

68
69 **The WA wrote a total of five letters to ASIC and the Treasury between 2004 and 2004. [I have**
70 **spoken to Denis Brailey, then President of RECA. See also the [Edwards letter](#) in reference to**
71 **the WA letters.**

72
73 **Senator WATSON**—That was not my question, with respect, Mr Lucy. My question was:
74 were concerns about Westpoint's operations formally raised with ASIC as early as 2001 by
75 the Real Estate Consumers Association and in 2002 by the Western Australian government
76 about an apparent gap in the Corporations Act in relation to promissory notes? I am not
77 asking about how many you received or whether it was financially viable. My question was
78 quite specific. It was about two organisations that allegedly approached you in 2001 and
79 2002 concerning a legislative gap.

80 **It seems Watson was very aware of the facts, and comes back on Lucy to answer the question.**

81
82 **Mr Lucy**—I will ask Mark to respond, but I was indeed responding to your point and your
83 comment regarding the apparent inability of regulators to protect consumers, and the
84 regulatory gap. That was the reason I was talking about that. But let us ask Mark to respond to
85 your specific questions.

86 **Lucy gets out of it by flicking the question over to Steward.**

87 **Mr Steward**—There were issues raised about the fact that promissory notes did not appear to
88 be regulated under the Corporations Act. There was certainly correspondence—I am not sure

89 there was any correspondence from the first organisation you mentioned in 2001—and
90 certainly there was ongoing discussion with the Department of Consumer and Employment
91 Protection in Western Australia and staff of ASIC about a whole range of consumer issues.
92 One of those issues was the fact that there was no coverage under the Corporations Act of
93 promissory notes, and in particular there was correspondence about consumer warnings that
94 both the Minister for Consumer and Employment Protection in Western Australia was issuing
95 in 2002 and that ASIC was also raising about mezzanine finance. The answer to your question
96 is, yes.

97 Mark Stewards was a key ASIC person in the case against Westpoint and would have
98 researched all available evidence on the matter. Note how he waffles before answering yes to
99 the question.

100

101 **Senator WATSON**—Obviously, you have confirmed the Western Australian government’s
102 acknowledgment of a gap in 2002. But you cannot recall correspondence? Could you check
103 your correspondence from the Real Estate Consumers Association?

104 **Mr Lucy**—We have checked that, and there is no correspondence. There were
105 communications, but there was no correspondence.

106 Given Denise Brailey’s claim above that RECA wrote to ASIC only two possibilities exist:

- 107 • This is a deliberate lie.
- 108 • ASIC’s records were incomplete.

109

110 A conversation with Denise Brailey indicates the latter was certainly true. How can ASIC
111 regulate if does not keep accurate records?

112

113 **Senator WATSON**—What was the nature of that communication?

114 **Mr Steward**—I think it was the same issue that was being discussed between ASIC officers
115 and officers of the Department of Consumer and Employment Protection in Western Australia,
116 that there was no coverage on the face of the Corporations Act for these sorts of promissory
117 notes.

118 Steward claims discussions between ASIC and the WA Government took place on the basis
119 there was no coverage in the Corporations ACT for these sorts of promissory notes. **Strange,**
120 **as ASIC gave Westpoint the authority to use these promissory notes. [See [Freehills Letter](#)].**

121 **Senator WATSON**—The lesson is that people have to write to you rather than just
122 communicate with you?

123 Watson’s query seems to indicate he believes ASIC will not take notice of an informant unless
124 they a provable formal document exists.

125

126 **Mr Lucy**—No, of course not.

127 **Senator WATSON**—You said they contacted you or communicated with you but did not
128 write to you.

129 Watson wants to know if ASIC possesses correspondence from the WA Government and
130 RECA.

131 **Mr Lucy**—Sorry; it was a misunderstanding. I thought you were using the word
132 ‘communicate’ as in written communications. That was the specific point that I was
133 responding to. You are quite right. I will make the point clear: yes, we received oral
134 communications.

135 **This is at odds with Brailey’s claims and the Edwards letter.**

136

137 **Senator WATSON**—My next question follows from that: how many Westpoint projects were
138 established between those initial concerns being raised and the eventual collapse of this
139 organisation?

140 **Mr Steward**—I am not sure what you mean by ‘projects’. Certainly in 2002 when there were
141 discussions between the Department of Consumer and Employment Protection in WA and staff
142 of ASIC and consumer warnings were issued, ASIC also started looking more closely at what
143 could be done to deal with the risk that seemed to exist. A matter was commenced in the
144 enforcement directorate of ASIC in January or February 2003 to look more closely at this issue.
145 That exercise has largely been ongoing since that time. I am not sure what you mean by
146 ‘different projects’. There have obviously been different actions and different formulations
147 since the beginning of 2003, but certainly there has been something ongoing since then.

148 **I can’t understand why Steward had problems with this. The meaning of the term project is**
149 **simple enough. Westpoint created issued a new, and “independent” mezzanine scheme for each**
150 **of the projects it undertook. Steward never answered the simple question f how many were**
151 **raised in the indicated period. I read this an indication that had ASIC taken early action, then**
152 **many of these projects (probabl all) would not have arisen.**

153 **Senator WATSON**—In other words, Westpoint added to its structure and continued to
154 borrow money to finance its new widened operations?

155 **Watson makes the point that Westpoint added to its structure (funded by the public). The**
156 **implied point is that they continued to this while ASIC wondered what it should do – and did**
157 **nothing.**

158 **Mr Lucy**—Absolutely. But, again, a lot of the money was in a structure that was determined
159 by parliament. Parliament specifically carved out promissory notes of greater than \$50,000,
160 and Westpoint exploited that.

161 **Lucy agrees (I doubt if he understood what Watson was up to). Lucy then goes on to blame**
162 **Parliament for the PN’s worth more than \$50,000, and Westpoint exploited the loophole.**

163 **Senator WATSON**—You are uncertain about your legislative powers, because you
164 acknowledge that you thought there was a gap. Is that right? You felt there was a gap at that
165 time?

166 **Watson’s words: “You are uncertain about your legislative powers, because you though there**
167 **was a gap. Is that right? You felt there was a gap at that time?” The question clearly indicates**
168 **he believes ASIC didn’t know what they doing, and didn’t have a sufficient grasp of the law.**

169 **Mr Steward**—There was an exclusion.

170 **Steward’s answer gives no indication of the nature of the exclusion.**

171 **Senator WATSON**—That is the impression you have given me, so I am giving you the
172 opportunity to clarify as to whether you believe there was a gap or there was not a gap.

173 **Watson asks Steward in a very straightforward manner whether Steward believes there was a**
174 **gap.**

175
176 **Mr Steward**—I am not sure about the word ‘gap’. There was an express exclusion for
177 promissory notes over \$50,000 from the definition of ‘debentures’; that was the problem. We
178 looked at what could be done given that that is what the situation appeared to be, that these were
179 not covered by the legislation that we are tasked to regulate. We developed an argument that we
180 thought had some merit and we thought we needed to raise directly with Westpoint to persuade
181 them that what they were doing, which purported to rely upon the exclusion, did not in fact do
182 so. That occupied several months in 2003. It would be fair to say there was a lot of
183 toing-andfroing between ASIC and Westpoint and in particular their lawyers, Freehills—they
184 might say ‘toing-and-froing’; we might say ‘cat and mousing’—over this issue. We eventually
185 realised by the end of 2003 that we were being stalled, we were being given the run around, and
186 we delivered an ultimatum to Westpoint to either comply with the argument that we had put
187 forward about the Corporations Act or we would take court action. We ended up taking court
188 action to force Westpoint to comply with the Corporations Act, based on a very difficult
189 technical argument that in part relied upon an interpretation of the Bills of Exchange Act rather
190 than the Corporations Act. Nonetheless, we had to fight for our jurisdiction and that is what we
191 did.

192 **Steward claims he is unsure about the word “gap”. He goes on to explain there was an exclusion**
193 **from the definition of “debentures” [in 2004 the Court later ruled the scheme did not involve**
194 **debentures - it was a MIS.] Despite the fact that ASIC had provided Westpoint with permission**
195 **to use the promissory notes, Steward then goes on to say how unreasonable Westpoint was. He**
196 **doesn’t mention that ASIC didn’t rescind the “no-action” letter to Freehills [ASIC never**
197 **rescinded the “no-action” letter]. Steward then talks about discussions with Westpoint**
198 **advising them to comply with their argument about the Corporations Act, or they would**
199 **prosecute. He talks about “catting and mousing” with the Westpoint lawyers. He states that by**
200 **the end of 2003 ASIC realized Westpoint was stalling them. His last few sentences are**
201 **interesting, as he goes on to say the very difficult ASIC prosecution argument was based more**
202 **on an interpretation of the Bills of Exchange Act rather than the Corporations Act. [Curious, as**
203 **ASIC does not regulate the Bills of Exchange ACT. Mark Stewards knew that see line 267.**
204 **Westpoint’s reluctance to take ASIC’s word for the argument was verified when it was thrown**
205 **out of court].**

206 **Senator WATSON**—If there was uncertainty, why did you not approach the minister to
207 introduce an amendment to clarify the law?

208 **Mr Steward**—I think the issue we were facing, as a practical pragmatic matter, was that we
209 waiting for law reform through the normal processes. I am not sure how long that would have
210 taken. We had to deal with something in the here and now and that is what we did.

211 **Steward claimed it would have taken too long. [There is a saying in the computer industry that**
212 **goes like this, “We never have time to get it right the first time round, but we always have time**
213 **to back and patch it time after time”].**

214 **CHAIR**—Senator Watson, we were going to take the afternoon break now until four o'clock.
215 If that suits you, we will resume at four o'clock with you in the chair.

216 ...

217 **Senator SHERRY**—I will ask a preliminary but overall question on Westpoint. Can you
218 give us the latest update assessment on, firstly, the level of liabilities—moneys owing—and,
219 secondly, the number of people affected? We had an update from Mr Lucy at the last
220 estimates, but has there been any further information on that macro impact?

221 **Mr Steward**—I do not think there is any change and I think those figures were the best
222 estimates that we had.

223 **Senator SHERRY**—Yes, I accept that.

224 **Mr Steward**—We conducted a questionnaire survey of investors and we are looking at those
225 results now to try to come up with a firmer figure, or a figure that we can justify with some data.
226 Similarly, in relation to the size of liabilities and losses incurred by the companies, we are
227 reliant on what the various insolvency practitioners will be reporting to us about that, so I do not
228 have any further updated figure on that at this stage.

229 **Senator SHERRY**—If there is a prima facie case of theft and fraud, there is a provision
230 under the SI(S) Act for compensation that may be awarded by the minister in those
231 circumstances. My understanding is that with respect to self-managed superannuation funds
232 that provision is not applicable.

233 **Mr Steward**—I think that is right. We have looked at it. That is the early indication.

234 **Senator SHERRY**—I have lots more detailed questions, but I just wanted to deal with those
235 macro matters.

236
237 **ACTING CHAIR (Senator Watson)**—Mr Lucy, I think you referred to 'toing-and-froing
238 by the solicitors' and I think you mentioned Freehills. You were very patient with the
239 solicitors right up until 2004 before starting to take action. Is that correct?

240 **Mr Lucy**—I would not accept that assessment.

241 **ACTING CHAIR**—That is an incorrect interpretation?

242 **Mr Lucy**—Yes.

243 **ACTING CHAIR**—You did not use the words 'toing-and-froing'?

244 **Mr Lucy**—I think it might have been Mark who used those words. It certainly was not in the
245 sense of toing-and-froing, it was all very relaxed and a nice easy dialogue; there was a
246 significant amount of tension, but it might be better for Mark to—

247 **ACTING CHAIR**—Perhaps Mark could explain the significance of his words
248 'toing-and-froing by the solicitors' until you became impatient in 2004.

249 **Mr Steward**—What I meant was that we did embark initially on a dialogue with Westpoint

250 through its solicitors to try to come up with an agreed approach. We thought that there was a
251 basis for Westpoint to agree that our interpretation of the legislation was one that they by the
252 catting and mousing was that we formed the view fairly quickly that we were not being
253 seriously entertained and that we were being stalled.

254 **If Westpoint were in breach of an Act, then the regulator had the clear duty to take immediate**
255 **action. Paticularly when there was large amount of public monies at risk.**

256 **ACTING CHAIR**—Your interpretation of the legislation was?

257 **Mr Steward**—We said a couple of different things. We said that what was being offered to
258 investors through the information memoranda that had been issued by the various Westpoint
259 companies was an undertaking to repay within the definition of a debenture in the Corporations
260 Act, regardless of the existence of the promissory notes, and that that undertaking to repay was
261 combined with a series of risk mitigation promises that meant it was something different. It was
262 something different within the definition of debenture in the Corporations Act, without even
263 getting to the fact that there were promissory notes being issued. The second argument was that
264 these were not in fact promissory notes that complied with the Bills of Exchange Act. That is
265 why I said earlier that part of the argument rested on a fairly unique way of tackling this issue,
266 which was a statutory interpretation exercise involving not just the Corporations Act but,
267 significantly, the Bills of Exchange Act, which we do not regulate.

268 **Hardly surprising Westpoint took no notice - ASIC does not regulate the Bills of Exchange**
269 **ACT.**

270
271 **ACTING CHAIR**—It was a very softly-softly approach, was it not?

272 **The Acting Chair expresses his disapproval.**

273
274 **Mr Steward**—Not at all.

275 **ACTING CHAIR**—You do not think so?

276 **Mr Steward**—No. As I said, we formed the view that we were getting the run-around and
277 we issued an ultimatum to the company.

278 **Not exactly a valid legal reason for taking action.**

279
280 **ACTING CHAIR**—In 2004?

281 **Mr Steward**—Yes, in January 2004.

282 **ACTING CHAIR**—So you were fairly confident about your powers?

283 **Mr Steward**—We were confident that we had a good argument. It was an argument that
284 seemed to be contrary to what was explicitly set out in the Corporations Act.

285 **Not an answer to the question.**

286
287 **ACTING CHAIR**—But that argument seemed to have been reinforced today when the matter
288 was raised with Mr David Love, who is the manager of Corporation and Financial Services,
289 Market Group. I am interpreting here, but my belief was that it was reasonably clear to him that

290 there was a mandate and he disputed whether a gap did exist in terms of regulatory power. That
291 was my view and I stand corrected. That is why I asked whom you consulted with.

292 Even a senior ASIC Manager didn't believe a "gap" existed.

293

294 **Mr Steward**—The fact is that the argument that we thought was a good one, we lost. We lost
295 the argument before the judge. We lost that argument, the issue is under appeal and we are still
296 awaiting a decision from the Full Court of the Western Australian Supreme Court. It is not a
297 simple, straightforward argument or a straightforward issue by any means. It is a very technical
298 issue, a very difficult issue, and it is beyond doubt that the Corporations Act does exempt or
299 exclude promissory notes with a face value of \$50,000 or more from the definition of
300 'debenture'. That is in black and white in the Corporations Act.

301 Steward again ignores answering the obvious question, and goes off to explain why he thinks
302 there is a gap. Whatever the reason Davis Love thought there was no gap is immaterial.

303

304 **ACTING CHAIR**—Why did you not seek to clarify your powers, say, under the
305 Managed Investments Act at an earlier date? It still has not happened. That would seem to
306 be the appropriate vehicle.

307 **Mr Steward**—The action that we took did include that as an alternative argument. Both
308 arguments cannot sit side by side. Either one is right and the other is wrong or vice versa, and
309 we raised both issues with the court in May 2004.

310 Again Steward does not answer the question of why ASIC did not clarify its powers at an earlier
311 point in time.

312 .

313 **ACTING CHAIR**—And they knocked you out on both counts?

314 Yes, they did.

315

316 **Mr Steward**—The court said that we were wrong on the promissory note issue but that the
317 promissory notes gave rise to interests in a managed investment scheme.

318 Denise Brailey told me that Doug Solomon had told her in 2000 that the Westpoint Schemes
319 were MIS's, and she had approached ASIC armed with information. How is it that Doug
320 Solomon and two courts recognized the schemes as Managed Investments Schemes but ASIC
321 didn't?

322

323 **ACTING CHAIR**—Did that then give you power to act?

324 **Senator MURRAY**—It sounds like a lose-win option.

325 **Mr Steward**—That was a ruling by the court in a substantive proceeding which both parties
326 appealed. Both parties appealed that. We appealed on the promissory note issue and Westpoint
327 appealed on the managed investment scheme issue. The question you are asking is: should we
328 have done something about the finding that it was a managed investment scheme? That was
329 certainly something that was under consideration. But in order to take action at that point and,
330 given that this trial was still on foot—the proceedings were still on foot—and the relief that we
331 were seeking as a consequence of that finding was still before the court, we needed to have
332 some additional here and now urgency or some here and now risk that meant the issue could not
333 wait. We were very concerned about things like financial vulnerability. We had sought further

334 audited accounts to be lodged by the Westpoint Group. They came back audited and
335 unqualified, so we did not seem to have any financial grounds on which to attack Westpoint at
336 that point. We had raised arguments before the court about misleading representations in the
337 information memoranda that were issued by Westpoint. We lost that argument. We did not
338 seem to have that.

339 Why did ASIC not ensure that KPMG's audits were on time, and qualified for each year since
340 Westpoint's registering. The fact is that this did not happen.

341

342 **ACTING CHAIR**—On misleading representations?

343 **Mr Steward**—Yes. We lost that argument. We had circulated to all the investors about the
344 action that we had taken in 2004. We did not hear any responses from them. In the meantime,
345 Westpoint was continuing to meet redemption requests. It was continuing to pay monthly
346 interest to investors. There did not seem, at that point, to be an urgent issue that would require
347 the court to take immediate action as opposed to continuing to hear the matter in the normal
348 course, which meant awaiting the appeal.

349 All investors in the above simply means those who invested in Emu Brewery and Bayshore
350 Mezzaanine. It did not include ALL Westpoint investors who obviously had an interest in the
351 outcome. Further, the letter ASIC circulated to the investors was of such a technical nature that
352 none of them understood it.

353

354 **Senator SHERRY**—On the appeal, do you have any indicative date, time line or idea of
355 when that appeal decision will be handed down?

356 Of course, the Court in 2006 found the Westpoint Mezzanine Model was a MIS.

357

358 **Mr Steward**—We do not know. The appeal was heard in February this year and we have not
359 heard anything from the court at this stage.

360 **Mr Lucy**—Allow me to recap a little on what Mark said, perhaps in layman's terms,
361 because that is what I present here. The matter in 2004 argued, firstly, that the
362 documentation was false and misleading. Part of the directions that the court gave us was
363 that we needed to write to all the investors, that is, to every one of the investors, in two
364 particular undertakings in a manner that was approved by the court, inviting the investors to
365 join our action that these were false and misleading communications from Westpoint. So
366 we wrote to every one of the investors and not one came back and said that they felt that
367 there was any false or misleading representation and that they wanted to join us. In the other
368 two areas of the court, the court gave us one, it gave Westpoint the other and we have
369 cross-appealed. So at that stage we had the option of going to the court and seeking the
370 appointment of a receiver. Because the issue of an appeal was on foot, the only ground on
371 which they would appoint a receiver was if there was some financial viability threat or
372 sustainability of business threat. At that stage, we sought audited accounts. They were
373 provided by KPMG, unqualified. At that stage, none of the complaints received into the
374 office related to the lack of payment of any interest or to rolling capital not being repaid. At
375 that stage, we felt that we had no opportunity to go to the court.

376 In reference to KPMG, isn't it an ASIC duty to ensure audits are reported each year?

377 **ACTING CHAIR**—It is becoming a lot clearer. I note that during the meeting of Westpoint
378 investors in late February this year, ASIC's Executive Director of Enforcement, Jan Redfern,
379 stated that the Westpoint investigation is 'high-priority, multi-faceted and resource-intensive

380 for ASIC'. Does ASIC share the concerns as reported in The Australian of 19 April 2006 by the
381 Australian Property Institute that Westpoint-style structures were not unique and that there
382 could be more Westpoint-style collapses on the horizon?

383 Those concerns have proved to be well founded. On the horizon is a not correct. They had been
384 alive and thriving in the marketplace for a considerable period of time.

385
386 **Mr Lucy**—Yes and yes. ASIC continues to support the concerns expressed by Jan Redfern to
387 the investors. We do take this issue very seriously and we have allocated very substantial
388 resources to it. Yes, there is the potential for further Westpoints.

389 Where is the evidence that ASIC took action after this statement, and more to the point, why
390 had ASIC not taken action on them earlier?

391
392 **ACTING CHAIR**—What action can be taken by ASIC or the parliament to intervene to stop
393 any further losses of this nature reasonably quickly?

394 **Mr Lucy**—In the first instance, the government traditionally and reasonably does not
395 undertake law reform where there is a matter before a court; they wait for the court to
396 determine whether or not there is jurisdiction and, if there is not jurisdiction, they act. At this
397 stage, we continue to be in a situation, as all of us are, including the investors, where simply we
398 do not know which way the court is going to determine in respect of the appeal. In respect of
399 the potential for others, we are surveilling the Australian financial market landscape very
400 closely. We have dialogue with a small number of entities where we have varying levels of
401 concern and we think that those issues are being managed satisfactorily.

402 Westpoint is a prime example of ASIC not going back to Parliament and seeking legislation to
403 help it carry out its duties more effectively. ASIC's reputation of sitting on its hands and doing
404 nothing until after the event has been earned.

405
406 Further, if ASIC couldn't do anything about these companies because of the current legislation,
407 why could it take action against Westpoint?

408
409 THE DISCUSSION NOW TURNS TO ADVERTISING. ALTHOUGH VERY IMPORTANT,
410 IT ADDS NOTHING TO THE NATURE OF THE ABOVE INFORMATION.

411
412 **ACTING CHAIR**—My next question concerns advertising. Can you assure the Senate that,
413 given mezzanine finance is recognised as a high-risk commercial product, currently in the
414 daily financial pages and on radio, no Westpoint products are still being advertised? They
415 have been, but I have not seen any lately.

416 **Mr Lucy**—When you say Westpoint products, what do you mean?

417 **CHAIR**—Mezzanine finance.

418 **Senator SHERRY**—Westpoint-like products.

419 **Mr Lucy**—That is what I am seeking clarification on.

420 **Mr Cooper**—The point is that these products are not illegal but we did a considerable amount
421 of work during 2005 that did not relate to Westpoint but to other entities and to assertions
422 made in advertising that these products were 'secure, certain, guaranteed'— language like

423 that. In one case we actually forced an issuer to offer a full refund to all investors that, we said,
424 had been misled. That was an issuer that had not run into difficulties like Westpoint; it was still
425 in business but, nonetheless, we forced them to offer all investors their full money back if they
426 so chose.

427 Presumably Cooper is talking about Fincorp, which has now failed. The Court made the
428 company give back their money because the prospectus was “deliberately false and
429 misleading”. This prospectus had initially passed ASIC’s inspection. Further, ASIC took no
430 punitive action against the company, which went on to extract almost \$100 million more from
431 the public before it failed.

432

433 **ACTING CHAIR**—Have you contacted the newspapers in relation to their social
434 responsibilities about taking advertising for these high-risk, mezzanine-type schemes and the
435 consequences that can have on consumers, if you do not feel that you can act in any other way
436 at the moment?

437 **Mr Lucy**—We have certainly had a very high level of dialogue with the media generally and,
438 indeed, it is the media that typically carry our consumer warnings.

439 **Senator SHERRY**—I love the way you describe that.

440 **Mr Lucy**—I think that they are very much aware of our attitude to this. Frankly, it really is a
441 very serious issue.

442 **ACTING CHAIR**—Absolutely.

443 **Mr Lucy**—It is true that people are continuing to invest in types of investment that we would
444 still regard as high risk.

445 **Senator SHERRY**—On this advertising issue, there are certainly Westpoint-type products
446 still on the market, aren’t there?

447 **Mr Lucy**—Yes.

448 Since 2000, how many times has ASIC made a serious attempt to issue warnings about products
449 and schemes through the national media?

450

451 **Senator SHERRY**—Have you taken any action in respect of Westpoint-type products that
452 you can name?

453 **Mr Cooper**—Yes, we have. Our typical tool is what we call an interim stop order or a stop
454 order that actually stops the capital raising, and we have done that with a number of issuers.

455 **Senator SHERRY**—I suspect I know a number of them you are going to name and I will ask
456 some more detailed questions. Can you name those you have taken action against?

457 **Mr Cooper**—Fincorp is an example.

458 **Senator SHERRY**—Given the issue in respect of the question over power, how have you
459 been able to do that?

460 **Mr Cooper**—That is a disclosure-based power, so we look at the disclosure document,

461 typically—in the case of debentures, a prospectus; in the case of other products, a product
462 disclosure statement. We form a view that there is inadequate disclosure and that enables us to
463 issue a stop order.

464 Disclosure has been a primary problem. I can't recall ASIC being very active in this direction.
465 One only has to look the reasons for each of the major collapses since 2005.

466
467 **Senator SHERRY**—Senator Watson raised the advertising issue. With due respect, even if
468 they stopped advertising, isn't the reality—I do not know whether this is true or not—that a
469 lot of these people are channelled into these types of product through a planner? They may
470 not be channelled as a consequence of any advertising; it may be the advice given by a
471 planner.

472 **Mr Cooper**—Typically not. I would have to disagree. In fact, our knowledge of the industry
473 suggests that Westpoint was unusual in that most of these products are what they call in the
474 jargon of the trade 'disintermediated'; in other words, they do not rely on a financial planner
475 chain. There are a couple of reasons for that. One is, as we saw in Westpoint, a substantial
476 amount of each dollar that is invested has to be shared through commissions. The other reason
477 is that by going through the vehicle of newspaper advertising these issuers can effectively
478 control the tap of funds. The worst thing that can happen to someone who is in the high-yield
479 market is that they actually have too much money on hand on which they have to pay high
480 interest and, unless they have got projects to lend it out to, they get themselves into financial
481 difficulty.

482 ASIC controls the planners. It is just another area in which they have played scant respect to
483 what was occurring.

484
485 **Senator SHERRY**—It is a mismatch of inflow of funds as against generation of return.

486 **Mr Cooper**—Correct. If you are paying nine per cent you do not exactly want to have a
487 whole lot of cash on deposit with one of the main banks because you are going to go out of
488 business in a big way.

489 **Senator SHERRY**—Even if the advertising ceased, it does not mean that these products are
490 not being offered.

491 **Mr Lucy**—It does not eliminate the risk.

492 **Mr Cooper**—That is right. They are still lodging documents with us and seeking to raise
493 funds on them.

494 **ACTING CHAIR**—It appears that we are now at the stage of mopping up and waiting for
495 court decisions. Given the resource-intensive nature of such an operation—Jan Redfern's
496 'high-priority, multi-faceted, resource-intensive' investigation—and the impact that these
497 operations are likely to have on ASIC's overall effectiveness, can you assure the Senate that
498 ASIC now has, to use a colloquialism, a fence at the top of the cliff—you have mentioned one
499 fence in terms of advertising, newspaper proprietors and others, so to speak—rather than an
500 ambulance at the bottom with regard to monitoring of high-risk public offers similar in structure
501 to Westpoint?

502 **Mr Lucy**—I can answer that in two parts. The first is that you refer to the fact that they have
503 been waiting on a determination by the appeal court and our investigation. The facts are that in

504 2005, notwithstanding the fact that we were still seeking communications with the auditor, still
505 not obtaining advice from the auditor as to issues to do with going concern and so on, and
506 largely still not receiving complaints from the public regarding the financial model of
507 Westpoint, our commission took the risk, and it was a risk, prior to Christmas and actually
508 sought the appointment of administrators. The timing of that was that we were aware that there
509 was a group of investments which were due to roll over and we felt that if we were to act it was
510 ideal, if not crucial, to act before that rollover, so we took the decision, and fate may well have
511 gone in a different direction, to seek the appointment of an administrator, which in turn brought
512 the whole organisation down to ground.

513 ASIC forever waiting for someone else to do something – never acting in a proactive manner.
514 Continuous monitoring and early intervention is the cornerstone of keeping any system
515 operating within the segin boundaries. ASIC has never learned this simple lesson.

516
517 **ACTING CHAIR**—You mentioned your relationship with the auditor. Did you have
518 some problems there?

519 **Mr Lucy**—That is a matter of an ongoing investigation. It is true that we did have dialogue
520 with the auditor on a number of occasions up until December 2005. The fact that we have now
521 commenced an investigation on a wide range of areas, including the role of the auditor, is a
522 matter that we have in front of us.

523 **ACTING CHAIR**—The last time the auditors or firm gave an unqualified clearance of the
524 accounts was in what year?

525 **Mr Lucy**—June 2004, but of course those were issued subsequent to that. The auditors have a
526 responsibility under section 311 to notify ASIC, the regulator, in the event that various events
527 occur with their clients, including, for example, concerns about going concern. That is not an
528 annual, yearly cycle.

529 In what and year did KPMG sign off on the Westpoint audits? Given the problems and
530 warnings from the outset, why did ASIC allow any laxity?

531
532 **ACTING CHAIR**—No. It is immediately it comes to their notice.

533 **Mr Lucy**—Precisely.

534 **Senator SHERRY**—On the issue of the auditor, KPMG is the firm in this case, isn't it?

535 **Mr Lucy**—Yes.

536 **Senator SHERRY**—We have not explored this, at least at these committee hearings, in
537 great detail, but you were on the Four Corners program.

538 **Mr Lucy**—Yes.

539 **Senator SHERRY**—I certainly did not know until I saw that program that Mr Beck, who is
540 part of the investigation and a primary operator involved in Westpoint, was the former chief
541 compliance officer with KPMG.

542 **Mr Lucy**—Yes, I understand that was the case, although I also understand that it was for a
543 relatively short period. But he did have an employee relationship with KPMG.

544 **Senator SHERRY**—Yes. That struck me as a little beyond coincidence that KPMG were the
545 auditors that had signed off the unqualified audit reports.

546 **Mr Lucy**—Really, we do need to be careful about that aspect because it is a matter of an
547 ongoing investigation.

548 **Senator SHERRY**—Yes. We have not asked about this, but you are now carrying out an
549 investigation in respect to KPMG and the auditing that occurred?

550 **Mr Lucy**—Yes.

551 **Senator SHERRY**—Good. I also notice that, on at least one of the research house reports,
552 KPMG was also the auditor that signed off on that.

553 **Mr Lucy**—I think you referred that to us at the last hearing.

554 **Senator SHERRY**—Yes.

555 **Mr Lucy**—Yes, we have taken that on board and that is also part of our consideration.

556 **Senator SHERRY**—But KPMG were the auditor in respect of that research house?

557 **Mr Lucy**—I believe that is the case.

558 **Senator SHERRY**—Do we know whether it is the same partner involved in the auditing of
559 Westpoint and the research house?

560 **Mr Lucy**—I have to take that on notice.

561 I have no doubt Lucy would have known, but there may have been good reasons for not
562 indicating who it was.

563

564 **Senator SHERRY**—We do know that there were planners associated with Westpoint who
565 were recommending Westpoint products through self-managed superannuation funds. Do we
566 know whether any of those self-managed superannuation funds, which were the channel
567 vehicle, were audited by KPMG? Is that a matter that is being examined at all?

568 **Mr Lucy**—I doubt whether we would know that yet. We are certainly now getting a fairly clear
569 profile on the investors, including those that were a part of the self-managed super fund group
570 and the quantum of investments, the nature of the investments and so on.

571 **Senator MURRAY**—That is a result of your survey?

572 **Mr Lucy**—Yes, it is. It was an online survey; indeed, it was a first and it has been very
573 effective. For example, investors totalling in the aggregate of something like \$300 million
574 have responded to the survey. It is becoming a very reliable piece. Again, that is something
575 which clearly we will look at down the track as to whether or not the auditors of the super
576 funds indeed have been truly independent.

577 **Senator SHERRY**—I just think it is passing coincidence that so many tracks lead to KPMG in
578 respect to auditing.

579 **Mr Lucy**—I do not think that we can assume that there is a track as far as the self-managed

580 super funds are concerned at this point.

581 **Senator SHERRY**—Not yet. On that issue, I am not concerned with your activities in respect
582 of self-managed super funds, but that is regulated by the tax office, is it not?

583 **Mr Lucy**—Yes.

584 **Senator SHERRY**—I questioned them about this yesterday. You are transmitting
585 information to the tax office in respect to the regulation of self-managed super funds?

586 **Mr Lucy**—Yes, we are.

587 **Senator SHERRY**—I am still concerned about what appears to be a sort of lack of ‘get up
588 and go’ in respect of the tax office. They are the regulator of self-managed super funds and
589 my understanding is that we are looking at a substantial proportion, if not the majority, that
590 was channelled through self-managed super funds?

591 **Mr Lucy**—About 30 per cent we think, which is a substantial amount.

592 **Senator SHERRY**—There is one other aspect of the Four Corners interview which was again
593 something I had not been made aware of. There was a Mr Carey, who was also associated with
594 Westpoint. He is under investigation, isn’t he?

595 **Mr Lucy**—Yes, he is.

596 **Senator SHERRY**—Apparently, according to that program, he is still operating, but
597 indirectly, through a company called Ferntree.

598 **Mr Lucy**—Yes, we understand that.

599 **Senator SHERRY**—Is he still operating as an advisor through this new company, Ferntree?

600 **Mr Lucy**—I will ask Mr Steward to advise, but I do think that we are getting very close to
601 saying that that is operational.

602 **Mr Steward**—What I can say is that Ferntree Financial Services was a business name under
603 an entity called Redchime. Redchime is a defendant in the proceedings that we commenced in
604 March this year, which has ultimately led to receivers being appointed to that entity, as well as
605 to a number of others, and some former directors of Westpoint. We now understand that that
606 business may be operating under a different regime now and that is something that we are
607 looking at.

608 **Senator SHERRY**—Which different regime?

609 **Mr Steward**—Pursuant to a different company. That is something we are interested in.

610 **Senator SHERRY**—Was Ferntree operating with a licence from ASIC?

611 **Mr Steward**—No.

612 **Senator SHERRY**—This fellow Carey has morphed into a new entity, Ferntree, and
613 apparently now into another unnamed entity. Short of locking him up and throwing away the
614 key, how do you contain this? The fellow keeps morphing into a new financial advisory

615 business.

616 **Mr Lucy**—We really respect your interest, but you have to assume that we are thinking along
617 the same lines and we do not want to go there as far as providing an answer, I am afraid.

618 **Senator SHERRY**—Has there been any preliminary analysis of the number of new clients
619 and moneys involved in this Ferntree entity?

620

621 **Mr Steward**—I think the understanding, and I will put it as an understanding because of what
622 the chairman has just said, is that Ferntree really operates more like a finance broker than a
623 financial services business. Its name is suggestive of something that perhaps may not be the
624 case, but its activities remain of interest, perhaps because of the name itself.

625 **Senator SHERRY**—You mentioned finance broking type activity. How is that regulated?

626 **Mr Steward**—I think there are state laws that govern the conduct of that style of business.

627 **Mr Lucy**—WA law in particular.

628 **Senator SHERRY**—Have you had any liaison with the WA—

629 **Mr Lucy**—I would rather not go there, I am sorry.

630 **Senator SHERRY**—You are aware that we had a discussion about broking earlier; you may
631 or may not have heard it. It is not regulated yet, uniformly, nationally?

632

633 —Yes.

634

635 **Senator SHERRY**—There is regulation in WA but we are awaiting the completion of a sort
636 of template regulation which apparently is a couple of years away.

637 **Mr Lucy**—Yes, we did view that, but the situation that might exist at the moment between
638 ourselves and Western Australia is not waiting for that sort of template.

639 **ACTING CHAIR**—You indicated that you sent letters out to a whole host of investors.

640 **Mr Lucy**—About 250.

641 **ACTING CHAIR**—And you invited them to join in an action with you?

642 **Mr Lucy**—Yes.

643 **ACTING CHAIR**—That was a suggestion from the court?

644 **Mr Lucy**—In fact, it was a direction of the court.

645 **ACTING CHAIR**—Why did you not take action yourself?

646 **Mr Lucy**—We did.

647

648 **ACTING CHAIR**—You took action at that stage?

649

650 **Mr Steward**—This was in proceedings that we had commenced and, because the proceedings

651 might have some impact on the investors' interests in those companies, we raised with the court
652 the interest that these third parties would have. As a result of that, the court, effectively at our
653 request, ordered us to write to all of these investors so that they understood what was
654 happening, which is what we did.

655 **ACTING CHAIR**—Nobody responded in the affirmative?

656 The document was written in “legalese”, and the investors did not understand it.

657 **Mr Steward**—That is right.

658 **ACTING CHAIR**—My question is: did you have the opportunity to go it alone to take action?

659 **Mr Lucy**—We did take that matter through the court, under the false and misleading
660 provisions, and the court ruled against us.

661 **ACTING CHAIR**—On what ground did the court rule against you?

662 **Mr Lucy**—Presumably one ground is the fact that no investor felt that there was any false or
663 misleading material provided to them.

664 **ACTING CHAIR**—Despite the fact that you, the experts, were of the view that the
665 information was false and misleading?

666 **Mr Lucy**—That is right.

667 **ACTING CHAIR**—So they took your view rather than that of an amateur investor?

668 **Mr Lucy**—They did not take our view.

669 **ACTING CHAIR**—They rejected your view?

670 **Mr Lucy**—Yes.

671 **ACTING CHAIR**—That is absolutely surprising, isn't it?

672 **Mr Cooper**—It is a key part of life at ASIC that we are subject to the rule of law.

673 **ACTING CHAIR**—Absolutely.

674

675 **Senator SHERRY**—It is surprising that, in terms of the court hearing, it was the weighing
676 up of the evidence. You gave evidence that it was misleading, and presumably no punter
677 turned up.

678

679 **ACTING CHAIR**—It has certainly put a slightly different light on your role and I thank you
680 for that.

681

682 **Senator SHERRY**—Unfortunately, we are not in receipt of the answers that I sought. I am
683 not blaming you. You would recall that I did ask on the last occasion about the
684 correspondence between the Western Australian Department of Consumer and Employment
685 Protection and the minister and indeed the meeting that apparently took place warning about
686 the activities of Westpoint. We do not have those answers.

687 I wonder if that document was one referred to in the Edwards letter?
688

689 **Senator MURRAY**—Senator Minchin said he would check it out during the tea break. Have
690 we had any response to that, Mr Chairman?
691

692 **Senator SHERRY**—We will see how we go. I may come back to that, because it places us in
693 the difficult position of having to go through all the questions that I asked you last time, Mr
694 Lucy. My general concern is that I am interested to know what, if any, the response from
695 ASIC, from the Treasurer and his parliamentary secretary was in respect of the warnings
696 about Westpoint activities. We do not have the answers yet.
697

698 Why hadn't Sherry received his requested answers after three months?
699

700 **Mr Lucy**—Can I say that I am sure that you will get the questions as soon as the minister
701 approves. To the extent that you would like to follow up out of session with a question, I am
702 happy for you to do so.

703 **Senator SHERRY**—Yes. I might get the opportunity to follow that up.

704 **Mr Lucy**—In June.

705 **Senator SHERRY**—Yes, in June. It is only just over a week away, isn't it? I should say I have
706 lots of questions with respect to your very useful shadow shopping exercise, but I might have to
707 leave those until June too, just in case—

708 **Mr Lucy**—What a pity.

709 **Senator SHERRY**—anyone in the media watching believes that I am going to let that one
710 pass today, given the time.

711 **Mr Lucy**—Thank you. To the extent that you choose, any advance advice that you might
712 give us of those questions will mean that we really are in a position to provide full and
713 comprehensive answers. That is a matter for you, of course.

714 **Senator SHERRY**—Of the ongoing investigations into financial advisers, what is the number
715 that has been identified so far?

716 **Mr Lucy**—Out of the shadow shopping?

717 **Senator SHERRY**—No, I am not going to shadow shopping. I am still on Westpoint.

718 **Mr Steward**—We have identified to date about 37 licence holders. Of course, they will have
719 a much larger number of representatives who would have been engaged in giving advice to
720 clients.

721 **Senator SHERRY**—So it is 37 licence holders and, underneath that, do you have any idea?
722 Are we dealing with hundreds here?

723 **Mr Steward**—I can only give you a guess. We have issued information requests to those 37,
724 seeking a range of information, and that is something that we are trying to gather ourselves. We
725 need that data from those 37.

726 **Senator MURRAY**—Are they primarily in Western Australia?

727 **Mr Steward**—No.

728 **Senator SHERRY**—They are all over the country, aren't they?

729 **Mr Lucy**—Yes, particularly the eastern seaboard and Western Australia—not so much in
730 South Australia or the Northern Territory.

731 **Senator SHERRY**—We are dealing with a much larger number of planners underneath the
732 37 licences. I must say that certainly the impression seems to be that it is about 37 planners,
733 but it is licences.

734 **Mr Steward**—That is right.

735 **Senator SHERRY**—Presumably, in going to the licence holders, it would be the role and the
736 responsibility of the compliance officers within the licence holders who oversee the regulatory
737 regime of the planners. They would have a central role in all of this?

738 **Mr Steward**—They certainly have a central role in helping to ensure that the licence holder
739 does what it is required to do to monitor the representatives.

740 **Senator SHERRY**—When did ASIC first conduct checks on financial advisers or
741 licence holders, or both, with respect to Westpoint?

742 **Sherry asks a pertinent question. ASIC controls the planners, and it a very easy task to know
743 what they are selling – and in what volume.**

744

745 **Mr Steward**—I am not quite sure what you mean.

746 **Senator SHERRY**—You had a concern about Westpoint.

747 **Mr Steward**—Yes.

748 **Senator SHERRY**—When did you first go to the licence holders and/or the financial
749 advisers?

750 **A very pertinent question.**

751

752 **Mr Steward**—I think our concern was about Westpoint fighting the jurisdiction fight and then
753 trying to go behind the accounts to look at the real financial position. They were the two main
754 broadly thematic concerns that we have had in relation to Westpoint.

755 **Does Steward's answer mean ASIC doesn't care what they sell? Or in what circumstance?**

756

757 **Senator SHERRY**—I understand that that battle is going on, but you have jurisdiction with
758 respect to licence holders and financial advisers whom you knew were recommending selling
759 products. You were aware that there was some distribution at least?

760 **Sherry sticks to his point.**

761

762 **Mr Steward**—Yes. I suppose we must have assumed that.

763 Not a satisfactory answer.

764

765 **Senator SHERRY**—Yes. That would be a reasonable assumption, but I am just interested to
766 know: when did you first go to the licence holders and the planners?

767 Sherry keeps boring in.

768

769 **Mr Lucy**—In 2006.

770 **Mr Steward**—Specifically about Westpoint, it was this year in relation to the information
771 requests. Of course, there are other surveillances that are carried out on licence holders on
772 that general basis but, specifically to do with Westpoint, it was this year.

773 By 2006 all Westpoint projects were in liquidation.

774

775 **Senator SHERRY**—That is one of my concerns. You say you have the ongoing battle about
776 Westpoint in the courts—that that is occurring and you are awaiting the outcome. You clearly
777 had jurisdictional responsibility in respect of the licence holders and the planners but you did
778 not initiate any investigative checking activity—I am not talking about enforcement activity—
779 until this year of those individuals who were distributing the product. That was even though you
780 are fighting a court battle over Westpoint and you had some concerns about Westpoint.

781 ASIC seizes on ASIC's lack of monitoring and action.

782

783 **Mr Steward**—I think that is right, and we did not have any complaints about advice that
784 people were getting, either.

785 **Senator SHERRY**—I accept that, but ASIC was sufficiently concerned to be taking action in
786 the court about the Westpoint entities. You were obviously concerned about that because you
787 would not have taken the court action otherwise. Why then at the same time, certainly earlier
788 than the beginning of this year, despite the fact that you had received no complaints from the
789 individuals, were you not at least carrying out some checks, surveys or whatever with respect to
790 the planners who were recommending and distributing the Westpoint products?

791 **Mr Steward**—I just think they are different issues.

792 Steward vaguely tries to defend ASIC's position and the battle continues.

793

Senator SHERRY—They are interconnected.

794 **Mr Steward**—The issue that we had in relation to Westpoint was whether the fundraising
795 was in compliance with the Corporations Act or not. But that is a very different issue—

796 **Senator SHERRY**—Yes, I understand it is a different issue.

797 **Mr Steward**—to whether or not the financial advisers properly understand what they are
798 advising on and are properly disclosing the nature of and the risks involved in investing in
799 those sorts of products.

800 **Senator SHERRY**—You initiated the court action because you had concerns about
801 Westpoint.

802 Steward's losing, so Lucy tries to come to the rescue.

803

804 **Mr Lucy**—There were two court actions. The first one was in 2004 and, in fairness, that would
805 not have given rise to a concern that we should go out and look at the financial planners. It is
806 true, though, that towards the end of 2005, when we were starting to have our own concerns
807 about its financial viability, it would have been open to us to start visiting financial planners at
808 that stage, and we did not.

809 **Senator SHERRY**—You have used that that description, that you had not received a
810 complaint.

811 **Mr Lucy**—Yes.

812 **Senator SHERRY**—You had your concerns about the entities, but you had not received a
813 complaint. Surely you would not have been receiving a complaint, because the entities
814 presumably were continuing to just pay out the money. The whole thing is a pack of cards
815 that has subsequently fallen down. How is the average punter investor to know anything?
816 You did know; they did not. Why wait for a complaint?

817 **Lucy is blasted out of the water.**

818

819 **Mr Lucy**—We thought that we knew. We were the odd man out, frankly, because the directors
820 and the auditors who are primarily responsible—the directors and officers in the first
821 instance—for running the company were saying to us, under our query, that the business model
822 was fine; there was no difficulty. The auditors were saying to us, similarly, that they did not
823 think there was any concern. Yet we were starting to develop a level of anxiety about it, which
824 reached the point late in 2005 where we sought the appointment of an administrator.

825 **Lucy tries to shift the blame.**

826

827 **Senator SHERRY**—When did ASIC first become aware of the size of the commission based
828 payments in respect of Westpoint investments being made to planners?

829 **Sherry brings the subject around to the size of commissions.**

830

831 **Mr Lucy**—In 2006, I believe.

832 **Senator SHERRY**—Approximately when would that have been?

833 **Mr Lucy**—Almost certainly immediately following our appointment, or seeking the
834 appointment, of an administrator, when things very quickly came to the surface. It was
835 probably in January this year, I expect. It was either December 2005 or January 2006, I
836 expect.

837 **ASIC controls the planners, but had no idea of what they up to until 2006.**

838

839 **Senator SHERRY**—Was the size of the commission itself an issue of concern to ASIC?

840 **Mr Lucy**—It certainly is a level of commission that is extremely high, and we have been the
841 very first to state that. In the first instance, our anxiety is to make sure that that is disclosed
842 and, if it is disclosed, then, high or not, in the first instance the financial planners have met
843 their responsibilities.

844 The fact is, the planners did not declare it, and ASIC has never taken any action on this point.

845

846 **Senator SHERRY**—Allegedly, people are protected by the disclosure of commissions.
847 What about the independence of the planner in recommending a product with such a
848 substantially high commission?

849 **Mr Lucy**—Again, we really are getting into enforcement territory, because that avenue is
850 exactly the sort of thing we are looking at when we are investigating the planners.

851 I repeat, planners did not declare their commissions, and ASIC has never taken any action on
852 this point.

853

854 **Senator SHERRY**—I am aware that you have issued a discussion paper that includes
855 comment on the issue surrounding the independence of advice and the impact of commission
856 selling.

857 **Mr Lucy**—Yes.

858 **Senator SHERRY**—Have there been any issues raised by investors in respect of the
859 so-called independence of advice? I understand some of the advisers worked for a
860 Westpoint related entity.

861 **Mr Lucy**—Certainly, at the meeting in Sydney between us and the investors there were a
862 number of investors who indicated that they were not aware of commissions of the order of 10
863 per cent having been paid. Whether or not that ultimately is the fact, time will tell. There was
864 also a suggestion that there were one or two ethnic community planners that seemed to be very
865 effective as far as spreading within the network of their particular community.

866 **Senator SHERRY**—When you say they had stated they were not aware, was it because they
867 had not read the documentation, the disclosure, or had it not been issued?

868 **Mr Lucy**—It was quite an emotional meeting, and a number of investors spoke of their own
869 circumstances. Some of them had a fairly high level of difficulty in communicating in English
870 and they were resorting to interpreters. I think that it would be perhaps unfair on those
871 investors to say whether or not they were specific enough to say whether or not they noticed it
872 was there but did not understand it or that it was not there. That is all part of our investigation
873 going forward, and that is exactly the sort of material we are collating at the moment.

874 The commissions were not declared.

875

876 **Senator SHERRY**—As to the issue we touched on earlier of the research houses—and we
877 touched on them at the last hearing—is that a matter that is being followed through?

878 **Mr Lucy**—Yes. I think it is ‘house’.

879 **Senator SHERRY**—That was going to be my next question. I am certainly aware of one.

880 **Mr Lucy**—I am aware of only one at the moment.

881 **Senator SHERRY**—It is one that is being investigated at the present time?

882 **Mr Lucy**—At the moment.

883 **Senator SHERRY**—Was ASIC made aware of the online superannuation ‘advertising
884 campaign’ run in metropolitan areas? This is related to Westpoint.

885 **Mr Lucy**—When was it being run?

886 **Why would ASIC know, they only regulate the market!**

887

888 **Senator SHERRY**—Earlier this year and, I understand, last year.

889 **Mr Lucy**—We would have to take that on notice. I am not immediately aware of it. We
890 should take that on notice.

891 **Senator SHERRY**—I am told that those who attended the workshops for Online Super— there
892 was an advertising campaign, and then people attended workshops—were allocated an ASIC
893 licensed financial planner who worked for Online Super. These licensed planners advised
894 attendees to establish a self-managed super fund. The workshops continued and, once the
895 investor had set up their self-managed super fund, they were then informed of the benefits of
896 investing in Westpoint mezzanine finance projects. That was one of the ways in which the
897 propaganda was disseminated, through this campaign. Are you not aware of that?

898 **Mr Lucy**—If they were giving advice in relation to Westpoint, you can be assured that they are
899 part of our investigation. If it is the case that people invested in Westpoint through that
900 organisation, yes, they will be part of our investigation.

901 **Its part of ASIC “investigations”. Why has no one has ever been prosecuted?**

902

903 **Senator SHERRY**—Apparently the licensed financial planners—they claimed they were
904 licensed; let us assume they were—were advising the SMSF clients to put all their money in
905 Westpoint mezzanine projects. The extent that that occurred is a matter of fact and
906 consequence. Is that one issue that is under investigation into the activity of planners—the
907 recommendation that all moneys go into Westpoint entities?

908 **Mr Lucy**—Yes, it is. That will also be an issue for the Australian Taxation Office, because
909 it also has that interest. Yes, is the short answer. ...

910 **NIMBY its an ATO problem.**

911

912 **Senator SHERRY**—Mr Lucy, are you aware of the press release put out by the Westpoint
913 Investors Group on 23 May 2006?

914 **Mr Lucy**—No. Indeed, I have had communications from them, including as late as this week,
915 but I cannot recall seeing that communication.

916 **An example of Lucy’s amazing feats of memory.**

917

918 **Senator SHERRY**—In that press release they raise a number of questions with respect to
919 ASIC. One of the issues raised is that ASIC should provide a copy of the warnings that were
920 issued to Westpoint investors. Is there any particular difficulty with that?

921 **Mr Lucy**—No. As I said, I have not seen the release that you have referred to.

922 The only warnings were vague statements on the ASIC website. They never appeared in
923 national media.

924
925 **Senator SHERRY**—And the location, date and publication of the warnings—

926 **Mr Lucy**—Yes.

927 **Senator SHERRY**—There is no particular difficulty in that?

928 **Mr Lucy**—No, I would not have thought so.

929 I have never seen the dates and the particular media entities in which the appeared.

930

931 **Senator SHERRY**—It is alleged by the Westpoint Group that their requests for a meeting
932 with Ms Redfern were not agreed to on three occasions.

933 **Mr Lucy**—I do not think that is a fair reflection, frankly, in that their request for a meeting and
934 the agenda for that meeting was discussed with Jan. Indeed, as late as this week they agreed to
935 hold a meeting in the manner that both they and we think would be the most fruitful. I expect
936 that meeting will occur within the next couple of weeks. They were angling for a meeting that
937 simply was not appropriate. There has been dialogue with the chairman of that group. He has
938 accepted that that was the case and has now accepted with Jan an approach for a meeting which
939 will be convened in the near future.

940 As the President of the Westpoint Investors Group, I can assure the reader that Sherry was
941 correct. Further, ASIC placed restrictions on the meeting such as Westpoint could not take
942 minutes.

943

944 **Senator SHERRY**—Will that be with Ms Redfern?

945 **Mr Lucy**—Yes, definitely. Whether I will attend that I am not sure. It depends upon what the
946 final agenda is. One of their key interests, of course, is how we are going with our investigation.
947 Of course, that is an appropriate expectation that they have. We are limited as to how much we
948 can communicate. I expect there is going to be an expectation gap, a difference, between what
949 they seek out of the meeting and what we can provide.

950 **Senator SHERRY**—You say you are limited in respect of communication. Is that a budgetary
951 limitation or a practical limitation?

952 **Mr Lucy**—No, it is a legal limitation. It is just prudence and nothing to do with the budget.
953

954 **Senator SHERRY**—In a letter from Freehills on 2 June 2004 to the directors of Emu Brewery
955 Mezzanine Ltd and Bayshore Mezzanine Pty Ltd it was revealed that ASIC was ordered by a
956 preliminary hearing on 1 June 2004 that notice be given immediately to all the promissory
957 note holders in both Emu Brewery and Bayshore fundraisings by sending them copies of the
958 originating summonses, counterclaims, orders and a pro forma letter prepared by ASIC giving
959 them 21 days to seek to be joined in the proceedings. Did ASIC follow through on that order?
960 If so, how?

961

962 **Mr Lucy**—Yes. That was the matter I was referring to when I was speaking with Senator

963 Watson, in that we were directed by the court to write to about 250 investors, which we did.
964 **Senator SHERRY**—You followed that through. You referred to not receiving feedback or a
965 response

966
967 **Mr Lucy**—Yes.

968 **Senator SHERRY**—Was that in respect of that matter as well?
969

970 **Mr Lucy**—No, not as well. That is that matter.
971

972 **Senator SHERRY**—Approximately how long after the order were those letters sent out?
973

974 **Mr Lucy**—We think it was 4 June. If that is incorrect, we will advise.
975

976 **Senator SHERRY**—So a couple of days?

977 **Mr Lucy**—Yes.
978

979 **Senator SHERRY**—If you could, let me know. I will not hold you to that precise date. Can
980 you provide a copy of that letter for estimates?

981 **Mr Lucy**—Certainly. We probably will not have the title of the investor, respecting the names
982 of the investors; we will just send you a—

983 **Senator SHERRY**—Just blank it out?

984 I have already dealt with the letter earlier. I repeat that I have yet to meet with an investor who
985 understood its contents.

986
987 **Mr Lucy**—Yes. Would you have any appetite to let us have a look at that letter that you refer
988 to?

989 **Senator SHERRY**—Which letter?
990

991 **Mr Lucy**—That Freehills letter?
992

993 **Senator SHERRY**—I will have to check on that. I do not think I have it here. I am not sure.
994

995 **Mr Lucy**—If that was possible, we would be very interested in that letter.
996

997 **Senator SHERRY**—Have you asked them for it?
998

999 **Mr Lucy**—They would probably claim it was privileged.

1000
1001 **Senator SHERRY**—I do not know whether I have it. I have some questions in respect of the
1002 Freehills letter. I will check to see if I have it. I would have to check with them.

1003
1004 I presume they are referring to the Freehills letter, which was issued in August 2000 to Freehills
1005 promising no action on the promissory notes. If that is the case, then serious questions must be
1006 asked about ASIC's ability to keep records.

1007
1008 **Mr Lucy**—I understand.
1009

1010 **Senator WATSON**—My question concerns the solicitors. I have been reflecting, Mr Steward,
1011 on your term ‘toing-and-froing’ in terms of the negotiations between ASIC and the solicitors
1012 and the scope, I suppose that would be the correct word, of the regulatory powers. Being a large
1013 firm, would you say they were acting in an intimidatory, overbearing or unreasonable way?

1014 **Mr Steward**—They may well say the same about us.

1015 **Senator WATSON**—Obviously they must have had some impact of terms of a degree of
1016 hesitancy on your part. Could you give the Senate some feeling of the sort of environment in
1017 which you suddenly placed yourself?

1018 **Mr Steward**—Firstly, I was not personally involved in this. But I have looked at and
1019 reviewed what occurred. It was no different to what often occurs when we have a view that we
1020 want to impose on someone that we are looking at. I am not too sure what you are seeking to
1021 characterise our negotiating position as, but it certainly was not timid or reluctant. It was
1022 forceful and willing, and theirs was the same.

1023 **Senator WATSON**—I would be surprised if they were timid. I am not querying your
1024 approach. But I could imagine very large firms could have the capacity to be quite
1025 overbearing and intimidatory.

1026 **Mr Steward**—No.

1027 **Senator WATSON**—So they just in a quiet way put their legal argument. Is that right?

1028 **Mr Steward**—Yes, that is right. We had opposing views.

1029 **Senator WATSON**—It was all done in a very professional manner, without threats on their
1030 part?

1031 **Mr Steward**—I am not sure what you are getting at. We delivered an ultimatum to them, if
1032 you want to call it that, about the way in which this issue was going to be resolved.

1033 **Senator WATSON**—Ultimately, but before you got to ultimatum stage—

1034 **Mr Steward**—I am not aware of any—

1035 **Senator WATSON**—You eventually lost patience, did you not?

1036 **Mr Steward**—Yes, we did.

1037 It seems Westpoint acted in a professional manner. They knew they were in a superior legal
1038 position. Steward’s admission about losing patience is damaging.

1039
1040 **Senator WATSON**—I am trying to work out why you did not act sooner and go in earlier
1041 with your ultimatum but instead allowed a fair bit of toing-and-froing, negotiation and lots of
1042 opportunities.

1043 **Mr Steward**—We were dealing with a very technical legal issue. They had advice that they felt
1044 supported their view. We had a view supported by advice and we were at loggerheads over it, as
1045 we are on a host of issues every day with a host of people. If your question implies that we did
1046 anything that was overbearing or threatening, that is certainly not the case.

1047 **Senator WATSON**—No, quite the other way this time.

1048 **Mr Steward**—No. It was a forceful, willing contest between two people who had opposing
1049 views. That is really what it was. At the end of the day, we felt that we were not getting
1050 where we needed to get to quickly enough, so we thought we had to bring it to a head.

1051 **CHAIR**—I suppose it is also relevant to this discussion to say that you are a regulator, not a
1052 prosecutor, and your core obligation is to secure compliance, which is done in a variety of
1053 ways but, at least in the initial phases, by discussion rather than any other mechanism?

1054 I am unsure that obtaining compliance, except in very unusual circumstance, is the best
1055 approach. The law is the law, any negotiations will usually lead to the offending party seeing
1056 how far they can bend the rules.

1057

1058 **Mr Steward**—That is certainly what we had on our mind. We were seeking to impose a fairly
1059 fundamental change on the way in which the Westpoint Group was going to conduct its
1060 fundraising activities in the future and going to be dealing with its current investors. Before
1061 taking such a major step, it was sensible for us to raise that and try and negotiate and persuade
1062 Westpoint to comply rather than simply go off to court straightaway.

1063 **Senator WATSON**—It seems a bit of a soft-touch approach. That is what I am really
1064 worried about. I have a view of a regulator as a bit of a policeman, in effect—

1065 **Mr Steward**—I disagree.

1066 **Senator WATSON**—who says, ‘This is the law, why are you not complying with it?’ Bang!

1067 I agree with Watson.

1068 **Mr Steward**—The difficulty was—

1069 **Mr Lucy**—The bang came through the court, and we lost.

1070 **Senator SHERRY**—I am actually not fundamentally disagreeing with you in respect of that
1071 action. My argument is that you should have taken action earlier and against a wider range of
1072 people for a wide array of reasons. I want to go back to the compensation issue. We know that
1073 self-managed super funds are not covered by the theft and fraud provision of the CIS Act. Are
1074 you aware of whether any of the persons who placed money have complained to FICS, as I
1075 think it is known?

1076 Sherry is right! ASIC should have acted earlier. A lot of people complained to FICS.

1077

1078 **Mr Lucy**—Yes, we are. There are a number that have complained.

1079 **Senator WATSON**—Right.

1080 **Senator SHERRY**—But FICS has a limit, doesn’t it, on the amount that it can award?

1081 **Mr Lucy**—Yes. It is \$100,000, but it can be waived by consent.

1082 I know of no case where it was waived by consent.

1083

1084 **Senator SHERRY**—Do you know of the approximate number of individuals who have sought

1085 to take that course?

1086 **Mr Lucy**—It is a work in progress. At this stage, it is a relatively low number.

1087 **Senator SHERRY**—There would be some, I would have thought, commonsense in persons,
1088 certainly those with relatively small amounts of money, under \$100,000, taking this avenue. It
1089 is a relatively quicker form of restitution.

1090 **Mr Lucy**—We would certainly support that observation and, indeed, we have been almost
1091 aggressive in trying to encourage investors to take that route.

1092 ASIC was very aggressive in this matter.

1093

1094 **Senator SHERRY**—Yes. None of those matters have been heard by FICS yet, have they?

1095 **Mr Lucy**—Not to my knowledge.

1096 **Senator SHERRY**—Under the CIS Act compensation, theft and fraud prima facie is not
1097 going to be applicable. FICS is a possibility for some people and, I suspect, a probability for
1098 some. That is another avenue. What other avenues are available for compensation?

1099 **Mr Lucy**—It is a question of whether or not there is any culpability sheeted home to the
1100 directors, officers and third parties such as auditors and, in the event that that is the case,
1101 whether or not that bears fruit. It is also a question of looking at the assets of particular entities
1102 and parties that may not be secured by way of a first-charge security to see whether or not
1103 there is any opportunity for introducing further funds there and then, ultimately, whether or
1104 not we conduct a section 50 process.

1105 **Senator SHERRY**—In respect of Westpoint—and there is a time issue,
1106 obviously—whatever assets are left after the receiver is finished, what is the position with
1107 auditors if there is a finding that they were negligent? Is it possible to access compensation
1108 from the auditing firm?

1109 **Mr Lucy**—Yes.

1110 **Senator SHERRY**—What section of the act would allow that?

1111 **Mr Lucy**—Just the law of negligence.

1112 **Senator SHERRY**—In terms of the investors, I frankly do not think there is a likelihood that
1113 there is going to be a substantial amount of money from the Westpoint entities, whatever is left
1114 over. If there was a negligent case prima facie to recover moneys from the auditors, would
1115 ASIC leave that to the individual investors to initiate or could it do that itself on behalf of
1116 investors?

1117 **Mr Lucy**—My expectation is that the liquidators and/or the receivers would take that action
1118 in the first instance.

1119 Once again, ASIC wants to wist for someone else to do something.

1120

1121 **Senator SHERRY**—Could ASIC do that itself?

1122 **Mr Lucy**—In the event that there was nobody else willing to take it and it passed the public

1123 interest test then, yes, we would take it.

1124 **Senator SHERRY**—It is probably too early, but I certainly think—

1125 **Mr Lucy**—It is too early, with respect. It is something which we are very much alive to.

1126 **Senator SHERRY**—One of the difficulties for many of the investors I have spoken to is, first,
1127 their frustration with the likely length that this will take. You understand that many of them are
1128 elderly.

1129 **Mr Lucy**—I totally understand.

1130 **Senator SHERRY**—It could be years away. Second, whatever money is left in Westpoint, it
1131 will certainly be less than they have put in. There are also the costs of litigation for them as
1132 individuals. These are all issues that they are concerned about.

1133 **Many investors have died as I write this in June 2010. The vast majority have just given up.**

1134

1135 **Mr Lucy**—Perhaps a smaller issue, but a side issue, is their own taxation circumstances.

1136 **Senator SHERRY**—Yes. On that issue and tax liabilities, have you had any liaison with the
1137 tax office? That is not something I asked the tax office about yesterday.

1138 **Mr Lucy**—Yes, because one of the issues will be the ability of the investors to crystallise the
1139 loss.

1140 **Senator SHERRY**—Yes. So you have obviously had some discussions with the ATO about it.

1141 **Mr Lucy**—Yes.

1142 **Senator SHERRY**—What information is known about the likely treatment?

1143 **Mr Lucy**—We cannot speak for the tax office on that. We have raised the issue, they are
1144 alive to it and clearly it is in the interests of the investors to have their position clearly
1145 understood as quickly as possible.

1146 **Senator SHERRY**—I can raise that. There will be plenty more estimates hearings over the
1147 next couple of years. I will raise it with the ATO.

1148 **Mr Lucy**—I have no doubt. It is an important issue for many investors.

1149 **Senator SHERRY**—Yes.

1150 **Senator WATSON**—On that question of the responsibility of the tax office in relation to their
1151 small superannuation fund regulatory powers, I have to point out that diversification of
1152 investment is just one issue that the trustees have to look at.

1153 **Mr Lucy**—It is.

1154 **Senator WATSON**—Obviously, I think it is going to be very hard to pin much on the tax
1155 office, given the fact that it is not mandatory for them to enforce or anything like that; it is
1156 just one of the issues.

1157 **The ATO did become a major problem for a number of investors.**
1158

1159 **Mr Lucy**—My understanding is that it is part of their qualifying test. We have had situations,
1160 for example, where investors have put investments into four separate Westpoint investments,
1161 saying, ‘There is the diversification.’ How the tax office will treat that is for the tax office. What
1162 we are raising with the tax office, the liquidators and so on is that the funds and the individual
1163 investors will want to crystallise a loss and they need to be in a position to be able to crystallise
1164 it, the earlier the better.

1165 **Senator WATSON**—That is a different issue.

1166 **Mr Lucy**—Quite right; it is.

1167 **Senator WATSON**—Senator Sherry is giving us the appearance that, perhaps, the tax office
1168 regulation was remiss.

1169 **Senator SHERRY**—I think it was. I think they are remiss in respect of self-managed super
1170 funds generally. I make no bones about it. They are not doing enough. There might be a range
1171 of reasons for it that the tax office cannot help, but they are not doing enough. To come back to
1172 Mr Lucy, one of the issues here is that the tax office, to be fair to them—and I am critical of
1173 their lack of action in respect of self-managed super funds generally—have not yet received
1174 the audited reports or accounts of the trustee entities, the self-managed super funds, in which
1175 moneys were placed in Westpoint, in many cases. That is the case, isn’t it?

1176 **Mr Lucy**—I cannot speak for the tax office. We would not know of that circumstance.

1177 **Senator SHERRY**—Coming back to the meeting that you had on, I think, 23 February with
1178 about 70 individuals in respect of Westpoint, have you given a commitment to them? I think
1179 you have referred already to the fact that some people were emotional and upset, which is
1180 understandable.

1181 **Mr Lucy**—Yes.

1182 **Senator SHERRY**—Did you give a commitment to come back with a response to the issues
1183 they raised?

1184 **Mr Lucy**—Yes. We have a specific website dealing with Westpoint and we have issued at
1185 least three specific releases on that already.

1186 **Senator SHERRY**—Specifically addressed to those people who were at that meeting?

1187 **Mr Lucy**—Yes. We advised them that we were setting that website up and we referred them to
1188 it. My recollection is that the first update was within 24 hours of that meeting and that we
1189 continued to refresh it as appropriate.

1190

1191 **The best I can say about the ASIC website is has never been a source of vey much information.**