



Did ASIC fail over Westpoint?

Accused of being too cautious over Westpoint, Jeff Lucy insists that ASIC had to wait for sufficient grounds to act, writes **Joanne Gray**.

Jeff Lucy is not the sort of guy to act on impulse. Colleagues describe the chairman of the Australian Securities and Investments Commission as placid, courteous, cautious. "You won't find him firing the first shot," says one. "He's not a fire-in-the-belly sort of guy."

After the Federal Court last week froze the personal assets of Westpoint founder Norm Carey, ASIC is moving on multiple fronts to get to the bottom of the financial debacle. But Lucy is also under pressure to explain why ASIC didn't act more swiftly and aggressively to shut down the property group before \$320 million or more of retail investors' funds had disappeared.

"There are people who are making suggestions, 'Where was ASIC?' " says Lucy. "No one has shown anything to me to suggest we were given information that reasonably we should have acted on."

Lucy has been ASIC chairman since May 2004, stepping up from deputy chairman to fill former chairman David Knott's shoes when he departed in 2003.

Like it or not, the public judges the companies and securities regulator not just through its actions, but also through the words and actions of its chairman.

The top job at ASIC is complex, and critics abound. As chairman of ASIC's predecessor, the Australian Securities Commission, Tony Hartnell took on the 1980s entrepreneurs with ferocity and some success, though provoking a damaging row with former federal director of public prosecutions Michael Rozenes.

Hartnell's successor, Alan Cameron, was a convincing performer, although some claim he wasn't hard enough on the big end of town. Knott wanted to raise ASIC's profile and pursued high-profile individuals such as Rodney Adler and Rene Rivkin.

ASIC staffers say that little has changed operationally at the regulator since Lucy took over. But externally, Lucy has adopted a lower profile, shunning the megaphone tactics of other regulators such as former competition head Allan Fels, who tried to scare companies into compliance.

Lucy is the first non-lawyer to head the securities regulator. The former PricewaterhouseCoopers managing partner from Adelaide says he is loath to ring alarm bells too soon. If ASIC prematurely acts against questionable corporations or financial schemes, he says, that can trigger a collapse which may not help the investors it is trying to protect. Without concrete evidence, sometimes it is better not to act.

"Investors frequently take the attitude that if the regulator gets involved, all that will do is to crystallise the problems, in which case crystallise the losses," says Lucy.

"Inevitably when we turn up it's an environment where no one wants us, least of all investors. Many investors live in the hope that the investment will eventually roll on and

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be successful. In the case of Westpoint, a highly speculative real-estate development, it's a moot point as to when it was the point where the business model was flawed."

Yet ASIC could have stepped in faster to stop Westpoint's retail fund-raising, instead of waiting until November 2005 to wind up an offshoot, York Street Mezzanine. Only now is it investigating the financial planners who were recommending Westpoint investments.

A November 2004 WA Supreme Court judgement gave ASIC the chance to halt the activities of the property developer, which had raised money from retail investors by issuing promissory notes. The notes take advantage of a legal loophole to raise money from the public without detailed disclosure.

The court found the notes constituted managed investment schemes, so the Corporations Act did apply, and that the notes were not debentures.



That gave ASIC the jurisdiction it was seeking over two Westpoint fundraising vehicles, Emu Brewery Mezzanine and Bayshore Mezzanine. Westpoint appealed against the managed investment schemes decision, while ASIC appealed against the debentures decision.

Former WA barrister Hugh McLernon, who now heads litigation fund IMF, argues that once ASIC had the WA Supreme Court decision it should have moved swiftly to seek court approval to wind up Westpoint, regardless of the appeals.

"Once you get that, you have in my view an obligation to start the procedure [to wind up the company]," says McLernon.

"That was ASIC's mistake. That's the procedure that's been set up and unless it's followed reasonably aggressively, the system doesn't get into gear. I actually believe ASIC did better than it normally does. The current structure was brought down because ASIC did it. The only question is whether they did it quickly enough."

But Lucy maintains that ASIC simply didn't know enough to act. "I asked that exact question, 'What were our alternatives at the time?'" says Lucy in an interview at ASIC's Melbourne headquarters. In fact it appears Lucy wasn't closely involved in the decision about how to proceed against Westpoint following the WA Supreme Court decision.

"The advice that I've received is that the decision by the court would not have permitted us to proceed [to seek orders to wind up Westpoint]," he says.

"We weren't so worried. We had audited accounts and suggestions that everything was OK. We didn't have complaints saying people weren't getting paid. So what was there to cause us that level of anxiety? Nothing."

Mark Steward, ASIC's deputy executive director enforcement, acknowledges the regulator may have been able to bypass the appeal process and seek a court order to wind up Westpoint. But he says it didn't think such an application would succeed, because to convince the court, ASIC would have needed evidence that

Westpoint was insolvent, or that investors weren't able to redeem their funds, or that they were concerned.

"You can theoretically injunct the scheme pending an appeal dealing with the same issue," says Steward. "But to do that in advance of the appeal being heard, we needed to identify some real grounds of urgency and detriment at that particular point in time. There wasn't the ammunition to argue that something needed to be done more quickly."

Instead, ASIC turned its attention to investigating the solvency of the group. Lucy says it wasn't clear until late 2005 that Westpoint's finances were awry.

Before that there weren't many complaints by investors about redemptions. It was paying its investors returns. There was no groundswell of concern from investors which would have led ASIC to take action any faster than it did, says Lucy.

But to IMF's McLernon, waiting for investors in an unregulated scheme to not get paid is "the ultimate mistake" for a regulator.

"It's always that way with a Ponzi scheme," he says. (A Ponzi scheme uses the assets of new investors to make profit payments to the old investors.) "Individual investors cannot protect themselves. That's why the legislation gives ASIC the special power to apply to wind these things up. ASIC has to use it."

And that's where the personality of the chairman, his view of ASIC's role, and the tone he sets, can be decisive. ASIC's argument is that regardless of the public's expectations and perceptions, it is not a prudential regulator. It polices a disclosure regime, and its legal teams are geared to trying to enforce disclosure. Lucy's view seems to be that ASIC isn't necessarily there to





step in and stop accidents from happening. And it wants legal certainty before it acts.

Bob Baxt, former chairman of the Trade Practices Commission who is now at law firm Freehills, argues that ASIC is far too cautious and its lawyers are "far too conservative".

"If regulators aren't prepared to stick their necks out when they believe they've got a test case, we're never going to have our laws properly tested," Baxt says.

In fact Westpoint secured the services of Freehills, one of the nation's most well-credentialed firms, throughout its dealing with ASIC. According to Westpoint founder

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Norm Carey, Freehills designed the promissory notes for Westpoint.

Westpoint sold its notes through financial planners, some of whom were on high commissions of 10 per cent or more.

"We certainly weren't fazed by the fact that whenever we had an issue with [Westpoint] they came back at us with a lot of aggression through their legal advisers," says ASIC's Steward.

McLernon says that it "definitely helped" Westpoint to have a respected firm like Freehills as its advisers. But he argues the real failure was the fact that the federal government, and in particular Treasurer Peter

Costello, dragged their feet because they did not require financial planners to contribute to a compensation scheme.

"That means it's highly likely that most people [who invested in Westpoint companies] will not get a cent back."

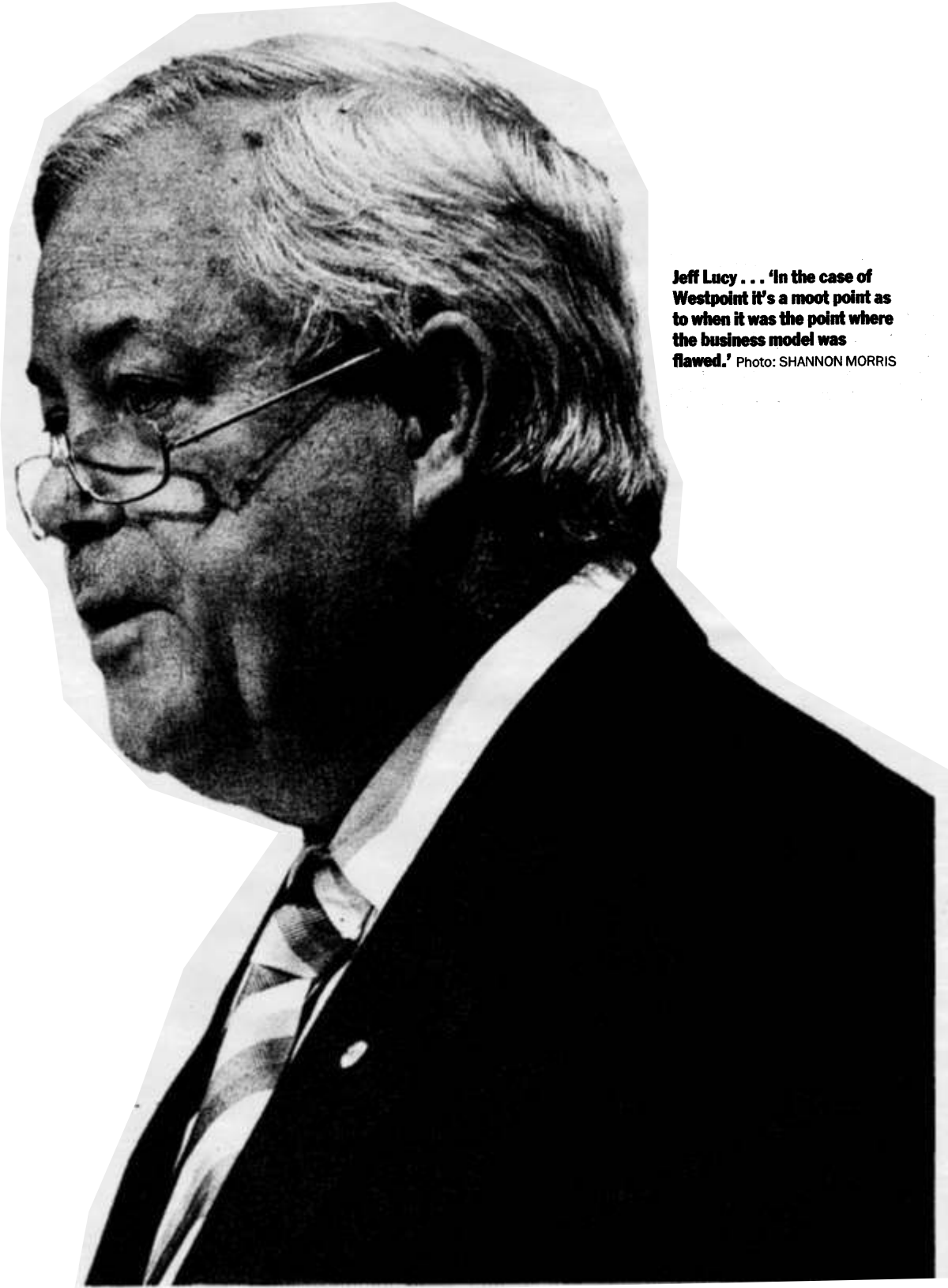
Lucy's three-year term expires in May 2007. He says he's engaged and committed to the job. He agrees that legal expertise among the three ASIC commissioners is important, but insists he is not at a disadvantage.

"I think that the balance of the commission needs to be two people with a legal background and one without. I've got training in corporate law. But we've got over 300 lawyers within ASIC. I'm advised what the law is."

As to his profile, Lucy is unapologetic. "You'll never please everybody. It's the responsibility of every chairman and every commission member to bring their own attitude to these issues. I think that we've got a good balance at the moment."

Deputy chairman Jeremy Cooper, meanwhile, is taking on a higher-profile role at ASIC. The former Blake Dawson Waldron lawyer has withdrawn from involvement in the Westpoint matter because his law firm has advised the company.

But Cooper was the major driver in the recent activity on conflicts of interest in financial services. He appears to be being groomed for the top job when Lucy departs. Meanwhile, the government has yet to replace former deputy chairman Berna Collier, who left to join the Federal Court bench in February.



Jeff Lucy . . . 'In the case of Westpoint it's a moot point as to when it was the point where the business model was flawed.' Photo: SHANNON MORRIS