Chapter 2

Issues considered at the oversight hearing

Overview of the proceedings

2.1 During its hearing the Committee investigated a number of issues, including:

- Policy refinement in the final transition year of Financial Services Reform (FSR), and in the lead up to the introduction of superannuation choice on 1 July 2005.
- Enforcement: ASIC's power to determine charges (HIH) and to adequately fund and staff large unexpected enforcement procedures.
- The appropriateness of the current division of powers between the three regulators—Australian Securities and Investments Commission (ASIC: financial services industry), the Australian Prudential Regulation Authority (APRA: banks and deposit-taking institutions) and the Australian Competition and Consumer Commission (ACCC: maintaining competitive markets)—to effectively regulate the market environment introduced under financial service reform.
- International enforcement issues and regulatory cooperation: the Alpine Offset matter and the implications of other international agreements.
- Government responses to recommendations made in committee reports, in particular: electronic banking fees; CLERP 9; and the introduction of the Australian Accounting Standards.
- Insolvency issues and the implementation of the Australian Accounting Standards.

2.2 The body of the chapter examines these issues in detail.

Financial services reform regime

2.3 The FSR compliance regime is disclosure-based. Full disclosure about the nature of the product, and the conditions attached to it, is the foundation of consumer protection under financial services reform.

2.4 In the closing days of FSR implementation, the effectiveness of the disclosure regime to protect consumers at a fair cost to business has emerged as a key issue. ASIC has commented on the excessive complexity and volume of the material being

provided, and has issued advice about its requirements for 'clear, concise and effective' disclosure documents.[1]

2.5 During the hearing, the Committee probed the relationship between the volume of the documentation and risk averse behaviour by providers. Senator Murray suggested that a reduction in liability imposed under the FSR regime might improve the quality, and reduce the quantity, of the disclosure documentation.[2] ASIC Deputy Chairman, Mr Jeremy Cooper, responded:

> The participants in the finance industry want to minimise risk as far as they possibly can, and they see voluminous product disclosure statements as the way that is partly achieved. We have asked ourselves whether the liabilities surrounding FSR are actually too harsh and drive this conduct further, but the big question is: how far would you have to reduce them, possibly at the expense of the rights of consumers and other claimants, in order to get the thing settled down? That has led us to think about whether mandating a short form product disclosure statement might work, where the more detailed information is somewhere else—possibly a web site or maybe in some other document that you could ask for. But the short form document would then have to very clearly explain that more detail was located elsewhere, and then a difficult question of how you apportion the liability comes up. Do you make the issuer liable for both documents—in other words, the short form that would be handed over as well as the long form material? That is probably the outcome that you would have to follow.[3]

2.6 Mr Cooper emphasised that any decision to reduce compliance costs for industry should take into account the potential for increased risk of financial loss by the consumer. ASIC Chairman, Mr Jeffrey Lucy, confirmed that lack of conciseness in Product Disclosure Statements and other documentation constituted inappropriate conduct and would not be tolerated by the regulator.[4]

2.7 Commenting on small business's complaints about the compliance burden, Mr Cooper said that the failure of lowly capitalised firms to use available electronic systems exaggerated the sense that disclosure paperwork requirements are excessive.[5]

2.8 The Committee's view is that while there are obvious efficiencies attached to online processing, the time taken to fill in the multiple forms, and providing the qualified staff to do it, obviously challenges some smaller businesses. ASIC's object should be to ensure that the disclosure obligations are doing what the law intends: protecting consumers at a reasonable cost to business.

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1 See Senate Economics Legislation Committee, *Estimates Hansard* (Additional Estimates), 16 February 2005, p. 99; *ASIC Media Release*, IR 04-71, 21 December 2004.

2 *Committee Hansard*, 15 March 2005, pp. 8–9.

3 *Committee Hansard*, 15 March 2005, p. 9.

4 *Committee Hansard*, 15 March 2005, p. 10.

5 *Committee Hansard*, 15 March 2005, p.11.

2.9 With this in mind, the Committee asked whether ASIC had adopted an overly prescriptive approach to regulation of the regime, moving away from the intended principle-based design. Mr Lucy answered:

> I think that the overwhelming response from the industry and the participants is that the FSR regime is the right regime for Australia. But it was a very significant undertaking. Almost everybody acknowledges that there are areas that need to be readdressed. I do not have a feel that that means throwing the baby out with the bathwater. I think it is very much a matter of looking at areas that should be sensibly finetuned.[6]

2.10 ASIC advised that the adjustment of policy in the area is the Government's responsibility. The Treasury is at present reviewing the FSR licensing and disclosure requirements, as announced by the Parliamentary Secretary to the Treasurer, the Hon. Chris Pearce MP in February 2005.[7] The Committee was re-assured, however, that ASIC had been consulted by Treasury during the review process.[8]

2.11 The Government confirmed the value of this consultation on release of its proposal paper, *Refinements to Financial Services Regulation*, on 2 May 2005.[9] The paper set out 25 proposed adjustments to the current arrangements. ASIC immediately announced that it would take the lead on eight projects, including: the release of a model Statement of Advice (SOA); the issuing of guidance and/or relief for the giving of personal advice; specific instances of general advice; and, authorisation requirements for general insurance issuers. ASIC would also undertake a discrete review of PS 146 on training requirements for advisers on basic deposit products.[10]

2.12 ASIC reported that most projects will be completed, or consultation finalised, by September 2005, with results released progressively.[11] These outcomes, within the context of the Government's broader review, will undoubtedly be significant. The Committee will monitor developments, and their implications for the financial services industry, and potentially inquire into them over the next reporting period.

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6 *Committee Hansard*, 15 March 2005, p.11.

7 *Australian Financial Review (AFR)*, 24 February 2005, pp.1, 10.

8 *Committee Hansard*, 15 March 2005, p. 10.

9 *Parliamentary Secretary to the Treasurer, Press Release* No. 012, 2 May 2005. Responses invited by 3 June 2005. See the proposals paper at Department of the Treasury website: www.treasury.gov.au/contentitem.asp?NavId=037&ContentID=973

10 *ASIC Media Release*, 05–110, 2 May 2005, pp. 1–2.

11 *ASIC Media Release*, 05–110, 2 May 2005, p. 1.

Choice in superannuation

2.13 With the imminent introduction of superannuation choice, the media has reported increasing anxiety about the timeframe for implementation of the choice regime, with service providers arguing they are not adequately prepared to comply.[12]

2.14 A number of areas of uncertainty exist. For some businesses, the main issue is the compliance risk associated with offering financial advice. Small business operators, in particular, have expressed concerns that they may breach the regime's requirements during informal discussions with employees about their industry fund scheme, or other superannuation options.[13]

2.15 At the hearing, ASIC advised that it is in the process of amending its requirements to give employers confidence under these circumstances. Specific advice will also be issued to advisers in the superannuation industry about the regulator's expectations and a website will provide direction for information.[14]

2.16 For consumers, there are concerns that the choice regime may increase investment risk if commercial interests unduly influence the nature of the financial advice given.

2.17 Financial services reform, along with technical advances and the globalisation of financial markets, has seen financial conglomerates emerge as the key organisational form in the Australian banking system. These conglomerates offer increasingly diversified products provided by a range of financial entities and using various commercial strategies.

2.18 Given the nature and composition of the financial services industry, the Committee asked whether there was increased risk that consumers may be subject to 'third line forcing' under the superannuation choice regime.[15]

2.19 Third line forcing describes a situation where the supply of goods or services is offered on condition that the buyer takes other goods or services from some other supplier. The implication is that, under choice, consumers could be pressured to change their superannuation arrangements as part of a suite of products offered by financial service providers, or by an employer. This would occur irrespective of whether the product components suited the consumer's needs, but with financial advantage to the provider.

2.20 ASIC advised the Committee that third line forcing is generally regulated as the anti-competitive market activity ‘exclusive dealing’ by the ACCC. However,

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12 *AFR*, 14 February 2005, p. 62.

13 *AFR*, 16 February 2005, p. 50.

14 *Committee Hansard*, 15 March 2005, p. 7.

15 *Committee Hansard*, 15 March 2005, p. 7.

where disclosure requirements apply to commercial relationships of the parties involved, it will fall under ASIC's jurisdiction.[16] In this instance, ASIC has in place requirements for managing licence holder conflicts of interest, and for disclosure where the choice of fund on offer may have been influenced by other commercial arrangements. To address jurisdictional concerns ASIC has a cooperation agreement with the ACCC, under which ASIC must provide assistance and information so that the ACCC can assess for this type of activity among financial services providers.[17]

2.21 ASIC representatives stated that the primary consumer protection mechanism under choice will be an education campaign. The message promulgated will be that superannuation choice is not compulsory, and that consumers should exercise caution. ASIC will also strongly promote to consumers that they should seek appropriate advice before changing funds. Follow up surveillance activities will monitor the advice given and ASIC will work with other agencies, including the Australian Taxation Office, to achieve a whole-of-government approach.[18]

2.22 After the introduction of compulsory superannuation in 1986, superannuation grew to become the second largest asset of Australian households, after the family home.[19] ASIC advised that it does have concerns about the introduction of superannuation choice, given the amount of funds involved and the unfamiliar territory it presents for the broad range of consumers, many of whom will not have had direct dealings with market-linked investment products before.[20]

2.23 The Committee shares ASIC's concern that superannuation choice can only be successful if consumers, who are often relatively inexperienced with financial products, have access to appropriate advice before choosing a superannuation fund. The Committee will observe ASIC's education campaign with interest.

Enforcement: HIH sentences

2.24 On 14 April 2005 Mr Rodney Adler, former Director of HIH Insurance Ltd, was sentenced to four and a half years jail, with a non-parole period of two and a half years, on four charges arising from his conduct as director of the HIH group of companies in 2000. In sentencing Mr Adler, Justice Dunford said:

> The offences are serious and display an appalling lack of commercial morality…Directors are not appointed to advance their own interests but to manage the company for the benefit of its shareholders to whom they owe

16 *Committee Hansard*, 15 March 2005, pp. 7-8.

17 *Committee Hansard*, 15 March 2005, p. 7.

18 *Committee Hansard*, 15 March 2005, p. 8.

19 *AFR*, 24 August 2000.

20 *Committee Hansard*, 15 March 2005, pp. 6; 7; 8.

> fiduciary duties…They were not stupid errors of judgement but deliberate lies, criminal and in breach of his fiduciary duties to HIH as a director.[21]

2.25 The next day, the former CEO of HIH Mr Ray Williams received four and a half years, with a non-parole period of two years and nine months, on three charges arising from his management of the HIH group between 1998 and 2000.[22]

2.26 During Additional Estimates in February, ASIC reported a 'significant result' on the HIH matter, having secured a guilty plea from Mr Adler to four serious criminal charges.[23] Meanwhile, media reports had suggested that ASIC had negotiated 'a deal' with Mr Adler to secure his guilty plea.[24]

2.27 At the oversight hearing, Mr Lucy emphasised that while ASIC bases it recommendations to the DPP on evidence gathered by the ASIC taskforce, it is the DPP that determines which of possible charges will be laid.[25] He explained that before ASIC enters into any investigation, it establishes whether it has a 'reasonably arguable' case; that the prospects of the investigation justify the expense of taxpayers' money and the consequences of the action, including whether the case could be successfully litigated. In most instances, external advice would be sought to assist the Commission decide whether litigation should be considered.[26]

2.28 Consequently, it appears to the Committee that media suggestions of a 'deal' between ASIC and Mr Adler are misinformed.

2.29 In response to questioning by Senator Wong about the decision-making process, Mr Lucy said that ASIC does not have set guidelines by which it determines its recommendations to the DDP. Instead, Mr Lucy, Mr Cooper and the Commissioner, Professor Berna Collier, make the decision based on the circumstances of the investigation and legal opinion. Mr Lucy advised that:

> …the Commission needs to have the flexibility of looking at matters on their facts and determining them based on what in our judgement is appropriate.[27]

2.30 Mr Lucy reconfirmed that once ASIC has made its recommendation to the DPP, it is then up to the DDP to determine the charges.[28] However, if the DPP

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21 Judgement 14 April 2005, quoted in *ASIC Media Release* No. 05-91, 14 April 2005, p.1.

22 *ASIC Media Release* No. 05-94, 15 April 2005, p.1.

23 See Senate Economics Legislation Committee, *Estimates Hansard (*Additional Estimates*),* 16 February 2005, p.87.

24 *AFR* Feb 19-20, 2005 pp. 20, 21.

25 *Committee Hansard, 15* March 2005, p. 21.

26 *Committee Hansard, 15* March 2005, pp. 22; 23.

27 *Committee Hansard, 15* March 2005, p. 22.

28 *Committee Hansard, 15* March 2005, p. 21.

considers that there are matters to be addressed outside of the boundaries of ASIC's advice, then the Commission will be further consulted and have input.[29]

2.31 Mr Lucy did not elaborate on the charges laid against Mr Adler given the status of the case. He agreed that ASIC would discuss the matter more fully at another meeting with the Committee, after Mr Adler had received his sentence.[30] Members of the Committee will take the opportunity to pursue these outstanding matters with Mr Lucy at the Senate Budget Estimates hearing this year.[31] If necessary, the Committee will request an additional subsequent meeting with ASIC to resolve these matters.

Funding of enforcement actions

2.32 ASIC expects this year to see the results of some very large and complex investigations, in particular: HIH, James Hardie and One.Tel, in addition to the Alpine Offset matter.[32]

2.33 The collapse of HIH was the biggest corporate collapse in Australia's history. ASIC's investigations have led to criminal prosecutions of nine senior executives, including directors of FAI, HIH and associated entities on 31 Commonwealth Corporations Act and Crimes Act (NSW) charges. On 15 April 2005, a further four defendants were awaiting trail, and one defendant had been charged and was awaiting committal hearings.[33]

2.34 In September 2004, the NSW Special Commission of Inquiry into Medical Research and Compensation, headed by barrister David Jackson, QC, found grounds for criminal charges against former executives of James Hardie Industries.[34] On the basis of the findings, ASIC immediately announced it would launch a broad inquiry into the James Hardie matter, which would go beyond the breaches found by the NSW inquiry.[35] In February, ASIC reported that the inquiry would be completed promptly, by mid-2005.[36]

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29 *Committee Hansard*, 15 March 2005, p. 24.

30 *Committee Hansard*, 15 March 2005, pp.20; 33.

31 ASIC is examined by the Senate Economics Legislation Committee during Estimates. A number of members of the Parliamentary Joint Committee on Corporations and Financial Services are also members of the Economics Legislation Committee.

32 Senate Economics Legislation Committee, *Estimates Hansard* (Additional Estimates), 16 February 2005, p. 87.

33 Statement by Mr Jeffrey Lucy, Chairman, ASIC, 15 April 2005.

34 See Special Commission of Inquiry into Medical Research and Compensation, Report, (D.F Jackson, QC Commissioner) New South Wales Cabinet, September 2004.

35 *ASIC Media Release* 04–305, 22 September 2004.

36 Following the introduction of NSW state and federal legislation which gave ASIC access, respectively, to Special Commission records and to relevant documentation from James Hardy. See *Bills Digest No. 74 2004–05* and *AFR*, 15 February 2005, p. 15.

2.35 In addition to these two major investigations, ASIC also continued with its investigations into the One.Tel and Offset Alpine matters.[37] Even though smaller in scale than the HIH and the Hardie matters, ASIC Chairman Mr Lucy reported the particular significance of One.Tel, which is being strongly litigated at a high cost to ASIC.[38]

2.36 The Committee sought to establish that ASIC operates within a funding framework that allows adequate regulation, investigation and litigation of such matters. This includes maintaining the staff and technological capacity to launch investigations promptly, particularly on matters which are commenced 'unexpectedly', for example, in the middle of the financial year.

2.37 Mr Lucy reported that the funding for the present actions is being drawn from the budget allocation for HIH, a total of $28.2 million over two years. This involved a reallocation of the money over the two funding periods:

> Of the $28.2 million, our expenditure in the 2003-04 year was $8 million. The budgeted expense for this year is $12.5 million, which leaves a balance to be carried forward of $7.7 million. We sought additional estimates in respect of James Hardie, OneTel and Offset Alpine of $6.887 million in the 2004-05 year. Those moneys were advanced. We have made a submission in respect of the 2005-06 year for James Hardie, and that is in the process of being considered by the government as part of its normal budgetary process.[39]

2.38 Mr Lucy advised that current funding arrangements are adequate. The additional estimates process provides a mechanism to acquire additional funds for unexpected, resource intensive and significant matters like the Hardie matter without undue delay or inconvenience to the process or to the community.[40] In relation to staffing for enforcement, ASIC told the Committee that some funding goes to employment of experts on contract. HIH staff—some fifty-five people—were additional to core staff allocations. Otherwise, Mr Lucy advised, staffing for enforcement is a management issue.[41]

2.39 Given that enforcement is a core activity for ASIC, the Committee encourages the Commission to be forthright to Government about its funding needs and to ensure that, even in exceptional circumstances, there is a buffer which ensures that

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37 The Offset Alpine matter was commenced in 1995, see *ASC Media Release* 95–65, 4 May 1995. The case history is available on the ASIC website. ASIC commenced its investigation into One.Tel in May 2001. See *ASIC Media Release* 01/179, 30 May 2001.

38 *Committee Hansard*, 15 March 2005, p. 30.

39 *Committee Hansard*, 15 March 2005, p. 26.

40 *Committee Hansard*, 15 March 2005, pp. 32; 33.

41 *Committee Hansard*, 15 March 2005, p. 31.

day-to-day enforcement management is in the hands of highly experienced enforcement officers.

2.40 To further establish ASIC's enforcement capability, Senator Wong asked that ASIC provide total figures on litigations commenced, but not completed, by ASIC during the reporting period.[42] ASIC also undertook to provide a breakdown of the expenditure, out of the $6.887 million allocated, for the Hardie, OneTel and Offset investigations. Responses are in **Appendix 1.**

Effectiveness of the regulatory framework

2.41 Given concerns about the number and size of the enforcement actions set out above, the Committee asked ASIC whether it was satisfied with the effectiveness of the regulatory carve up—between ASIC, the ACCC and APRA—to deal with such matters, and whether the present arrangements contribute to regulatory overlap or omission. Mr Lucy offered the following assurance:

> I think the system is working well…we do have memoranda of understanding. They require that there is very real and effective communication and dialogue between the three agencies. Certainly, at commission level and officer level, that dialogue is regular. We believe it is effective, so there is no enthusiasm from ASIC for the government to review the structures. We are comfortable with how things are working and we are not communicating with the government that there should be any change.[43]

2.42 Mr Lucy also made comparisons with the United Kingdom's system, which has a single regulatory structure to oversee securities markets and prudential matters.

2.43 ASIC recently met with the Head of the UK's Financial Services Authority (FSA), Mr John Tiner. Mr Tiner had been reported to observe that the FSA model has advantages over the Australian separation of ASIC and APRA.[44] Mr Lucy emphasised that there are strong differences between arrangements in the UK, principally in that the FSA is funded by industry and has no enforcement function. Nevertheless, ASIC has a strong dialogue with the FSA, exchanging documents and staff, to fortify the effectiveness of the two regimes.[45]

2.44 In conclusion, ASIC acknowledged that there are concerns about how past arrangements failed to prevent events like HIH, but considered that the current regulatory regime, and arrangements between ASIC and APRA, should help prevent such occurrences in future.[46]

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42 *Committee Hansard*, 15 March 2005, p. 28.

43 *Committee Hansard*, 15 March 2005, p. 34.

44 *AFR*, 15 February 2005.

45 *Committee Hansard*, 15 March 2005, p. 34.

46 *Committee Hansard*, 15 March 2005, p. 30.

2.45 The Committee will continue to closely assess the effectiveness of the regulatory structure through its inquiry mechanisms. It is currently examining the cooperation arrangements between ASIC and the ACCC in the relation to the regulation of property investment advice and the timeshare industry.

International enforcement issues and regulatory cooperation

2.46 The Committee canvassed a number of matters at the oversight meetings which relate to our international obligations, and may have significant implications for the regulator.

Offset Alpine case—the 'Kennedy matter'

2.47 A recent finding on the Offset Alpine case, otherwise known as 'the Kennedy matter', has overturned a constitutional challenge to ASIC's power to investigate matters referred prior to the Commission's creation.[47] The matter also indicated the international community's increasing willingness to provide access to information, an important mechanism to defeat terrorism and other criminal activities which rely on the illegal secretion of funds.

2.48 At the meeting, the Committee explored the Offset Alpine matter with ASIC, asking in particular about the constitutional implications and the status of the case in Switzerland.

2.49 Mr Lucy confirmed that findings in the last week, which had raised constitutional issues previously dealt with by the *Hughes* and *Wakim* cases,[48] had settled clearly and firmly in ASIC's favour, with costs being awarded against Mr Kennedy. The matter is now with the courts in Switzerland, where appeals have been made against the magistrate's decision to release information to ASIC.[49]

2.50 Senator Murray asked whether the case is likely to increase cooperation between the Swiss and Australian authorities.[50] ASIC reported that quite significant developments are occurring internationally:

> the IOSCO group, which is the international securities regulators, I think are working very effectively organising other countries to be willing signatories to a memorandum of understanding, which provides an obligation on co-regulators to provide access to information. The barrier in several countries, in particular Switzerland and Japan and there are others,

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47 See Kennedy v Australian Securities & Investments Commission & Ors [2005] FCAFC 32 (10 March 2005); *ASIC Media Release* 05–56, 10 March 2005; and *Committee Hansard*, 15 March 2005, p. 16.

48 *The Queen v Hughes* (2000) 171ALR 155 and *Re Wakim; Ex parte McNally* (1999) 163 ALR 270.

49 *Committee Hansard*, 15 March 2005, p. 16.

50 *Committee Hansard*, 15 March 2005, p. 17.

> is the banking secrecy provisions. There is no doubt that there is significant global pressure on a number of those countries to address their banking secrecy laws. At the end of the day though, inevitably, it is not with the regulator; it is a political decision. It is a decision of the respective parliaments as to whether or not they are willing to prescribe to their regulator the obligation to provide information to co-regulators around the world. Certainly there is clearly a move for countries that have that facility to provide that openly through signing a memorandum of understanding. We are also aware that there is significant political pressure on countries that at this stage have not been willing to sign because they are not able to do so.[51]

2.51 ASIC confirmed that, from an Australian perspective, the Swiss determination on the matter would not affect Australian law, which is unambiguous and clear, but there are indications of an increased willingness among regulators internationally to provide back-to-back disclosure, with some countries demonstrating political support for these developments.[52] In this instance the Swiss and Australian governments have entered into an MOU which requires back-to-back disclosure when criminal activity —not 'simply' tax evasion—is implied. Hence the Swiss willingness to assist in the Offset Alpine matter.[53]

2.52 The Committee asked whether these developments may facilitate pursuit of criminals who have benefited from banking secrecy provisions in the recent, and mid, past. ASIC was hesitant to confirm this, asserting the necessity of having a trigger for any investigation into past or present activities; that is, there must be a detectable offence under the Corporations or ASIC Act.[54]

2.53 Nevertheless, the Committee anticipates some progress in these matters, given favourable indications from the Swiss and the increased cooperation between regulatory authorities internationally.

Cooperation with the United States Public Company Accounting Oversight Board

2.54 Another instance of international cooperation investigated was ASIC's meeting with the United States Public Company Accounting Oversight Board (PCAOB) in February 2005. ASIC told the Committee that the US hopes to fast-track an agreement with Australia, Canada and potentially the United Kingdom to provide a process for review of auditors under the Sarbanes-Oxley Act of 2002.[55] The Act sets out a prescriptive regulatory regime which would extend CLERP 9 requirements to

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51 *Committee Hansard*, 15 March 2005, p. 17.

52 *Committee Hansard*, 15 March 2005, p. 18.

53 *Committee Hansard*, 15 March 2005, p. 19.

54 *Committee Hansard*, 15 March 2005, p. 19.

55 *Committee Hansard*, 15 March 2005, p. 35.

include routine inspection of 30 top audit firms and scrutiny of matters such as how they evaluate, compensate and promote partners.

2.55 Chairman Lucy had been reported saying that ASIC would have to review the law and evaluate its capabilities to comply with the extra responsibilities if Australia signed onto the agreement with the PCAOB.[56] The Committee asked for confirmation of these implications, which Mr Lucy provided:

> To the extent that we are looking at auditors and companies under CLERP 9, it goes without saying that we have the jurisdiction to do so. To the extent that we are willing to take on activities for the American regulator, that clearly requires law reform, because without that we would not have the jurisdiction to do so. So at this stage we are identifying the areas in which law reform would be required and that is a matter in which we have engaged Treasury. They are looking at that particularly. Our expectation is that there will probably still be ongoing dialogue and work with the Americans. I do not think that it will be simply ASIC going out to the top 30 companies and looking at their activities from a Sarbanes-Oxley perspective. I think that we will do that from a CLERP 9-ASIC perspective. But to the extent of Sarbanes-Oxley, I think that there will be a dual approach where there will still be some engagement by the American PCAOB.[57]

2.56 The Committee considers the full implications (including funding, jurisdiction and efficiency) of any agreement with the PCOAB should be investigated by the Government. Any decision to proceed with such an agreement should be accompanied by appropriate additional funding for ASIC. This Committee may choose to inquire into any proposed agreement with the PCAOB.

Government responses to committee recommendations

2.57 At this oversight hearing, the Committee evaluated the government responses and ASIC's implementation of previous recommendations made by this Committee.

Electronic banking and fee disclosure

2.58 In its *Report on Fees of Electronic and Telephone Banking* in 2001 the Committee made three priority recommendations on fees and fee disclosure.[58] ASIC had set up a fee disclosure working group to develop a transparency framework which would also, among other things, evaluate the Committee's recommendations.[59]

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56 *AFR*, 17 February 2005, p. 9.

57 *Committee Hansard*, 15 March 2005, p. 35.

58 These comprised: development of a real-time framework for fee disclosure; transparency in all electronic and telephone banking; and, the abolition of fees applied by banks to foreign automatic teller machine transactions. *Report on Fees of Electronic and Telephone Banking*, February 2001.

59 *Committee Hansard*, 15 March 2005, p. 1.

2.59 The Committee asked ASIC about that working group's progress, referring in particular to high transaction fees charged for the use of foreign Automatic Teller Machines (ATMs). The Committee recommended that Government should replace these fees with direct charging, which would reduce the cost by two thirds. This has not been adopted, and fees for foreign transactions continue to rise.[60]

2.60 Commenting on this ASIC advised that the banking industry has nevertheless achieved some cost reductions for consumers through the provision of free access for a designated number of transactions, although this has somewhat complicated the potential for full fee disclosure, especially where the quota is rebated. Fee disclosure is now mostly dealt with through bank statements, rather than by the upgraded ATM technology envisaged by the Committee in 2001. Real time disclosure through ATMs remains difficult.[61]

2.61 Mr Lucy reported that the ASIC working group had now completed its survey report, which would be 'discreetly' provided to the industry within a month. ASIC expected that the findings in the report would prompt the Reserve Bank to take address these matters, and would inform the bank's consideration of the draft standards for EFTPOS and VISA Debt payment systems, which had recently been released for public comment. Apart from making its findings available, however, ASIC had not decided whether to provide commentary or advice on the drafting of these standards.[62]

2.62 The Committee considers ASIC should ensure the Reserve Bank draws on its expertise in consideration of these standards and encourages ASIC to publicise the evidently significant findings of its surveys by making a submission to the bank's public consultation on the standards. The findings should be publicly accessible, even if selectively released, to better inform debate about these matters.

ASIC's response to CLERP 9 report recommendations

2.63 In Part 1 of the Committee's report on the CLERP (Audit Reform and Corporate Disclosure) Bill 2003 (June 2004), the Committee addressed concerns about analyst independence.[63] ASIC's submission to the inquiry had made the point that various types of conduct cannot be effectively regulated by an obligation to manage conflicts or disclose conflicts.

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60 Senator Chapman cited Reserve Bank research showing that foreign ATM transaction fees had continued to rise, with four major Australian Banks now charging $1.45 on each transaction, up five cents since 2001 from a low 40c in 1995. Approximately 40 percent of all ATM transactions are conducted via foreign ATMs. See *Committee Hansard,* 15 March 2005, p. 4.

61 *Committee Hansard,* 15 March 2005, pp.2–3.

62 *Committee Hansard,* 15 March 2005, p. 3.

63 *CLERP (Audit Reform and Corporate Disclosure) Bill 2003, Part 1: Enforcement, Executive Remuneration, Continuous Disclosure, Shareholder Participation and Related Matters*, July 2004.

2.64 The Committee recommended that the Government should examine ASIC's submission to Treasury on the matter, along with its surveillance report on research analysts.64 The Government rejected that recommendation in its response to the report, implying that the matters under comment had already been addressed by ASIC.

2.65 At hearings, ASIC advised the Committee that it had in fact issued detailed policy guidance, Policy Statement 181 on managing conflicts of interest, prior to the introduction of the CLERP 9 legislation on 1 January 2005.[65] In the guidelines, the identified issues had largely been addressed. ASIC further stated that, in drafting the guidance note, it had deliberately sought not to adopt a prescriptive approach, the emphasis of the regulatory regime being on 'managing conflicts' not 'prohibiting conduct'.[66]

2.66 However, Senator Wong reminded ASIC that, in its submission on prohibition of certain types of conduct, the regulator had identified two matters in particular as warranting prohibition. These were:

- trading by an analyst in products that are the subject of a current research report; and
- trading by an analyst against a recommendation or opinion contained in a current research report.[67]

2.67 ASIC was equivocal about the identified items but did not reject the general position of its submission. It reported, however, that the issue was a policy matter, and that the Government had made its decision.[68]

2.68 The Committee then invited ASIC to comment on a number of other recommendations made in the CLERP 9 report, Parts 1 and 2, and which the government response had identified as matters to be dealt with by ASIC.

2.69 The first recommendation invited ASIC to develop a guidance note to promote the adoption of whistleblower protection schemes as a feature of good corporate governance.[69] ASIC generally endorsed this recommendation.

2.70 The next, recommendation 10, related to requirements for reporting of links between board remuneration policies and company performance.[70] ASIC advised that this would require consultation with the Australian Stock Exchange.

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64 Recommendation 25

65 See *ASIC Media Release* IR04–42, 30 August 2004.

66 *Committee Hansard,* 15 March 2005, p. 12.

67 *Committee Hansard,* 15 March 2005, p. 13.

68 *Committee Hansard,* 15 March 2005, p. 14.

69 Recommendation 2, *CLERP (Audit Reform and Corporate Disclosure) Bill 2003, Part 1.*

70 *CLERP (Audit Reform and Corporate Disclosure) Bill 2003, Part 1.*

2.71 ASIC was then asked to respond to the recommendation on the infringement notice regime. ASIC stated that it had adequately addressed this in its May guidance note. Further, it confirmed that it was satisfied that there is adequate separation between ASIC's investigation and adjudication functions.[71]

2.72 The final issue related to the requirement for accounting bodies to liaise with ASIC to ensure there complaints handling procedures are adequate. ASIC endorsed this as a general principle but pointed out the limitations on accounting bodies ability to compel compliance.[72]

Report on Australian Accounting Standards

2.73 The Committee recently tabled its report on the introduction of the Australian Accounting Standards, in which it made a recommendation that ASIC should provide an additional month for small and medium enterprises to comply.[73] The Committee asked whether ASIC would adopt the recommendation and was gratified to receive the following consideration from ASIC's Chairman:

> We have been invited to look at two areas. The first is whether or not some form of accommodation should be given to auditors dealing with the smaller end of town—in particular recognising the fact that they frequently have a closer relationship with a client than perhaps the larger companies. The other alternative is the extended period. We are looking at both. At this stage, frankly, the suggestion is more likely to be for an extended period as distinct from giving any relief to auditors.[74]

2.74 The Committee looks forward to rapid official confirmation of this view, given that the standards have now commenced.

Insolvency issues and implementation of the new accounting standards

2.75 Senator Murray asked about ASIC's response to insolvency malfeasance, commending the Commission's increased focus on the area. Mr Lucy reported the establishment of the new National Insolvency Coordination Unit. The Unit takes an early intervention approach: surveillance activities lead companies to reassess director's duties and recapitalise, or to enter into some form of administration if

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71 *Committee Hansard*, 15 March 2005, pp. 14–15.

72 Recommendation 18, *CLERP (Audit Reform and Corporate Disclosure) Bill 2003, Part 2: Financial Reporting and Audit Reform*, June 2004; *Committee Hansard*, 15 March 2005, p. 16.

73 Recommendation 1, *Inquiry into the Australian Accounting Standards tabled in compliance with the* Corporations Act 2001 *on 30 August and 16 November 2004*, 10 February 2005.

74 *Committee Hansard*, 15 March 2005, p. 35.

necessary.[75] Mr Lucy considered that there was still a need for on-going reform, as the incidence of insolvencies had probably been reduced by strong economic conditions.[76]

2.76 The Committee then asked about the potential effect of the new accounting disclosure requirements, introduced by the International Financial Reporting Standards (IFRS), on the number of insolvencies.[77] Mr Lucy expressed confidence that the new requirements are being sensibly interpreted by the banks; ASIC did not expect that the presentation of accounts under the new standards regime would lead to a greater incidence of insolvency brought about by a squeeze on credit lines.[78] Mr Lucy emphasised, however that the success of the regime rests upon the attitude of the banks, and on the communication of the executive view through to all management levels.[79]

2.77 The Committee notes that on 26 April 2005, after the oversight hearing, ASIC issued guidance to listed entities outlining its expectations about the new accounting disclosure requirements for full-year financial reports.[80] Nevertheless, the Committee remains concerned about a significant policy change which, in the main, rests upon 'the attitude of the banks' for its success, and will carefully monitor the effect of the new standards on the number of insolvencies.

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75 *Committee Hansard*, 15 March 2005, pp. 3–4.

76 *Committee Hansard*, 15 March 2005, p. 4.

77 See Australian Accounting Standard 1047 *Disclosing the Impacts of Adopting Australian Equivalents to International Financial Reporting Standards*

78 *Committee Hansard*, 15 March 2005, pp. 3–5.

79 *Committee Hansard*, 15 March 2005, p. 5.

80 *ASIC Information Release* IR 05–16, 26 April 2005.