

Date: 21 October 2013

“The performance of the Australian Securities and Investments Commission”

Senate Standing Committee on Economics  
Parliament House  
PO Box 6100  
Canberra ACT 2600

Dear Mr Chair:

I have taught and written extensively in the areas of corporate law and insolvency law for the past 11 years which has caused me to assess ASIC’s role from a number of different perspectives. Please consider these comments as part of your committee’s review.

In recent years, two trends regarding ASIC have emerged. Firstly, ASIC has been given increasing responsibility for important areas of corporate and financial regulation, including stock market regulation, financial services licensing, consumer protection in financial services, business names registration and credit regulation. These matters add to ASIC’s already full regulatory brief covering general corporate regulation and administrative matters (document lodgments, searches and maintenance of registers). During this time while ASIC’s funding has increased, much of the funding has been tied to particular projects (such as key investigations into HIH and other high profile matters), and the numbers of staff working at ASIC has only increased from 1221 in 2000 to 1738 in 2012 (according to ASIC’s Annual Reports). The increases in funding and staffing are wholly inadequate to account for exponential increase in ASIC’s responsibilities. This is demonstrated by the information provided by ASIC’s regulated population survey that shows only a handful of employees responsible for each area, which leads to infrequent surveillance and enforcement.

Secondly, ASIC has received consistent criticism from the media, the general public and from parliamentary committees. This criticism has the common theme that ASIC is not doing enough to protect the public and take enforcement action against those who may have broken the law. It is often the case that a major corporate collapse or scandal, where investors lose large amounts of money, will generate criticism of ASIC’s performance. Why wasn’t more done? Why didn’t ASIC prevent the problems from arising? Such criticisms are, in my view, only partially valid. Criticisms based on a failure to prevent corporate scandals or collapses represent a misunderstanding of the focus of corporate regulation in Australia. Australia’s corporate regulatory framework is based largely on the disclosure paradigm. Rather than vetting documents (such as prospectus documents and annual reports) ASIC is merely the body that receives copies of those documents. It is up to investors to read the information and make a

complaint if they discover a problem. I'm sure ASIC does act proactively where it has reason to do so, but with over 2 million companies to deal with ASIC cannot read and assess every document. Blaming ASIC for failing to stop a company ripping off investors or collapsing following a scandal is a little like blaming the police for failing to stop a bank robbery before it happens.

A major element of ASIC's role is reacting to information that it receives, including information from whistleblowers, public complainants and mandatory disclosure (such as auditor's and liquidator's reports). The bulk of this information is given after the events have occurred, and the volume of information is immense with tens of thousands of complaints every year. If ASIC fully investigated every complaint it would never get anything done. While it has protocols for escalating matters up the enforcement chain, it cannot hope to take action for every breach of the law. Neither should the public expect it to do so. However, the progressive increases in ASIC's role, powers and responsibilities has created an expectation that ASIC should be doing more. ASIC is involved in most aspects of corporate life, from registration, lodgment of documents, public disclosure, fundraising, takeovers and insolvency. ASIC has been made into a super sized regulator, but does not have the resources to do the job properly. It has arguably been given too much to do and should be refocused by examining whether it can effectively regulate all of the areas within its current role.

ASIC is responsible for over 2 million companies, from the small mum and dad business to the largest public companies. It cannot prevent companies from failing or fraud being committed. Nor can it prevent investors who fail to read regulatory documents in corporate fundraising activities (either through ignorance or indifference) from investing in unsuitable or unprofitable financial products. While ASIC does a lot of good work on improving financial literacy and alerting investors and consumers to known scams and the risks involved in financial investments, I argue that ASIC is being asked to do too much, and is not given sufficient resources to undertake its role or to fulfill many of its responsibilities. Providing 24 staff members to regulate corporate insolvency, with over 10,000 companies collapsing every year demonstrates this point. Decisions have to be made about effective resource allocation and some areas are wallowing in the backwaters.

ASIC should however be more accountable for its enforcement strategy. ASIC's approach at enforcing contraventions of the Corporations Act and the ASIC Act has been skewed towards easy cases (such as straightforward penalties for minor breaches of the Corporations Act) and high profile matters involving large businesses. ASIC's commissioners have previously boasted in public speeches about its success rate in litigation of 97% and above. It may be said that such a statistic represents a timid regular unwilling to tackle hard cases. ASIC however needs to see its role as a responsive regulator who is not simply there to catch the crooks but rather to work with business (both large and small) at achieving appropriate regulatory outcomes. While ASIC does undertake regular consultations with industry, these are similarly skewed towards larger enterprises and their advisors.

There is a wholesale failure to address SME companies involved in important issues such as phoenix companies and rampant insolvent trading. Conflicts of interest and poor corporate governance practices in anything but the largest public companies are virtually invisible to ASIC. ASIC devotes so much resources to dealing with large financial institutions and mining companies that it ignores small business. Complaints about a lack of action are met with a standard response of a lack of resources, or a lack of impact on the broader economy. With over 10,000 companies failing each year, ASIC is focusing on the biggest and tallest individual trees and missing the forest. I have commonly heard investors whose complaints to ASIC have been met with a suggestion to take action themselves. This misses the point and demonstrates that ASIC sees its role as focused on large enterprises and system wide regulation, not investor protection. ASIC routinely does not seek compensation orders in its corporate enforcement actions (aside from the major HIH actions) and rarely brings representative proceedings (with recent matters such as Storm and Westpoint notable exceptions). ASIC welcomes the use of investor class actions because that means that compensation to investors is one less thing on its agenda.

ASIC needs to focus on less high profile court cases that take years and consume millions of dollars in expenses, and devote more attention onto the SME sector and take enforcement action that does not necessarily involve expensive and time consuming court action. There should be an expansion of the use of regulatory tools such as enforceable undertakings, penalty notices and disqualifications. ASIC seems overly focused on criminal prosecutions followed by major civil cases where extensive banning orders and penalties are likely. In the area of phoenix companies ASIC has powers to disqualify persons from taking part in the management of corporations, but the powers are rarely used, except in cases of negotiated settlements and these are relatively few in number each year. Similarly, liquidators provide thousands of reports on failed companies that include possible insolvent trading and other serious breaches of the Corporations Act but these lead to only a handful of actions (outside of straightforward actions based on failures to lodge documents) being taken.

Perhaps the clearest demonstration that ASIC is not doing a good enough job is that we cannot hold it fully accountable because it does not produce any comprehensive statistics. ASIC's annual reports have been transformed into regulatory highlights documents that focus on major matters but fail to give comprehensive enforcement statistics. For example, how many directors have been disqualified under s 206F of the Corporations Act in the last year, or the last 5 years? This is one of the major provisions dealing with phoenix activity but the public has no idea how it is used by ASIC, or indeed whether it is used by ASIC. While ASIC publishes information through its media releases, the search engine for these publications is wholly inadequate and does not allow for targeted searching without producing hundreds of results, most of which are irrelevant to the search. The public has very little information about what action ASIC takes for all but the highest profile matters. ASIC's databases hold millions of documents that could produce comprehensive statistics to assist in policy developments and law reform, but almost none of it is disclosed to the public. Those wishing to discover information on particular companies must pay fees to ASIC or its licensed information providers, which effectively locks

out the general public and keeps scrutiny at a minimum. While ASIC is mandated by legislation to charge for access to documents, it should be required to produce better statistics to allow for proper accountability.

In summary, I encourage the committee to:

1) review the scope of ASIC's responsibilities and consider whether some of its functions would be better handled by another regulator. It must be doubted whether areas such as insolvency and credit regulation can be adequately regulated as part of a super regulator or whether they should be moved into a more focused agency that can devote the resources and expertise needed to enforce the law.

2) increase ASIC's funding and staffing resources, but also to demand higher levels of accountability through regular comprehensive statistics being produced to inform policy development and law reform. ASIC should be given funding to employ a full time statistician, similar to the role recently created by AFSA (formerly ITSA).

Sincerely,

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