

**Proof Committee Hansard**

**PARLIAMENTARY JOINT COMMITTEE ON CORPORATIONS AND FINANCIAL SERVICES**

**Oversight of the Australian Securities and Investments Commission**

**(Public)**

**MONDAY, 3 DECEMBER 2012**

**SYDNEY**

**Question on Notice**

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**Mr FLETCHER:** Mr Savundra, you said that you had referred the matter to the AFP. When did that happen?

**Mr Savundra:** I cannot recall the date precisely but it certainly occurred after the parliamentary report was delivered. We had had requests for information via the AFP prior to that time but certainly—

**Senator BOYCE:** You had made requests or they had requested you

**Mr Savundra:** We had made international requests for information through the AFP. Prior to the report we had not sought to formally refer the matter to the AFP for investigation.

**Mr FLETCHER:** And the Crime Commission?

**Mr Savundra:** I will take that on notice, if that is okay.

**ANSWER**

The Australian Securities and Investments Commission (**ASIC**) referred material concerning Trio Capital Limited (in liquidation) and Jack Flader Jr to the Australian Federal Police (**AFP**) on 22 June 2012. ASIC initially approached the Police about this referral on 15 June 2012.

In respect of the Australian Crime Commission after initial contact a meeting was held between ASIC and the Commission on 20 June 2012.

We have reviewed our records and have confirmed that a number of Interpol requests have been made through the AFP since October 2009. These requests were made to assist ASIC with our Trio investigation.

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**Question on Notice #2**

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**Senator BOYCE:** Are you able to give the costs of the Storm case, including that of the forensic accountant?

**Mr Medcraft:** I will take that on notice.

**Senator BOYCE:** If we could have a breakdown of the costs of the case to ASIC.

**Ms Gibson:** I think we would probably prefer not to provide that in a public forum, just because at some stage there will need to be some discussion about outcomes of the case and costs.

**Senator BOYCE:** That was going to be my next question: have costs been awarded or not awarded?

**Mr Medcraft:** In the case of Storm it is still in court at the moment, but we can confidentially give you the number.

**Ms Gibson:** I am not sure.

**Mr Medcraft:** We will take it on notice.

**ANSWER**

In view of the pending litigation in which ASIC is involved arising from the collapse of Storm Financial, ASIC does not consider it appropriate to comment on the cost of the Storm case at this point in time.

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**Question on Notice #3**

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**Banksia debentures**

**Mr FLETCHER:** Is debenture secured over specific assets?

**Mr Price:** Yes, a floating charge.

**Mr FLETCHER:** Is it mainly commercial property or residential property or a mix?

**Mr Price:** I might take that question on notice. It is a bit of a mix, but I think it is mainly commercial property, just from memory.

**Mr FLETCHER:** The other aspect to that question, on notice, is what is the proportion of established property and property under development?

**Mr Price:** Again, I will take that on notice.

**ANSWER**

The Banksia Securities Limited loans by underlying security type (based on value):

- 22% was commercial property,
- 46% was residential property,
- 9% was industrial property,
- 18% was rural property and
- 5% was other property.

The Cherry Fund Limited (CFL) loans by underlying security type (based on value):

- 36% was commercial property,
- 21% was residential property,
- 6% was industrial property,
- 34% was rural property and
- 4% was other property.

*(Source 7.3.2 on Pg 19 of Receivers' Report dated 7 December 2012)*

There are 128 Banksia Securities Limited loans with an aggregate value of \$147 million with internal loan classifications which incorporate a development element of "construction", "land bank" and "vacant land". This equates to approximately 28% of the Banksia loans by value as possible property development.

There are no CFL loans classified "construction", "land bank" or "vacant land" indicating there are no development loans.

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**Question on Notice - #4**

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**Banksia investors**

**Mr Price:** It is an important point generally. One of the other things that the task force is doing is to consider if there are any breaches of the law. Obviously if we do find anything we will seek to hold people to account.

**Mr Medcraft:** We will look at directors; we will look at auditors; we will look at trustees. Basically we will look at all the gatekeepers, as we always do, including financial advisers.

**CHAIR:** So what are the consequences for—

**Mr Medcraft:** Sorry; the sad thing was—how much superannuation money was in—

**Mr Price:** A little over \$100 million, off the top of my head, in superannuation money was—

**Senator BOYCE:** How many people?

**Mr Price:** I will need to take that on notice.

**ANSWER**

There are 843 different Super Funds (SMSFs) with investments totalling \$112 million as at the date of appointment on 25 October 2012. *(Source Receivers Profiling Sheet dated 27 October 2012)*

This equates to 17.26% of the total \$652 million investors funds by value.

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**Question on Notice #5**

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**CP 189 – FOFA: Conflicted Remuneration**

**Mr FLETCHER:** I want to go to the paper that you have recently put out, *Consultation Paper 189 Future of Financial Advice: Conflicted remuneration*. A concern has been raised with me that this is likely to apply to investment firms which operate for non-retail clients as well as retail clients. Is that ASIC's understanding of the scope of the paper and the scope of these remuneration arrangements?

**Mr Kell:** No. I will take it on notice to check on that but, no, that is not our understanding.

**Mr FLETCHER:** To expand on the concern, it has been put to me that this firm and other firms in the investment management market serving non-retail clients typically operate on the basis of a bonus structure as well as a base remuneration structure for their portfolio managers. A driver of bonus amongst other things is the amount of additional funds under management that they are able to secure. They are concerned that that remuneration structure will no longer be open to them if the arrangements in paper 189 come into effect.

**Mr Kell:** It is a little hard to provide a definitive answer on an example like that off the bat so we are happy to take it on notice and get back to you quickly. Generally, it is not intended to apply in a purely wholesale context.

**Mr FLETCHER:** Is that are concern that has been raised with you on the consultation process?

**Mr Kell:** Again, I could check on that. It certainly has not been prominent in the responses to the paper to date to my knowledge.

**ASIC Response**

Under the Corporations Act, a benefit is only conflicted remuneration if:

- it is given to a financial services licensee, or a representative of a financial services licensee, who provides financial product advice to persons as retail clients; and
- it could reasonably be expected to influence the choice of financial product recommended to retail clients or the financial product advice given to retail clients.

The conflicted remuneration provisions do not apply in relation to services provided to wholesale clients. This position is reflected in our proposed regulatory guidance on the conflicted remuneration provisions.

From our consultations with industry, we consider that industry understand this.

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**Question on Notice- #6**

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**Discretionary trusts**

**Senator BOYCE:** Leading on from what you were just talking about, the issue has been raised that it may be possible to define a discretionary trust that operates a family business as a financial product. Has that issue ever been raised with you? If so, how?

**Mr Tanzer:** I have to take that on notice, Senator.

**Answer**

As you are aware, ASIC deals with particular matters as they arise, including considerations of whether something falls within the definition of a financial product under the *Corporations Act 2001*. While we are unable to comment on specific entities, I advise that it does not appear from our records that this issue has been raised with ASIC in any formal sense.



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**Question on Notice #7**

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**MF Global – client money**

**Mr FLETCHER:** I want to ask some questions about MF Global. It is reported that a number of Australians have had their balances in accounts with that international broker frozen following its collapse in the US. How actively is ASIC involved in efforts to recover those moneys?

**Ms Gibson:** There are two positions. Firstly, the MF Global subsidiary in Australia is being wound up. I thought that there was some money in the course of being released from the local broker. I do not know about the position of Australians with funds in the US or UK fund directly. Some of the moneys that were invested here went through to London. There is some money frozen there. We are in constant dialogue with the receivers. The receivers are seeking to negotiate a situation with the US administrators to extract some money that is held in London.

**ASIC Response:** The issues in these types of external administrations can be very complex, with a mix of competing interests, and often require court intercession as was the case with MF Global Australia Limited (**MFGA**). MFGA was one of the largest futures brokers and providers of contracts for difference (**CFDs**) in Australia. Due to significant financial difficulties faced by its US-based parent, administrators were appointed to MFGA on 1 November 2011. MFGA subsequently went into liquidation on 2 March 2012.

Since the collapse of MFGA, ASIC has continued to monitor and engage with the liquidators of MFGA, as appropriate, including;

- obtaining regular updates on the progress of the administration and liquidation of MFGA;
- monitoring the various court applications to assess the legal and policy implications; and
- engaging with the liquidators on disclosure to clients and creditors, including on issues associated with the liquidators' remuneration and costs.

The liquidators of MFGA instituted representative proceedings to obtain court orders regarding the distribution of client monies and amounts recovered from clearing houses and counterparties. Representatives of various categories of claimants appeared in these proceedings. On 29 August

2012 Justice Black of the NSW Supreme Court handed down his decision in these proceedings<sup>1</sup>. Following the decision, the liquidators of MFGA commenced a first partial distribution to clients on 31 October 2012. To date approximately \$201 million (or an average of 63 cents in the dollar) has been distributed to clients and a further distribution is expected after Christmas.

There had been a dispute between MFGA and MF Global UK Limited (in special administration) (**MFGUK**) over approximately \$36 million held by the ASX. This had been the subject of separate proceedings in the Federal Court. On 14 December 2012 the liquidators of MFGA announced they had reached an agreement with the special administrators of MFGUK to settle this dispute. Relevantly, the dispute has been settled on the basis that:

- MFGUK will receive an amount of GB£400,000 (approximately AU\$592,680); and
- MFGA will receive the balance of the disputed funds, being approximately AU\$35.2 million.

The liquidators of MFGA anticipate receiving the funds from ASX shortly and will look to make a further distribution to clients (specifically, futures clients) as soon as practicable.

**Mr FLETCHER:** It is reported that, although the clients were told that their moneys were going into a so-called client segregated account, they actually went into a pooled account and, when the firm collapsed, that became part of the pool of assets that creditors tried to recover against. Is that right?

**Ms Gibson:** I had thought that when the money was frozen that this was the subject of much discussion, although I might have to come back to you on notice about this. It has been to court and tested before Justice Black. He gave quite a long judgment in working out how the moneys that are available are to be divided up between the various classes of investor. Whether money is in a client segregated account is one of the criteria.

**ASIC Response:** At the time of its collapse, MFGA held a substantial amount of funds in client segregated accounts. As an Australian financial services licensee and market participant MFGA was required to keep 'client money' in a client segregated account, separate from its own funds. Under the Corporations Act, moneys held in client segregated accounts are held in trust. However, the Corporations Act does not require a licensee to maintain a separate account for each client. Additional funds were subsequently able to be recovered from clearing houses and counterparties with which MFGA had open positions. Justice Black found the client segregated accounts maintained by MFGA should be grouped into four pools, representing the four product lines of MFGA (namely, futures, CFDs, online FX and margin FX). In addition, his Honour found that amounts recovered from clearing houses and counterparties were, on receipt by MFGA, to be held on trust under Chapter 7.8 of the Corporations Act. Accordingly, the funds recovered from counterparties are only available for distribution to the relevant client pool and not for general distribution to other creditors.

**Mr FLETCHER:** I am interested in understanding whether clients of MF Global are in a different position to clients of an Australian broker that they used to transact on the ASX or whether they are in exactly the same position.

**Ms Gibson:** We would need to take that on notice to give you a fully correct answer.

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<sup>1</sup> MF Global Australia Ltd (in liq) [2012] NSWSC 994

**ASIC Response:** Under the ASIC market integrity rules, brokers holding client funds to trade on Australian futures markets are required to place those funds into a segregated account. As a market participant, MFGA adhered to this requirement. The clearing of MFGA futures trades was conducted by MFGUK. Clearing is a capital intensive business and it is common for one entity in a group, with a large capital base, to be a clearer in multiple markets for number of trading participants in the group. There had been a dispute between MFGA and MFGUK over the funds held by the ASX at the time of MFGA's collapse, however this dispute has now been settled.

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**Mr FLETCHER:** There was a suggestion in one of the press reports that a particular difficulty was that ASIC had granted an exemption to MF Global to allow it to use its British business as the market participant in Australia. Is that right or not?

**Ms Gibson:** I would need to take that on notice. I am not sure whether we or the ASX would have done that. If the problem was clearing participants, then probably the ASX would have done that.

**ASIC Response:** MFGUK, an entity regulated by the UK Financial Services Authority, had been granted an exemption by ASIC from the requirement to hold an Australian financial services licence for certain financial services it provided to wholesale clients. The Corporations Act contemplates the granting of such exemptions.

The decision was made by the ASX to allow MFGUK to be a Clearing Participant.

**Mr FLETCHER:** All right. That was all I had.

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**Question on Notice #8**

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**Financial advice and the super cap**

**Senator BOYCE:** I have had a couple of people complain to me about not receiving the best advice from their financial service providers or advisers, which has caused them to go over the cap on superannuation. Has that issue been raised with you? If so, what is ASIC thinking about that?

**Mr Kell:** We are aware of the issue and the fact that the change in the level of the cap means that advisers should be revisiting the strategies and arrangements that were put in place prior to July this year. First and foremost, it is an issue about which the ATO has been providing educational material and information to investors. That material talks about the cap and how they can manage that. We have not been receiving a significant number of complaints about this, but I will take it on notice to check whether we have had any. I will also check on whether we have referred any of those to the Financial Ombudsman Service for them to look at the quality of the advice that has been provided. At this stage, it has not been a big issue in terms of complaints that have come to us. We are aware of it. We think that it is the sort of issue that, as a matter of course, should be captured in knowledge d skills updates for financial advisers. We would like to see it incorporated into the training that advisers get.

**ASIC Response**

ASIC has not received a significant number of complaints from consumers who have received advice that has caused them to exceed the concessional contributions cap. ASIC has, in fact, received 1 complaint and 2 breach notifications regarding excessive contributions to date in the 2012 calendar year. Both breach notifications were in respect of the conduct of one financial adviser.

One of these matters is being considered at the Superannuation Complaints Tribunal and the other two were managed through the relevant Australian financial services licensee's dispute resolution framework.