

**Senate Standing Committee on Economics**

**ANSWERS TO QUESTIONS ON NOTICE**

**Treasury Portfolio**

**Budget Estimates**

1 June – 3 June 2010

**Question: BET 22**

**Topic: Brien Ernest Cornwell Case #2**

**Hansard Page: E117-118 (01/06/2010)**

**Senator XENOPHON asked:**

**Senator XENOPHON**—I am conscious of time. Under the conditions of the enforceable undertaking, Brien Cornwell was required to report back to ASIC regularly with progress of the undertaking. Did this occur? When this did not occur, did ASIC chase up the matter? On what occasions did Mr Cornwell contact ASIC pursuant to that undertaking?

**Mr D'Aloisio**—Again, I am more than happy to take on notice all the specifics of it and give you an answer. As I say, in the general sense we would follow up enforceable undertakings.

**Senator XENOPHON**—Again, you may take some of these on notice. I hope you will be able to answer some here. From the moment that ASIC was made aware of Brien Cornwell's actions and made an order against him, how long did it take for an enforceable undertaking to be reached?

**Mr D'Aloisio**—I will get that as well.

**Senator XENOPHON**—According to papers that I have received, Brien Cornwell signed the enforceable undertaking in December 2007 but it was not signed by ASIC until May 2008. If that is the case, what was the reason for the delay? Does ASIC concede that this gave Brien Cornwell an additional five months to move his assets? This is on the basis of the paperwork I have been shown.

**Mr D'Aloisio**—I can only take that on notice.

**Senator XENOPHON**—Again, according to information I have received, could you confirm that is the case? If so, why the delay? Further to that, on the basis of the enforceable undertaking with Brien Cornwell and the fact that no moneys have been returned to investors, does ASIC feel that there needs to be a review of enforceable undertakings as a mechanism to deal with such matters? Can it understand why members of the public, particularly the victims of Mr Cornwell, can feel completely let down by the system in terms of enforceable undertakings?

**Mr D'Aloisio**—With regard to the first part of that question, Senator, I can say that I do not think we would be seeking an amendment to the enforceable undertaking provisions. I think from what you are referring to and depending on the facts—talking again more generally—what we would need to do is make an assessment. Rather than go for an enforceable undertaking, we would actually go to court. If we feel there is money there or likely to be money there and there has been wrongdoing, it would probably be better for us to go straight to court rather than go through an enforceable

## Senate Standing Committee on Economics

### ANSWERS TO QUESTIONS ON NOTICE

#### Treasury Portfolio

#### Budget Estimates

1 June – 3 June 2010

undertaking. So we would not need to amend the enforceable undertaking provisions. I think we would have other powers that we could proceed under, but in this case we did not. Obviously there will be reasons why that was not the case, and I will look into it.

**Senator XENOPHON**—Further to that, during the negotiation of the terms and conditions of an enforceable undertaking, does ASIC use its power to freeze assets? Did it do so in this case?

**Mr D'Aloisio**—Again, I cannot speak for the case. Generally speaking, if we feel that it will protect investors and there could be a pool of money that could be returned to them, we would seek freezing orders, if we can establish them.

**Senator XENOPHON**—My understanding is that freezing orders were not sought in this case. Given what Senator Joyce has said about the way Mr Cornwell and his wife are living, you can understand why that is particularly galling to investors.

**Mr D'Aloisio**—I understand the thrust of what you are putting. As I have said to Senator Joyce, I will look into that and we will give you a response on all those issues.

**Senator XENOPHON**—As far as investors go, some of them understood that an enforceable undertaking, if not a guarantee, gave them some security in a broad sense that they would be paid. But it is fair to say that an enforceable undertaking is not a guarantee of any sort?

**Mr D'Aloisio**—It depends on its terms, Senator. If one of the terms is a payment of money and ASIC is satisfied that the money was there and took steps to protect it, then yes, that could happen. But that would be unusual with an enforceable undertaking, I must say, in my experience.

**Senator XENOPHON**—One of the specific issues that has been raised by me in relation to Mr Cornwell is that given that the Palais investment was sold for \$5 million, how can ASIC now advise investors that neither Newcastle Palais Holdings nor Mr Cornwell has the financial capacity to make repayments as required? There is a real issue there about that particular asset.

**Mr D'Aloisio**—I am sorry, but I do not have the facts.

**Senator XENOPHON**—No. I understand that a lot of these have to be taken on notice. I think you can understand the despair of many of the investors—the victims of this matter—as I think Senator Joyce has outlined. Finally, in relation to this, if enforceable undertakings are in effect unenforceable, as in this case, will the Cornwell case and other cases prompt ASIC to look at a review of mechanisms to protect investors in such cases?

**Mr D'Aloisio**—Clearly the answer would be yes. As I said earlier, I suspect that it would not be necessary for us to seek legislative change to enforceable undertaking provisions. I think what it would indicate to us is that we probably should be looking at other powers that we could be using under the Corporations Act, which more

## Senate Standing Committee on Economics

### ANSWERS TO QUESTIONS ON NOTICE

#### Treasury Portfolio

#### Budget Estimates

1 June – 3 June 2010

directly enable us to get court orders for the compensation or for other fines and so on. We will look at it in the context of the way you have asked the question. But I think really our choices are that you look at the wrongdoing. You make an assessment as to whether it is just the corporation or whether it is the corporation and the directors, the shareholders and who else—the investors—and whether it is a registered scheme or unregistered scheme. From that you will make an assessment of the nature of the actions you may take. In some cases, you may, as for example in Westpoint, go directly against individuals rather than the companies. In other cases, you may concentrate on the companies. So it is a case of looking at the facts.

**Senator XENOPHON**—Chair, I do have five questions in relation to Westpoint, but I can wait my turn or I can keep going and take five minutes.

**CHAIR**—I think Senator Bushby is anxious.

**Senator XENOPHON**—I will wait my turn for the Westpoint questions. Mr D'Aloisio, insofar as the answers that you will provide on notice, can you provide any documents or supporting documentation in terms of a paper trail of the enforceable undertakings and dates and times when things were followed up and the like?

**Mr D'Aloisio**—Certainly enforceable undertakings are a public record and they are on our website. We can provide them. As to whether I can provide any other papers, I will need to look into that.

**Senator XENOPHON**—Insofar as—

**Mr D'Aloisio**—Insofar as I can as a matter of law.

**Senator XENOPHON**—Insofar as those documents reflect what level of compliance was there with respect to the enforceable undertaking.

**Mr D'Aloisio**—I see what you mean, yes.

**Senator XENOPHON**—And what follow-up there was by ASIC to follow up Mr Cornwell and his activities, thank you.

#### **Answer:**

Senator Xenophon has raised questions concerning what is known as the "**Newcastle Palais scheme**", which involves company director (and former solicitor) Brien Cornwell.

#### *Background to the matter*

The Newcastle Palais scheme involved the proposed development of commercial and residential premises on land in Newcastle (the "**Palais Royale land**") owned by a company known as Newcastle Palais Holdings Pty Ltd ("**Newcastle Palais**"), as trustee for the Newcastle Palais Unit Trust. It was the trust's objective to develop the Palais Royale land.

## Senate Standing Committee on Economics

### ANSWERS TO QUESTIONS ON NOTICE

#### Treasury Portfolio

#### Budget Estimates

1 June – 3 June 2010

In early 2006 investors were encouraged to invest money into the development. The scheme promised investors high returns over 18 months to 2 years, and the investment was to be made by way of the purchase of units in a trust. The primary vehicle for investment was the Palais Investment Trust, of which Empower Invest Pty Ltd ("**Empower Invest**") was the trustee. Each unit in the Palais Investment Trust was intended to be converted into a unit in the Newcastle Palais Unit Trust, representing an interest of 1% of the development. Ten investors bought ten units in the Palais Investment Trust, investing a total of \$769,500. With the exception of one investor, the investors' money was paid directly to Newcastle Palais.

A complaint was made by an "investigative journalist" to ASIC around the time investments were made in early 2006, with the basis of the complaint being that the promoters of the Newcastle Palais scheme, Ken Watson (director of Empower Invest) and Brien Cornwell (of Newcastle Palais), were offering an unrealistic return on the investment.

ASIC's focus in investigating the matter centred upon affirmative remedies that would prevent the continued promotion of the scheme, thereby protecting the public, and enabling the return of funds to existing investors should they seek a refund. It was agreed in December 2006 that the matter be resolved by way of consent orders and possibly an enforceable undertaking to cover the refund of any moneys to the investors. The reason an enforceable undertaking was chosen as opposed to a Court order was that none of the investors were complaining or seeking a refund at the time. As such, neither a compulsory refund nor the winding up of the scheme was considered justified at the time. Investors had an option of seeking a refund in accordance with the enforceable undertaking. It should be noted that no evidence came to light that the development of the Palais Royale land was not a true objective of the Newcastle Palais scheme, nor that there was any perceptible misuse of the investors' funds, including for the enrichment of, in particular, Brien Cornwell.

*Q: From the moment that ASIC was made aware of Brien Cornwell's actions and made an order against him, how long did that take for an enforceable undertaking to be reached?*

About 1 year and 11 months.

An enforceable undertaking was signed by Ken Watson, in his own right and as director of Empower Invest, in September 2007, and by Brien Cornwell, in his own right and as director of Newcastle Palais, in December 2007. ASIC would not accept the undertaking until such time as the Court had made Orders in relation to the misconduct aspects of the matter.

On 9 May 2008 declarations and orders were made by consent by the Supreme Court of NSW. The declarations were to the effect that Newcastle Palais and Empower

## Senate Standing Committee on Economics

### ANSWERS TO QUESTIONS ON NOTICE

#### Treasury Portfolio

#### Budget Estimates

1 June – 3 June 2010

Invest (together "**the Companies**"), and Ken Watson and Brien Cornwell (together "**the Directors**"), had promoted an unregistered managed investment scheme, and provided financial services without a license, and the orders restrained the Companies and the Directors from continuing that misconduct.

The orders were supplemented by the undertaking, which ASIC accepted on 9 May 2008 under section 93AA of the ASIC Act from the Companies and the Directors (the "**Enforceable Undertaking**"). The Companies undertook to:

- inform investors in the scheme of ASIC's concerns about the Newcastle Palais scheme;
- offer to refund money invested;
- make a refund to any investor who accepted the offer; and
- report to ASIC on any refunds requested and paid to investors.

The Directors undertook to use their best endeavours to ensure the Companies complied with the Enforceable Undertaking.

*Q: Further to that, during the negotiation of the terms of an enforceable undertaking, does ASIC use its power to freeze assets? Did it do so in this case?*

Whether ASIC applies to the Court to seek a restraining order in respect to assets depends upon the situation in the particular case. Such an order requires, among other things, that the Court be satisfied that it is necessary and desirable for the purpose of protecting the interests of a person who may have claim against the person/entity against whom the order is sought.

ASIC did not in the Cornwell case seek such an order given the attitude of investors at the relevant time.

*Q: If that is the case, what was the reason for the delay? Does ASIC concede that this gave Brien Cornwell an additional five months to move his assets?*

*Q: Again according to information I have received, could you confirm that is the case? If so why the delay?*

As noted above, the Enforceable Undertaking was signed by Watson in September 2007, and by Cornwell in December 2007. ASIC would only accept the undertaking once Orders were in place formalising its position in respect of the Companies' and Directors' misconduct. The earliest date provided by the Court to hear the matter was 9 May 2008.

ASIC made inquiries in 2009 in relation to the assets of the Companies and Directors, and found no evidence that the five month period between the signing of the

## Senate Standing Committee on Economics

### ANSWERS TO QUESTIONS ON NOTICE

#### Treasury Portfolio

Budget Estimates

1 June – 3 June 2010

undertaking and its acceptance provided opportunity to Brien Cornwell, or Ken Watson or either of the Companies to "move assets".

*Q: When an enforceable undertaking is agreed to, what monitoring and/or follow-up does ASIC conduct to ensure it is met? What monitoring or follow-up occurred in the case of Brien Cornwell?*

*Q: Brien Cornwell was required to report back to ASIC regularly with progress of the undertaking. Did this occur? When this did not occur, did ASIC chase up the matter? On what occasions did Mr Cornwell contact ASIC pursuant to that undertaking?*

The monitoring or follow up of an Enforceable Undertaking is dictated by the terms of the particular undertaking.

In the present instance, the Companies and Directors complied with the terms of the Enforceable Undertaking to communicate ASIC's concerns to the investors, and advise them of their right to request a refund.

While all investors requested a refund, at the time payment was due from the Companies, in about July 2008, it came to ASIC's attention that the investors had separately entered into discussions with the Companies and the Directors about alternative arrangements for repayment. Information received by ASIC from the Directors suggested that the investors were seriously considering an alternative to a cash refund. The Companies provided a report on their communications with investors to ASIC in early September 2008, along with further details of the alternative security being offered in lieu of immediate payment. It appeared at that time that the Companies did not have the liquid assets immediately available to make a refund to investors.

ASIC reserved its rights to take further action in relation to the apparent breach by the Companies in their failure to refund investors, and proceeded to make further inquiries. In particular, in September 2008 ASIC communicated with a solicitor who was at that time acting for the investors, who confirmed that negotiations were ongoing, and investors were positively considering alternative arrangements.

The tipping point in the negotiations between the investors and the Companies and Directors was in about November 2008, when unannounced to all parties, including ASIC, Newcastle Palais sold the Palais Royale land for a significant sum.

*Q: Given that the Palais investment was sold for \$5 million, how can ASIC now advise investors that neither Newcastle Palais nor Mr Cornwell has the financial capacity to make repayments as required?*

Despite the land selling for well in excess of the debt owed by Newcastle Palais to a secured lender, \$5 million against a mortgage of approximately \$1.5 million, it subsequently came to light that Mr Cornwell had subjected the Palais Royale land to a

## Senate Standing Committee on Economics

### ANSWERS TO QUESTIONS ON NOTICE

#### Treasury Portfolio

##### Budget Estimates

1 June – 3 June 2010

cross-collateral guarantee in respect of another of his property developments, Melaleuca Estate at Port Stephens. The same lender was involved in respect of both the Newcastle Palais scheme, and Melaleuca Estate. Mr Cornwell has since explained that the payout under the guarantee was in the nature of a loan from Newcastle Palais to Melaleuca Estate Pty Ltd, and accordingly the balance of the sale proceeds was fully applied under the arrangement. Newcastle Palais apparently has no other assets available to it.

Upon learning of the sale of the property in early December 2008, ASIC made further inquiries, including obtaining documents pertaining to the sale of the Palais Royale land (which confirmed the distribution of the whole proceeds of the sale of the property to the mortgagee), interviewing Mr Cornwell in July 2009, and liaising with the lender's legal representatives in August 2009. ASIC has this year continued to assess the financial position of the Companies and the Directors, as well as the progress of the Melaleuca Estate property development and its litigation against Port Stephens Council, with a view to determining whether there is any prospect that the Enforceable Undertaking can be complied with.

*Q: On the basis of the enforceable undertaking with Brien Cornwell and the fact that no monies have been returned to investors, does ASIC feel that there needs to be a review of enforceable undertakings as a mechanism to deal with such matters?*

The outcome in relation to a single EU is not an appropriate basis to draw conclusions about whether a review is required.

*Q: Finally, in relation to this, if enforceable undertakings are in effect unenforceable, as in this case, will the Cornwell case and other cases prompt ASIC to look at a review of mechanisms to protect investors in such cases?*

As stated above the Cornwell case is not a sound basis to conclude either that:

- Enforceable undertakings are unenforceable; or
- The mechanism needs review.

*Q: As far as investors go, some of them understood that an enforceable undertaking, if not a guarantee, gave them some security in a broad sense that they would be paid. But is it fair to say that an enforceable undertaking is not a guarantee of any sort?*

It is correct that an EU is not a guarantee.

*Q: Can you provide any documents or supporting documentation in terms of a paper trail of the enforceable undertakings and dates and times when things were followed up and the like?*

This is an operational matter and we are not in a position to provide documents.

**Senate Standing Committee on Economics**

**ANSWERS TO QUESTIONS ON NOTICE**

**Treasury Portfolio**

Budget Estimates

1 June – 3 June 2010

*Q: Insofar as those documents reflect what level of compliance was there with respect to the enforceable undertaking.*

See answers given earlier.

*Q: And what follow-up there was by ASIC to follow up Mr Cornwell and his activities, thank you.*

The history of the matter, and ASIC's follow up on the Companies' non-compliance with the Enforceable Undertaking has been set out above.

More recently, on 12 July 2010 ASIC filed in the Supreme Court an application pursuant to s.93AA of the *Australian Securities and Investments Commission Act 2001 (ASIC Act)* seeking:

- A declaration that the Companies are in breach of the Enforceable Undertaking;
- An order that the Companies comply with the Enforceable Undertaking and repay investors;
- Such further orders as the Court thinks appropriate.

Empower Invest has indicated that it will submit to any order made by the Court in relation to its failure to repay investors in accordance with the Enforceable Undertaking.

ASIC's process was before the Supreme Court on 16 August 2010, when it was ordered that Newcastle Palais put on any affidavit evidence upon which it wishes to rely by 26 August, and that the process be heard on 30 August 2010.

ENDS