REPORT OF THE

SELECT COMMITTEE

INTO THE

FINANCE BROKING INDUSTRY IN WESTERN AUSTRALIA

Presented by Hon Ken Travers MLC, Chairman

Report

SELECT COMMITTEE INTO THE FINANCE BROKING INDUSTRY IN WESTERN AUSTRALIA

Date first appointed:
June 21 2000

Terms of Reference:
(1) A select committee of three members shall be appointed.[1]

(2) The committee be appointed to inquire into and report on reasons for losses associated with the finance broking industry in Western Australia, including but not limited to:
  (a) the statutory responsibilities relating to the finance broking industry;
  (b) avenues for legal redress for investors;
  (c) consideration of the adequacy of existing legislation to prevent a recurrence of the events which led to the loss by investors who relied on finance brokers.

(3) The committee in its proceedings avoid interfering with or obstructing any enquiry being conducted into related matters and in particular inquiries by —
  (a) the police;
  (b) any liquidator or supervisor of any company;
  (c) the Gunning Inquiry;
  (d) ASIC; or
  (e) any prosecution.

(4) Proceedings of the Committee during the hearing of evidence are subject to SO's 322, 323, 324, 330 and 331 but subject always to the right of any member of the Committee to exclude strangers under SO 358.

(5) The Committee have power to send for persons, papers and records and to move from place to place.

(6) The committee report to the House not later than 31 October 2000[2], and if the House do then stand adjourned the committee do deliver its report to the President who shall cause the same to be printed by authority of this order.

[1] Changed to 5 members when the new Committee was established on August 17 2000.
[2] The House granted the Committee an extension of time to report to December 7 2000.

Members:
Hon Ken Travers MLC
Hon Graham Giffard MLC
Hon Ray Halligan MLC
Hon Norm Kelly MLC appointed August 17 2000
Hon Greg Smith MLC appointed August 17 2000

Staff:
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CHAPTER 1
INTRODUCTION

THE FINANCE BROKING INDUSTRY

Background

1.1 In November 1998, problems in the finance broking industry in Western Australia were raised in the Legislative Assembly. At that time, it was claimed that people had lost money as a result of investing in private mortgage schemes. The Legislative Assembly was informed that several finance broking firms could be named, but to keep the matter simple, only the example of Global Finance Group Pty Ltd **("Global")** would be raised. The Legislative Assembly was told that approximately 60 people had been identified as having sustained losses through investing with Global. It was also advised that retirees had been invited to invest in development schemes and within months of investing, the monthly interest payments that they had been promised had stopped, and the securities that they had been given, turned out to be almost valueless.[1] Fifteen months later, the Gunning Committee of Inquiry into the operations of the Boards and Committee in the Fair Trading portfolio **("Gunning Inquiry")** was established. The Gunning Inquiry was required to review and report on the effectiveness and efficiency of the eight Boards, including the Finance Brokers Supervisory Board **("Board")**, and the Building Disputes Committee.

1.2 On a motion moved by Hon Ken Travers MLC on April 5 2000, the Legislative Council determined on June 21 2000 that a select committee be established, the Select Committee into the Finance Broking Industry in Western Australia **("previous Committee")**. During the debate, Hon Ken Travers indicated that he believed that the terms of reference of the Gunning Inquiry were too narrow and that a more wide-ranging inquiry was required. This Committee did not report to Parliament before prorogation. A new select committee, the Select Committee into the Finance Broking Industry in Western Australia **("Committee")** was established on August 17 2000 using the same terms of reference as the previous Committee.[2] All material obtained by that select committee was available to the new select committee.

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1 Parliamentary Debates (Legislative Council) (Hansard) Thirty-Fifth Parliament Second Session 1998, November 12 1998, p. 3397.

2 The previous Committee comprised three members. This Committee comprised five members, three of whom form a quorum.

1.3 On October 18 2000, the House granted an extension of time to report to November 30 2000. On November 23 2000, the House granted a second extension until December 7 2000.

1.4 At the time that the Committee was appointed, it was apparent that a large number of investors had sustained losses amounting to millions of dollars. Many self-funded retirees had lost money, much of which was unlikely to be recovered. Several finance brokers had already been charged with fraud or stealing-related offences. Two of those charged had been industry members of the Board at varying times. Since then, several more people have been charged and police investigations are continuing.

1.5 The Committee heard evidence from 53 witnesses. A list of the witnesses is attached as Appendix 1, and a list of written submissions is attached as Appendix 2. Hearings were mainly in public but some were held in private in line with the Committee's terms of reference or through the invoking of Standing Order 358.[3]

1.6 On September 1 2000, the Gunning Inquiry presented its report (**"Gunning Report"**) on the effectiveness and efficiency of the Board. The Gunning Inquiry confirmed the existence of serious problems in the finance broking industry and its regulation by the Board. The Gunning Report stated that its investigations and police investigations, suggested that a significant number of finance brokers, together with property developers and land valuers, brought about losses to investors through "*deficient, if not unscrupulous*"[4] business practices, and that the regulatory system failed to identify the problems in the industry until it was too late to prevent the losses.[5]

1.7 The Committee's time frame was extremely tight and this created additional pressures. The Committee wishes to express its sincere appreciation to all the Legislative Council Committee Staff who assisted it, and in particular Ms Lyn Zinenko, Ms Jan Paniperis and Ms Anne Turner.

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3 Standing Order 358 states: *"When a committee is examining witnesses, strangers may be admitted, but shall be excluded at the request of any Member, or at the discretion of the Chairman of the committee and shall always be excluded when the committee is deliberating."*

4 Report of the Gunning Report Committee of Inquiry into the Finance Brokers Supervisory Board (September 1 2000) **("Gunning Report")**, p. vii.

5 Gunning Report, p. vii.

THE INDUSTRY

Finance Brokers

1.8 Finance brokers have been part of the Australian financial landscape for well over a century. There are a number of categories of business operating in the industry, including:

- traditional mortgage brokers;
- equipment finance brokers;
- commercial finance brokers;
- mortgage originators;
- mortgage managers; and
- financial managers.[6]

1.9 The *Finance Brokers Control Act 1975* **("Act")** defines "finance broker" as "*…a person who, as an agent, in the course of business negotiates or arranges loans of money for or on behalf of other persons* [excluding listed exceptions]."[7] In recent years, the private mortgage market, which moves away from traditional lending sources such as banks, has grown extensively, not only catering for private mortgages where there is one investor and one borrower, but also for pooled mortgages where there is one borrower and many lenders. In recognising the expansion of the pooled mortgage market, in its consumer booklet issued in April 1999, the Ministry of Fair Trading in Western Australia **("Ministry")** described a finance broker as "*…a business which endeavours to bring together people who have sums of money to lend (lenders) and those who require funds for private and business purposes including the purchase and development of property (borrowers).*"[8]

1.10 The private mortgage loan usually involves a loan based on a first mortgage over real estate as security, with the loan typically limited to 70% of the property's value. Private mortgage loans are typically interest only, with the borrower paying interest each month, and repaying the entire principal at the end of the term. Often, when the loan becomes due, the lender will not collect the principal, but will allow it to "roll

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6 For a comprehensive description of these categories, see Gunning Report, Appendix F.

7 *Finance Brokers Control Act 1975*, s.4.

8 Ministry of Fair Trading, *Finance Broking and Mortgage Investments – A guide for Private Investors*, (Perth) April 1999, <http://www.fairtrading.wa.gov.au/publications/consumer_notes/guide_investors.html>

over", that is, to be reinvested into a new loan. Private mortgages can be pooled mortgages where a finance broker pools together money belonging to several lenders and lends it to a particular borrower for a specific project. Finance brokers, often called mortgage brokers, arrange these private mortgages. The problems in the finance broking industry which were examined by this Committee arose mainly out of the pooled mortgage area of the market.

Investors

1.11 Changes to legislation in Australia over the last few decades have resulted in many people now taking personal responsibility for their financial independence upon retirement and being less reliant on the social security system. Consequently, they are more proactive in making decisions about how to best manage their retirement funds.

Legislative Initiatives

1.12 These social and economic changes have highlighted inadequacies in the control of finance brokers, and have resulted in massive financial losses. Before 1998, the law of contract, and principal and agent, applied generally, and there were limited controls over some activities of finance brokers in related legislation in some states. However, no Australian State had specific legislation in place to deal with finance brokers until 1969 when Victoria introduced the *Finance Brokers Act 1969* (Vic). This legislation came about because of misappropriation of clients' funds by finance brokers in the Eastern States, and before long, similar problems began to surface in Western Australia.

1.13 In early 1974, the Law Reform Commission of Western Australia **("Commission")** was asked to consider and report on the question of whether legislation should be enacted to control the activities of mortgage brokers. At that time, Victoria was the only Australian State where legislation directly controlled finance brokers. In its report, the Commission defined a mortgage broker as "*…a person who in the course of business as an agent negotiates or arranges loans of money for or on behalf of another for reward…*"[9] and indicated that this definition, for the purposes of the report, included finance brokers. The Commission found that mortgage brokers, and by extension, finance brokers, should be subject to statutory control.[10] The Commission recommended that mortgage brokers should:

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9 Law Reform Commission of Western Australia, *Report on Mortgage Brokers* **("LRCWA Report")**, September 20 1974, p. 3.

10 LRCWA Report, p. 14.

- be licensed, the only requirement being one of fitness;
- keep trust accounts which should be subject to audits;
- be required to contribute to a fidelity fund or take out a bond; and
- that there should be exemptions from compliance with proposed legislation for those classes of people who were adequately covered by other legislation, for example, banks and insurance companies.[11]

1.14 In 1998, the Australian and Securities Investment Commission (**"ASIC"**)[12] assumed responsibility for pooled mortgages. This occurred as a result of mortgage businesses developing new business practices throughout the 1990s. ASIC formed the view that pooling had become more common and hence required protection. Since December 17 1999, all pooled mortgage schemes fall within the ambit of the Corporations Law (**"CL"**) and ASIC.[13] Assuming responsibility for pooled mortgages has produced some confusion because although ASIC analyses the nature of the services provided and scrutinises the operator's involvement with the commercial decisions, schemes with less than twenty investors are not captured. Clearly there is a gap which has the potential to be exploited.

REGULATION IN WESTERN AUSTRALIA BEFORE JULY 1 1998

State Regulation

1.15 In April 1975, the *Finance Brokers Control Bill 1975* was introduced into the Western Australian Parliament to provide for the regulation of finance brokers. In the second reading speech, the Minister for Works stated that "[t]*he need for legislation is emphasised by the conviction recently of a mortgage broker. He had misappropriated more than $170,000 in a number of dishonest dealings, leaving nine of his clients with little chance of getting their money back. This Bill is designed to remedy this sort of situation*."[14] The Act received assent on November 20 1975 but did not commence until one year later on November 1 1976 and is still in force today.

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11 LRCWA Report, pp. 14-15.

12 The Australian Securities and Investments Commission (ASIC) is a body established by the *Australian Securities and Investments Commission Act 1989* (Cwth) to regulate companies and the securities and futures industry in Australia. It replaces the previous Australian Securities Commission (ASC), however its operations are similar. ASIC has investigative, hearing and advisory powers.

13 Gunning Report, p. 226.

14 Parliamentary Debates (Legislative Assembly) (Hansard) Twenty-Eighth Parliament, Second Session, November 4 1975, p. 4037.

1.16 The Act made provision for the licensing, regulation and supervision of finance brokers. For the purposes of administering the Act, the Board was established. The Board comprises five members, one a legal practitioner, one a person experienced in commercial practice, two elected industry members and a chairman. The Board was, among other things, empowered to order investigations, grant licences and discipline errant brokers. Prior to 1980, the Board had decided that brokers must take out a $50,000 bond even though the Commission had recommended that "[i]*f practicable, mortgage brokers should be required to contribute to a fidelity guarantee fund either alone or in conjunction with land agents. If neither of these alternatives is practicable, some other system should be introduced, such as requiring mortgage brokers to take out a bond with an approved surety.*" [15]

1.17 The Act has only ever been amended with minor changes, the most substantial amendments being the 1996 amendment which replaced annual certificates with business certificates for a prescribed period[16] and the 1999 amendment which defined terms already existing under s.5 of the Act.[17]

Commonwealth Regulation

1.18 As well as the State Act, the *Corporations Act 1989* (Cwth), a part of the CL, regulated prescribed interests, which can be described as various schemes, common enterprises or investment contracts.[18] In the early 1990s there was some confusion about what actually comprised "prescribed interest schemes". The Australian Securities Commission, as it was then, took the view that mortgage businesses were probably not prescribed interests unless they involved the pooling of client funds. This meant that far fewer schemes were caught by the CL. However during the 1990s the industry changed with mortgage operators developing new business practices and pooling becoming more common. Mr Jamie Ogilvie, Regional Commissioner, ASIC said:

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15 LRCWA Report, p. 14. By the time of the second reading speech in November 1975, the Government had opted for a bond on the basis that it would take time for a fidelity fund to build up to a satisfactory level.

16 *Business Licensing Amendment Act 1995*, Part 5.

17 *Acts Amendment and Repeal (Finance Sector Reform) Act 1999*, s.79.

18 The area of prescribed interests has been repealed and this type of interest is now being regulated by the new *Managed Investments Act 1998* (Cwth).

> *"With regard to recent events, we were aware of activities in the finance broking industry throughout the 1990s although I should caveat that remark by saying that we were not aware of the extent of pooled mortgage activity in the finance broking industry until we commenced that investigation into Global Finance."*[19]

1.19 ASIC had issued class-order exemptions in most states relieving private mortgage businesses from having to comply with the prescribed interest provisions of the CL as these businesses were often subject to regulation by respective State law societies or others. No exemptions were granted in Western Australia as the Western Australian Law Society had advised the Western Australian Regional Office of ASIC **("WARO")** that its members did not engage in pooled mortgage schemes. In 1992, WARO was also informed by the Board, the Department of Consumer Affairs[20] and the Institute of Finance Brokers that very few brokers advertised regularly for private lenders, managed the collection and payment of interest through their trust accounts or held clients' funds. Those bodies also indicated that there were no problem indicators in the industry that justified further action. ASIC believed that the Act covered the mortgage business of finance brokers[21] and consequently the Australian Security Commission's and ASIC's involvement in mortgage schemes in Western Australia was minimal. ASIC indicated that they had contacted the Ministry, the Board, the industry and various other people and bodies who had replied that there were no problem indicators in the industry. Mr Joe Hockey, Federal Minister for Financial Services and Regulation, in a letter dated March 20 2000 to the Attorney General, reminded the Attorney General that the Attorney General had responded to ASIC's inquiry on October 27 1998 about the new approach and the Attorney General had replied:

> *"I do not believe that mortgage investment schemes are an issue for solicitors and finance brokers in WA and accordingly, I have no comment to make."*[22]

1.20 However, in 1997, ASIC commissioned an inquiry into the national mortgage investment industry because of problems in other States. The Ministry advised

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19 Transcript of Mr Jamie Ogilvie's evidence given to the Committee on July 3 2000, p. 2.

20 The Department of Consumer Affairs was the forerunner to the Ministry.

21 *The Australian Securities and Investments Commission's Submission to the Gunning Report Inquiry*, May 19 2000 (**"ASIC Submission"**), pp. 3-4.

22 This reply is contained in a letter to the Hon Peter Foss, QC MLC, Attorney General and Minister for Justice, dated March 20 2000 from Hon Joe Hockey MP, Minister for Financial Services and Regulation, Ministry File 13182, Vol. 1.

WARO of an impending review of the management of the finance brokers industry and the Act and asked for advice about its role in the regulation of finance brokers. The ASIC Submission indicated that the Ministry also referred to an identified class of private lenders who required a greater level of protection.[23]

The Current Position in Western Australia

1.21 In response to the nationwide problems in the industry, the Commonwealth Government clarified its regulation under the new *Managed Investments Act 1998* (Cwth) which amended the CL to include the regulation of some managed investments. Generally, managed investments are caught by the CL, however there are two classes of exemption:

- mortgage services for 20 or less investors, that is where a mortgage practice operator is providing mortgages to no more than twenty investors,[24] and
- small-industry supervised schemes.

Small-industry supervised schemes apply to the operation of a mortgage business where the total principal of loans does not exceed $7.5 million. These schemes are supervised by an ASIC-approved industry supervisory body. There are certain constraints on these schemes, and among other things, they are not applicable to development loans, or where interests of the scheme are offered interstate, except in State border areas. The schemes are also not applicable to loans where the sum to be secured by mortgage is more than 80% of the unencumbered value of the mortgaged property.

1.22 The Act remains in force, and control of finance brokers is with the Board. Currently, the Ministry's licensing database shows there are 454 individual finance brokers' licences and 134 finance brokers' business certificates.[25] To practise as a finance broker, the person or body must hold a licence. To run a finance broking business, both a licence and a business certificate is required. The application fee for a licence is $324, and there is a holding fee of $150 payable every three years. Holders of business certificates are not required to pay a holding fee. No fee is payable to obtain a business certificate in the first instance, but a renewal fee of $324 is payable every three years. The majority of finance brokers' licence applications impose a condition

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23 ASIC Submission, pp. 6-7.

24 Where investors are represented by a nominee company, each investor is counted as a members of the scheme, not the whole nominee company. See ASIC Submission, p. 21.

25 Ministry facsimile to the Committee, November 22 2000. However, the Western Australian *Government Gazette*, "List of Persons Holding a Finance Brokers Licence and Business Certificate" shows 166 registered under the Act as at December 1 1999.

to successfully complete *Finance Broking Practice 1 and 2* of a Technical and Further Education **("TAFE")** certificated course in finance broking.

1.23 In June 1989, the Board resolved that from January 1 1990, an applicant for a finance broking licence had to pass the TAFE course subject to exemptions. Only in 'exceptional circumstances' would the Board grant a licence subject to the completion of just two of the modules known as Finance Broking Practice 1 and 2.[26] Clearly the Board intended that finance brokers should possess an appropriate academic qualification. However, Board Minutes up to January 1999, when the TAFE course was overhauled, show that the majority of finance brokers' licence applications were subject to the mere completion of those two modules, not the entire course. What was intended to be a licence condition in "exceptional circumstances" appears to have become the norm.

1.24 In January 1999, the Board accepted a new qualification, *Certificate IV of Finance Broking,* as the prescribed licensing education criterion.[27] Despite this, the Board has continued to approve licences for applicants on the condition that the applicant successfully completes only the two modules *Finance Broking Practice 1 and 2* amounting to 70 hours of tuition.[28] It would appear that these applicants were required to demonstrate some industry experience but the Committee was unable to identify any clear criteria upon which these exemptions were granted.

1.25 According to the course description, Finance Broking 1 enables the participant to "*…describe the code of conduct and the legislative requirements of the industry.*" Finance Broking 2, enables the participant to "*…describe the ethics of the industry*"[29] amongst other things.

1.26 The Committee has been unable to ascertain the specific content of *Finance Broking Practice 1 and 2* before January 1999 when the TAFE course was overhauled. The new *Certificate IV of Finance Broking* course teaches trust accounting concepts, however, to date, undertaking it has not been a mandatory requirement of the licence.

1.27 In Western Australia, there are presently five ASIC licenses issued to finance brokers. These brokers are licensed by the Board as well as ASIC and dual fees are payable.

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26 Minutes of the Board, dated June 21 1989.

27 Minutes of the Board, dated January 13 1999.

28 TAFE *Course Information, Certificate IV in Finance Broking,* p. 2.

29 The module which teaches accounting concepts, trust accounting and the auditing process, trust account journals and ledgers is not mentioned in Board minutes as a condition of an applicant's licence after January 1999.

There are no small-industry supervised schemes as ASIC has not received any applications for bodies interested in supervising schemes. As a transitionary measure, ASIC has permitted mortgage business operations that are caught as managed investment schemes to either comply with CL to continue operating, or alternatively "run their business down" by October 31 2001. ASIC is allowing this to be done on a no action basis, provided that an audit certificate was lodged before June 30 2000 with ASIC. There appears to be no supervision of these brokers by the Board or ASIC.

CHAPTER 2
EXPERIENCES OF THE INVESTORS

2.1 The Committee heard evidence from eighteen investors, and received 36 written investor submissions. The majority of investors who suffered losses are retirees, some elderly and frail. The level of knowledge of investors ranged from some who were financially unsophisticated to others, including a retired bank manager, who had industry knowledge and experience. The Committee heard testimony of betrayals of trust and the sad and, in some cases, tragic ramifications of the losses including the ill health and deaths of some investors and the loss of the financial independence that had been planned for retirement. One investor, who is 85, with a disability and cared for by her daughter, told the Committee that she was left money by her late husband to ensure that neither she nor her daughter would ever be in need. Her husband went through the depression, and worked hard during his entire life to provide for his family, and now they were dependent on social security to survive. Many investors' submissions and oral evidence reflected an ideological position about self funded retirement and not being a burden on the public purse.

2.2 Many investors were in difficult situations where they could not claim social security because their investments, even though they were worthless, were deemed to be income-earning assets. Investors told the Committee that this further complication created bitterness among retirees who felt aggrieved that they had worked and paid taxes their entire lives only to be treated like second class citizens in their time of need. One investor, Mrs Dorothy Burns, said that $150,000 lent to Mr and Mrs Johnson, borrowers, had provided no dividends since 1997, and there is no prospect of recovery of the principal amount as Mr and Mrs Johnson are in bankruptcy. The investment, a shop at Westminster, has not sold. The estate agent told Mrs Burns that it might take years to sell the shop, and even then it would have to be sold at a very low price. However, Mrs Burns told the Committee that even though the investment was "*a thing around our necks*", Centrelink was classing it as an asset.[30] Similarly, Mr Carl Lens, investor, in a letter sent to the Office of the Minister for Seniors referred to his "lost capital" being deemed by Centrelink to be earning interest.[31] For other investors, their frozen retirement income meant they had to return to work. Mr Bob Arnold, President, Association of Independent Retirees Inc, in a letter to the

30 Transcript of Mr Carl Lens' and Mrs Dorothy Burns' evidence given to the Committee on August 1 2000, p. 8.

31 Mr Carl Lens, "Letter to each member of the Liberal Party, c/- the Minister for Seniors" dated May 3 2000, Ministry File 13182, Vol. 5.

Minister of Fair Trading, advised that many self-funded retirees had been "*…gutted both financially and mentally*".[32]

2.3 Some investors told the Committee that they appreciated that a higher interest rate meant a higher risk. Further, a number of investors had been informed by accountants, lawyers or financial planners that first mortgages were safe. Investors have commented that they are of a generation which believed that first mortgage investments were secure. Investors believed that if the borrower defaulted, the property would be their security, as they were never providing more than 70% of the money required. This turned out to be false, as the property had often been overvalued, and the borrowed amount was over 100% of its value. Miss Kerry Webb, investor, told the Committee that:

> *"We felt that if a borrower defaulted, then we may not get our interest but we would certainly recover our capital. You have to pay a price. If anything went wrong and we missed out on a few months interest, that is not nearly as important as if we lost our capital. If you lose the capital, it cannot be replaced. I have no hope of being able to replace this capital. Once that is gone, you do not have the ability to earn income anyway."*[33]

This was echoed by other investors.

2.4 Ms Linda Key, a former legal practitioner member of the Board, told the Committee that trust is an essential part of the finance broker's business.[34] The Committee heard from several investors that they had confidence in their brokers. Mr Peter McEvoy, retiree, said that he had no reason to doubt that Blackburne & Dixon (for example) "*…were not fully accredited, honourable finance brokers of the highest integrity.*"[35] Mrs Myrtle Webb, investor, told the Committee that when she queried Mr John Margaria, Director, Global, about late interest, he would say, "[d]*on't worry, Mrs Webb. If anything goes wrong, I will pay you back from my own personal pocket.*"[36] Investors told the Committee that brokers would come to their homes and cultivate their confidence and they had every reason to trust their brokers as the first few deals had progressed satisfactorily. Investors, in a letter to the Minister for Fair Trading, Hon Doug Shave MLA **("Minister")**, commented on how they admitted to

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32 Letter to the Minister from Mr Bob Arnold, dated May 30 2000, Ministry File 13182, Vol. 6.

33 Transcript of Miss Kerry Webb's evidence given to the Committee on August 2 2000, p. 11.

34 Transcript of Ms Linda Key's evidence given to the Committee on July 28 2000, p. 12.

35 Transcript of Mr Peter McEvoy's evidence given to the Committee on September 6 2000, p. 6.

36 Transcript of Mrs Myrtle Webb's evidence given to the Committee on August 2 2000, p. 22.

Blackburne & Dixon that they had to place their trust in the finance broker as the borrowers were unknown to them.[37]

2.5 Some investors told the Committee that they also placed their confidence in the industry because it was supervised by the government. Investors said they believed that it was safe to invest in a project involving supervision by two boards, that is the Finance Brokers Supervisory Board and the Land Valuers Licensing Board, both of which came under the auspices of the Ministry. However, things did go wrong and investors told the Committee that they believe that the government agencies did not exercise due care in issuing valuers' licences and supervising finance brokers.[38] Miss Kerry Webb, investor, told the Committee that her financial planner, accountant and solicitor advised that the investment would be safe because finance brokers were licensed and regulated, and that they were subject to disciplinary action taken by the Board and Ministry.[39] Investors said that their own trust of brokers was reinforced by government supervision and felt that the Ministry was there to protect the unskilled investor from being "conned". Investors felt that they had constantly been told by government agencies that they were naïve and did not "check out" the finance brokers. Miss Kerry Webb said "[t]*he brokers were supposed to be licensed. The valuers were licensed. I do not know what more I can say…".*[40]

2.6 The Committee heard that faith in the power of the supervisory and regulatory system evaporated very quickly when investors looked to the Board and the Ministry to take action when problems began to surface. One investor stated that the Board refused to listen to her complaints and sent her to the Ministry. Investors told the Committee that there appeared to be a lack of proactivity on the part of both the Ministry and the Board, and confusion over roles.

2.7 Investors told the Committee that their misery is being compounded by the actions or inaction of the supervisors. Investors said they believe that they are being pitted against each other as registered and unregistered mortgagees. Investors also said that they believe that much time and money is being wasted by the liquidators and supervisors, and the continuous litigation is vexatious, or alternatively is litigation to avoid settlement of the claims.

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37 Letter to Minister, dated March 14 2000, Ministry File 13182, Vol. 3.

38 Transcript of Mr John Durbin's evidence given to the Committee on August 2 2000, p. 2.

39 Transcript of Miss Kerry Webb's evidence given to the Committee on August 2 2000, pp. 17-18.

40 Transcript of Miss Kerry Webb's evidence given to the Committee on July 28 2000, p. 9.

2.8 Many investors spoke highly of the assistance offered by Ms Denise Brailey, President of Real Estate Consumers Association **("RECA")** and were grateful for her efforts after their negative experiences with the Board and the Ministry.

CHAPTER 3
PRECONDITIONS FOR INVESTOR LOSSES

INITIAL LOSSES

3.1 The evidence given to the Committee concentrated around the reasons for the losses, and was focussed on statutory responsibilities, adequacy of relevant legislation and legal redress for investors. As the evidence progressed, a series of recurring themes emerged. Evidence revealed that there were abuses of trust, dishonesty, lack of professionalism, incompetence and inertia and that these themes appeared in both the miscreants and regulators. What emerged from the evidence was a poor ethos within the industry which allowed many retirees to lose their livelihoods and independence, which together with the social and economic changes, brought about fertile conditions in which unscrupulous brokers and others could operate.

Class of Investors

3.2 In a letter to ASIC in October 1997, the Ministry sought advice about its role in the regulations of finance brokers. In this letter the Ministry identified an emerging class of lenders, described as superannuants and other private lenders who invest their life savings, but have little knowledge of the financial market, and who, the Ministry suggested required a greater level of protection.[41] Evidence to the Committee indicated that term deposit interest rates had fallen considerably, and many retirees were finding it difficult to make ends meet on the interest that was being paid by banks.[42] These people were looking for better interest rates and were attracted to what they considered to be safe investments, that is "*…first mortgages on bricks and mortar*".[43]

3.3 Evidence to the Committee shows that these investors, mainly retirees, were targeted. Mr Ian Parker, Chairman, Global Investors Coordinating Committee, in a letter to *The West Australian* referred to this practice as "*…financial stalking of the elderly and vulnerable*".[44] Mr Ben van Stokkum, investor, told the Committee that he responded

41 ASIC Submission, p. 7.

42 4-4.5% was indicated by Miss Kerry Webb in her transcript of evidence given to the Committee on July 28 2000, p. 8.

43 For example, Mrs Margaret [Frances] Maber's transcript of evidence given to the Committee on September 9 2000, p. 8, and also Mrs Dorothy Burns' transcript of evidence given to the Committee on August 1 2000, p. 23.

44 *The West Australian*, February 14 2000, Ministry File 13182, Vol. 3.

to an advertisement in the *Sunday Times* in 1997 stating that it was advisable for retired people who were receiving very low interest from a bank to invest in real estate as the money invested would be loaned only to a maximum of 70% of the valuations and was "*as safe as houses*".[45] Ms Penny Searle, investor, told the Committee that she was aware of Global advertising "*…in "Have a Go" which is a publication of the elderly. In the left-hand top of the page I think they advertised in there very regularly. I do not subscribe to it, despite my age. I do remember seeing it on many occasions, but they used to regularly appear Wednesdays and Fridays in The West."*[46] The Committee was told by investors that they trusted their brokers who gave every appearance of acting in the investors' best interest and that investors also felt that there was added protection in that finance brokers were required to be licensed under the Act.

Supervision under the Act

3.4 The Committee heard evidence which indicated that in contrast to the amount of money handled by brokers, the industry was inexpensive to enter as a trader, the only financial outlay being the premium for a bond for $50,000 and the minimal fees outlined in paragraph 1.22 above. Many investors told the Committee that they thought that because brokers were licensed, they were being regulated and supervised. Mr John Durbin, investor, told the Committee that if the finance broker was licensed, he believed that he must be "kosher".[47] Miss Kerry Webb, investor, in her submission said she was "*…encouraged to believe in the safety of our investments because brokers and valuers were licensed and supervised by government regulatory authorities".*[48] Mr Graeme Grubb finance broker's character statement, given to new lenders, referred to Mr Grubb being "*…a licensed Finance Broker under the Finance Broker's Control Act."*[49]

3.5 In addition to this, there appeared to be a lack of appropriate action being taken against licensed finance brokers who breached the Act or the Code of Conduct under the Act **("Code")**. Ms Penny Searle, investor and company director, told the Committee that finance brokers were well aware of the small penalty for breaches outlined in the Act, and believed that they were "untouchable".[50] Ms Searle told the

45 Transcript of Mr Ben van Stokkum's evidence to the Committee given on September 6 2000, p. 4.

46 Transcript of Ms Penny Searle's evidence given to the Committee on July 28 2000, p. 26.

47 Transcript of Mr John Durbin's evidence given to the Committee on August 2 2000, p. 26.

48 Submission to the Committee by Miss Kerry Webb dated July 13 2000, p. 1.

49 Letter to the Minister, May 6 2000, Ministry File 13182, Vol. 5.

50 Transcript of Ms Penny Searle's evidence given to the Committee on July 28 2000, p. 11.

Committee that she has had many dealings with the finance broking industry through her business, and that her perception was that finance brokers "*…are laughing and they are saying, 'We're still going to continue because no-one can get us, can they?'*" Ms Searle stated that when she questioned what she perceived to be deceitful behaviour, her understanding of responses from brokers was that that behaviour was standard industry practice.[51]

3.6 This perception is vindicated by the minimal punishment meted out to Mr Grubb, finance broker, who the Board found had breached ss. 48 and 59 of the Act.[52] In considering the matter, the Board considered the financial hardship suffered by Mr Grubb, and "*…severely reprimanded Mr Grubb and reminded him of the responsibilities set out in the Finance Brokers Code of Conduct.*"[53] He was then ordered to pay costs of $690.00. Several instances of breaches of audit requirements appear throughout the minutes with fines sometimes at $200 and others at $300. One broker who traded for three years without a current Annual Certificate, and could not give a legitimate excuse to the Board for doing so, had no action taken against him for this breach of the Act, but was simply required to give an undertaking that he would not do it again.[54] Other instances of problems with finance brokers appeared in the minutes of the Board, and are discussed later in this report.

Increase in Magnitude of Losses

3.7 The Committee heard evidence that towards the latter part of 1998 and early 1999, there was a flurry of activity in the industry. This activity included an increase in the number of loans being brokered, properties being traded amongst borrowers, and in the use of overvaluations to borrow money. The Committee further heard that investors from this period would suffer the worst losses. The Committee was not able to quantify the full extent of this activity.

3.8 Mr Jeffrey Herbert, Supervisor of Global, told the Committee that in relation to Global investors, "[t]*he people who will suffer the worst losses are those who put their money in most recently where there has been a maximum amount of dilution of funds through the mixing of moneys between project accounts in borrower groups, where nothing has happened and they may have got some money back in interest.*"[55] Mr

51 Transcript of Ms Penny Searle's evidence given to the Committee on July 28 2000, p. 11.

52 Section 48 deals with trust accounts, and s.59 deals with the contents of the auditor's report.

53 Minutes of the Board dated November 17 1993, p. 1.

54 Minutes of the Board dated March 9 1994, p. 2.

55 Transcript of Mr Jeffrey Herbert's evidence given to the Committee on July 7 2000, p. 12.

Herbert told the Committee that these people might lose 80% of their money, as money put into the trust account was not used for the specified projects, but had gone elsewhere. He said that they may receive a percentage at the sale of the property, but it would be minimal. Mr Herbert told the Committee that these people would be the ones who put their money in just before Global went into liquidation in late 1998 or early 1999.[56]

Other Influences

3.9 Apart from the factors above, the Committee heard evidence which indicated that unscrupulous borrowers, valuers, lawyers, auditors, bankers, and real estate agents, working in concert, contributed to the climate of risk. Ms Linda Key, former legal practitioner member of the Board, said:

> *"There are people who are less than honest and the point I am making here is that it is the structure of the whole thing, the naivety of the lenders, the lack of real regulation of the operations in the industry, the trust relationship that brokers engender in the way they do business. If you are an individual who wants to see a way of making easy money, this is one you can go for."*[57]

[56] Transcript of Mr Jeffrey Herbert's evidence given to the Committee on July 7 2000, p. 12.

[57] Transcript of Ms Linda Key's evidence given to the Committee on July 28 2000, p. 13.

CHAPTER 4
THE FINANCE BROKERS

CONDUCT OF FINANCE BROKERS

4.1 The conduct of some finance brokers, and especially many of those who dealt with pooled mortgages during the 1990s, has been described by ASIC in its submission to the Gunning Inquiry, dated May 19 2000 **("ASIC Submission")**. The ASIC submission stated that during the eighteen months prior to May 2000, ASIC carried out surveillance of several finance brokers in Western Australia and identified a series of objectionable practices by finance brokers including unethical and illegal behaviour, poor business practices and a general lack of professionalism.[58] Evidence to both the Gunning Inquiry and this Committee reinforces the existence of these practices.

Ethical Climate

4.2 The ASIC Submission suggested that a definite unethical and immoral culture existed in the industry. It stated that brokers did not seem to comprehend that conflicts of interest could arise in their dealings, and that a fiduciary duty[59] to lenders could exist. This is supported by evidence from investors who have told the Committee that they have recently discovered that documents of offer contained misleading errors of fact, inaccurate lender to borrower ratios, and that "stooges"[60] were used. Ms Penny Searle, investor, told the Committee she had discovered that a mortgage already existed on land prior to the raising of money for the building, which was what she had

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58 ASIC Submission, p. 12. The ASIC submission indicates that in May 1999, surveillance inspections were carried out on five brokers, and because these inspections revealed some undesirable practices, although not serious enough to warrant immediate action, it was decided to make follow up inspections after the completion of other mortgage broker matters which were taking up significant resources. In December 1999, ASIC undertook an initial mail out to brokers who fell within managed investment schemes, and resulting from the responses or lack of responses, commenced surveillance on 20 brokers in February 2000.

59 According to *Butterworth's Australian Legal Dictionary*, p. 471, a "fiduciary duty" is the duty to act in good faith for the benefit of another. People subject to a fiduciary duty are not permitted to profit from their positions (other than where expressly permitted) or to put themselves in a position where the fiduciary duty and personal interest may conflict.

60 Mr Jeffrey Herbert confirmed that "stooges", or "stand-ins" were investors who were used as bait to indicate that an investment was worthwhile, and who withdrew as soon as others joined. Transcript of Mr Jeffrey Herbert's evidence given to the Committee on July 7 2000, p. 5.

invested in. She told the Committee that the mortgagee had agreed to become a second mortgagee at the broker's request,

> *"…which was hidden from the investors coming in for the building costs, on the promise that he would be replaced with somebody else later down the track, which happened…*[the borrower] *did not pay any interest, and yet the second mortgagee got paid interest out of the first mortgagee's funds."*[61]

4.3 Ms Searle said that she had always believed that brokers must obtain approval for additional mortgages, however investors often did not become aware of other mortgages because they were all registered at the same time.[62] Mr Lens, investor, told the Committee that he eventually discovered that he did not have a first mortgage, but in fact a second mortgage, and that the first mortgagee was the finance broker.[63] One investor told the Committee that he had not been told that a borrower was also the guarantor for other companies.[64] Other investors told the Committee that their interests did not appear on the titles that they had agreed to, but on totally different titles. Ms Searle also told the Committee that she had discovered that finance brokers were keeping higher penalty payments and were therefore making money out of late interest payments.[65]

4.4 The ASIC Submission states that brokers neither disclosed the nature of the relationships between the borrower and the broker, nor the benefits they would receive from borrowers and this was confirmed by evidence given to the Committee. Miss Kerry Webb, investor, told the Committee that she invested in a company where the two directors were the broker and the borrower, and both were guarantors.[66] Mr Carl Lens, investor, told the Committee that he was encouraged to put his money into a project because the broker himself had invested $29,000. Mr Lens said that he felt safe because he trusted the broker and the broker's position.[67]

4.5 Ms Linda Key, a former legal practitioner member of the Board, who had researched corporate and entrepreneurial crime as a post graduate study, told the Committee that

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61 Transcript of Ms Penny Searle's evidence given to the Committee on July 28 2000, p. 22.

62 Transcript of Ms Penny Searle's evidence given to the Committee on July 28 2000, p. 22.

63 Transcript of Mr Carl Lens' evidence given to the Committee on August 1 2000, p. 20.

64 Transcript of Mr John Moulsdale's evidence given to the Committee on August 1 2000, p. 2.

65 Transcript of Ms Penny Searle's evidence given to the Committee on July 28 2000, p. 15.

66 Transcript of Miss Kerry Webb's evidence given to the Committee on July 28 2000, pp. 10-11.

67 Transcript of Mr Carl Lens' evidence given to the Committee on August 1 2000, p. 18.

it is the nature of the finance broker's business to encourage trust to persuade investors to give money for investment. She said that "*…it is a situation where the naïve can be exploited and because of the creation of trust between the lender and the broker, if you put that with a situation where there is no real regulation of the broker, then it is an open invitation to those who wish to earn their income from taking advantage of situations to practise their skills in every profession*".[68]

4.6 Mr Jeffrey Herbert, Liquidator of Global, told the Committee that:

> *"A lot of the investors were relatively unsophisticated, and believed that, while they were receiving interest regularly, and not receiving reports from Global that indicated that there were problems, nothing was going wrong. There are horrendous cases, as we have described, where they received interest over a number of years out of the money they had put forward and not from the borrower at all."*[69]

He went on to say that:

> *"…the documents that were exchanged between the investors and Global provided for some part of the proceeds put forward by the investors being used to pay interest to them, commonly 12 months' interest. It was not an uncommon provision, in a case where a property development was taking place, given that, in the case of developments, no money really flows from the property for some period. …The interest must come from somewhere, so it can be provided, and certainly was often provided in Global's case, that 12 months' interest can come out of the money that these people put in. Most of the investors were probably unaware of that fact, because they had not read the documents properly, but it was happening. In a lot of cases involving Global, investors received interest from their own cash for periods beyond 12 months. One investor made an appeal to the Taxation Review Tribunal recently, to try to get a refund on the tax she paid on what she argued was essentially her principal, and not income at all. That is in process at the moment, and is a very difficult argument to run properly."*[70]

Mr Herbert said that Global also claimed a commission on the payment of that interest back to the investor.

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68 Transcript of Ms Linda Key's evidence given to the Committee on July 28 2000, p. 13.

69 Transcript of Mr Jeffrey Herbert's evidence given to the Committee on September 28 2000, p. 20.

4.7 Investors told the Committee that in retrospect they have discovered that brokers simply lied. False representations were made about borrowers' assets, and in one case the asset base of a borrower was used repeatedly to borrow money,[71] representations were made that properties had been finished and listed for sale, when in reality the properties were mere shells[72] Mrs Dorothy Burns, investor, told the Committee that she had expected that her broker would make inquiries about the people he was lending money to, however she has since learned that if someone brought a proposal, it was taken at face value, no checking was done. She said, "[t]*hey did not look into the background because apparently bankrupts and all sorts of people have been borrowing the money from all these retirees*." [73] It appears that this lack of ethics also flowed into the handling of investors' money.

4.8 Some finance brokers were particularly skilful at selling a proposal to investors. Mr Dominic Casella, property developer and borrower, told the Committee that when seeking investors for proposals, the broker *"would have to do a sell job on it."*[74] Mr Casella said that he financed Mr John Margaria to establish Global because Mr Margaria was *"very good at his job"*[75] at Blackburne & Dixon, in arranging loans. Mr Casella said he wanted to go into business with Mr Margaria because he was *"a genius of a person ...he could raise money"*.[76]

Mishandling and Misappropriation of Investors' Money by Finance Brokers

4.9 Evidence given to the Committee outlined much mismanagement and misappropriation of funds. Miss Kerry Webb, investor, told the Committee that there were recurring scenarios that involved, "*…unauthorised use of investor funds held in broker's trust accounts, including taking funds for personal use and advancing funds from one project to another project involving the same borrower. The incomplete registration of all mortgagees on certificates of title is another consistently occurring problem*."[77]

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70 Transcript of Mr Jeffrey Herbert's evidence given to the Committee on September 28 2000, p. 20.

71 Transcript of Mr John Durbin's evidence given to the Committee on August 2 2000, p. 43.

72 Transcript of Miss Kerry Webb's evidence given to the Committee on July 28 2000, p. 14.

73 Transcript of Mrs Dorothy Burns' evidence given to the Committee on August 1 2000, p. 34.

74 Transcript of Mr Dominic Casella's evidence given to the Committee on October 18 2000, p. 4.

75 Transcript of Mr Dominic Casella's evidence given to the Committee on October 18 2000, p. 15.

76 Transcript of Mr Dominic Casella's evidence given to the Committee on October 18 2000, p. 16.

77 Transcript of Miss Kerry Webb's evidence given to the Committee on July 28 2000, p. 4.

4.10 Mr Jeffrey Herbert, Supervisor of Global, described to the Committee what happened within Global, which demonstrates the type of problems experienced by investors. He told the Committee that generally investors put money into a particular project on the expectation that the money would be used to buy a property, subdivide it, have buildings erected on it and sell it, and they would be paid from the proceeds of the sale of the property. Normally loans would be rolled over after 12 months. Mr Herbert said that the finance broker, Mr John Margaria, Director of Global, regularly wrote to investors telling them that the loan had expired, but because of the exemplary nature of the conduct of the borrower, he recommended that it be rolled over. For some years, investors received their interest on the money invested, however when things began to go wrong, investors found that land had been bought, but nothing had been built, that no interest had been paid by the borrower and that the money which they received as interest was in reality their capital on which they were paying tax. Money had been siphoned off within particular borrower groups, between projects, and investors discovered that some of their money had gone into another project belonging to the same borrower.[78]

4.11 The ASIC submission was critical of finance brokers using nominee companies, trustees controlled by the broker, or "stand-ins" to hold mortgage interests. The use of nominee companies and trustees was for administrative convenience, the benefit being that the broker need not alter the registration details on the Department of Land Administration's 'transfer of land' document. However, it is apparent that security for the lender is diminished because the lender does not have a legal interest but an equitable interest[79] and this creates potential problems where there has been a mixing of funds. "Stand-ins" are related parties or business associates who are registered as a co-mortgagees when some but not all of the loan amount required has been raised at the time of settlement. Then, as further lenders are discovered, they take over the stand-in's interest. Again, there are problems with this practice, for example, if the stand-in's interest is not assigned promptly, then the lender only has an equitable interest. If the total sum is advanced to the borrower when not all funds have been raised, it would suggest that other funds in the trust account are being misappropriated. The extent of these practices only came to light when liquidators and supervisors were appointed and clearly jeopardises the return of funds to investors.

4.12 It was difficult for the Committee to ascertain the extent of the practices outlined above, of finance brokers who have not had supervisors appointed.

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78 Transcript of Mr Jeffrey Herbert's evidence given to the Committee on July 7 2000, p. 12.

79 According to *Butterworths Australian Legal Dictionary*, p. 426, an "equitable interest" is an interest in property that can only be enforced by the courts.

4.13 The Committee received serious allegations regarding Mrs Kay Blackburne, finance broker, and secret commissions. Further, during the course of the Committee's hearings, it received evidence which called into question evidence Mrs Blackburne gave to the Gunning Inquiry regarding her knowledge of the relationship between Mr Don Turton, investor, and the Minister.

4.14 The Committee sought to call Mrs Kay Blackburne before it to enable these matters to be examined. The Committee was unable to contact Mrs Blackburne during the time that the Committee was taking evidence and therefore was not able to examine these matters further.

CHAPTER 5
THE FINANCE BROKERS SUPERVISORY BOARD

ESTABLISHMENT OF THE BOARD

5.1 The Board was established to administer the Act[80] and comprises five members appointed by the Governor. The Governor may also appoint a person with similar prescribed qualifications as a deputy to each member and this deputy is entitled to attend Board meetings in the absence of the member for whom he or she is deputy. The term of office is four years and each member is eligible for re-election or re-appointment. The Governor may terminate the appointment of a member for inability, inefficiency or misbehaviour. Further, the Minister, under the *Statutory Corporations (Liability of Directors) Act 1996*, has the power to enforce the duty of individual Board members to act with loyalty and good faith. Meetings can be held at any time, and three members constitute a quorum.

5.2 The Board has wide powers to look into the business organisation of a finance broker. This includes ordering a finance broker to appear before the Board, producing documents, inspecting documents and ordering audits. The Board has the power to reprimand, suspend a licence and fine finance brokers if there has been a breach of the Act or the Code. The Board can also apply to the District Court to have a supervisor appointed to a finance broker in circumstances where the Board has reasonable belief that a finance broker is incapable of conducting business, or is not conducting it in accordance with the Act. While the Act states that it is "[a]*n Act to make provision with respect to the Licensing, Regulations, and Supervision of Finance Brokers,…*"[81] it is clear from its origins that its object was to protect investors by controlling finance brokers.[82]

COMPOSITION OF THE BOARD

5.3 In its 1974 report on finance brokers, the Commission recommended that the supervising authority comprise a legal practitioner with a minium of eight years' practice, an accountant/auditor, a licensed finance broker and one other person.[83]

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80 Division 1 of the Act.

81 Long title of the Act.

82 Parliamentary Debates (Legislative Assembly) (Hansard) Twenty-Eighth Parliament, Second Session, November 4 1975, p. 4037.

83 LRCWA Report, p. 10.

However, this recommendation was not accepted, and s. 7 of the Act sets out the composition of the Board that was decided by Parliament. This comprises a Chairman, a person experienced in commercial practice, a lawyer and two finance brokers.

Industry Members

5.4 Witnesses to the Gunning Inquiry expressed reservations about industry representation on the Board. These included Mr Murray Allen, Parliamentary Commissioner for Administrative Investigations in Western Australia (the Ombudsman).[84] Since 1986, only five industry members have been elected to the Board. These were the late Mr Owen Blackburne, Mr John Bell, Mr Edward Brunton, Mr Herbert Fisher, and Mr Ray Weir. Mr Brunton has been a continuous member between 1986 and 1999, while Mr Weir and Mr Fisher have served more than once at different times,[85] as well as deputy members at other times. Mr Blackburne died in 1994.

5.5 Mr Herbert Fisher was elected to the Board on April 1 1992 until 1995, and again on May 4 1999 until February 2000 when he resigned. On June 8 2000, he was charged by police with fifteen counts of fraud in relation to dealings with the Peppermint Park Holiday Chalets, Busselton. Mr Fisher and his co-accused, Mr Gregory Kennedy, will appear at a preliminary hearing on January 15 2001.

5.6 Mr John Bell was elected to the Board on March 21 1995 and remained until March 1999. On June 21 2000, Mr Bell was charged by police with nine counts of fraud in relation to dealings in the Vasse River Resort, renamed Willows Motor Inn, and is now awaiting trial.

5.7 Mr Ray Weir, who was a deputy member on the Board between 1986 and 1990, and also between 1995 and 1999, was first appointed to the Board in March 1991 and resigned in April 1992 because he had been declared bankrupt. He was again appointed to the Board on May 4 1999 and resigned on November 8 2000. After Mr Weir's bankruptcy was discharged he re-applied for his licence but could not raise the $50,000 bond. He requested that the Bond be reduced to $2,000 and after that was refused, applied to the Board for an exception under s. 5(2).[86] Board Minutes dated

84 Gunning Report, p. 154.

85 Document entitled *Finance Brokers Supervisory Board Members 1988-2000* provided to the Committee by the Board.

86 Section 5 (2) states that the Minister may except any person or class of persons from the meaning of "finance broker". However, the Minister has to be satisfied that apart from the Act, adequate safeguards exist against loss to others by any defalcation of that person. Being granted an exception means the applicant does not need to apply for a finance broker's licence.

April 9 1997 suggest that the Board was suspicious of Mr Weir's application for an exception and did not approve it, noting that "*…in this particular instance, the real reason the application is made is because the applicant is not able to provide a surety bond for $50,000.*" The Board advised the Minister to reject the application for an exception and suggested to Mr Weir he "*…make more strenuous efforts to obtain the surety of $50,000*".

5.8 Mr Weir gave evidence before the Committee on two occasions. At the first hearing, he told the Committee that his relationship with Mr Phillip Lewis, finance broker, convicted of fraud and jailed, was one of landlord and tenant, and before Mr Lewis was granted his finance broker's licence, they would conjunct on proposals. He gave the Committee the impression that his business relationship with Mr Lewis was brief and superficial. However, the Committee subsequently discovered that this did not appear to be the case. This was confirmed at the second hearing. The Committee was not satisfied with his evidence, and remains unconvinced by Mr Weir's responses to questions. In his evidence, Mr Weir was sometimes uncooperative and often vague on critical points of concern to the Committee.

5.9 Mr Owen Blackburne was appointed to the Board on November 18 1986 and retired in 1990. Mr Dominic Casella, borrower, told the Committee, that Mr Owen Blackburne was involved in secret commissions right up until the time of his death.[87] Mr Simon Read, Liquidator of Global, also indicated to the Committee that he recalled that in 1994, in administering a company called Amelia Developments, his "*… investigations indicated very clearly that transactions involving Mr Casella, Mr Owen Blackburne and Amelia Developments were unusual to say the least.*"[88] He explained to the Committee that there were allegations of overstatement of loan applications with the knowledge of Blackburne & Dixon, Mr Blackburne's company. He continued to say that the main sources of concern were instances where Mr Casella borrowed one million dollars through Blackburne & Dixon. He told the Committee that "*Blackburne & Dixon were well aware that the project for which they needed the funding may have required only $800,000 and a further $200,000 was required for a completely unrelated exercise; in this case I believe for the establishment of a lingerie shop by Mr Casella.*"[89] Mr Read told the Committee that he was aware of other occasions involving Mr Blackburne and properties sold to Mr Casella which had been owned by the three parties at times in the past.[90]

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87 Transcript of Mr Dominic Casella's evidence given to the Committee on October 18 2000, p. 2.

88 Transcript of Mr Simon Read's evidence given to the Committee on July 7 2000, p. 18.

89 Transcript of Mr Simon Read's evidence given to the Committee on September 28 2000, p. 24.

90 Transcript of Mr Simon Read's evidence given to the Committee on September 28 2000, p. 24.

Chairman

5.10 Mr Urquhart's narrow interpretation of the Act, particularly as it related to the role of the Board, was contrary to the views expressed by a number of other witnesses. Given Mr Urquhart's training as a lawyer, and his role as chairman, it is understandable that his views predominated at Board meetings.

5.11 It appears that under the chairmanship of Mr Urquhart, the Board failed in its role of protection of investors.

ADMINISTRATION OF THE ACT

5.12 The long title of the Act states that it is "[a]*n Act to make provision with respect to the Licensing, Regulation, and Supervision of Finance Brokers, and for related purposes.*" Although the Act prescribes for the licensing, regulation and supervision of finance brokers, the minutes reflect a pre-occupation with the licensing functions of the Board at the expense of its supervisory and regulatory functions. Mr Ray Weir, Industry member of the Board, in a facsimile to *The West Australian*, asserted that "*…decisions in respect to licensing, and renewals of licences, is the primary function of the Board*".[91] The minutes show that typically meetings focussed on applications for licences and interviewing applicants.[92]

Supervision of Trust Accounts and Audits

5.13 The Act provides for audits and also penalties for breaches. Division 2 of the Act entitled *Trust Accounts* directs that every finance broker must maintain at least one trust account. Money paid into this trust account is not available for the payment of a debt of any other creditor of the finance broker. Section 48(3) stipulates that loan money received by a finance broker in the course of negotiating a loan cannot be withdrawn from his or her trust account except for completing the loan or paying interest. A finance broker can only pay trust account money to the person lawfully entitled to receive it. Also, the Act prescribes that the finance broker must keep full and accurate accounts of all money received and held in trust, keep the accounts in such manner so that they can be audited and correctly balance the accounts at the end of each month.

5.14 The Act requires that a finance broker must have his or her accounts audited annually and that the auditor must deliver the report to the Board within three months. It

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91 Facsimile to *The West Australian*, from Mr Ray Weir, dated June 6 1999, Ministry File 12130, Vol. 5.

92 However, they also reflect that despite what appears to be a rigorous assessment of some applicants, the granting of licences was inconsistent.

prescribes that the auditor's report must contain a statement about whether the trust accounts have been kept regularly and properly written up, whether the trust accounts have been ready for examination at the periods appointed by the auditor, whether the finance broker has complied with the auditor's requirements, and whether in the opinion of the auditor the accounts are in order. If the auditor discovers that the accounts are not in order, involve dishonesty or discovers a deficiency in trust money, the auditor must fully set out the facts in the report. In addition to these provisions, the Board has the power to order an audit of a trust account if it is in the public interest to do so.[93] The Act prescribes a penalty of $300 for breach of any trust account provisions.[94] This penalty has not been altered since the inception of the Act in 1975.

5.15 The minutes indicate that there were areas where the Board ought to have noticed that problems were developing and taken urgent action to ensure that these problem areas were not allowed to flourish, a significant example being trust accounts. The minutes reflect that during 1993, four hearings were conducted for breaches of ss. 50 and 66 of the Act. These sections provide the duty to have trust accounts audited, or to provide a statutory declaration to that effect if no money has been deposited in the trust account for the twelve-month period. However the following year, there were no hearings at all, and the Board merely noted "*with concern*"[95] that there was a list of outstanding audits which were due by December 1993. This pattern of late audits was reflected in the minutes as a continual problem not attended to by the Board.

5.16 In 1995, the Board refused to renew the annual certificates of four finance brokers because their audits were overdue, however this appears to be a "one off" action and the minutes show that the following year audits continued to be overdue, and nothing more appears to have been done to break the pattern. One finance broker, Parcae Pty Ltd, was listed as having an outstanding audit for year ending December 1997 which still had not been received by October 1998. At that point Parcae Pty Ltd was given another 14 days to comply and then if no audit was received commence an inquiry under s. 82(1). Nothing more was done except that the Board noted in its December minutes that Parcae Pty Ltd was now no longer trading.

Global Finance Group Pty Ltd

5.17 Global's trust account and the auditing of it, highlights the Board's ineffectual handling of the requirements of Division 2 of the Act. The Gunning Report indicates

93 Section 68 of the Act.

94 Sections 47-62 of the Act.

95 Minutes of the Board dated May 11 1994, p. 8.

that audit reports from Global auditors, Marsden Partners, showed overdrawn client ledger accounts in December 1995, June 1996 in a special audit, again in December 1996 and December 1997.[96] The minutes of the Board do not reveal any discussion about this pattern.[97]

5.18 By contrast, the first mention in the minutes of any problems with the Global trust account was on February 12 1997. The minutes show that the Board noted the memo from Mr Wyber, Investigator, about the qualified Global audit report for the year ended December 31 1996 which showed not only debit balances in client ledgers but also qualifications relating to treatment of interest on the trust account, and recommended that the matter be investigated. The minutes do not mention any legal opinion or any discussion surrounding it. However, the Gunning Report states that Mr Gavin Wells, a legal officer at the Ministry, had already indicated through an undated legal opinion sought by the Board, that Global was acting illegally.[98] This also was never referred to in the minutes, which suggests that either the minutes were not properly kept, or alternatively that these matters were never discussed. The Committee is concerned about the prospects of either of these alternatives.

Debit Balances in Trust Accounts

5.19 Mr Douglas Solomon, lawyer for some investors, told the Committee that "[a] *trust account in overdraft is a contradiction in terms. That people can talk about a trust account in deficit, that an audit submitted to a statutory board can provide for that, and for that body to continue trading is horrendous.*"[99] He said that two years ago, he first interviewed a group of Global investors involved in an overvalued property who had received no interest for some months. He told the Committee he was alarmed to see overdrawn ledger cards. Mr Solomon pointed out that, as a solicitor, he was required to keep a trust account and he believed that it was a totally unacceptable practice for money to be paid out to the borrower before the total required amount was collected from the lenders. He said further that in the legal profession, trust account breaches have dire consequences. Mr Solomon explained that if his "*...trust account goes into overdraft and my auditor submits a report to the legal practice board, as he should, and I cannot thoroughly explain that by reference to mere inadvertence, and if there is any reason to suppose dishonesty and misappropriation from that trust*

96 Gunning Report, pp. 64-77.

97 During this period, the only mention of Global in the minutes was the notice of the renewal of its business licence, which appears in the Minutes of the Board dated June 12 1996.

98 Gunning Report, p. 67.

99 Transcript of Mr Douglas Solomon's evidence to the Committee on October 5 2000, p. 13.

account, I would expect my licence to practise as a solicitor to be on the line for that one breach. I would expect it to be provisionally liable to be cancelled, or at the most, to get one chance".[100] He also told the Committee that he suspected that this was an endemic practice among some finance brokers.[101]

5.20 Mr Roger Nicholas, auditor of Global and partner of Marsden Partners told the Gunning Inquiry that he had conversations with the Board about debit balances in trust account ledgers. Mr Nicholas said "*…the opinions that were given to us were that providing there was sufficient broker's own money in the accounts that covered the deficiencies, that was acceptable to the board.*"[102]

5.21 Minutes dated June 11 1997 indicate that the Board instrumented a change to the information required in the auditor's report. Individual client balances were no longer required, just the total balance of client accounts.[103] This was brought about because in January 1997, an auditor alerted the Board that the practice of allowing debit balances in trust accounts was illegal. In response, the Board sought a legal opinion from the Ministry as to whether this was so and following receipt of that opinion, the Board determined that in future, individual client balances were no longer required. The Committee has been unable to obtain and examine the Ministry's legal opinion. The decision to alter the audit report from recording individual client balances to the total balance of client accounts occurred during the time when a pattern of gross deficiencies had been identified in the Blackburne & Dixon trust account by its auditors.

Use of Lawyers' Trust Accounts

5.22 The Act provides that every finance broker must keep a trust account and s. 48(1) states that:

> *"Every finance broker shall maintain at least one trust account, designated or evidenced as such, with a bank in the State and shall, as soon as practicable, pay to the credit of that account all moneys received by him for or on behalf of any other person in respect of loans negotiated or arranged by the finance broker or in respect of interest on such loans collected by him".*

100 Transcript of Mr Douglas Solomon's evidence to the Committee on October 5 2000, p. 13.

101 Transcript of Mr Douglas Solomon's evidence to the Committee on October 5 2000, p. 10.

102 Gunning Report, p. 70.

103 Gunning Report, pp. 68, 69.

5.23 Board minutes of August 9 1995 indicate, in relation to a complaint being investigated, that "*Gamel Ward Pty Ltd directs trust account moneys through his solicitor, John Byrne. The Board understands that Gamel Ward Pty Ltd has an operational trust account.*"[104] The Board requested Ministry staff to investigate the existence of a trust account. The Board's minutes of September 13 1995 note that a Ministry officer advised them that a trust account for Gamel Ward Pty Ltd existed and that "[s]*tatements for the period 1.7.94 to 30.6.95 revealed a credit balance ranging from $26,000 to $2,100.*"[105] The Board's minutes do not indicate that any further action was taken on this matter.

5.24 Over eighteen months later, on April 9 1997, the Board interviewed Mr Gamel about the renewal of his business certificate.[106] He told the Board that any funds received would be through a solicitor's trust account as no money goes into the Gamel Ward Pty Ltd's trust account. The Board minutes suggest that it acquiesced with this arrangement which is contrary to s. 48(1). The reason why Mr Gamel used his solicitor's trust account remains unclear.

5.25 A finance broker at Gamel Ward Pty Ltd, Mr John Ward, went on to become a finance broker at First Charter Mortgage Services Pty Ltd **("First Charter")**. Mr Ian Clairs, Lawyer, told the Committee in some instances money from lenders went directly into his trust account and not through the broker's trust account. He said that First Charter had become wary of putting money into its trust account, however he did not know why this was so. He told the Committee that the directors of First Charter perceived that it was important for the lenders' money to go straight into his trust account so that "*it was seen to be properly dealt with*".[107] Mr Clairs told the Committee that he thought that it was a direction of the finance broking industry or ASIC, and that it might "*have something to do with the audit*".[108] Mr Clairs also said that he had a reasonable knowledge of the Act and that his conduct under that Act in allowing the use of his trust account was appropriate.[109]

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104 Page 4.

105 Page 3.

106 Mr Gamel was interviewed because the Board had concerns about his understanding of the concept of "*bona fide* control" of a business. By his own admission, Mr Gamel spent one third of his time overseas.

107 Transcript of Mr Ian Clair's evidence given to the Committee on October 9 2000, p. 3.

108 Transcript of Mr Ian Clair's evidence given to the Committee on October 9 2000, p. 3.

109 Transcript of Mr Ian Clair's evidence given to the Committee on October 9 2000, p. 3.

Random Inspections of Trust Accounts

5.26 In 1995, the deputy registrar discussed a plan for pro-active inspection of trust accounts, and while random checks were instigated, it appears that they were carried out in an unstructured fashion, rather than as a clear supervisory tactic. A number of random audits were conducted and appear to have been mainly in regional areas.

5.27 An internal Board memorandum dated June 5 1996 indicates that a proactive inspection of the trust accounts of Leon K Jamieson and Associates had identified concerns with the practices adopted by this broker. The concern related to the broker drawing on trust money prior to receiving bank clearance on deposited cheques.

5.28 The Board minutes of June 12 1996 indicate that the Board resolved that the deputy registrar was to stress the concerns of the Board to any brokers adopting these practices. The Board does not appear to have taken any further action on these concerns and the random inspections would appear to have faded away.

HANDLING OF COMPLAINTS

5.29 There were many complaints made to investigators about interest payments not being received. However, the minutes of the Board disclose that on several occasions complaints were withdrawn without examining the underlying reasons for non-payment of interest once the outstanding interest had been paid. Ms Penny Searle, investor, told the Committee that she clearly had the impression that the Board had a policy of not pursuing complaints after the complainant was paid out. Ms Searle, told the Committee that she had presented evidence to Mr Jack Willers, an investigator and officer of the Board, which clearly indicated problems with Global.[110] The matter was resolved for Ms Searle but she still wanted to continue to pursue her complaint because she believed that there were systemic problems within the industry and she wanted to save other investors the problems she had experienced. Ms Searle told the Committee that when she told Mr Willers that she intended to continue pursuing her complaint, he became very angry. However, despite the obstructions, she continued to pursue her complaint.

5.30 In his evidence, Mr Ray Weir, industry member of the Board, agreed that there were problems with the complaint process. He said that only one or two complaints reached the Board for formal hearing. He told the Committee that the balance of those complaints were either continuing or, in the majority of cases, dismissed either

[110] Ms Searle said that Mr Willers' response was that she should get private legal advice, as there appeared to be an agency agreement between her and Global. Transcript of Ms Penny Searle's evidence given to the Committee on July 28 2000, p. 17.

because he believed that they were outside the jurisdiction of the Board, or the party making the complaint did not provide enough evidence for the matter to be concluded.

5.31 Mr John Urquhart, former Chairman of the Board, told the Committee that where complaints were made, and if the person complaining about a problem failed to contact the investigating officer, or failed to do anything to go ahead with the complaints, quite often it would be taken off the list of cases. Mr Urquhart said, "[y]*ou must appreciate that nothing can go to the board if the person who lodges the complaint is not willing to attend before the board. There has been a perception by the Press and some others that the board can pick itself up and tell a licensed person that it will investigate him. It is just not possible.*"[111] However, s. 13 of the Act expressly states that:

> "*The Registrar may, of his own motion, and shall at the direction of the Board, and an inspector shall, at the direction of the Board or Registrar, make any investigation or inquiry that the Registrar or the Board considers necessary or expedient for the purpose of --*
>
> *(a) determining any application or any other matter before the Board;*
>
> *(b) determining whether or not finance brokers are acting in conformity with the special conditions, if any, of their licenses and business certificates and are complying with the requirements of this Act; and*
>
> *(c) detecting offences against this Act.*"

5.32 Mr Douglas Solomon, lawyer for some investors, told the Committee that he disagreed with Mr Urquhart's interpretation of the powers and duties of the Board, and said that it was "*…a matter of great regret for me, as a practising legal practitioner of more than 20 years standing, to have heard the views of the chairman of the board that, despite these sections, which expressly confer powers and duties on the board, the board was unable to exercise the powers and fulfil the duties because of what he perceived to be rules of natural justice*."[112]

5.33 Mr Solomon also indicated in his submission to the Committee that the Board took the view that it was unlawful for the Board to exercise the functions expressly conferred by ss. 13 and 14 because that would be a breach of the administrative law rule that a person may not be both prosecutor and judge in a matter. Mr Solomon stated that he

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111 Transcript of Mr John Urquhart's evidence given to the Committee on July 7 2000, p. 4.

112 Transcript of Mr Douglas Solomon's evidence given to the Committee on October 5 2000, p. 4.

believed that in exercising its powers of superintendence, the Board would not be acting as a prosecutor but simply superintending the powers of investigation and inquiry by the Board's own officers.

5.34 In his evidence to the Committee, Mr Urquhart stated that "[t]*here must be a division between the disciplinary process and the investigation process. I have said this throughout my time on the board since 1992, but it does not seem to get across to some people. The board cannot be investigator, prosecutor and the judge, it is just not possible. I stand and fall on that. If I am wrong in my decision, then I am wrong with regard to that and I would have to resign from the board.*"[113] Mr Urquhart resigned his position on September 12 2000 shortly after the release of the Gunning Report.

BOARD HEARINGS

5.35 A range of evidence received by the Committee indicates that the Board conducted its hearings in an excessively formal manner, which, along with other factors, led to extensive delays in finalising matters. Mr Urquhart told the Committee on July 7 2000, that three formal hearings were taking place. He said that two had been given hearing dates, but that "*Margaria is different because that was just adjourned*".[114] Mr Urquhart went on to say that Mr Maragaria's case was coming up for "*mention*" and that evidence was complete for Mr Fermarnis, but that they were waiting for final submissions from counsel. He said that the Gamel Ward matter had been adjourned to a date to be fixed. On November 13 2000, the Registrar of the Board informed the Committee that hearings in relation to Mr Margaria and Mr Gamel have been adjourned *sine die.*[115] Postponing cases indefinitely without any day being fixed for resumption appears to have been a common practice of the Board and is continuing.[116]

TOLERANT APPROACH OF THE BOARD

5.36 Minutes of the Board reveal a tolerant approach to dealings with finance brokers. An example of this is what would appear to be an overly tolerant approach to particular brokers. At the inquiry into the conduct of Mr Graeme Grubb held before the Board on November 17 1993, the Board found that Mr Grubb had breached the provisions of the Act which provide for the necessity of a trust account and the requirements of the

113 Transcript of Mr John Urquhart's evidence given to the Committee on July 7 2000, p. 5.

114 Transcript of Mr John Urquhart's evidence given to the Committee on July 7 2000, p. 3.

115 According to *Butterworths Australian Legal Dictionary*, p. 1084, "*sine die*" means to postpone indefinitely.

116 Currently, there are two hearings in progress before the Board; both are adjourned *sine die*.

auditor's report.[117] In deciding on consequences of these breaches, the Board considered the submissions made on behalf of Mr Grubb that he was experiencing financial hardship, and consequently did not order a fine, but "*severely reprimanded*"[118] him and ordered him to pay costs of $690.00. Other brokers were fined for less serious offences.[119]

5.37 Mr Grubb came before the Board again on February 10 1999 to answer the Board's concerns about the large number of complaints received since November 1997. The Chairman told Mr Grubb, "*…that it is apparent to the Board he does not know the 'nuts and bolts' in running a business and in managing an office and the last thing they want* [meaning the Board] *is an inquiry before them.*"[120] The Board pointed out areas of concern including the lack of attention to detail, the failure to return telephone calls, and the general mismanagement of the office. Mr Grubb responded that he was embarrassed by the large number of complaints received by the Ministry, and indicated that he would employ extra staff to use the computer and attend to client queries. He also referred to his poor computer keyboard skills, his ill health and stated that with correct medication he should be able to manage his business properly. The minutes reflect that no action was taken at that time.

5.38 One month later, four new complaints had been received by the Board. These complaints related to the same issues, that is non-payment of interest or refund of principal and interest, plus a dishonoured cheque for $30,000 issued by Mr Grubb. The action that the Board considered appropriate was to seek an examination of Mr Grubb's bank statements. The same minutes reflect that there had been a complaint by an investor that Mr Grubb had not recorded her interest on the Certificate of Title. The Board decided that if the interest was not on the Certificate of Title, then an inquiry would be forthcoming at the next meeting. Despite this resolution, there is no mention of an inquiry in the minutes of April 14 1999. Finally, in May 1999, after considering the special audit report the Board had requested, the Board determined that Mr Grubb was operating in an unsatisfactory manner and sought to appoint a supervisor.

5.39 Another example of questionable tolerance was towards the firm of Blackburne & Dixon. The minutes of the Board dated July 12 1995, show that a transcript of examination in the liquidation of Amelia Developments Pty Ltd implicated

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117 Sections 48 and 59 of the Act.

118 Minutes of the Board dated November 17 1993, p. 1.

119 Inquiries into breaches of ss. 48 and 59 on September 8 1993 where one broker was fined $200 and another $300. See Minutes of the Board dated September 8 1993, pp. 1-2.

120 Minutes of the Board dated February 10 1999, p. 9.

Blackburne & Dixon Pty Ltd in financial dealings in relation to unauthorised "draw downs" and inflated property values. The Board decided that an audit under s. 68 should be carried out on Blackburne & Dixon's accounts. The audit was not carried out until November 1995. The audit report agreed with the findings of the transcript of examination. The minutes of January 10 1996 indicate that the auditor's report had been considered by the Board and that the Board had decided that a continuing audit of accounts and investigation proceed immediately. The Board was advised by the Manager of the Real Estate Branch of the Ministry that the Ministry may not be in a position to fund a further audit. It was resolved that a continuing audit be conducted by Mr Frank Bull, Deputy Registrar, with the assistance of Mr Gary Wallace, Investigator, who would conduct the investigation. Mr Wallace denied such involvement. He told the Committee that he did not handle the trust account side of things and that the Ministry had always been divided so that investigations into trust accounts were handled by other people, in this case by Mr Bull.[121] It is difficult to ascertain what communication was made with Blackburne & Dixon, however it does not appear that they were requested to fund the original audit and pay for the continuing audit at that time.

5.40 The minutes of February 14 1996 show that Mr Wallace was seeking a legal opinion from the Ministry as to whether a case could be made on the breaches identified in the audit report. Yet the minutes of the same meeting reveal that Mrs Kay Blackburne and Mr Ken O'Brien were issued with unconditional licences.

5.41 The Board inquiry into Blackburne & Dixon was conducted on April 29 1996, nine months after the first indication that there had been a breach and the Board's decision was not handed down until January 8 1997, a further eight months later. The Board found that there were breaches to the Act and the Code, and imposed a fine of $500. As well as this, costs of $5,500 were awarded against Blackburne & Dixon. These costs included the original auditor's fees of $1,185. Over eighteen months passed from the time the information was supplied to the Board to resolution.

THE ISSUE OF "FIT AND PROPER PERSON"

5.42 The concept of "fit and proper person" was another area where concerns were recognised within the Board, but never clarified to the extent that clear policy guidelines could be established. For example, the investigation into Blackburne & Dixon indicated problems within the firm, however both Mrs Blackburne and Mr O'Brien were granted unconditional licences on the same day that a legal opinion was being sought about the anomalies discovered during an audit of the firm's accounts. It

[121] Transcript of Mr Gary Wallace's evidence given to Committee on September 27 2000, p. 5.

appears that no thought was given as to whether these people were "fit and proper" to hold a licence, and in particular, an unconditional licence, even though the Board had arranged a special audit of the firm's accounts.

5.43 The minutes show that the Board lacked resolve when dealing with brokers who were unfit to hold licences. A glaring example of this is the matter of Mr Ken Polla. Several complaints had been received against Mr Polla, and action was being taken to recover moneys from the bond under s. 35(5) of the Act. However, the Board decided to consult with the compliance section regarding the feasibility of an inquiry seeking the cancellation of a broker's licence.[122] This appears strange considering the Act is clear that the Board has power to suspend or cancel a licence.[123] Whether the compliance department was consulted cannot be ascertained, however six months later, the Board asked for a legal opinion as to the grounds upon which Mr Polla's licence could be cancelled.[124] Eventually, in September 1994, Mr Polla supplied a statutory declaration surrendering his licence, but the Board was adamant that it should be cancelled and the Board requested direction from the Ministry Legal Officer as to how this could be achieved. The minutes of March 8 1995 indicate that "*Inspector Bull is working in consultation with the Ministry legal officer in obtaining evidence to prove the allegations. Affidavits are being prepared.*"[125] Mr Polla's licence was not discussed again, and in fact, the Board's list of licensed finance brokers shows that Mr Polla surrendered his licence March 5 1993.

5.44 Minutes show that the Board noted newspaper articles showing that a broker had been jailed for 4.5 years for fraud and stealing: "[i]*n the circumstances, the Board requested that the matter be referred to the Ministry Legal Officer Gordon Gray for determination on whether Mr Deadman 'is a person of good character and repute and a fit and proper person to hold a licence'"*.[126] Three months later, after much time spent by the investigator, Mr Deadman surrendered his licence. Amid complaints by the Board about time taken for investigations, it seems that much time was wasted on a matter that should have been easily resolved.

5.45 The issue of "a fit and proper person" did not appear before the Board again until December 1997 when the Board discussed a newspaper article which stated that the Police Commissioner had breached his duty of care by issuing a shooter's licence to a

122 Minutes of the Board dated November 10 1993.

123 Section 83 of the Act.

124 Minutes of the Board dated May 11 1994.

125 Minutes of the Board dated March 8 1995, p. 3.

126 Minutes of the Board dated August 9 1995, p. 9.

person who was not a fit and proper person. The Board referred the article to the legal officer to determine any possible impact on the Board in carrying out their obligation to issue licences to "fit and proper" persons. However, even though the issue was related to a breach of a statutory duty similar to the duty imposed on the Board under the *Statutory Corporations (Liability of Directors) Act WA 1996*, it did not appear again in minutes after that date and was not mentioned in the 1998/99 Annual Report of the Finance Brokers Supervisory Board.

5.46 It is noteworthy that since 1992, the Board suspended only two finance brokers' licences:[127] one for failure to lodge an audit/statutory declaration for the year ending December 31 1994; and the other for the breach of the special condition on a licence.[128] However, when placed alongside the liberties taken by some of the more notorious finance brokers, the "misdeeds" of these two brokers seem insignificant.

THE "CLIENT" ISSUE

5.47 Investors told the Committee that they had complained to the Ministry during 1996-97 but their complaints were not investigated because the Ministry took the stance that the lender was not the "client" of the finance broker as described in the Code. Minutes dated November 12 1997 reveal the Board's first grasping of the term, "client" in the Code and at that time, the Board decided the word "client" referred to either the borrower or the lender, depending on for whom the broker is acting. The Board further decided that where the broker acted for both parties, then the broker had a responsibility to both.

5.48 The Gunning Report stated that:

> *"A significant obstacle in dealing with complaints against finance brokers arose in early 1998, when legal advice within the Ministry identified a potential difficulty flowing from the proper construction of the word client within the Code of Conduct".*[129]

5.49 The previous Committee summonsed the legal opinions regarding this issue from the Ministry but the Ministry refused to provide them to the Committee. The previous Committee dissolved because of the mid-year prorogation of Parliament before it was able to report the matter to the House.

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127 Minutes of the Board dated August 9 1995.

128 Minutes of the Board dated March 3 1999.

129 Gunning Report, p. 185.

5.50 Four months after first raising the meaning of the word "client" and following consideration of Ministry advice, the Board resolved not to recommend amendments to the Code "*at the present time*"[130], the excuse being that the Board was awaiting the outcome of the Industry Reference Group. Mr Patrick Walker, Chief Executive and Commissioner of the Ministry of Fair Trading, confirmed this and added that the Board declined the advice and did not amend the Code despite encouragement to do so by the principal legal officer. Eight months later, Mr Gary Buchholz, Registrar of the Board, warned Board members that the word "client" could have such an impact on Global complaints, that he considered it necessary to refer the matter "*…to the legal officers and seek a Queens Counsel opinion which may result in there being a need to amend the Code of Conduct*".[131]

5.51 According to Mr Walker, complaints were still considered and assessed regardless of the definition of "client". He advised the Committee that the Ministry endeavoured to deal with complaints in other ways.[132] However, it is clear that investors who received a letter from Mr Willers, Investigator, stating that the "*Ministry's view is that the matter should not be referred to the Board…because they were not the broker's client*"[133] felt "fobbed off" by the inaction of the Board and the Ministry. Other complainants were advised to commence their own civil action against Gamel Ward Pty Ltd because they were not clients.[134] Ms Penny Searle, investor, told the Minister that it was numerous investors' experiences that they could not get a hearing of complaints by the Board and the failure to act was "*being exploited by finance brokers*".[135]

5.52 The Board, in its 1997-98 Annual Report stated that the Ministry's view of the term "client" "*…has proved fatal to a number of investigations into the conduct of a number of brokers. The Board will consider amending the Code.*"[136] One year later in its 1998-99 annual report, the Board stated, "[o]*n other matters, difficulties*

130 Minutes of the Board dated March 11 1998.

131 Minutes of the Board dated November 11 1998, p. 9.

132 Transcript of Mr Patrick Walker's evidence given to the Committee on October 9 2000, p.10.

133 Letter in Ministerial file February 16 2000, Ministry File 13182, Vol. 4.

134 Minutes of the Board dated May 13 1998.

135 Letter to the Minister from Ms Penny Searle, dated March 3 2000, Ministry File 13182, Vol. 4.

136 Annual Report of the Board, 1997-98, p. 7. However, Mr Ray Weir, Industry Member of the Board, in a letter to Mr Patrick Walker, Chief Executive, Ministry of Fair Trading, dated March 9 1999, Ministry File 12130, Vol. 4, stated that this "offending" paragraph was not in the draft annual report and questions whether the Ministry altered the draft after it was approved by the Board to discredit the Board for political reasons and to promote the Ministry's pro-deregulation policy.

associated with the definition of the 'client' within the meaning of the Code of Conduct prevented further follow up…".[137] Despite the Board recognising that the word "client" was problematic and receiving Ministry advice to amend the Code, the Board failed to adequately resolve this issue. Instead of shifting blame onto the Ministry for the Board's inaction, the Board could have amended the Code, had the word "client" tested through a formal inquiry or suggested to the Ministry that it continue to ascribe the same interpretation to the word as in the past.

THE ISSUE OF OVERVALUATIONS

5.53 The Board's 1994/1995 Annual Report referred to overvaluations to secure finance, being "*…a general area of concern which bears mentioning*".[138] In an interim report dated August 1 1995 to the Board from Mr Gary Wallace, Investigator, regarding Blackburne & Dixon, which is attached as Appendix 3, concerns were expressed about possible overvaluations to obtain finance and it was recommended that the Code be amended to address this problem. This report was considered at the Board meeting on August 9 1995 and the recommendation regarding overvaluations does not appear to have been addressed.

5.54 By July 1997, the Industry Reference Group had also identified this problem in its interim report.[139] Mr Robert Castiglione, former Ministry legal officer, who joined the Ministry in early 1998 told the Gunning Inquiry he was aware of "*general discussions within the Ministry*" about overvaluation of security properties and how this was a problem for the industry. The Board's 1997/1998 Annual Report referred to "*…substantial losses suffered by private investors in transactions where properties offered as security for loans were found to be grossly overvalued.*"[140] The evidence suggests that overvaluations were known to be a significant problem as far back as 1994 with neither the Board nor the Ministry adequately addressing this issue.

PROTECTION FOR INVESTORS

5.55 Many investors indicated that they felt their investments were secure because the industry was supervised by a government body, that is the Board. However, many investors who appeared before the Committee expressed disenchantment with the Board. Complaints such as untimely delays in investigating complaints, dissatisfaction with hearings before the Board, the attitude of the Board towards

137 Annual Report of the Board, 1998/1999, p. 8.

138 Annual Report of the Board, 1994/1995, p. 9.

139 Gunning Report, p. 87.

140 Annual Report of the Board 1997/98, p. 9.

investors and the inertia in starting investigations and appointing supervisors, among other things, were presented to the Committee. The minutes of the meetings of the Board between 1993 and 2000 validate investors' concerns, as well as those concerns identified by the Gunning Inquiry.

Bond/Fidelity Fund

5.56 The Gunning Inquiry stated that the "… *most outstanding deficiency in the Act that emerged from the Inquiry is the absence of adequate redress for investors who suffer loss as a result of defalcation (fraudulent or criminal behaviour) by a broker.*"[141] The Law Reform Commission of Western Australia, in its report on mortgage brokers in 1974 had recommended a fidelity fund as a first option for protection for investors, however a $50,000 bond was decided upon.[142] That this was not adequate protection was mentioned as early as 1983.[143] The bond situation appeared in minutes of the Board on and off for almost ten years until 1991 when the minutes of the Board indicate that Executive Director of the Ministry of Consumer Affairs, Dr M. Forrest, attended for discussions on the implementation of a fidelity fund. He advised that the Minister was "…*pursuing the notion of having finance brokers admitted to the 'Fidelity Guarantee Fund' established under the Real Estate and Business Agents Act but had met with stiff opposition from members of the real estate industry.*"[144] The minutes indicate that Dr Forrest hoped that the real estate industry could be persuaded to allow admittance of finance brokers into their fund by requiring finance brokers to contribute at the same level that it currently cost them in premiums to obtain a bond, and setting a maximum amount that could be claimed from the fund for each broker found guilty of misappropriation of trust funds. The minutes show that Dr Forrest indicated that the Minister was well aware of the inadequacies of the present bonding arrangements and would keep the Board informed of developments with the fidelity fund.

5.57 It appears that negotiations continued until a working party was set up regarding the establishment of a composite fidelity fund. The minutes of April 8 1992 indicate that Mr Edward Brunton, industry member, advised the Board that he attended the inaugural meeting of the working party. The minutes show that Mr Brunton advised that discussions took place between the Settlement Agents Supervisory Board, the

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141 Gunning Report, p. 265.

142 See paragraph 1.13 above.

143 Minutes of the Board dated September 6 1983 indicate that the Minister wanted to know the best way to overcome the bonding system. Matters discussed were whether the $50,000 was unrealistic, and protection for the public against defalcation was necessary.

144 Minutes of the Board dated October 2 1991, p. 10.

Real Estate and Business Agents Supervisory Board, and industry members, and that there were reservations expressed by the real estate industry "*…given the magnitude of the losses known to have been suffered by the clients of the failed finance brokers, C W Jacka & Co and G D Trewenack.*"[145] The composite fidelity fund did not come to fruition and was only occasionally referred to in further minutes of the Board.

5.58 In 1995, the Board resolved to refer the bond to the Ministry legal officer to review the wording of the bond into plain English and that comments be sought from the Institute of Finance Brokers on raising the bond from $50,000 to $100,000.[146] However, Mr John Bell, industry member, advised the Board on November 8 1995 that the Institute of Finance Brokers did not support the increase. Towards the end of 1999 Cabinet endorsed compulsory professional insurance for all finance brokers handling private investors' funds.[147]

5.59 The Board minutes of September 20 2000, indicate that professional indemnity insurance was discussed. The Board decided that the draft policy they were using did not address the problems of dishonesty or defalcation of a principal of a finance broker dealing in private funds, and therefore the bond should be left in place until a more satisfactory arrangement could be found. The minutes also indicate that the Board "*…believed that some of the issues identified by recent information which had been made available to the Board would suggest that professional indemnity insurance may offer some limited protection, although it was clearly not a solution to the fraud or dishonesty of the broker.*"[148] The Board resolved at that meeting that professional indemnity insurance to a minimum of $1 million be compulsory for all brokers with an unrestricted licence. However, this will not apply until a business certificate is due for renewal. Brokers who hold a restricted licence can remain without professional indemnity insurance.

5.60 While the Committee notes the decision to require professional indemnity insurance, it is of the view that even if this requirement had been put in place some time ago, it would have provided limited assistance to those investors currently facing losses.

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145 Page 6.

146 Minutes of the Board dated July 12 1995, p. 4.

147 Gunning Report, p. 267.

148 Minutes of the Board dated September 20 2000, p.3.

Board and Investors

5.61 The Gunning Report indicated two areas where it believed the Board was confused about its role.[149] Firstly, there was the Board's "non reaction" to the increasing number of complaints with no analysis undertaken.[150] Minutes of Board meetings and evidence given to the Committee show that concerns were raised by various Board members only to be recorded and never revisited. In minutes dated March 12 1997, Mr Edward Brunton, an industry member of the Board, expressed his concern "*…at the number of active complaints received and that obviously resources were a contributing factor but ramifications resulting from the large list could become an embarrassment to the Board"*. Complaints had more than doubled from 21 in 1995 to 46 in 1998, and continued to rise to 139 in 1999,[151] however this issue was not raised again in the minutes.

5.62 Secondly, the Board "*…saw no role for itself in the area of consumer education*".[152] The Gunning Report concluded that "*…the final result is that the limitation of its role perceived by the Board, and the atmosphere of deregulation after 1996 resulted in there being no effective investor protection flowing from the Act*".[153]

5.63 In December 1998, the Industry Reference Group reported and suggested community education programs to protect investors. Prior to this time, there had been efforts on the part of the Ministry to produce a program for endorsement by the Board but these efforts failed to crystallise. Board minutes dated September 9 1998 indicate that Mr Gary Buchholz, Registrar, and Mr Jack Willers, Investigator, told the Board of an intention to produce a pamphlet informing investors, such as retirees, what they should know and questions to ask, should they consider an investment. The pamphlet would be an educational tool providing information on the types of investments available. However, the concept languished until two months later when Mr Buchholz again raised with the Board the production and distribution of an information brochure for such persons as superannuants and retirees advising them of matters they need to give consideration to when contemplating entering into private investments. Despite these intentions the brochure was not published until after Cabinet, in March 1999,

149 Gunning Report, pp. 91-92.

150 Mr Gary Newcombe, Director, Projects, Ministry of Fair Trading, in evidence given to the Gunning Inquiry, thought the Board should be primarily responsible for the analysis but also the Ministry should have undertaken some analysis, p. 91.

151 Gunning Report, p. 53.

152 Gunning Report, p. 255.

153 Gunning Report, p. 258.

endorsed the Industry Reference Group's suggestion that a brochure be produced concerning finance brokers and mortgage investments.[154]

5.64 The Board's attitude appears to be one of reluctance to advise investors of problems with brokers. The Board seemed to align itself with the interests of finance brokers, not the investors. Given that the original purpose of the Act was to protect investors, it is extraordinary that the Board was not proactive in publishing warnings about the practice of overvaluation to the investing community throughout 1996, 1997 and 1998. The Board rarely published material, but in one edition of the *Finance Brokers News* mention was made about overvaluations. However, this material was only made available to finance brokers, not the investing public.

5.65 Another example of this appears in the Board minutes of January 8 1997, which state that the Board discussed issuing a media statement following the inquiry into Blackburne & Dixon. This was opposed by Mr Edward Brunton on the basis of the likelihood of an appeal to the District Court, and the Board suggested that an article could appear in the next finance brokers' newsletter. The Committee, due to time and resource constraints, was unable to inquire into the reasoning behind the Board's actions on this matter.

5.66 The Gunning Report stated that "[t]*he existing regulatory system failed to identify the exploitation which was occurring until it was too late to be able to do anything to prevent the losses which resulted.*"[155] The Gunning Inquiry found that complaint handling by the Board and the Ministry was reactionary, and no steps were taken to analyse trends which emerged from the increased numbers of complaints from 1996 onwards. It also found that the administration of the audit provisions of the Act failed to flag serious problems and stated that this was brought about by such factors as the limited scope of the audits, poor auditors, an inefficient system for dealing with the audit certificates, and a lack of reference of qualified audits to the Board. In addition to the findings of the Gunning Report, evidence to the Committee indicated other areas where the Board did not carry out its statutory functions.

154 Gunning Report, pp. 217-218.

155 Gunning Report, p. 255.

CHAPTER 6
THE MINISTRY OF FAIR TRADING

6.1 The Gunning Report states that "*…the overall thrust of the evidence is to the effect that finance broking matters were a relatively low priority*"[156] within the Ministry. Further, the Industry Reference Group was aware of the recent losses in other States but "*apparently oblivious*"[157] to what was happening in its own State.[158] The Industry Reference Group claimed to recognise potential risks but this did not translate into any initiative for over two years. Membership of the Industry Reference Group comprised representatives of financial institutions, mortgage and finance brokers industry bodies, consumers, consumer organisations, the Ministry and the Board.[159]

6.2 During the period when significant problems in the industry began to emerge, the Board was within another Directorate. The Gunning Report found that neither the Director at the time nor the Manager of the Finance Industry Branch, Mr Buchholz, who was also Registrar, had any knowledge or experience in relation to the industry. While the Committee considers that industry knowledge could be advantageous, it believes that the most important issue is that staff has the necessary skills to investigate and monitor the industry. It is for the Board to have industry knowledge and skills. However, it is certain there were frequent staff changes at the Ministry and poor management related to staff being allocated according to their availability, not their skills, experience or knowledge.

6.3 Mr Robert Castiglione, former Ministry legal adviser, told the Gunning Inquiry about undirected and untrained investigators within the Ministry. There appears to have been a lack of systems and procedures to deal with received evidence and chaotic filing. Mr Gary Wallace, Senior Compliance Officer, Ministry of Fair Trading, told the Committee he was responsible for investigating finance broking matters from the mid 1980s until 1997. He referred to an ongoing problem with records in the Ministry "*since before 1992*".[160] Clearly there were internal management problems and divisions. For example, Mr Patrick Walker, Chief Executive, explained that the concerns of the legal staff would not necessarily have come to his attention as Chief

156 Gunning Report, p. 136.

157 Gunning Report, p. 217.

158 Gunning Report, p. 217.

159 Industry Reference Group, Final Report, December 1998, p. 3.

160 Transcript of Mr Gary Wallace's evidence given to the Committee on September 27 2000, p. 3.

Executive and neither the Minister nor the Ministry have authority to direct the Board.[161] However, evidence from two of the Registrars of the Board indicates their belief that the Minister can direct them, including to initiate an investigation into a finance broker. Mr Castiglione told the Gunning Inquiry that the Ministry legal officers were confident to only take matters so far, displaying a confidence in the fact that there were two legal practitioners on the Board.[162]

6.4 An example of the poor record keeping and procedures of the Ministry was provided to the Committee when it requested information from the Ministry on an investigation into Blackburne & Dixon. The Ministry was only able to provide copies of transcripts of interview and associated notes conducted with Mr Ken O'Brien and Mrs Kay Blackburne. The Ministry was unable to locate the audio tapes of these interviews. While the transcripts indicate serious matters which should have been further investigated, the Ministry was not able to advise the Committee of any further action taken or the outcome of this investigation as they could find no other records.

6.5 The Gunning Inquiry identified excuse-making behaviour by the Ministry. For example, complaints about the non or late payment of interest, that is the "management" of the investment being beyond the scope of the Act or Code. Counsel for the Ministry had argued that non payment of interest could be indicative of default on the part of the borrower but the Gunning Inquiry refused to be drawn on the specifics of this issue, preferring the generic issue, this being that:

> "*…it is not an answer to say that the borrowers' defaults are not a breach of the Act, and that on that basis the Board had no part to play. The fact that a significantly greater number of investors were losing their money through borrower defaults should have been a matter of concern for the Board.*"[163]

6.6 In evidence to the Committee, Ms Penny Searle, investor, gave an example of poor Ministry communication and a lack of a communication systems database. She said:

> *"I was not aware that there was a past record with Global, for instance. I am horrified to know now that in fact there was qualified accounts on Global prior to us lodging complaints, which then raises the question, why on earth did they not listen to us if that was already known to the Ministry of Fair Trading at that time, or is the Ministry*

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161 Transcript of Mr Patrick Walker's evidence given to the Committee on October 9 2000, p. 10.

162 Gunning Report, pp. 190-191.

163 Gunning Report, p. 55.

of Fair Trading so spread out that communication lines are very bad."[164]

MINISTER

6.7 Mr Gary Newcombe, Director, Projects, Ministry of Fair Trading, told the Committee that "[t]*he Minister is responsible for the Finance Brokers Control Act and the board. He is unable to direct the board, as the Act contains no specific authority for the minister to issue directions to the board. The board may contact the minister directly and occasional reports directly to him on matters of policy and administration.*"[165] While the Minister cannot direct the Board in its duties, he or she has general ministerial responsibility for the integrity of the Board, and also for its members.[166] There appears to have been very little communication between the Board and the Minister. The Committee, due to time and resource constraints, has not been able to ascertain when the Minister first became aware of the extent of the problems within the industry, the Ministry and the Board, or why the response has been so slow.

6.8 In his letter of resignation, Mr John Urquhart, former Chairman of the Board, expressed his concerns that legislative changes urged by him and his predecessors on the Board and proper strategies to ensure that the Ministry and the Board were appropriately funded have not been implemented. He also expressed concern that the recommendations of the Industry Reference Group have not been implemented. Mr Urquhart stated that in each of the annual reports from June 30 1992 to June 30 1996 he had referred to changes in the Act, and further pointed out that the Board is not responsible for ministerial change. He accused the present Minister of not acquainting himself with the background of the Act.

6.9 Mr Charles [Bill] Mitchell, Policy Adviser to the Minister for Fair Trading, told the Committee, *"I am a fair trading policy adviser. I provide advice to the Minister in relation to fair trading matters. I act as an adviser to the Minister. People come through me when they want to speak to the Minister about fair trading matters. I evaluate letters as to whether they should be sent to the Minister for further action…".*[167] Mr Mitchell said that when he first transferred from the Retail Branch of the Ministry of Fair Trading to the office of the Minister in May 1997, he recalled that he *"…had a chat with some of the managers from the various sections…"*[168] and this

164 Transcript of Ms Penny Searle's evidence given to the Committee on July 28 2000, p. 21.

165 Transcript of Mr Gary Newcombe's evidence given to the Committee on July 24 2000, p. 9.

166 *Statutory Corporations (Liability of Directors) Act 1999,* s.5.

167 Transcript of Mr Charles [Bill] Mitchell's evidence given to the Committee on October 6 2000, p. 1.

168 Transcript of Mr Charles [Bill] Mitchell's evidence given to the Committee on October 6 2000, p. 5.

appears to be the only briefing which occurred. He said that he had never met with the Board, but he had familiarised himself with the issues contained in the annual reports. He told the Committee in answer to the question of legislative change there was no reason to do anything but accept the Board's advice to not act until the industry review had been completed. Mr Mitchell told the Committee that he was aware of complaints made by Ms Penny Searle and Mr Carl Lens in September 1998, although he said that he "*suspected that he was aware*" that there were some concerns about Mr Graeme Grubb, and recalled that 25 complaints were made in the latter half of 1998, but could not recall whether complainants had written to the Minister.

RELATIONSHIP BETWEEN THE BOARD AND THE MINISTRY

Funding

6.10 The Board has always been reliant upon the Ministry for funding. Although the Act does not clearly arrange for allocation of funding, the Board has been under the umbrella of the Ministry and its predecessors since its inception. The Act stipulates fees and allowances for members;[169] all other officers are appointed under s.12 of the Act in accordance with Part 3 of the *Public Sector Management Act 1994.* The Act does not legislate for funding for day to day running of the Board.

6.11 This lack of clarity in funding has brought about a situation where the autonomy of the Board has in effect been eroded by its reliance on funding and resources from the Ministry. Mr Edward Brunton, former industry member of the Board, told the Committee that:

> *"…it was just a pity that the way the* modus operandi *had developed over a long period was that I do not think the ministry ever thought it was subservient to the Board. I add that, in my mind, I was not working for them; they were working for me, but that never came across and that is a contributing factor in where we are today."*[170]

Dual Roles of Officers of the Board

6.12 The position of Registrar of the Board has always been held by a Ministry employee. Until recently, registrars have combined this role with other Ministry duties.

6.13 Mr Ray Weir, former industry member of the Board, told the Committee that it had only recently come to the Board's attention that the Board should appoint its officers.

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169 *Finance Brokers Control Act 1975,* s.11.

170 Transcript of Mr Edward Brunton's evidence given to the Committee on September 29 2000, p. 37.

This came about from a legal opinion supplied by the Ministry. He said that he suspected that the Ministry had been appointing officers for many years. Mr Weir stated that regardless of the manner of appointment, the officers of the Board did carry out the job properly.[171]

6.14 Mr John Urquhart, former Chairman of the Board told the Committee:

> *"The audit section was dealt with by the Ministry. I was not involved in that inquiry, so I did not have a hands-on approach into that aspect of it. All the audit matters were dealt with by the ministry. The Board has no expertise in auditing. The Board gives directions as to how a special audit should be done, on advice from the Ministry. Many of the questions which might have been raised by the auditor would have been discussed with people from the ministry. It is up to them to advise us as to what they consider should be done in the circumstances."*[172]

Legal Advisers

6.15 The Board relied on legal advice from the Ministry's staff. Legal opinions were not provided to the Committee, however the minutes of the Board indicate that the Board requested legal opinions regularly and mostly followed the advice given. Board minutes and evidence reveal that legal advice on particular issues often changed. Whether these changes occurred because of regular staff changes is unknown.

Investigators

6.16 Mr Edward Brunton, former industry member of the Board, told the Committee that "[i]*t was evident that the investigators never really had the expertise. One of them for instance, would telephone a broker when he had a complaint against him.*"[173] He said that investigators did not know what they were looking for and in defence of the Ministry, there was no doubt that it was driven by a budget. He told the Committee that the Ministry is aware of the significant costs involved in the failure to sustain a charge, and therefore the Ministry understandably appears to be reluctant to aggressively pursue contraventions of the Act or Code.[174]

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171 Transcript of Mr Ray Weir's evidence given to the Committee on September 29 2000, p. 14.

172 Transcript of Mr John Urqhart's evidence given to the Committee on September 28 2000, p. 5.

173 Transcript of Mr Edward Brunton's evidence given to the Committee on September 29 2000, p. 34.

174 Transcript of Mr Edward Brunton's evidence given to the Committee on September 29 2000, p. 34.

6.17 The Gunning Report summarises the state of the supervision and regulation of the finance broking industry. It states:

> *"What is evident…is that throughout the 1990s, no-one within either the Board or the Ministry assumed any leadership in addressing issues of concern in relation to the regulation of finance brokers."*[175]

[175] Gunning Report, p. 39.

CHAPTER 7
OTHER PLAYERS

VALUERS

7.1 The Committee heard expert evidence from Mr Patrick Rowland, Acting Head of the Department of Property Studies, Curtin University of Technology, about the role and function of valuers within the finance broking industry. According to Mr Rowland, valuers produce "market valuations" of properties by inspecting the location and physical attributes of a property, as well as examining documentation, primarily the certificate of title, for encumbrances and caveats. The assessment focuses on what the property might sell for on a particular date with some assumptions normally stated in the valuation report, such as the definition of "market value".[176] Valuers should make it clear to clients that it is an opinion of a value as at a certain date; it is not a guarantee that the client will receive the figure stipulated in the report.

7.2 Mr Rowland admitted to possible shortcomings within the industry. For example, the lender may want to lend the money and may pressure the valuer to come up with a higher figure. The pressure comes from whoever is instructing the valuer. If the instructions come through finance brokers who want to make a loan, the pressure is from one direction only - that is, to get the highest figure possible. Mr Rowland said:

> "*An ethical valuer would not succumb to that. Assuming there will always be a few valuers who are not of a high standard, if we have a system in which the instructions come from the party who wants the highest valuation that will make it possible for those weaknesses to occur.*"[177]

7.3 Mr Simon Read, Supervisor of Global, told the Committee that he had conducted investigations into a large number of valuations done mainly by Mr Ron O'Connor, who has been charged with several counts of fraud. He said that the "*…results of those investigations indicate that valuations were consistently above the realised values for properties.*"[178] Mr Read said further that he had looked at valuations of properties that are currently outstanding and also at properties that have settled in the period of Global's existence. He said that the valuations in some cases were

176 Transcript of Mr Patrick Rowland's evidence given to the Committee on August 8 2000, p. 2.

177 Transcript of Mr Patrick Rowland's evidence given to the Committee on August 8 2000, p. 18.

178 Transcript of Mr Simon Read's evidence given to the Committee on September 28 2000, p. 21.

significantly higher that the realised value. He told the Committee that he had found "*…evidence of selective use of sales histories to provide valuations and, generally, we questioned the values and the valuations that were obtained and the methods that the valuers used to value the properties. There are questionable valuation techniques.*"[179]

7.4 Mr Read told the Committee that a number of valuers were used, not only Mr O'Connor. He said that Mr O'Connor represented a significant proportion of the valuations that were conducted by "*…those types of individuals where we found most problems with their borrowings, especially Mr Casella, Mr Sadek and Mr Johnson. In some cases he was the only valuer used by those individuals. There have been other valuers. Nine times out of 10 those valuations were accurate or reasonably accurate.*"[180] Mr Read confirmed to the Committee that the valuer was not chosen at random, and there was a specific appointment by Global, and one valuer was particularly used by Mr Casella and Mr Sadek.

7.5 Concerns with valuations carried out by other valuers were brought to the attention of the Committee.

LAWYERS

7.6 In her evidence to the Committee, Ms Denise Brailey said, "[t]*he crux of the matter is that finance brokers could not act without lawyers. Al Capone had an attorney. The committee needs to understand that very well. The lawyers have not been picked up yet. They are the nub of the issue.*"[181] She told the Committee that RECA had a list of recurring names of several lawyers involved. As a generic example of lawyers' involvement, she said, "[c]*onveyancing for a property for $500,000 and arranging for a mortgage of $1.2 million cannot be done on the same day without something being wrong. That is something of which the lawyers were well aware. It is not a one-off thing; it was repeated many times.*"[182]

7.7 Mr Ian Clairs, Lawyer, told the Committee that he prepared documentation on behalf of the mortgagee. He said that it was one of the areas of concern that there was a lack of contact between the lawyer and the mortgagee, because the only contact was the instructions coming from the broker. He said that he knew that a number of solicitors took the view that they were acting for the broker, but he perceived the broker to be an agent instructing the solicitor on behalf of another person. Further into his evidence,

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179 Transcript of Mr Simon Read's evidence given to the Committee on September 28 2000, p. 21.

180 Transcript of Mr Simon Read's evidence given to the Committee on September 28 2000, p. 21.

181 Transcript of Ms Denise Brailey's evidence given to the Committee on September 26 2000, p. 6.

182 Transcript of Ms Denise Brailey's evidence given to the Committee on September 26 2000, p. 7.

Mr Clairs told the Committee that he did not get an authority from the lenders (mortgagees) to take instructions from the broker, and that he thought that that would be superfluous. Mr Clairs said that the broker provided a notice to the lender, to be signed by the lender, indicating that the lender was clear about what he or she had agreed to do. He said he was then given instructions in accordance with the notice to the lender and a notice to the borrower. Mr Clairs indicated that he assumed that because the funds were forthcoming, the lender had agreed to advance the funds. However, Mr Clairs continued to say that the funds might still be forthcoming if there was fraud by the broker by giving instructions contrary to the lender's instructions. Mr Clairs also told the Committee that he did not see the notice to the lender but "*…proceeded on the basis that the broker had authority to give me instructions to prepare the mortgage.*"[183] In answering the Committee's questions, Mr Clairs could not recall the specifics of projects that he had been involved in and that had failed.

7.8 Concerns regarding lawyers' conflict of interest arose during the inquiry and the Committee believes that the role of lawyers needs to be further investigated by an appropriate body.

ST GEORGE BANK LIMITED

7.9 Mr Mark Conlan, Supervisor and Liquidator of Rowena Nominees Pty Ltd, told the Committee that the government provided funding for him to investigate and ascertain the merits of pursuing an action against the St George Bank. This is because Rowena Nominees Pty Ltd's trust account was overdrawn on 84 days between June 1997 and May 10 1999.[184]

7.10 The Committee is mindful that its terms of reference do not permit it to interfere with or obstruct any inquiry being conducted into particular inquiries by any liquidator or supervisor of any company; or any prosecution. With this restriction, the Committee merely raises the issue of possible recovery against St George Bank by the liquidator of Rowena Nominees Pty Ltd for breaches of trust law.

7.11 Mr Conlan said that if there is a successful action against the St George Bank, funds will be paid to him as liquidator. However, it would need to be settled by the courts as to whether recovered money would be available to investors only or investors and Rowena Nominees Pty Ltd's creditors. Ultimately the courts will issue orders about where the money is to be disbursed.

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183 Transcript of Mr Ian Clairs' evidence given to the Committee on October 9 2000, p. 5.

184 Mr Michael Hawkins, 'Briefing Notes to the Minister', May 10 2000 contained in Ministerial file 13182, Vol. 5.

BORROWERS

7.12 Many investors gave evidence that borrowers were unscrupulous and dishonest. The Committee heard evidence from witnesses that they are fearful for their safety from some borrowers.

7.13 Mr Dominic Casella, property developer and borrower, said the late Mr Owen Blackburne arranged finance for his proposals. Mr Casella alleged Mr Blackburne blackmailed him into signing a one-third partnership on a proposal for which it was too late to arrange alternative finance. According to Mr Casella, he objected strongly to this arrangement, but admitted it was not disclosed to the investors. He also told the Committee that it was normal practice to borrow in excess of 100% of the value of the property and as a borrower he could see nothing wrong with it. Mr Casella said: "*I think probably 120 per cent or 130 per cent of the value I purchased it for.*" Mr Casella said, "*…for instance, a bank would lend 60 per cent of valuation, or 60 per cent of purchase price, whichever was the least, it would always be difficult* [to obtain funds]. *Also, the types of deals we used to organise with Blackburne & Dixon meant that we would accrue the interest, whereas banks do not like having accrued interest in a deal. They want the payments to be made on a monthly basis, out of the cash flows. In this case, we would actually borrow the servicing money that we required.*"[185]

7.14 Mr Casella also said in his evidence that he and Mr John Miller provided $40,000 or $50,000 to establish Global in a joint venture with Mr John Margaria. As part of this arrangement, each of the three partners in Global would also receive a one third share in property developments undertaken by Mr Miller and Mr Casella. He explained that he thought this arrangement would be satisfactory because he could disguise it by putting the money through trusts. This is despite the arrangement appearing to be the same as the blackmail that Mr Casella said Mr Owen Blackburne forced on him and to which he had strongly objected. He further said that this arrangement did not proceed.

7.15 Other borrowers offered to give evidence to the Committee but time did not allow this to occur.

AUDITORS

7.16 The Act stipulates that every finance broker must have the trust account audited each calendar year and that the auditor conduct the audit in accordance with accepted auditing practice, including selective testing and as the Board directs.[186]

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185 Transcript of Mr Dominic Casella's evidence given to the Committee on October 18 2000, p. 7.

186 Section 50.

7.17 The Gunning Report concluded that:

> "*…the audit provisions of the Act, designed to flag serious problems, failed to achieve that purpose. The limited scope of the audit, an apparent failure in some cases by auditors to identify serious problems, an inefficient system for dealing with audit certificates, and a lack of reference of qualified audits to the Board, all contributed to that failure.*"[187]

7.18 Mr Jeffrey Herbert, Liquidator of Global, told the Committee that anybody who is registered to audit is able to do so and that some auditors have more experience than others and some have more experience in specifically auditing trust accounts. Some firms perform less audit work and their results are "… *less than satisfactory in some cases*".[188] He agreed with the Committee that experience was the essential ingredient.

7.19 Mr Simon Read, Liquidator of Global, said

> *"Following our investigations into the affairs of the company, it surprised me greatly that there were no audit qualifications in respect of some of the transactions that we had clearly identified and certainly the significant misappropriation of funds, which was quite obvious in my casual perusal of the records of the company* [sic].[189]

187 Gunning Report, p. 255.

188 Transcript of Mr Jeffrey Herbert's evidence given to the Committee on September 28 2000, p. 26.

189 Transcript of Mr Simon Read's evidence given to the Committee on July 7 2000, p. 4.

CHAPTER 8
CONTINUING LOSSES

SUPERVISOR

8.1 The Act makes provision for the appointment of a supervisor. Section 73(1) provides that if the Board applies to the District Court for authorisation to appoint a supervisor, and the court is satisfied that there are reasonable grounds to believe that a finance broker is not capable of conducting his or her business properly, the District Court can give authorisation.

8.2 Section 74 provides that if an order is made under s.73, the Board can appoint a person with the remuneration and indemnity that the Board thinks fit, and can authorise an advance from the Treasury to carry on the business of the finance broker. The appointment must be in writing, and be signed by the Chairman or by two members of the Board.

8.3 Section 75(1) indicates that the duties of the supervisor are to *"…carry on the business for the purpose of concluding or disposing of matters commenced but not concluded on behalf of clients of the business, and, where necessary, for the purpose of disposing of, or dealing with, documents relevant to those matters…*".

8.4 Section 78 gives the District Court power to discharge or vary any order made under s. 73, and power to direct that any funds in any account affected must be paid to the Treasury. Two supervisors have been appointed under s.73, one to deal with Rowena Nominees Pty Ltd and the other with Global.

8.5 Many investors have expressed concern to the Committee about the way in which the supervisors and liquidators are handling the aftermath of the losses and believe that they are creating further losses. Issues such as a conflict of interest arising when the supervisor is also the liquidator, lawyers and accountants pitting registered investors against unregistered investors, and problems associated with receiving payment after properties have been sold, are just a few of the complaints made by investors.

Mr Graeme Grubb - Finance Broker

8.6 Mr Mark Conlan, from the firm of RSM Bird Cameron, Chartered Accountants told the Committee that in late April or early May 1999, he was appointed as an independent accountant for Mr Graeme Grubb Finance Broker under an agreement between ASIC and Graeme and Margaret Grubb, directors of Rowena Nominees Pty Ltd. Approximately three weeks later, he was appointed provisional liquidator, and in

late July was appointed official liquidator. Mr Conlan stated that at about the same time, he was also appointed supervisor by the Board. He told the Committee that "[u]*nder the role of supervisor, funding was provided to conduct activities designed to cease the Graeme Grubb finance broking business activity and also facilitate the allocation of the various funds that might be recovered from mortgages to the mortgagees. That role has been extended since, in that further support has been provided to review the affairs of the auditors' conduct and also to now take forward possible proceedings against St George Bank and the auditors of the finance brokers trust account.*"[190]

8.7 The terms and conditions of Mr Conlan's appointment as Supervisor of Rowena Nominees Pty Ltd are included in the letter attached as Appendix 4.

8.8 Mr Conlan further stated that because the Act is very limited in the duties outlined for supervisors, he had had to make numerous applications to the court for direction in dealing with the tasks he had. He said that at the time of giving evidence, there were eighteen applications before the court relating to investors.

8.9 In his evidence to the Committee, Mr Douglas Solomon, lawyer for some investors, was scathingly critical of the actions of the supervisors. He stated that the State should have intervened long ago in the "…*supervisors' process of pitting victim against victim, and officiously intermeddling in the property and affairs of innocent victims*…".[191] He further stated that in his opinion, the supervisors were acting beyond the very limited functions of a supervisor under s. 75 of the Act.

8.10 Mr Jeffrey Herbert, Supervisor of Global, told the Committee that there were complicated legal issues surrounding the investors. He indicated that there were two "camps", that is, those investors who held registered mortgages, and those who did not. He told the Committee that the investors believe that the full costs of the lawyers representing them should be covered.[192]

8.11 The role of the supervisor appears to be problematic and is still to be clarified by the court. Until this happens, there will be inconsistencies in appointment and role of supervisors under the Act. Instances such as the suspension of Mr Peter Fermanis' licence highlight this. The draft minutes of the Board dated November 8 2000 state that "[t]*he Board directed that Mr Fernanis' licence and business certificate be suspended for a period of two years, effective from 8 February 2001*." The draft

190 Transcript of Mr Mark Conlan's evidence given to the Committee on July 4 2000, p. 2.

191 Mr Douglas Solomon's written submission tabled during the hearing on October 5 2000, p. 9.

192 Transcript of Mr Jeffrey Herbert's evidence given to the Committee on September 28 2000, pp. 5-9.

minutes show that during the three-month period until February 8 2001, restrictions were placed on Mr Fermanis disallowing him from soliciting private funds. However, no supervisor has been appointed.

8.12 The Committee was not able to satisfactorily ascertain why supervisors have not been appointed to other failed mortgage brokers such as Blackburne & Dixon and Leon K Jamieson and Associates.

Submission from Ms Penny Searle

8.13 The Committee received a subsequent submission from Ms Penny Searle dated November 3 2000, attached as Appendix 5, which outlined her continuing concerns with the administration and regulation of the finance broking industry in Western Australia. This submission contained serious allegations that there were still ongoing problems in the finance broking industry, even under the *Managed Investments Act 1998* (Cwth) and that she had raised these matters and offered documented evidence to ASIC, and felt a sense of *déjà vu* when advised that ASIC has limited resources and her request for an investigation must be made by a formal written submission to the Regional Commissioner.

8.14 The Committee was not able to investigate the matters raised in Ms Penny Searle's submission as it was received late in Committee deliberations. The allegations contained in the submission are of great concern and the Committee is of the view that they need urgent investigation.

CHAPTER 9
LEGAL REDRESS

LEGAL REDRESS

9.1 Several investors have set a representative action[193] in motion. The lawyer for these investors, Mr Douglas Solomon, indicated in his submission that in his opinion, the Board was established by the Act to protect lenders as is clear from the express reference to lenders and prospective lenders in s. 83(2)(b) of the Act. Mr Solomon stated in his submission that s. 48(3) protects lenders and prospective lenders not only at the time of negotiating loans but also in collecting interest after a loan is made.

9.2 Mr Solomon stated that the Board "…*owed a common law duty of care to a class of citizens comprising lenders, who have made loans arranged by finance brokers whose licences should have been cancelled, to take reasonable care to prevent reasonably foreseeable loss and damage.*"[194] He continued to say that while there is an immunity conferred by s. 87 of the Act, this immunity is provided only for members and officers of the Board for acts or omissions by a particular member or officer or by the Board. No immunity is provided for the Board itself as a body corporate.[195]

9.3 He stated that "[Section] *83(2)(b) makes it clear beyond argument that a licence could be cancelled by FBSB* [Finance Brokers Supervisory Board] *on account of conduct towards a lender or prospective lender. Furthermore, s. 83(2)(d) shows FBSB could act concerning the widest possible range of misconduct by a finance broker*."[196]

9.4 In his submission, Mr Solomon stated that in his opinion, the State of Western Australia would be liable for wrongs of the Board. He said that the functions, powers and duties under ss. 13, 14 and 82 of the Act are directly imposed by the Act.

9.5 Mr Solomon also stated that the supervisors have acted outside the powers set down by the Act, and as they have been appointed by the Board, the Government will be liable for any claims for damages against these "*officious intermeddlers*", either

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193 *Butterworths Australian Legal Dictionary,* p. 1013, described a "representative action" as a legal action where several parties to a court proceeding who have the same interest in the proceedings are represented by one of the parties. Three criteria must be satisfied: a common interest, a common grievance, and the relief sought must be beneficial to all parties represented by the party on the record.

194 Mr Douglas Solomon's submission to the Committee dated October 5 2000, p. 2.

195 Mr Douglas Solomon's submission to the Committee dated October 5 2000, p. 1.

196 Mr Douglas Solomon's submission to the Committee dated October 5 2000, p. 1.

through the fact that they are responsible for the Board, or alternatively under express indemnities given by their terms of appointment under s. 73 of the Act.

9.6 The Committee notes that Mr Conlan, in his role as supervisor, is not indemnified by the Board but is required to take out his own professional indemnity insurance.

9.7 The Committee took legal advice on avenues of legal redress for investors who have incurred losses against finance brokers. As well as canvassing whether there could be an action against the Government or the Board, the Committee also asked whether investors would have a reasonable prospect of success against the Board or the Government given the present state of the law.

9.8 Legal advice to the Committee suggested that a cause of action may exist in tort[197] for negligence against the Board. The claim would be based on the Board's failure to carry out its statutory duties concerning the supervision of finance brokers, and specifically, the investigation and follow up of complaints. However, an investor would face obstacles establishing the four substantive elements of the claim. These elements are that:

- the Board owed the investor a relevant duty of care;
- a breach of the duty of care occurred;
- the Board was negligent; and
- the breach caused the investor a foreseeable loss.

9.9 The Committee's legal advice also indicated that investors may face procedural difficulties such as time limits for the bringing of any action. Furthermore, any case brought by an investor is likely to be complex, costly and drawn out. A claim in negligence would raise relatively novel issues in Australian law, namely the liability of a public body in exercising regulatory powers over a particular area of commercial activity.

9.10 The Committee cannot comment on whether an action against the Board or the Government would be successful, however it acknowledges that there are serious obstacles to be overcome. The Committee raises the question that even if an investor has a reasonable prospect of success, the resources available to defend the action would be considerable, whereas an investor might have limited resources. Even though an investor may have a cause of action, legal redress may not realistically be available to that investor.

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197 A tort is a civil (as opposed to a criminal) wrong.

9.11 The Committee invited the Attorney General to provide a submission to the Committee on the question of whether any causes of action exist against the Crown, the Board, the Ministry, or any other entity. The Attorney General advised the Committee that "[a]*lthough one role of the Attorney General is to advise the Parliament, the principal role, as the first law officer of the Crown, is to provide advice to the Crown, not against it.*"[198]

LEGISLATION

9.12 Due to time and resource constraints, the Committee was not able to examine proposals for legislative change.

198 Letter to the Committee from Hon Peter Foss QC MLC, Attorney General; Minister for Justice, dated October 25 2000.

CHAPTER 10
CONCLUSIONS

INVESTORS

10.1 Investors have lost significant sums of money, which were, in some cases, their life savings. Many, particularly the elderly, will never have the opportunity to replace this lost capital. The losses have caused significant distress to many investors.

10.2 Centrelink's inflexibility in the treatment of failed investments as deemed income and assets is causing significant hardship and distress to investors.

FINANCE BROKERS

10.3 There needed to be collusion between finance brokers, borrowers, valuers, lawyers, auditors, and their associates, which enabled them to engage in the practices which ultimately caused the substantial losses that have occurred in the industry. Due to time and resource constraints, the Committee was not able to determine the full extent of the network of relationships between these key participants.

10.4 There were inadequate professional standards established or observed in the industry.

10.5 Some finance brokers targeted particular groups of people and established a relationship of trust which they ultimately abused.

10.6 Many of the finance brokers who dealt in pooled mortgages were able to give the appearance of being successful and competent financial managers over a number of years. Subsequently their business practices were found to be unsustainable.

10.7 There was a practice of creating new investment projects to obtain funds for borrowers to repay investors on previous projects which were financially unsound. It became increasingly necessary to inflate valuations to attract the required capital to pay out investors on existing projects. While this practice had been occurring for some time, it increased in the late 1990s and this caused a significant increase in the losses to investors.

BOARD

10.8 The Board was ineffective in the administration of the Act, the supervision of the industry and had a narrow view of its enforcement powers. Further the Board failed to make any genuine effort to rectify any real or perceived limitations in carrying out its functions.

10.9 The Board, particularly in recent years, failed to assert its authority as the regulator of the industry and also failed to act independently from the Ministry.

10.10 There was confusion within the Board and the Ministry as to their respective roles and responsibilities. This contributed to the failure to properly regulate the industry.

10.11 The actions of a number of the industry representatives on the Board are questionable and the Committee is concerned that this may have contributed to the failure to properly regulate the industry. However, due to time constraints the Committee was unable to fully examine this matter.

10.12 The Board did not adequately determine what constituted a "fit and proper" person to be licensed as a finance broker.

10.13 The Board was inconsistent in its treatment of non-compliant finance brokers.

10.14 The Board's supervision of trust accounts was totally inadequate and it failed to use the full powers of the Act.

10.15 The Board adopted procedures for hearings which led to significant and unnecessary delays.

10.16 The Board should have undertaken a greater role in supervising the investigations being conducted by its officers.

10.17 The Board did not take into consideration allegations or investigations against finance brokers when considering the renewal of their licences.

10.18 The Board, when it became aware of particular problems, for example, overvaluations, failed to issue any warnings to investors.

10.19 It is likely that the Board exceeded its legal authority in its contractual relationship with the supervisor for Rowena Nominees Pty Ltd.

10.20 The Board failed to fulfil its mission statement which is to "*…safeguard the public interest by influencing the standard of service delivery in the finance broking industry*".[199]

[199] Annual Report of the Board, 1998/1999, p. 2.

MINISTRY OF FAIR TRADING

10.21 The Ministry assumed responsibility for investigations but failed to conduct these with due diligence.

10.22 The Ministry's investigations were focussed on assisting the settlement of individual complaints rather than investigating whether the brokers were engaging in improper or illegal practices.

10.23 The Ministry's use of legal interpretations of the Act and Code limited its investigation of complaints.

10.24 The Board did not have sufficient resources to properly carry out its functions and the Ministry was aware of this over a period of years, but failed to provide the necessary level of resources.

10.25 Since the problems in the finance broking industry became public in late 1998, the Ministry's overall response has been inadequate and defensive.

10.26 Since the introduction of the *Managed Investments Act 1998* there has not been a clear delineation between the respective roles and responsibilities of the Board and ASIC.

10.27 Notwithstanding the complexity of the situation that the supervisor for Rowena Nominees Pty Ltd has been placed in, his actions have, with the support of the Ministry and Board, caused distress and significant legal costs for investors. This has come about because many investors feel that other investors' interests are being promoted at the expense of their own.

10.28 The Committee has been unable to ascertain the legal basis on which the supervisor has allowed investors to receive interest payments from money which has been paid into trust accounts when the question of who is entitled to the capital is still pending.

10.29 In the absence of a negotiated outcome, the courts will be the only avenue for determining issues of entitlement.

THE ACT

10.30 While it is arguable that the Act could be improved in some areas, it is not unworkable and it cannot be used as an excuse for the lack of action by those responsible for its administration.

FURTHER INQUIRY

10.31 The Committee is unanimous in its view that a further inquiry is required into the finance broking industry in Western Australia. Committee members are divided over whether this further inquiry should take the form of a Royal Commission, or alternatively, by the reappointment of the Gunning Inquiry to investigate the finance broking industry, with expanded terms of reference to allow it to investigate all matters. In particular, any further inquiry should examine the links between and roles played by finance brokers, borrowers, valuers, lawyers, auditors and their associates.

10.32 Hon Ray Halligan MLC and Hon Greg Smith MLC do not support the conclusion that the further inquiry takes the form of a Royal Commission, but agree with the remainder of paragraph 10.31.

CHAPTER 11
RECOMMENDATIONS

The Committee recommends that:

Recommendation 1: The Government appoints a further inquiry into the finance broking industry in Western Australia. This inquiry should be either a Royal Commission or the reappointment of the Gunning Inquiry with expanded terms of reference. The inquiry should examine in particular, the links between, and roles played by, finance brokers, borrowers, valuers, lawyers, auditors and their associates. Further, the inquiry should also consider and report on the actions required to prevent the losses which have occurred in the finance broking industry from recurring in either this industry or similar industries.

Note Conclusion 10.32, page 70.

Recommendation 2: If the Government fails to implement Recommendation No 1, a further parliamentary inquiry be appointed by the next Parliament.

Recommendation 3: The Government provides financial assistance to all investors involved in test cases which are seeking to determine the legal issues surrounding investors' entitlements.

Recommendation 4: The Government genuinely seeks to reach agreement with investors over compensation and assistance without expensive court action.

Recommendation 5: The educational requirements for the licensing of finance brokers be reviewed and rigorously applied.

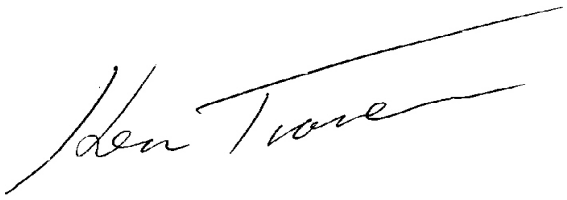
Recommendation 6: Education courses be developed to assist self-funded retirees to safely manage their funds.

Recommendation 7: The respective roles and responsibilities of ASIC and the Board be clarified as a matter of urgency.

Recommendation 8: The role of the supervisor and the nature of the relationship between the Board and the supervisor be clarified as a matter of urgency.

Recommendation 9: A list of finance brokers containing all relevant information be readily accessible to the public.

Recommendation 10: The allegations contained in the submission from Ms Penny Searle as outlined in paragraph 8.13 be urgently investigated.



Hon Ken Travers MLC **December 7 2000**

Chairman