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## **PROSECUTION, SURVEILLANCE AND DETERRENCE: THE ASC EXPERIENCE**

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Thank you for the opportunity to speak to you today. I think I can assume that most of you will have heard of the Australian Securities Commission through the media, perhaps in the course of being blamed for putting someone in jail or being blamed for not putting someone in jail. This too-tough/too-soft dichotomy is part of the business of being the national corporate regulator and is something we have learned to live with. Generally speaking, we take the view that if we are being criticised from both ends of the spectrum we are probably doing well.

In fact, the prosecution of corporate criminals through the courts is only one part of the ASC's activities. We also oversee the licensing system for financial advisers and dealers, supervise the work of auditors and liquidators, and scrutinise fundraising and takeover documents. Another major task is the keeping of the files: we collect information from all Australia's companies—about 760,000—and compile it onto a national electronic database, which is accessible to any member of the public for a nominal charge.

We do not see that these activities are distinct. They form a system of interactive parts for a method of regulation which protects the public, investors, shareholders, and creditors, without imposing undue burdens on the Australian business community. But there is a bit more to it than simply prescribing particular activities. We take the view that the Corporations Law, which we administer, not only lays down the mechanical rules by which business operates, but also provides the framework for behaviour which is ethical, responsible, and in keeping with community standards.

Individuals whose business-related activities contravene the Law and adversely affect others are therefore the subject of the enforcement actions for which the Law provides.

There will, unfortunately, probably always be a number of individuals who believe they are smarter and tougher than the Law. Sixty years ago, these were the people who were holding up banks because, as one smartly-dressed American gangster put it, "that's where the money is". Today that sort of thing is unfashionable, not to say dangerous. Those people see corporate scams as the next best thing. The best we can do is try to catch and imprison them.

In this sense, a successful prosecution is, in itself, useful: it takes the villain out of circulation and provides some measure of compensation—either psychological or, in the case of a civil action, material—for those wronged. But, more than this, it provides that key commodity: credibility—evidence of the will and the ability to take action where we see it as necessary. It is a way of saying that if you break the Law we will find you and punish you, and do our best to put you in jail for as long a time as the law will allow. In a word: deterrence.

This has an important effect on those in the business community who might grab the opportunity to break the Law for a quick gain if they see no downside. If a person who is considering a contravention opens the newspaper and sees a story of a financial adviser who cheated his clients going to jail, or a former high-flier being arrested and being brought to face a court, then there is a good chance that the "marginal " case will decide to stay on the right side of the line, after all.

Of course, the theory of deterrence only works if there is a good and ongoing record of prosecutions, dealing with a wide variety of offences, to support it. As it happens, the ASC's record is quite good. In major criminal cases completed between 1 July 1993 and 30 September, we had nineteen successful prosecutions, compared to five unsuccessful cases.

In minor cases for the same period, we were successful in 180 cases, compared to forty-four being discontinued.

For the financial year 1992-93, in major criminal matters completed we had thirty-four convictions and only three acquittals. In minor criminal matters, we had well over 600 convictions.

The ASC may also bring civil charges, designed to gain compensation for those who have been hurt by the contravention. In fact, compensation

actions are sometimes accorded a higher priority than criminal actions, although the two often run together.

In major civil actions completed during the July-September 1993 quarter, there were nine out of eleven cases where orders or settlements were made in the ASC's favour. Of the 216 minor civil cases, we were successful in 152 cases.

For the financial year 1992-93, we were successful in sixty out of ninety-three major cases, and in 512 out of 627 cases.

A constant irritation is the length of time that the very large cases require, both in the preparation of the brief that we provide to the Director of Public Prosecution, who runs the case on behalf of the Crown, and in the court system itself. Many of the large cases of the late 1980s are only now reaching the courts. To stand a good chance of success, there must be a great deal of documentation: the Linter trial now under way involves thirteen filing cabinets of documents—and that is just the amount used in the prosecution, not the investigation. Cases like Rothwells, Quintex, Independent Resources, and Bond Corporation have each involved the collection and collation of, quite literally, millions of documents. But climbing this mountain of paper is necessary if we are to prove the things we want to prove.

The cases we investigate involve quite different circumstances. However, I think it is fair to say that the constant thread running through our prosecution activities is the issue of directors' duties. The key sub-section of the Corporations Law in this regards is 232(2), which states:

An officer of a corporation shall at all times act honestly in the exercise of his or her powers and the discharge of the duties of his or her office.

The clearest cases of breach of the duty of honesty are those involving theft or other misuse of a company's property. But the position of directors also carries other responsibilities. Another crucial provision is sub-section 232(4), which states:

In the exercise of his or her powers and the discharge of his or her duties, an officer of a company must exercise the degree of care and diligence that a reasonable person in a like position in a corporation would exercise in the corporation's circumstances.

Prior to the beginning of the Corporations Law on 1 January 1991, the Companies Codes contained similar provisions, section 229.

The importance of directors' duties can be seen in the charges of some of what we call the "Big 16" list. This is the list of large cases which the ASC inherited from the 1980s, following a string of spectacular corporate collapses.

Most of the individuals involved in the "Big 16" cases have or are alleged to have breached director's duties, along with other offences. For example:

- Christopher Skase, former chairman of the Qintex Group, faces thirty-two counts of improper use of his position for personal gain, over an amount of \$7.4 million of shareholders' funds
- Brian Yuill, former managing director of the Spedley group of companies, was found guilty of misusing his position to authorise payments of \$2.8 million to his own companies, with the funds being repaid by Spedley Securities own funds
- Richard and Reuben Lew, former directors of Estate Mortgage Ltd, received jail sentences for breaches of directors duties in unauthorised funding arrangements
- Michael Fuller and Joseph Cummings, former directors of companies connected with the Independent Resources Limited Group, have been committed for trial for improper use of their position in arranging unauthorised credit facilities and loan guarantees
- Alan Bond, former chairman of Bond Corporation Holdings Ltd, faces charges of breaching his duties as an officer of the company and furnishing false information to other directors and the auditor
- Katy Boskowitz, a former director of Linter Group Ltd, is currently being tried for breaches of directors' duties over a deposit of \$220,000,000 for a fraudulent purpose; and arrest warrants have been issued for another former director, Abe Goldberg, who is currently living in Poland.

I might also note that there are other 'Big 16' cases where responsibility rests directly with the directors. Budget, for example, involves a misleading prospectus; the charges in Rothwells are related to fraudulent conduct. In both cases, it is role of the director that interests us.

Aside from the 'Big 16', most other cases accorded national priority status have involved, *inter alia*, breaches of directors duties. For instance:

- Robin Greenburg, former managing director of Western Women Management Pty Ltd and Western Women Financial Services Pty Ltd, was imprisoned on charges including misuse of her position as a director, relating to the misappropriation of over \$4 million of investors' funds
- charges have been laid against a number of directors of Pro-Image Studios, alleging negligence and breaches of director's duties in that a profit of almost \$20 million was recorded for the 1987/88 financial year when in

fact a loss of approximately \$2 million was disclosed in the management accounts: dividends of almost \$7 million were paid out by the company.

We have done our best to obtain maximum publicity when we have obtained convictions, especially those resulting in jail terms. The prospect of imprisonment, as opposed to a fine, provides the maximum possible deterrence.

We also see that if members of the public see that the regulator is active and successful, they are more likely to provide us with information in the form of complaints. We receive and scrutinise thousands of complaints, and check the substance of the complaint against the information we hold on our own files, as well as the corporate database. We have the power to require company documents, visit company premises, and conduct interviews. Obviously, a proportion of complaints are the result of a misunderstanding of the Law or of a particular situation, but by and large we see information provided by the public as an important resource in the regulatory process.

However, we recognise that, as the old saying goes, an ounce of prevention is worth a pound of cure. To this end, we have set up a number of programs aiming at identifying problems before they grow into crisis. We have established surveillance programs involving:

- dealers and investment advisers surveillance, which involves the detailed inspection of the records and activities of securities industry licensees
- financial reporting surveillance, which involves the checking of companies' financial statements for compliance with the Law and accounting standards
- fundraising documents vetting, which involves the checking of prospectuses
- takeover documents vetting, which includes the examination of independent experts reports
- fund managers and trustees surveillance; and
- the abuse of the corporate form.

This last program, "the abuse of the corporate form", may sound a little peculiar, and I would like to explain it in more detail. I see it as an area which will grow in importance, and which may correct the misconception that the ASC is concerned only with "the big end of town": the million-dollar scams, and glamour crooks, and headline cases. In fact, we are also very active in the smaller-business sector.

Essentially, "the abuse of the corporate form" program involves the targeting of individuals who use a company structure yet do not fulfil their

obligations as company officers, including the lodgement of correct and timely information with the ASC, and those who have been banned from acting as a director or officer of a company yet continue to do so. Section 229 of the Corporations Law states that bankrupt persons, and persons convicted of fraud or of a serious corporate offence cannot, without leave of the Court, be involved in the management of a company in any way.

We try to identify such prohibited people and remove them from management positions. This aspect of the program has been fairly successful: during 1992/93, there were prosecution actions in 17 cases and 253 instances of changes of office holders instigated by the ASC. The penalties facing prohibited people found to be involved in management are fairly stiff, involving up to a \$5,000 fine and/or a year in jail.

Another key element in this program involves the use of section 600 of the Law. This section gives the ASC the power to, if appropriate, issue orders banning an individual from being involved in the direct or indirect management of a company for a period (usually five years). The ASC takes the view that an individual who has been involved in two company collapses which paid less than 50c/\$1 to creditors upon liquidation should be called upon to show cause why they should not be banned.

I emphasise here that we are not after honest people who are simply the victims of recession or bad luck, but those who set up companies as a scam, obtaining credit and running up bills while paying themselves handsome salaries. When the company is wound up as insolvent, creditors and employees can be badly burned. The insult sometimes added to the injury is when the same people start up another company a few doors down - or even in the same premises, with equipment purchased from the previous company - and begin the process again.

We believe we are slowly making inroads into this problem, which seems to be largely located in the small-business sector. In 1992/93, the ASC issued 218 notices to show cause, resulting in 81 disqualifications.

The section 600 program also involves a public register of people banned by the ASC (or by the ASC's predecessors under previous comparable laws). This list of names, which includes the period of disqualification, is available from any ASC Business Centre. At present, there are about 300 people on the list of disqualified persons. (The register only contains the names of people disqualified by the ASC under section 600, not by reason of bankruptcy or fraud convictions.)

As I have said, the ASC is an organisation that covers a lot of ground. I hope that I have illustrated some of our work directed towards prosecution, surveillance and deterrence. The ASC is still a young organisation, having begun operation only in 1991. But I believe we have made a difference, and have established a substantial presence in the business community. As the 'Big 16' cases are wound up, we plan to allocate more resources to surveillance activities. There will always be a role for investigation and prosecution work, but we will be pleased if we can reduce the number of persons who seriously contravene the Corporations Law to the minimum - the hard core, for want of a better term. There is obviously a fair way to go, but we feel we are making steady progress.