

CORRECTED VERSION

LAW REFORM COMMITTEE

Inquiry into property investment

Melbourne place — 12 November 2007

Members

Mr C. Brooks

Mr R. Clark

Mr L. Donnellan

Mr M. Foley

Mrs J. Kronberg

Mr E. O'Donohue

Mr J. Scheffer

Chair: Mr J. Scheffer

Deputy Chair: Mr R. Clark

Staff

Executive Officer: Ms K. Riseley

Research Officers: Ms K. Buchanan and Ms S. Brent

Committee Administration Officer: Ms H. Ross-Soden

Witnesses

Mr M. Hayes, Commercial Law Section, and

Ms K. Cheng, Property and Environmental Law Section, Law Institute of Victoria.

The CHAIR — Thank you, Michael Hayes and Karen Cheng, for coming to speak to the Committee. There are a couple of preliminaries. The proceedings here are subject to the Parliamentary Committees Act, which means that parliamentary privilege is extended to both of you, but it is not extended to you if you leave the building or go outside the confines of this hearing, so that is important to note. Hansard reporters are taking down all our words throughout the discussion. A transcript will be sent to you shortly, and you are free to make any changes that you think make it more accurate, but you cannot change the meaning of it. Without further ado, we have just on half an hour. We will give you however much time you want to talk to us. I suppose you could speak to the submission that we received from you, which I believe is a copy of what you sent to the Commonwealth Joint Committee in 2005. Thank you for sending that along. Then we will have a bit of a discussion about some of the things you want to follow up. It is over to you.

Mr HAYES — Thank you, Chair. Firstly, my background is that of a commercial lawyer. I am the Institute's commercial lawyer and principally deal with commercial and taxation issues. Karen Cheng is our property and environmental lawyer.

We substantially, I guess, stand by our submission that went to the previous inquiry. From here I think it is probably pertinent to give you an opportunity, once we have spoken a little bit, to hear about where we see the evolution of these proposals as they stand now existing for 2007 and beyond. There is perhaps a feeling amongst our membership, particularly the ones I have had the most feedback from — that is, my 4000-odd commercial members; they are commercial, and most of them are specialists in their various commercial law fields — that we need to tread a little carefully with any proposed regulation of this industry for a number of reasons. Firstly, we would like to see it achieved with some sort of surgical precision, moreover to ensure the target that we are aiming for is managed and that we do not inadvertently stifle market dynamics and perhaps regulate areas in the market that are not adequately suited right now to any cumbersome regulation, because they themselves have a self-regulatory mechanism that seems to work quite well.

There are terms that are used in our previous submission, like 'inflated property prices'. Often that is a term that regulators should be mindful of, because it can be a subjective term and the equation mechanics of that are often best regulated by the market itself, as opposed to us intervening and attempting to deem a valuation on a property. But we are mindful of the need to ensure that the so-called spruikers, those that we have seen the market adequately manage through the processes of the information and, of course, the intervention of regulatory authorities. Those authorities, particularly the ACCC, have dealt with most rather effectively. Although I do not want to speak out of school here, I think one that comes to most people's minds is the Henry Kaye example.

There is a need to ensure there is a statutory intervention to protect people, but I think that is right now one that could be adequately harmonised with the Trade Practices Act and existing state legislation that protects consumers against misinformation. Whether there is a need for a whole new Act is something yet to be fully worked through, and no doubt this Committee will have some view on that. To the extent that you can adequately protect people 100 per cent of the time from making decisions in the property market or investment decisions, I do not think that is realistic. There is a role for the market to determine its proper balance, and I guess there is also a real need to ensure that people are encouraged to seek professional advice, but not nannied to the point where it is an extra cost to those people, through statutory necessity, if they do not elect to exercise that right.

But aside from that, I think you are familiar with our position. I would say our position is evolving, as market dynamics do. We need to be mindful that any statutory imposition needs to take into account the changing nature of the property market, and the changing and increasingly complicated methods of communication and marketing that are being used, because they are not static and often legislation is a little slower to react. I now pass over to Karen Cheng on that basis and perhaps she could perhaps offer a comment from her perspective and then we will allow you to ask us any questions you may have.

Ms CHENG — As a representative of the Property and Environmental Law Section of the Law Institute of Victoria, I have invited comments from my members but have not received anything conclusive from them as Michael did. Certainly I am inclined to agree with what Michael has said, but ultimately I think the LIV stands by what is contained in the submission — that there may be scope for regulation, but it has to be carefully drafted. The term Michael used was 'with surgical precision'. It is mainly to ensure that the interests of bona fide property developers are not prejudiced. That would really be my statement about it.

Mr FOLEY — Having listened to Michael’s presentation here and having read Michael Brett Young’s ‘Risky business’ editorial, I detect they are perhaps not on the same page there. Perhaps this is my reading of it, and I take you to a point. Michael Brett Young makes a number of comments about aggressive investor schemes, target publics, unconscionable behaviour, inflated prices, lack of regulation and so on, but he finishes by saying lawyers need to maintain the highest integrity and:

... it is also important that a coordinated regulatory regime be implemented to address deficiencies existing in the regulation of equity release products and the aggressive property promotion industry.

Does that line up with what the Commercial Law Section necessarily wants?

Mr HAYES — I do not think they are inconsistent, but Karen is certainly a little bit more familiar with that than I am.

Ms CHENG — Yes.

Mr HAYES — But I will come back to it once she has spoken to it.

Ms CHENG — I worked with Mike Brett Young on his paper for that month. I suppose we did draw quite extensively on what our previous position was in our 2005 submission to the Commonwealth inquiry. We considered the ‘how to become a millionaire’ property investment schemes in that particular column and also the increasing area of providing advice on equity release products, or equity products such as the reverse mortgages and whatnot. Ultimately the LIV’s view is as contained in its earlier submission, but we are at pains to say it is evolving, and all the points that Michael Hayes made previously stand insofar as it is a very static area, so any legislation has to be very carefully drafted in that regard.

Mr HAYES — We represent a broad range of membership, and none of them agree. I have everyone on the spectrum from arch conservatives to people who want everything regulated.

Mr FOLEY — That is what happens when you let plaintiff lawyers run an organisation.

Mr HAYES — I guess what I am trying to do today is canvass the broad range of views. I do not want to leave you with the impression that we have got a fixed, non-evolutionary approach to this. Basically we need to react to the market dynamics and represent our client interests as encouragingly as possible without putting them off. I guess in any analysis you are always going to find a need to regulate in these sectors, because there are going to be victims of unscrupulous operators, but I think what we are arguing is that perhaps the balanced approach be applied, and no doubt this Committee will achieve that. As to some of the specific types of schemes, I am sure there is a strong argument, as our CEO alluded to, to regulate those pretty tightly. But I think we do not want to achieve a situation where we overregulate and we perhaps achieve a disincentive structure and inadvertently stifle good parts of the market operation that do not need to be regulated at this stage. I know in that article he refers quite specifically to some schemes, and I certainly do not have an issue with what was written there.

The CHAIR — Just to clarify on one of those points I do not think there is a big distance between where we are coming from and what you are saying in that the terms of reference do say quite clearly in paragraph (a) that we have to look at ‘how best to control the exploitation of Victorians in the context of keeping the burden on business as low as possible’. So there is clearly an eye to making sure that whatever we might recommend as a Committee in relation to legislative or regulatory changes that that would be not detrimental to the market or to the way that people operate businesses. So I do not think there is a disagreement about that.

Mr HAYES — Sure.

The CHAIR — But I guess it is fair to say, not that we are having a debate about this, that our primary concern is to look at Victorian consumers who are experiencing detriment and to try to get some sense of quantification around that and some sense of impact and then see what we can do that appropriately addresses that without turning everything upside down or indeed introducing new legislation. As you said, there may be some small modifications that might assist them. That is really where our orientation is. You talked about your membership. Earlier witnesses we have had have listed lawyers as one of the professions that give advice to people about property investment, and we just wondered whether you as an Institute have undertaken any research or whether you have got any views on the extent of the number of lawyers who either provide investment advice about property or who in fact are involved in marketing investment properties.

Mr HAYES — The Commercial Section would be more likely to have that jurisdiction, and of the 4000-odd members we represent in that area it is highly — and this is anecdotal, mind you; there is no actuarial data at this stage —

The CHAIR — So you have not done the research or anything?

Mr HAYES — Not at this stage. We are doing a lot with taxation right now. I have been with the institute near enough to six months now, and one of my self-imposed KPIs is to make sure we start tabulating data on these types of things. Tax is my highest priority because of the complexity and, of course, propensity for high risk claims. In relation to the issue of who does it, it would be fair to say that most commercial lawyers would be called upon to give advice on schemes like this, whether they be directly related to the client's personal wealth/private wealth management or particularly and increasingly superannuation advice. As for the numbers, no, I cannot give you a mathematical computation, but certainly I can say to you that the overwhelming majority would be called upon to do it. I am a practitioner, and I have done it all my career. I do not think I would be any different to anyone else.

The CHAIR — Do the regulations that apply to the legal profession deal with lawyers' tendering of property investment advice? Are there constraints and frameworks there?

Mr HAYES — There are, absolutely. The Legal Profession Act, which I am intimately involved with as far as developing guidelines for in different other areas, regulates tightly our profession. It is arguably one of probably the most stringently regulated professions in the 21st century you are likely to find in this country. Practitioners ethically are not permitted where there is a conflict of interest to get involved in this sort of stuff. If they do, they have got to declare that interest and get the parties to sign off on it, to approve any involvement. You would probably be familiar with the provisions in the Estate Agents Act — I think it is 5A from recollection — that provide authority for lawyers to transact property, but I do not think there is a provision in there that deals specifically with the marketing consent or marketing issues. So there is always an involvement of commercial lawyers in property transactions as part of their day-to-day business. It is unavoidable.

The CHAIR — Yes, involvement in transactions is different from providing property investment advice, is it not. We all use lawyers all the time for — —

Mr HAYES — Yes. Could I ask you then what you consider to be the type of the advice you are alluding to?

The CHAIR — If a person has funds and they wish to invest them — and we have heard many witnesses talk about the Australian love affair with property investment as being the preferred investment for a whole set of reasons and that it has been difficult to persuade them that other kinds of investments might be more to their advantage, but given that historical situation, then advice around property investment would be where they are told that this particular property is a good buy and you will maximise your return on it over a period of time — it would be that related to a particular property or properties.

Mr HAYES — Profit profiling, I think you are alluding to, or those types of things would be something that members would have to be careful advising on because if they are not an accredited financial adviser, then they would not be able to do it. But if there were an obvious risk in a transaction or contractual defect of some significance, or any significance, they would be obligated to advise on that and caution against it.

Ms CHENG — Our role as lawyers is basically to advise of the risks in any potential investments or transactions from a legal perspective and from there our clients make decisions about whether or not to proceed. Insofar as to whether it is a sound financial investment, if there are no legal consequences we are technically not supposed to provide advice, I believe. We would be encouraging our members not to engage in providing financial advice about the soundness of an investment.

The CHAIR — On property investment — I am not clear — you are saying that your advice is that lawyers should not or do not?

Mr FOLEY — Unless they are registered as financial advisers.

Ms CHENG — Say, for instance, if there are some clear adverse legal consequences or in the context of a mortgage, we would be providing advice about the legal consequences of a mortgage and what happens if you

default, but insofar as buying into a particular suburb over another suburb, or whether one particular purchase is more appropriate or a 'better investment' than another, then we would not technically be providing that advice.

Mr BROOKS — It has been put to the Committee by other people that there should be a separation — the lawyer acting for a seller should be totally independent of a lawyer acting for a buyer, so I think there was a case in Queensland, for example. I was wondering what the LIV's view on that would be.

Ms CHENG — There are laws in respect of that.

Mr HAYES — You are talking about a practitioner involved in a transaction of the one asset, are you?

Mr BROOKS — Yes.

Mr HAYES — They are not allowed to do that.

Mr BROOKS — In Victoria?

Mr HAYES — Yes, absolutely. The Act prohibits it. You have to get consent from the parties. It is unlawful to act for buyer and vendor in those situations.

Mr FOLEY — It was not so much that, was it? The declaration as to if a lawyer is acting for a property developer, financial adviser or somebody else — —

Mr BROOKS — Any party connected with the property.

Mr FOLEY — Should they be required to declare who they are working for as part of the process?

Ms CHENG — Say, for instance, if you have a developer — —

Mr FOLEY — So it might be hands several parts away from the actual transaction.

Ms CHENG — Just to clarify, if you have a developer and purchaser is interested in buying an apartment in a particular development and the developer suggests a particular law firm as the conveyancer or solicitor for the transaction?

Mr FOLEY — For instance.

Ms CHENG — Okay. We actually have not been able to obtain feedback from our member practitioners in relation to that. From a personal perspective I think there may be some merit in that, but speaking for the Law Institute of Victoria this is something we would need to explore in greater detail if you would like to take it further.

Mr FOLEY — You might like to have a look at the 2000 Queensland legislation and get the Law Institute's view on it.

Mr HAYES — I am familiar with it. Certainly our Act has broad-ranging jurisdiction over ethical behaviour. There would arguably be a case where a practitioner had knowledge perhaps of over-inflated pricing and did not intervene to perhaps withdraw themselves from the transaction. Is that what you are alluding to — that there is perhaps a conflict?

Mr BROOKS — That is more about separating those two sets of advice completely or separating the advice to the buyers completely from anyone.

Mr HAYES — That tends to lend itself more to the conflict equation. The minute there is an identifiable conflict or a perceived conflict, and it is quite often subjective and it is up to the practitioner to call it, they are really obligated to declare and withdraw or get consent. It is likely to be impossible to get consent from purchasers in the broader market.

Mr FOLEY — Have there been any examples of the Law Institute taking action against members in property-related transactions as lawyers as opposed to anything else?

Mr HAYES — I could not answer that now. Karen might have something on it

Ms CHENG — I am also not in a position to answer that now. We can certainly make inquiries with the relevant department in the law institute and if the information is able to be made public, we can certainly get back to you on that.

Mr FOLEY — There have been lots of accusations in these hearings. I am sure they are not members of the Law Institute, but they are people who perhaps are not model corporate citizens.

The CHAIR — What is the procedure that is laid out? What are the steps a client would follow to do that?

Ms CHENG — There is the legal services ombudsman and a dedicated committee which handles these types of complaints. If there is a complaint made, it is appropriately actioned.

The CHAIR — Is the Ombudsman different from the Legal Services Commissioner?

Mr FOLEY — One became the other. The Ombudsman is now the Commissioner.

Mr HAYES — There is an appellant line. You are probably aware there are a number of statutory agencies that have some jurisdiction in the regulation of practitioners' conduct. The Legal Services Board has a delegate; the Law Institute in certain respects; the Ombudsman sits outside that; and the Legal Practitioners Liability Committee deals more with the mechanical aspects of a claim against a practitioner.

Ms CHENG — That is correct, though; the Commissioner is the one who handles these investigations.

The CHAIR — So a person who was involved in receiving property advice from a lawyer of some sort and felt they had not been dealt with properly and felt themselves aggrieved, they would go to the Commissioner.

Ms CHENG — Yes, I believe that to be the case and then it would be appropriately actioned. There is an arm of the Law Institute of Victoria which considers these professional standards complaints and the like.

The CHAIR — We could perhaps follow up with you to get some data what that looks like.

Ms CHENG — Yes, certainly and if the information can be made public, I would be happy to disclose it.

The CHAIR — Could I also ask you about the legal profession's fidelity fund. Do you know about that?

Ms CHENG — I am not entirely familiar with the procedures.

The CHAIR — Maybe we need to follow up with that as well.

Mr HAYES — What would you like to know?

The CHAIR — This question relates to the fact that if the government did decide to introduce licensing for people who are providing property investment advice, what do you think the impact of that would be on lawyers who provide that advice? I know that that is a bit contingent on the previous answer, but I ask you to have a go at it anyway.

Mr HAYES — Really the scope of what you are intending is something that I would have to explore a bit more fully. I do not want to fob you off.

The CHAIR — No, I understand.

Mr HAYES — But the gist is that our members deal in the most minute detail on everything, and if I was to go with them with something as broad as, 'What are you doing about regulating?', I would be in trouble, I think.

The CHAIR — Sure. Others have not had quite the same hesitation in responding. The other thing I want to ask you is that in your submission that went to the Commonwealth you talked about a consumer information campaign in terms of the things you think should be done, referring to a consumer information campaign coupled with a central bureau providing information and advice that would be an essential supplement to the proposals. As to a consumer information campaign, one of the issues that has come up all the way through these hearings is the importance of consumers knowing and understanding what is involved. Can you background some of the thinking around that?

Mr HAYES — Karen would probably be better on the education stuff.

Ms CHENG — I was not a party to this particular submission, but I do note that the LIV did make that particular comment. Insofar as the specifics of what the information campaign would entail, it is obviously designed to inform the general public and alert them to the potential issues that can arise and the remedies that may be available, and how to go about making educated decisions about property, consulting with financial advisers and obtaining independent valuations and the like. It is really just targeting the current issues that are prevalent in this particular area and designing a campaign that is intended to address some of the shortcomings and risks for consumers and potential remedies, or the remedies that are available.

The CHAIR — The last thing, unless other people have questions they want to raise, again relates to the 2005 submission to the Commonwealth and that the Law Institute was critical of the current legal avenues that are available to investors. Given that that is really part of what we are thinking about, what do you think the government should be doing to improve that?

Mr HAYES — Firstly, I think there is the issue of that resourcing of adequate education and the support of an educational framework. When I consider that most of my experience has really been involved in the sale of businesses, mergers and acquisitions and the overlay of due diligence and how thorough that is, I think we would be encouraging any requirement that compelled sellers to provide full disclosure on the product. That disclosure and the mechanical aspects of that disclosure would be something you would want to think through. But aside from the support of an educational framework, we would hope there would be some remedy structure available to purchasers who were misled. I was talking to Karen on the way up here; we are both intimately familiar with the Trade Practices Act and the ACCC. Powers arguably exist; it is a matter of using and getting the resources to use those powers and perhaps piggybacking on the appropriate statutory agency and encouraging it to resource investigations, and prosecutions, I guess.

As to the need for a separate statutory instrument in Victoria, I do not think there is a position you would find from us that says there is not one, but we would want to see a bit more detail in the draft of the bill and I guess the surrounding rationale for that type of thing. In a nutshell, yes, an educational framework, a resourced educational framework, a compulsion to ensure that there is full and frank disclosure, and some sort of sanction for people who do not comply with the educational framework that is required.

The CHAIR — Thank you very much.

Mr HAYES — Thank you for the opportunity. We would be happy to be of any further assistance.

The CHAIR — You will receive a copy of the transcript and no doubt Susan and Kerryn will be in contact with you if there is anything we need by way of follow up.

Committee adjourned.