ROYAL COMMISSION INTO MISCONDUCT IN THE BANKING, SUPERANNUATION AND FINANCIAL SERVICES INDUSTRY

MODULE 5: SUPERANNUATION

SUBMISSIONS IN RESPONSE TO CLOSING SUBMISSIONS OF COUNSEL ASSISTING

FILED ON BEHALF OF THE IOOF ENTITIES[1]

INTRODUCTION

1 These submissions of IOOF are in response to the written closing submissions of Counsel Assisting dated 24 August 2018.[2]

2 As noted in the Closing Submissions,[3] Christopher Kelaher and Mark Oliver provided witness statements to the Commission on behalf of IOOF,[4] and both appeared before the Commission and were cross-examined.[5] In addition, a large number of documents were produced by IOOF in response to 40 Notices to Produce issued by the Commissioner.[6]

3 IOOF submits that none of the matters considered by the Commission and identified in the Closing Submissions supports a finding that IOOF may have breached s 52(2) of the SIS Act, or engaged in conduct falling below community standards and expectations.

ISSUES ADDRESSED

4 The Closing Submissions raise the following issues which are addressed in these submissions:

Issue 1: whether Questor "*may have breached s 52(2)(c) of the SIS Act by reducing distributions to unaffected members of the TPS, using the general reserve (an asset of the Fund) to compensate those members, and refusing to replenish the general reserve*";[7]

Issue 2: whether Questor may have breached s 52(2)(d) of the SIS Act by:

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[1] Being IOOF Holdings Limited (**IOOF Holdings**), Questor Financial Services Pty Ltd (**Questor**) and IOOF Investment Management Limited (**IIML**) (together, **IOOF**).

[2] The written submissions of Counsel Assisting will be referred to below as the **Closing Submissions**. The acronyms used in the Closing Submissions are adopted in these submissions.

[3] Closing Submissions at [180].

[4] Mr Kelaher provided two Witness Statements, each dated 26 July 2018, being Rubric 5-58 (the **Questor Statement**), which is Exhibit 5.116 (with its annexures), and Rubric 5-19 (the **IIML Statement**), which is Exhibit 5.115 (with its annexures). Mr Oliver provided one Witness Statement dated 26 July 2018, being Rubric 5-38 (the **Oliver Statement**), which is Exhibit 5.99 (with its annexures).

[5] Mr Oliver attended on 9 and 10 August 2018 pursuant to a Summons dated 1 August 2018 (Exhibit 5.98), and Mr Kelaher attended on 10 August 2018 pursuant to a Summons dated 30 July 2018 (Exhibit 5.114).

[6] NTP-513; NP-537; NP-546; NP-579; NP-612; NP-664; NP-723; NP-776; NP-810; NP-836; NP-848; NP-873; NP-888; NP-913; NP-937; NP-962; NP-967; NP-974; NP-975; NP-976; NP-983; NP-984; NP-998; NP-1025; NP-1047; NP-1048; NP-1063; NP-1064; PRIV-017; PRIV-018; PRIV-019; NP-1079; NP-1081; NP-1082; NP-1088; NP-1126; NP-1127; NP-1138; NP-1139; NP-1180.

[7] Closing Submissions at [228.1].

(i) "*Giving priority to the interests of IDPS-like members by wholly compensating them from the NCS settlement money, while partly compensating TPS members from the general reserve*"; and

(ii) "*Giving priority to the interests of Questor by compensating TPS members from the TPS general reserve and then refusing to replenish that reserve, rather than using Questor's own funds*".[8]

Issue 3: whether Questor may have engaged in misleading or deceptive conduct in breach of s 12DA of the ASIC Act by sending the letter to TPS members asserting they would receive compensation for a "*historical distribution error*";[9]

Issue 4: whether IIML may have breached s 52(2)(c) of the SIS Act, and prioritised its own interests over the interests of superannuation members in breach of s 52(2)(d) of the SIS Act, by "*not applying the new IES pricing to existing members who would be better off, particularly in circumstances in which IIML considered it was unlikely that members would move of their own accord*";[10]

Issue 5: whether IIML may have engaged in conduct falling below community standards and expectations in relation to representations made to APRA in its 19 April 2017 letter;[11] and

Issue 6: whether "*the continued failure of IIML and IOOF Holdings to understand their duties to superannuation members, and to take steps to properly recognise and manage conflicts of interest, constitutes conduct falling below community standards and expectations*."[12]

ISSUE 1

Reducing distributions to unaffected members of the TPS

5 IOOF submits that it is not open to the Commissioner to find that Questor may have breached s 52(2)(c) of the SIS Act by reducing distributions to "*unaffected members of the TPS*".[13] This is for the following reasons (each of which is put in the alternative).

6 *First*, all members subject to reduced distributions were made whole (including as to interest) via the compensation and remediation plan implemented by Questor.

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[8] Closing Submissions at [228.2].

[9] Closing Submissions at [228.3].

[10] Closing Submissions at [229.1].

[11] Closing Submissions at [229.2].

[12] Closing Submissions at [230].

[13] By unaffected members, IOOF assumes that this is a reference to "new members (who joined the CMT after the over-distribution) and existing members who made additional contributions to the CMT": Closing Submissions at [211].

7 Apart from the issue concerning the use of the general reserve, this fact is not in dispute. In particular, Mr Kelaher gave the following evidence under cross examination:[14]

> MR HODGE: That is, ultimately, the members were put back into the position they should have been?---Yes, that's the ultimate test and that was the overarching belief throughout the transaction that was caused by a third party custodian.

8 It follows that any findings of the Commission as to Issue 1 must pay due regard to the fact that Questor ensured that all members were put back into the financial position that would have existed had the original over distribution error not occurred.[15] This is not a minor point of peripheral significance. It must be the central and primary consideration when assessing whether or not the best interests of members have been properly accounted for and prioritised.[16]

9 *Secondly*, this issue concerned a reduction in distributions from the CMT to its institutional investors, being the IDPS-like and the TPS.[17] Accordingly, the reduction in distributions was undertaken by Questor as RE of the CMT.[18] It follows that s 52(2)(c) of the SIS Act has no application to the reduction in distributions. This is because the provision only applies to the performance of the trustee's duties and the exercise of the trustee's powers (the trustee in this instance being Questor as RSE of the TPS). It follows that the submission that it is open to the Commissioner to find that the reduction in distributions may have breached s 52(2)(c) of the SIS Act must be rejected.[19]

10 *Thirdly*, the unstated assumption behind Issue 1 is that distributions could have been reduced without impacting unaffected members of the TPS. However, as noted by Mr Kelaher in the Questor Statement,[20] this was not possible, as a diluted distribution could only be applied across all units, and not at a member level. Mr Kelaher was not challenged on this point in cross-examination, and there no basis upon which his evidence on this issue could be doubted.

11 *Fourthly*, the duty contained in s 52(2)(c) of the SIS Act is a duty to act in the best interests of the beneficiaries *as a whole*. It does not follow that, because some members might be differently affected by a decision of a trustee, the trustee will have breached its obligations to perform its duties and exercise its powers in the best

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[14] Transcript, 10 August 2018, Christopher Kelaher, P-4608.

[15] Which was confirmed by Ernst & Young in its independent report prepared for Questor (**EY Report**) at tab 5 of Exhibit CK-2, IFL.0006.0003.4008 at .4111.

[16] As for the proposition that members have not been made whole because Questor used the general reserve to compensate them (eg Transcript, 10 August 2018, Christopher Kelaher, P-4652), see paragraphs 16 to 22 below.

[17] Questor Statement at [50(a)].

[18] Closing Submissions at [207].

[19] Closing Submissions at [228.1].

[20] Questor Statement at [55(g)].

interests of the beneficiaries. As for the interests of the beneficiaries as a whole, it has been held by the Victorian Court of Appeal that:[21]

> [T]he true view is, not that the Court is to be satisfied that the transaction is expedient or advantageous in the interest of each and every beneficiary considered separately, but that the Court must take into consideration the interests of all the beneficiaries, and, upon a broad and commonsense view of the matter, must be able to conclude that the proposed transaction can fairly be said to be expedient for the trust as a whole.

12 It is submitted that, applying this test, Questor has plainly satisfied its duty to act in the best interests of the beneficiaries as a whole. This is for the following reasons:

(a) the initial over-distribution from the CMT to its institutional investors (the IDPS-like and the TPS) resulted from an error by the custodian (**NCS**) in calculating returns to members;

(b) the only practicable way to restore the deficiency to the CMT was to claw back the over-distributions by way of diluted quarterly distributions by reducing the cash rate within the Fund and, once the over-distribution had been recovered, to then reconcile the under and over-payments to individual members (in accordance with the methodology reviewed and approved by Ernst & Young in the EY Report). The alternative would have been to commence recovery actions against each and every member of the TPS and investor in the IDPS-like who had received an over-distribution. This would have been inefficient, costly, and not in the interests of members as a whole;

(c) there was also a practical inability to apply the dilution of distributions only to members of the TPS who received the initial over-distribution. It was not an available alternative to reduce distributions only to affected members of the TPS, as distributions are made by the CMT to Questor as trustee/RSE of the TPS, and are then passed onto members of the TPS; [22]

(d) the methodology and timing for the payment of compensation can fairly be said to be expedient for the trust as a whole. In particular, as stated in an IOOF Memorandum dated 18 August 2016 sent to APRA:[23]

> Questor as RE made the payment to IDPS-like investors first because there were delays in applying compensation to TPS Super Fund members while the RSEL resolved complex tax issues. The RSEL needed to carefully consider the implications of paying compensation to members where that compensation might be considered to be a concessional contribution.[8] The process of paying out super members (mainly closed accounts) is also a more onerous, time consuming and manual process than for paying out IDPS-like investors.

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[21] *Royal Melbourne Hospital v Equity Trustees Ltd* (2007) 18 VR 469 at 469 [166] per Bell AJA, citing *Re Dawson (deceased)* [1959] NZLR 1360. This case was decided in the context of the court's expediency jurisdiction, which concerns the ability of a court to confer investment powers upon a trustee where it is expedient to do so.

[22] See above at paragraph 10.

[23] Exhibit 5.129 (IOOF Memorandum dated 18 August 2016, IFL.0006.0003.4075 at .4079) referred to in cross-examination of Mr Kelaher at Transcript P-4652 at line 35.

> Questor as RE of the CMT did not consider it prudent to delay payment, or make partial payments to IDPS-like investors given its legal and fiduciary duties to those investors in its capacity as RE … Questor as RE of the CMT did not believe TPS Super Fund members would be disadvantaged if the IDPS-like investors were paid out while outstanding tax issues for TPS Super Fund members were being resolved.

8. Tax advice confirmed that where a member is compensated by the reserve to an amount in excess of 5% of the members' account balance, this would be classified as a concessional contribution. Therefore, the RSEL concluded that those with compensation above 5% would be compensated by the NCS settlement and those below would be compensated by the NCS settlement and reserves. This meant that members were not adversely effected by an increase in their concessional contributions.

(e) Mr Kelaher was cross-examined on other aspects of this Memorandum,[24] but the accuracy of the above statements was not the subject of any challenge. In addition, Mr Kelaher's Questor Statement referred to the need to resolve these tax issues before finalising compensation payments to members of the TPS, including by awaiting the outcome of a private ruling from the ATO, allowing Questor to treat the compensation payments as non-concessional contributions;[25] and

(f) all members were fully compensated, and suffered no loss.

13 Accordingly, in light of the above, IOOF submits that the compensation and remediation plan can fairly be said to be expedient for the trust as a whole.

Use of the general reserve and refusal to replenish the general reserve

14 The Closing Submissions assert that it is open to the Commissioner to find that Questor may have breached s 52(2)(c) of the SIS Act by using the TPS general reserve to compensate members of the TPS and by refusing to replenish the general reserve.[26] For the reasons given below, IOOF submits that neither finding is open to the Commissioner.

15 In summary, IOOF submits that the use of the TPS general reserve to compensate TPS members for loss in the amount of $1.616 million[27] was a lawful and appropriate course of action to adopt in the circumstances (which included the original error by NCS, the compensation paid by NCS, the absence of any proper basis to assert a claim against any other entity for that loss, and the fact that any legal action to seek additional compensation would have been unlikely to result in any additional recovery, but would have resulted in the expenditure of legal costs).

Nature of the general reserve

16 The general reserve of the TPS is not allocated to specific accounts held by members.

[24] Transcript, 10 August 2018, Christopher Kelaher, P-4657.
[25] Questor Statement at [55(s)].
[26] Closing Submissions at [228.1].
[27] Questor Statement at [57(a)].

17 The amounts in the general reserve are not taken from the superannuation contributions of members or returns attributable to members, but rather comprise:

(a) asset/liability mismatches and historical unreconciled differences;
(b) unallocated bank or ATO interest;
(c) frozen investments from redemptions of members through financial hardship claims;
(d) timing differences associated with the allocation of distribution income to members;
(e) selling and tax accrual adjustments for investment holdings; and
(f) unallocated reserves/surpluses arising from successor fund transfers.[28]

Nature of a beneficiary's interest in the fund

18 The Closing Submissions refer to the general reserve as "an asset of the fund",[29] and also suggest that it is "an asset of the members".[30] These matters were put to Mr Kelaher in cross-examination, and his answer was that his understanding is that the general reserve is not an asset of the members, although he agreed that it is an asset of the trust.[31]

19 The fundamental issue is that, while members have a beneficial interest in the assets of the fund,[32] a member's interest depends upon the terms of the trust.[33] Specifically, cl 2.3 of the TPS Trust Deed provides that a member's beneficial interest does not entitle the member to:

(a) interfere with the rights or powers of the Trustee in its dealings with the Assets of the Fund;
(b) exercise any rights, powers or privileges in respect of any Assets of the Fund;
(c) require the transfer to the Member of any of the Assets of the Fund; or
(d) otherwise claim any interest in any particular part or Asset of the Fund.[34]

20 Thus, while members of the fund can be said to have a beneficial interest in the assets of the fund, including the general reserve, the extent of that right is determined by the terms of the TPS Trust Deed. Other than in the case where the fund is wound up, members cannot call for a distribution of amounts in the general reserve, and have no right to take any part of the general reserve with them should they exit the TPS.

21 The amounts contained in the general reserve, in accordance with the TPS Trust Deed, are to be used for:

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[28] Reserves Policy, 19 August 2013, IFL.0027.0001.0737 at .0750.
[29] Closing Submissions at [214], [228.1], and [713].
[30] Closing Submissions at [226].
[31] Transcript, 10 August 2018, Christopher Kelaher, P-4640. Mr Kelaher said that his understanding is that there is a distinction between these two concepts, but that he was not a trust expert and was not qualified to answer the question. See also Closing Submissions at [226].
[32] See The Portfolio Service Retirement Fund Trust Deed at cl 2.3, IFL.0027.0001.0139 at .0155.
[33] *CPT Custodian Pty Ltd v Commissioner of State Revenue* (2005) 224 CLR 98.
[34] See The Portfolio Service Retirement Fund Trust Deed at cl 2.3, IFL.0027.0001.0139 at .0155.

(a) meeting losses or expenses (including tax);

(b) transfers to a Contribution Account of a Member of a Personal Plan; and

(c) other purposes which the Trustee determines.[35]

22 Accordingly, whilst members may have a beneficial interest in the general reserve asset, the Trust Deed specifies that this does not entitle the member to require the transfer to them of any part of that asset or to otherwise claim any interest in the general reserve. That said, the trustee may (and here did) decide to use the general reserve to make a payment to particular members to compensate them for loss.

23 In these circumstances, it cannot be said that the use of the general reserve may have breached s 52(2)(c) of the SIS Act.

The obligation in s 52(2)(c) of the SIS Act and the decision to use the general reserve

24 The Closing Submissions assert that the use of the general reserve to compensate members "may have … breached s 52(2)(c) of the SIS Act".[36] However, no explanation is offered as to how the use of the general reserve by Questor might be said to result in a breach of s 52(2)(c) of the SIS Act. It does not follow from the mere fact that the general reserve was used to compensate members that the trustee has failed to perform its duties and exercise its powers in the best interests of the beneficiaries. Section 52(2)(c) did not expand the general law.[37]

25 To refer simply to the use by Questor of "an asset of the fund" as though that were the only relevant matter against which to assess any breach of duty is misconceived. Here, the trustee exercised its powers under the TPS Trust Deed to pay members compensation for loss from the general reserve, which was one of the stated purposes of the general reserve. Without more, this cannot amount to a breach of s 52(2)(c) of the SIS Act. The Closing Submissions do not explain how this otherwise legitimate use of the general reserve is transformed into a possible breach of the law simply because the general reserve is an asset of the fund.

26 Furthermore, the EY Report confirmed that the remediation calculations and methodology accorded with industry guidelines and practice and IOOF's internal policies, and that the remediation methodology "*materially returns investor balances to the financial position that would have existed had the error not occurred*".[38]

27 In addition, the decision whether or not to use the general reserve is an exercise of a discretionary power. Even in the context of s 52(2)(c), "*[t]he exercise of a discretion by a trustee will not be reviewed if the discretion is exercised in good faith upon real*

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[35] See The Portfolio Service Retirement Fund Trust Deed at cl 10.13, IFL.0027.0001.0139 at .0171.

[36] Closing Submissions at [228].

[37] *Commonwealth Bank Officers Superannuation Corp Pty Ltd v Beck* (2016) 334 ALR 692 at 719 [136]; *Manglicmot v Commonwealth Bank Officers Superannuation Corp Pty Ltd* (2011) 282 ALR 167 at 191 [121].

[38] See tab 5 of Ex. CK-2, IFL.0006.0003.4008 at .4111, referred to at [31] of the Questor Statement.

or genuine consideration and in accordance with the purposes for which the discretion was conferred."[39]

28 There was no challenge made during the hearings to Questor having exercised its discretionary powers under the TPS Trust Deed in good faith upon real or genuine consideration and in accordance with the purposes for which the discretion was conferred. It is submitted that no such challenge could properly have been made on the materials. Questor, in its capacity as trustee of the TPS, exercised this discretionary power for a proper purpose (to compensate the members) and with a "proper consideration"[40] as to whether or not it was in the best interests of members.

29 In particular, proper consideration was given to whether it was in the best interests of members to use the general reserve because Questor had determined (i) it was not responsible for the error; (ii) NCS was ultimately the party at fault;[41] and (iii) that if the general reserve was not used, given no other party had any liability for the error, there was no other source of compensation available.

30 The evidence available to the Commissioner does not provide a proper basis upon which to form the view that this determination by Questor was not made in good faith or in accordance with the purposes for which the discretion was conferred.

31 Whilst it would be appropriate for Questor to pay compensation out of its corporate funds for any loss caused by its own default, there is no basis upon which it could be said that Questor's acts or omission caused any such loss in the present case.

32 In particular, whilst "*it could be argued that Questor as responsible entity may have been able to provide a greater level of oversight in relation to NCSs calculations and distributions*",[42] this is plainly not an admission that Questor was arguably legally responsible for causing a loss.

33 Further, it was put to Mr Kelaher in cross-examination that this was something he might think was "*arguable*", to which he replied "*I think I've offered that with the benefit of hindsight you can reflect on these, but at the time no*."[43]

34 It follows that it cannot be said that Mr Kelaher has made any admission as to the potential legal liability of Questor as RE for the error made by NCS.[44]

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[39] *Commonwealth Bank Officers Superannuation Corp Pty Ltd v Beck* (2016) 334 ALR 692 at 719 [136].

[40] *Commonwealth Bank Officers Superannuation Corp Pty Ltd v Beck* (2016) 334 ALR 692 at 719 [137]-[139].

[41] Questor Statement at [52].

[42] Questor Statement at [52(a)]. Mr Kelaher was taken to this part of his statement in cross-examination: Transcript, 10 August 2018, Christopher Kelaher, P-4610. However, he was not taken to the remainder of that sub-paragraph, which importantly provided as follows: '*NCS was responsible for the accuracy of the calculations, as it was engaged to perform this role. As such, Questor as RE was entitled to rely on NCS in this respect. Further, there was no evidence that any increase in oversight by Questor as RE would have avoided NCS making the error*'.

[43] Transcript, 10 August 2018, Christopher Kelaher, P-4610.

[44] Cf *Dovuro Pty Ltd v Wilkins* (2003) 215 CLR 317 at 327 [25] per Gleeson CJ; [2003] HCA 51 ("*care that needs to be taken in identifying the precise significance of admissions…Common sense may dictate that they be used with caution by a fact-finder. And it is always necessary for the fact-finder to consider precisely what it is that is being admitted…The statement that the appellant '[failed] in its duty of care to inform growers as to the*

35 In any event, in circumstances where Questor had determined that it was not responsible for the error, it is not open on the available evidence to conclude that Questor "*failed to give proper consideration*"[45] to whether or not it was in the best interests of members of the TPS to compensate them from the general reserve.

36 It is, therefore, not open to the Commissioner to find that Questor as RSE breached s 52(2)(c) of the SIS Act by using the general reserve to compensate members. In order for such a finding to be open, it would be necessary for the Commissioner to find that Questor's conclusion that it was not at fault in causing the error was incorrect. It is submitted that no such finding is open. In any event, it is not clear that Questor as RSE would have breached s 52(2)(c) of the SIS Act merely because it was in error in arriving at the conclusion that it was not responsible. Moreover, the fact that Questor had identified itself as a possible source of compensation ought to be seen as *discharging*, and not disregarding, its statutory obligations.

ISSUE 2

Compensation of IDPS-like investors and TPS members

37 The Closing Submissions assert that it is open to the Commissioner to find that Questor may have breached s 52(2)(d) of the SIS Act by giving priority to the interests of the IDPS-like investors by wholly compensating them from the NCS settlement fund, while partly compensating TPS members from the general reserve.[46] For the reasons given below, this assertion must be rejected.

38 The assertion wrongly implies that it was possible to compensate the TPS members wholly from the NCS settlement fund (as opposed to partly from the general reserve).

39 NCS agreed to pay $1.565 million in compensation.[47] The total value of compensation required by the TPS was $2.775 million, plus an accrued interest component of $13,875 (a total of $2.789 million).[48] Assuming that Questor, in its capacity as RE of the CMT, gave 100% of the NCS compensation to the TPS, there would still have been a shortfall of $1.224 million.

40 In light of the above, the issue raised in the Closing Submissions in relation to s 52(2)(d) must be that Questor failed to prioritise the interests of the TPS members over the IDPS-like investors by not giving the TPS members 100% of the NCS settlement fund.

41 However, for the reasons set out above at paragraph 12(d), the methodology and timing for the payment of compensation as between members of the IDPS-like and

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presence of these weed seeds' cannot be an admission of law, and it is not useful as an admission of failure to comply with a legal standard of conduct. There is no evidence that the author of the statement knew the legal standard.").

[45] *Commonwealth Bank Officers Superannuation Corp Pty Ltd v Beck* (2016) 334 ALR 692 at 719 [137]-[139].

[46] Closing Submissions at [228.2].

[47] Closing Submissions at [212].

[48] Closing Submissions at [214]. See also IFL.0006.0003.4061.

members of the TPS appropriately prioritised members of the TPS and can fairly be said to be expedient for the trust as a whole.

42 Further, the real gravamen of the complaint appears to be that Questor used the general reserve to compensate members. It can hardly be said that the same allegation of a breach of s 52(2)(d) would be levelled at Questor if it had, as Counsel Assisting suggested, used its own money to compensate the members for the shortfall, notwithstanding that it was not responsible for the error. There would be no failure to give priority to the interests of members of the TPS because all members would have been compensated. If this is the true nature of the complaint then the proportions of the NCS settlement fund used to pay investors of the IDSP-like vis-à-vis members of the TPS are irrelevant. The issue turns upon whether the general reserve was an appropriate source of compensation, which for the reasons given above, it was.

Use of general reserve to compensate TPS members

43 IOOF rejects the suggestion that it is open to the Commissioner to find that Questor may have prioritised its own interests by compensating TPS members from the TPS general reserve and then refusing to replenish the general reserve. Accordingly, IOOF also rejects that it is open to the Commissioner to find that Questor may have breached s 52(2)(d) of the SIS Act. In this regard, IOOF also refers to paragraph 75 of these submissions and the subsequent transfer of these superannuation members to another IOOF superannuation fund and the material benefits obtained by these members in priority to IOOF shareholders.

44 For the reasons given above in relation to Issue 2, for a finding to be open that Questor may have prioritised its own interests by compensating members from the TPS general reserve, it is necessary for the Commissioner to find that:

(a) the use of the general reserve by Questor in the circumstances of this case was not lawful, which, for the reasons set out above at paragraphs 15 to 36, is not open; and

(b) Questor's conclusion that it was not at fault was incorrect. Such a finding is not open to the Commissioner for the reasons discussed at paragraphs 30 to 34.

ISSUE 3

45 IOOF rejects the assertion that it is open to the Commissioner to find that Questor may have engaged in misleading or deceptive conduct in breach of s 12DA of the ASIC Act by sending the letter to TPS members asserting they would receive compensation for a "historical distribution error."[49] The evidence demonstrates that the statements in the letter,[50] including the statement regarding a "*historical distribution error*", are true and, in any event, are not capable of being misleading. This is for the following reasons.

[49] Closing Submissions at [228.3].
[50] IFL.0029.0001.1164.

46 *First*, the evidence of Mr Kelaher was that the reference to a "*historical distribution error*" in the letter was a reference to the original error which caused the over-distribution, being the over-distribution of $6.16 million to unit holders in May 2009.[51] Indeed, there was no other distribution "error" involved in this matter. The other distribution, being the under-distribution was not an "error".[52] It formed part of Questor's deliberate remediation strategy following the over-distribution error. The reference in the letter therefore cannot be a reference to any event subsequent to the initial over-distribution. Having regard to this fact, everything which follows in the balance of the paragraph in the letter is true.

47 *Secondly*, neither the cross-examination nor the Closing Submissions sought to articulate how a recipient of the information contained in the letter could have been led into error. Such articulation is necessary before any finding could be made that Questor may have engaged in misleading or deceptive conduct in breach of s 12DA of the ASIC Act.

48 Although Mr Kelaher gave evidence that the reference to a "*historical distribution error*" was "*not precise*" and that "*it's potentially capable of being misleading*",[53] he was plainly referring to the imprecision in the reference to the "*distribution error*", in particular whether it referred to the initial over-distribution or the subsequent reduced distributions. This is clear from the way in which the cross-examination proceeded. In particular, the cross-examination appeared to wrongly assume that the reference to the "*distribution error*" was to the later reduced distributions, and when Mr Kelaher corrected that assumption, Counsel Assisting did not dispute Mr Kelaher's interpretation, and the following exchange occurred (in relation to the statement in the letter to the IDPS-like members):[54]

> I see. You think the historical distribution error that's being referred to there is the original error of over-distributing? ---I grant you, that – yes, it's – it's not precise. By "not precise", would you be prepared to accept that it is misleading?---Yes, it's capable of being misleading.

49 Mr Kelaher was then shown the same statement in the letter to members of the TPS and was simply asked "*And again, do you agree with me this statement is misleading?*" to which he responded "*Yes, it's potentially capable of misleading*."[55]

50 It is submitted that, fairly understood in context, Mr Kelaher's evidence on this point related to the imprecision in the letter regarding which "*distribution*" was being referred to. This imprecision could not form the basis for any finding of misleading or deceptive conduct in breach of s 12DA of the ASIC Act.

51 *Thirdly*, in any event, this statement by Mr Kelaher cannot form the basis of any conclusion that IOOF may have engaged in misleading or deceptive conduct. In

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[51] Transcript, 10 August 2018, Christopher Kelaher, P-4642 at lines 11-12.

[52] Closing Submissions at [217].

[53] Transcript, 10 August 2018, Christopher Kelaher, P-4642 at lines 15-18; Transcript, 10 August 2018, P-4643 at lines 36-37.

[54] Transcript, 10 August 2018, Christopher Kelaher, P-4642.

[55] Transcript, 10 August 2018, Christopher Kelaher, P-4642.

Dovuro Pty Ltd v Wilkins,[56] Gummow J held that, whilst a party may admit the facts from which a conclusion of law may then be drawn:

> Different questions arise where, as here, the suggested admission includes a conclusion which depends upon the application of a legal standard. In *Grey*, Glass JA considered an admission sought from a witness to the effect that he had assigned certain choses in action at law or in equity. His Honour said:
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> > "By extorting from a party an admission that he was negligent, or that he was not provoked, or that his grandfather possessed testamentary capacity, there is added to the record something which is, not merely of dubious value, but by definition valueless, owing to the witness' unfamiliarity with the standard governing his answer."
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> That reasoning, which in terms applies to the suggested "admission" by Dovuro, has been applied in cases arising under the Act. In *Eastern Express Pty Ltd v General Newspapers Pty Ltd,* a question arose as to whether certain statements amounted to an express admission of a proscribed purpose for the application of s 46 of the Act. Lockhart and Gummow JJ said on that subject:
>
> > …… In the case of alleged contraventions of s 52 of the Act, admissions by a trader in the course of cross-examination that his conduct was 'misleading' and 'deceptive' cannot be relied upon to usurp the task of the court to judge the legal quality of that conduct.

52 *Fourthly*, in any event, and notwithstanding the above, it is well settled that conduct is not misleading or deceptive simply because it may cause the recipient to be confused or to wonder about something.[57] The aim of the communication was to inform members, in a concise manner, that there had been an error and that they were being compensated. The fact that the explanation could have been more detailed or more precise does not make it misleading.

53 *Fifthly*, during the evidence given by Mr Kelaher, the central complaint from Counsel Assisting appeared to be that Questor had in fact made a deliberate decision to reduce the distributions. However, the Closing Submissions fail to say how the letter misrepresented that position.

54 In light of the above, IOOF submits that it would not be open to the Commissioner to make a finding that Questor may have engaged in misleading and deceptive conduct in breach of s 12DA of the ASIC Act by sending the letter to TPS members asserting that they would receive compensation for a "historical distribution error".

ISSUE 4

Application of new IES pricing

55 IOOF submits that it is not open for the Commissioner to find that IIML may have breached its obligations under ss 52(2)(c) and 55(2)(d) of the SIS Act by prioritising its own interests over the interests of its superannuation members by not applying the new IES pricing to existing members who would be better off. The evidence before the Commissioner demonstrates that IIML, consistently with its obligations in s 52(2) of the SIS Act, acted in the best interests of the beneficiaries of the fund *as a whole*[58]

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[56] (2003) 215 CLR 317 at 340-341 [70]-[71].

[57] *Parkdale Custom Built Furniture Pty Ltd v Puxu Pty Ltd* (1982) 149 CLR 191 at 198, 209; [1982] HCA 44.

[58] See paragraph 11 above.

and at no time prioritised its own interests over the interests of its beneficiaries. IOOF offers a number of reasons for this submission.

56 *First*, the new IES pricing was part of IOOF's broader "Evolve" strategy, being a significant investment in IOOF's administration systems. This strategy had three objectives:

(a) to "deliver lower fees to all members";

(b) to "minimise account erosion"; and

(c) to allow IIML, as trustee, to continue "to invest in the future growth and value enhancement of all members".[59]

57 Each of these objectives clearly demonstrates that the best interests of members were at the forefront of IIML's consideration when implementing changes to its IES pricing.

58 *Secondly*, if IIML had simply moved all of the existing members onto the new IES pricing this would have adversely affected the interests of the beneficiaries of the fund as:

(a) "some would be worse off";[60] and

(b) it would have compromised IIML's "ongoing approach to continuously improving services"[61] – it is an oversimplification simply to equate low fees with members' best interests. Any diminution in the range and quality of services to members flowing from a fee reduction must be taken into account assessing whether that reduction is in the members best interests – a factor IIML took into account in implementing the IES new pricing structure; and

(c) applying the new pricing to all members would not have been "financially viable" and "economically sustainable".[62] According to the evidence of Mr Oliver, if IIML had moved all of members onto the new IES pricing "then the price changes would simply not be sustainable and therefore not in the interests of all members".[63]

59 *Thirdly*, while IIML considered the revenue impact of the new IES pricing (as any responsible trustee is required to),[64] there is no evidence to suggest that this was an influential or a predominating factor affecting IIML's assessment of the introduction of the new pricing structure, or that any preference was given to it; nor was any such proposition put to Mr Oliver in cross-examination. Indeed, at the time, the strategy of the new IES pricing was recorded as being "not revenue driven – the key driver is to

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[59] IFL.0006.0001.4636 at .4811.

[60] IFL.0006.0001.4836 at .4843.

[61] IFL.0006.0001.5149 at .5157.

[62] IFL.0006.0001.5149 at .5157. See also IFL.0006.0001.4636 at .4843 which notes that applying the pricing change to all members would be "unsustainable and unviable".

[63] Transcript, Mark Oliver, 10 August 2018, P-4601 at line 5.

[64] IFL.006.0001.4636 at .4843.

facilitate a sustainable and viable transition to a more cost-effective structure for all members".[65] This is further evidenced by the Board's consideration and rejection of another alternate strategy, open to IIML, which was to establish a new fund for new members at a new price point. IIML acknowledged the potential longer term detrimental impact to existing members and therefore prioritised members' interests over its own.[66]

60 *Fourthly*, the evidence demonstrates that IIML recognised, assessed, and managed the potential conflict between members obtaining lower pricing and the trustee's interest in seeking to retain the higher pricing for the benefit of its parent, IOOF Holdings. The issue of the potential conflict was noted in a document circulated by Mr Mota, a senior executive of IOOF Holdings.[67] The potential conflict was then considered by Mr Oliver and his team.[68] It was addressed by taking into account the best interests of members as referred to above in paragraphs 56 to 58.[69] It was further addressed by the directors of IIML expressly acknowledging the conflict and the need to give priority to members.[70] Only the independent directors on the board of IIML voted on the new pricing proposals, with those directors who were also directors of IOOF Holdings abstaining so as to avoid any potential conflict.[71] Finally, in voting on the IES proposal, the two independent directors expressly considered and noted the potential conflict and the need to prioritise the interests of members.[72]

61 *Fifthly*, the new IES pricing was offered by IIML to all members in circumstances where, under the then existing pricing, members were assessed against the market to be the beneficiaries of top quartile returns and bottom quartile fees.[73] Even assuming that the IES pricing was sustainable across all members (which for the reasons given it was not), this would have led to "a large number of members being only marginally better off"[74] under the new IES pricing.

62 *Sixthly*, IIML was simply not able to identify those members who would actually be better off as a result of the new IES pricing. An assessment as to whether an existing member would have been better off under the new IES pricing depended on whether the member and their financial adviser subsequently agreed that the member would be charged a new separate advice fee.[75] This agreement was direct with the adviser and

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[65] IFL.006.0001.4636 at .4843.

[66] IFL.0032.0001.1227 at .1229.

[67] Transcript, Mark Oliver, 10 August 2018, P-4591 at line 30; Transcript, Mark Oliver, 10 August 2018, P-4593 at line 10.

[68] Transcript, Mark Oliver, 10 August 2018, P-4592 at line 12.

[69] See also Transcript, Mark Oliver, 10 August 2018, P-4594 at lines 16 to 39.

[70] IFL.0006.0001.4636 at .4642.

[71] IFL.0006.0001.5149 at .5157; Transcript, Mark Oliver, 10 August 2018, P-4597 at lines 10 to 13.

[72] IFL.0006.0001.5149 at .5158.

[73] IFL.0006.0001.5149 at .5157.

[74] IFL.0010.0001.0160 at .0164.

[75] IFL.006.0001.4636 at .4843. IIML operates an 'open architecture' model which means that persons can become members of the fund even it those persons are advised by advisers with no connection to IOOF. See also: Transcript, Mark Oliver, 9 August 2018, P-4561 at line 22.

not visible in all cases to IIML. This issue was outlined in the paper presented to the IIML board prior to it deciding to implement the new IES pricing:

> A significant number of existing IES members have advice relationships which include a grandfathered advice commission arrangement. As a result, it may be misleading to view the price differential as simply attributable to the fund. If a member were to move to the new fee arrangement (which does not include advice related commission) they may be charged separate advice fee from their adviser. The financial impact of each individual member is unquantifiable. It would depend on whether the member sought advice and the agreed fee for that advice.[76] (emphasis added)

63 *Seventhly*, and in part to address the inability of IIML to determine whether a particular member would be better off, IIML offered the new IES pricing to all members.[77] It notified members of the new pricing using "an active engagement programme … developed using online, telephony as well as written communications".[78] It then identified and followed up the subset of members who would most likely benefit from the new IES pricing to ensure each member was able to assess their own suitability for any change and make a determination based on their own individual circumstances.[79] IOOF's "active engagement programme" was, in part, designed "to minimise the risks of disengagement" which contributed to members being unlikely to move to the new IES pricing.[80]

64 *Eighthly*, no evidence has been identified demonstrating that IIML prioritised its interests over the interests of members. On the contrary, IIML gave priority to the members' interests and disregarded its interest in retaining the existing fee structure (the very fact that IIML voluntarily introduced the *lower* IES pricing, providing all members with access to equal or improved pricing, also needs to be taken into consideration when assessing this issue).

65 In these circumstances, IOOF submits that it is not open to the Commissioner to find that IIML may have breached s 52(2)(c) of the SIS Act by failing to act in the best interests of members or s 52(2)(d) of the SIS Act by prioritising its interests over the interests of members, when it did not apply the new IES pricing to existing members who would be better off, as at no point in time did this prioritisation take place.

ISSUE 5

Letter to APRA dated 19 April 2017

66 IOOF submits that it is not open to the Commissioner to find that IIML made representations to APRA in its 19 April 2017 letter in circumstances where it had no reasonable basis to do so, and accordingly rejects that it is open to the Commissioner

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[76] IFL.006.0001.4636 at .4843. It should again also be noted that advisers do not need to be, and many are not, aligned with IOOF. See also: Transcript, Mark Oliver, 9 August 2018, P-4561 at line 22.
[77] IFL.0006.0001.4636 at .4651.
[78] IFL.0006.0001.4636 at .4884.
[79] Transcript, Mark Oliver, 10 August 2018, P4601 at line 36.
[80] IFL.0006.0001.4636 at .4843.

to find that IIML engaged in conduct falling below community standards and expectations.[81]

67 The Closing Submissions assert that the statement in IIML's letter to APRA that two options were presented to the rectification committee was untrue because there were no contemporaneous documents recording this process (in particular, as to the presentation of the options to the rectification committee, or that Questor as RSE made any such decision to reduce the distribution over three years rather than immediately).[82]

68 The absence of documents recording these matters cannot support a conclusion that the statement in the letter was untrue. Far more would be required by way of evidence, particularly given the evidence of Mr Kelaher which was to the same effect as the relevant statements in the letter to APRA.[83]

69 Nor does it follow from the fact that such documents are not in evidence before the Commission that there was no reasonable basis for making these statements.

ISSUE 6

70 The Closing Submissions state that "*[i]t is open to the Commissioner to find that the continued failure of IIML and IOOF Holdings to understand their duties to superannuation members, and to take steps to properly recognise and manage conflicts of interest, constitutes conduct falling below community standards and expectations*."[84]

71 IOOF submits that no such finding is open to the Commissioner in light of the evidence given at the Commission for the reasons given below. Further, IOOF operates a ClientFirst strategy which always gives priority to the superannuation member vis-à-vis the IOOF shareholder. This strategy embraces IOOF's purpose, which has been developed from a member's perspective and drives behaviours always towards the member.[85]

Duties to superannuation members

72 *First*, there was no evidence presented to the Commission of any "*continued failure*" of IIML and IOOF Holdings to understand their duties to superannuation members. No such direct allegation was put to either of the witnesses summonsed to give evidence. Although, the conduct of a Royal Commission is not subject to the rules of evidence, it is submitted that it is not open to the Commission to make findings about matters not put squarely to a witness so that the witness might have an opportunity to respond.

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[81] Closing Submissions at [229.2].
[82] Closing Submissions at [233].
[83] Questor Statement at [55].
[84] Closing Submissions at [230].
[85] IFL.0013.0001.0057 at .0075, contains a description of IOOF's ClientFirst strategy.

73 *Secondly* and in any event, it is IIML and not IOOF Holdings that owes duties to members of the funds of which IIML is both the trustee and RE.

74 *Thirdly*, it is submitted that IIML understands the duties it owes to members of funds for which IIML is both the trustee and RE, and there was no evidence adduced in the hearings which would support a finding to the contrary.

75 *Fourthly* and by way of illustration, the very same TPS members were, in 2016 and as part of the *Evolve Strategy* referred to above in paragraph 56, transferred to a different IOOF superannuation fund, obtaining the benefit and security of a general reserve some 40 times larger, modern, stronger technology systems, and more favourable service and product offerings.[86] Importantly, these members also obtained the benefit of lower administration fees in excess of $10m recurring as a result of the greatly increased scale in the new fund, none of which would have occurred if IIML was not discharging its duties to members in priority to IOOF shareholders.

76 The Closing Submissions[87] refer to one letter sent to APRA by IIML in relation to the Questor matter.[88]

77 That letter contained a number of responses to issues raised by APRA. The Closing Submissions refer to concluding remarks made in that letter and state that IIML: [89]

> asserted that "in terms of the so-called pub test, which in these circumstances is a proxy for members best interests, it is the board's view that the test has been passed." It is submitted that "the so-called pub test" is not a "proxy" for the statutory covenant imposed by s 52(2)(c) of the SIS Act, which requires the trustee "to perform the trustee's duties and exercise the trustee's powers in the best interests of the beneficiaries."

78 It would be a mischaracterisation of this statement to suggest that it provides evidence that IIML does not understand its duties to superannuation members. A fair reading of that statement in the context in which it was provided suggests otherwise. In particular, IIML was not seeking to define or delimit the proper construction of the specific statutory provision referred to in the Closing Submissions. The letter concerned specific issues arising from the CMT over-distribution, and Questor's remediation and compensation plan. The outcome was that all members were placed in the same financial position as they would have been in had the initial over-distribution not occurred.[90] The statement in the letter that "*in these circumstances*" the so-called pub test was a proxy for members' best interests must be understood in this light and was intended to reflect community standards. It cannot reasonably be taken as a statement by IIML about its broader understanding of the statutory

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[86] See IFL.0006.0001.1033 at .1218.

[87] Closing Submissions at [221].

[88] IFL.0006.0003.4093.

[89] Closing Submissions at [221].

[90] In this respect, IIML refers to the submissions at paragraphs 16 to 22 above in relation to the use of the general reserve, and in particular the fact that it is not allocated to any specific member and that members have no entitlement to exercise any rights, powers or privileges in respect of the assets of the fund, or otherwise claim any interest in any particular part or asset of the fund, which includes the general reserve.

covenant imposed by s 52(2)(c) of the SIS Act, as suggested in the Closing Submissions.

79 Furthermore, the Questor matter in general could not be said to provide any basis for a finding of a "continued failure of IIML and IOOF Holdings to understand their duties to superannuation members". In addition to the matters noted above concerning the Questor CMT over-distribution issue, IOOF notes that the over-distribution occurred in 2009, came to the attention of Questor in 2011, and was reported to ASIC in 2012. The amount of the over-distribution was $6.16 million. The total amount of compensation required to make good the loss to certain unitholders of the Fund and the IDPS-like as a result of the reduced distributions was $3.18 million. At the time of the initial over-distribution error, the CMT had funds under management of $1.4 billion,[91] and in 2017 the Fund (which now includes the CMT) had over $25 billion of funds under management.[92]

80 Separately, the Closing Submissions also note that, at a board meeting of IOOF Holdings on 1 August 2018, the Board resolved that:

(a) an independent chairman would be appointed to the IIML board, Mr Kelaher would step down from his position on the IIML board, and another independent director would be appointed; and

(b) IOOF would investigate separating the RSE and the RE, potentially as a result of the acquisition of the ANZ wealth entities by IOOF.[93]

81 Somewhat surprisingly, it would appear that the Closing Submissions seek to level criticism at IOOF for implementing these changes; changes which were agreed with APRA in June 2018, after having been suggested by IOOF in March 2018. Given the focus of the Commission on potential conflicts of interest relation to IIML, it is reasonable to think would be welcomed.

82 The criticism appears to be that the changes were not implemented in the right spirit, and ought to have been accompanied by an acknowledgment by IIML that they were being implemented only because IIML agreed with all of APRA's concerns. In particular, the Closing Submissions assert that:

> Mr Kelaher did not agree that these changes were being made because IOOF (or IIML) accepted that there were legitimate governance concerns that needed to be addressed. As he put it, for IOOF it was "a matter of indifference". Rather, IOOF had made a pragmatic decision: it was easier to make the changes rather than having to keep dealing with the complaints from APRA.[94]

83 It is submitted that any such implicit criticism is unfair, and that the important fact is IIML decided to do what APRA asked. It must be recalled in this context that this was not a directive from APRA or an enforceable requirement – IIML has chosen to

[91] See tab 17 of Ex. CK-2, IFL.0029.0001.1190.
[92] IIML Statement at Annexure B.
[93] Closing Submissions at [187]-[188].
[94] Closing Submissions at [188].

implement this change voluntarily and in fact had suggested them to APRA in March 2018.

84 In addition, the reference to it being "*a matter of indifference*" needs to be read in context. The relevant statement by Mr Kelaher in his evidence was as follows:

> And in relation to the splitting of the RSE and the RE, was there a recognition at the board level or at the board meeting that there were problems with that DRE structure? ---No, I – I think there was just a desire – it – it's a matter of indifference. These structures had – had evolved over time and were sort of de rigueur 10 years ago. Maybe they weren't appropriate any further. And – so I guess in the current environment, it was seen as that that was the preferred structure. We really don't have any – any particular barrow to push in that.[95]

85 Plainly enough, the point which Mr Kelaher was making was that the IIML Board was not seeking to advocate for the existing structure or resist any change out of any self-interest or benefit to IIML. His evidence was to the effect that the structure had evolved over time from what was customary 10 years ago, and he accepted that "*in the current environment*" the structure could be changed and that, in doing so, it did not affect IIML's interest detrimentally or require IIML to push "*any particular barrow*".

86 In light of the above, it is submitted that there is no basis for any finding that IIML's decision to implement this change is evidence of "*a continued failure of IIML and IOOF Holdings to understand their duties to superannuation members*."[96]

Conflicts of interest

87 IOOF submits that there is no evidence of any "*continued failure … to take steps to properly recognise and manage conflicts of interest.*"[97]

88 It is submitted that the evidence was to the contrary effect. In particular, IOOF relies upon the following matters:

(a) the decision to implement the board changes described above, which were the subject of a board resolution on 1 August 2018, it having first suggested those very changes to APRA in March 2018;

(b) the Questor Statement contains a detailed discussion[98] of the more recent steps taken to enhance the recognition and management of conflicts of interest. For example, and in addition to the board changes mentioned above:

(i) IIML's Conflicts of Interest Management Framework and Compensation and Remediation Framework include active mechanisms in place to record and deal with perceived conflicts;

(ii) directors are required to observe and confirm that trustee decisions are in the best interests of members and that trustee (board) decisions are separated from investment decisions. IIML's board will continue to

[95] Transcript, 10 August 2018, Christopher Kelaher, P-5607.
[96] Closing Submissions at [230].
[97] Closing Submissions at [230].
[98] See Questor Statement at [65]-[73].

include two (increasing to four) non-executive directors who do not sit on the board of IIML's parent, IOOF Holdings, thus enabling the trustee board to make decisions free from any perceived pressure from other entities within the group; and

(iii) where a board submission presents a potential conflict, it is noted in the minutes together with details of the conflict treatment plan; and

(c) similarly, the Oliver Statement refers to a number of ways in which IIML and IOOF Holdings properly recognise and manage conflicts of interest.[99] For example:

(i) compliance with a Conflicts of Interest Framework;

(ii) quarterly review of conflicts registers to monitor identification and reporting of potential conflicts;

(iii) declarations of potential conflicts in board and committee meetings and a requirement that all board submissions have a compulsory conflicts section and treatment plan where required, completed with assistance from the Legal and Compliance Division and overall oversight by the company-secretarial function; and

(iv) as part of quarterly reporting to the IOOF Risk and Compliance Committee, registers of breaches and incidents are tabled together with analysis of the positive assurance process to assist with the identification of conflicts and appropriate management action.

89 In light of the above, it is submitted that there is no basis for any finding that there has been a continued (or any) failuree to take steps to properly recognise and manage conflicts of interest.[100]

[99] Oliver Statement at [64]-[66].
[100] Closing Submissions at [230].