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TRANSCRIPT OF PROCEEDINGS

O/N H-919880

THE HONOURABLE K. HAYNE AC QC, Commissioner

**IN THE MATTER OF A ROYAL COMMISSION
INTO MISCONDUCT IN THE BANKING, SUPERANNUATION
AND FINANCIAL SERVICES INDUSTRY**

MELBOURNE

9.30 AM, FRIDAY, 17 AUGUST 2018

Continued from 16.8.18

DAY 49

MS R. ORR QC appears with MR M. HODGE QC, MR A. DINELLI and MS E. DIAS as Counsel Assisting with MR T. FARHALL
MS P. NESKOVCIN appears for Westpac
MR R. DICK SC appears with MR J. WATSON and MS E. BEECHEY for APRA
MR P. COLLINSON QC appears with DR P. BENDER for ASIC

THE COMMISSIONER: Yes, Mr Hodge.

MR HODGE: Commissioner, the first witness this morning is Ms Rowell from APRA.

THE COMMISSIONER: Yes.

<HELEN ROWELL, AFFIRMED [9.30 am]

<EXAMINATION-IN-CHIEF BY MR DICK

THE COMMISSIONER: Thank you very much. Do sit down. Yes, Mr Dick.

MR DICK: Thank you, Mr Commissioner.

Ms Rowell, is your full name Helen Rowell?---It is.

And is your current business address the APRA offices at 1 Martin Place, Sydney, New South Wales?---That's correct.

Could you inform the Commissioner of your current position at APRA?---I'm the Deputy Chairman of APRA.

And have you received a summons to appear at this round of hearings of the Commission?---I have.

And do you have that summons with you?---I do.

I tender that - - -

THE COMMISSIONER: 5.297, the summons to Ms Rowell.

EXHIBIT #5.297 SUMMONS TO MS ROWELL

MR DICK: Ms Rowell, you've prepared a witness statement for this round of hearings?---I have.

And that's a statement dated 14 August 2018?---Yes, I believe so.

And you have the original of that statement with you?---I do.

Now, could you just turn to paragraph 50 of the statement, please?---Yes.

Do you see in the second line of para 50 there's a barcode reference for a document there?---I do.

And there's a change that you wish to make to that?---I do, yes.

And if I could just read on to the record that the correct reference should be 0007.0007.0001?---Yes.

Is that correct?---Yes.

And then could you turn to - - -

THE COMMISSIONER: Just – do you mind making the change and amending it and initialling it.

MR DICK: Yes.

THE COMMISSIONER: Is what I'm struggling to say.

MR DICK: And then, Ms Rowell, could you turn to para 128 of your statement?---Yes.

And there's a reference there to a date 2014?---Yes.

And does that need to be changed?---It needs to be changed to 2017.

And could you make that change and initial it, please?---Yes.

Now, with those corrections - - -?---Yes.

- - - are the contents of your statement true and correct to the best of your belief?---They are.

Commissioner, I tender the statement and the exhibit.

THE COMMISSIONER: The statement and exhibits to the statement of Ms Rowell of 14 August '18 is exhibit 5.298.

EXHIBIT #5.298 STATEMENT AND EXHIBITS TO THE STATEMENT OF MS ROWELL DATED 14/08/2018

MR DICK: Thank you. And Ms Rowell, do you also have a working copy of your statement and exhibit?---I do.

Thank you.

THE COMMISSIONER: Thank you, Mr Dick. Yes, Mr Hodge.

<CROSS-EXAMINATION BY MR HODGE [9.33 am]

MR HODGE: Thank you, Commissioner.

Ms Rowell, I want to start by just asking you some questions so that we can understand or help the Commission to understand the way in which APRA approaches the regulation of the superannuation industry?---Yes.

APRA has prudential responsibility in relation to areas other than superannuation?---APRA has prudential responsibility for banking and insurance and superannuation.

And in relation to superannuation, does it take a different approach to that which it adopts in relation to banking and insurance?---In a general sense, no. We adopt a similar regulatory philosophy and supervision philosophy across all of our industries. There are some nuances according to the specific legislation.

And is the way APRA describes its approach to prudential regulation one that is principles-based and risk-based?---That's correct.

And I think you explain – and we might bring it up – at page 2 of your statement, page 2, paragraph 24, that the way you would describe principles-based is:

> *To give emphasis to the achievement of sound prudential outcomes in setting regulatory requirements and expectations, without necessarily seeking to specify or prescribe the exact manner in which those outcomes must be achieved.*

?---That's correct.

Could you just explain a little more to us about that? Is the way in which you set out the principles base – is the way in which you set out the principles base for entities through the prudential standards that you issue?---That's correct. So in general terms, the relevant industry legislative Acts set out quite high level requirements, and the APRA principle prudential standards elaborate on those high level requirements to set, in essence, principles-based objectives that would support the achievement of what's in the law.

How does principle-based standards relate to the idea of legislative prescriptions on certain behaviour?---The – there's a consistency, I think, in that if you – if you meet the principles that are set out in the – in the principles-based standards, if you

achieve the objective of the prudential standards then you would be expected to also then meet the legislative obligation that has been prescribed.

So to take – if we move from prescriptions to proscriptions, if there's a proscription in the legislation on doing something that is other than for the sole purpose of maintaining retirement benefits, is that something that, from APRAs perspective, is ultimately achieved by following the principles that are set out in the prudential guides or standards?---Well, it can be. I think you need to look to both the legislation and the prudential standards to determine whether the obligations of any individual entities are being met.

If APRA takes the view that a particular entity isn't achieving or following the principles that are set out in a prudential guide, what is the action that it would take?---It would depend on the – on the specifics of the circumstances and the issue at hand. We have a range of actions that we can take, from heightened supervision through to specific administrative actions, like appointment of experts to do an in-depth review, through to issuing requirements through supervisory letters for a matter to be addressed, and ultimately through to potentially taking legal action if that is warranted by the seriousness of the matter.

When you say taking legal action, can you take legal action because an entity isn't achieving the principles that are set out in a prudential standard?---It's very hard to answer that in a general way. It is – again, it depends on what the particular matter in issue at hand is, and also there are a range of actions available to APRA under the law, and the triggers for exercising those vary according to the specific piece of – provision of the legislation that is relevant.

Perhaps if I put the question a different way. Is it ever possible for APRA to say an entity – a superannuation entity has contravened a prudential standard?---That is possible.

And if APRA says that an entity has contravened a prudential standard, what are the consequences that can follow from that under the legislation?---Again, it would depend on the – on the particular matter. In general terms, we would be able to direct the institution to comply with the prudential standard. But, again, whether we would do that or whether we would take some other action would depend on the circumstances. Our primary focus is trying to achieve the objective of the legislation and protect the interests of members.

If we take as an example the fit and proper prudential standard?---Yes.

Maybe – you've exhibited that to your statement. So if we bring up – this is exhibit HR1-3 to Ms Rowell's statement, and the relevant standard is at APRA.0007.0005.0267. Have you got that there, Ms Rowell?---I have, yes.

So we see at the beginning what's explained is:

The prudential standard sets out minimum requirements for RSE licensees in determining the fitness and propriety of individuals to hold positions of responsibility.

?---Yes.

Now, this is a standard that would be – or is or was drafted by APRA?---That's correct.

And is this the standard that would set out the principles in relation to fitness and propriety?---Yes.

And then if we go to page .0268?---Yes.

And paragraph 6?---Yes.

And we see that there's a requirement that:

An RSE licensee have a fit and proper policy.

?---Yes.

And if a – if an entity didn't have a fit and proper policy, assuming that occurred, what is it that APRA could do in that event?---Well, we would require them to establish a fit and proper policy.

And is that a power that you have under the Act, to give a direction to them to do so?---I believe so.

And then if they didn't do it, what would happen?---I – I'm not a lawyer. I understand that we would be able to take some sort of legal enforcement action.

And if we then go over to page .0271?---Yes.

And this is setting out what the criteria are to determine if a responsible person is fit and proper?---Yes.

And it appears to be, perhaps, reflecting what's in the SIS Act, expressed at a very general level?---That's correct.

And if an entity's criteria for assessing a fit and proper person was inadequate, then APRA could do something?---Yes. We would be able to – again, depending on the level of deficiency, either recommend that they make improvements to their particular policy, or if we felt that it was completely adequate, that would be a stronger requirement for them to do so.

And then if we go to page .0273?---Yes.

This sets out the process for assessment of fitness and propriety?---Yes.

And the fit and proper policy has to contain a process for determining whether or not – I'm sorry, has to contain a process for applying the fit and proper policy?---That's correct.

And needs to explain how it is that the RSE licensee is going to go about determining whether somebody is fit and proper?---That's correct.

And if the statement – I'm sorry, if the fit and proper policy didn't contain adequate provisions for determining whether somebody was fit and proper or an adequate process, then what is it that APRA would do?---It would be the same. We would recommend or require changes according to the degree of deficiency that we felt was inherent in the policy or process.

And so all of these things take us through the development of a process and the embodiment of a process and the embodiment of a criteria?---Yes.

And then when it comes to the question of is a person fit and proper, a question that presumably must be asked on an ongoing basis how does APRA go about dealing with that question?---Well, the requirement to determine whether someone is fit and proper actually rests with the RSE licensee that has to implement their policy, and – and apply the process in their policy. And so APRA would undertake supervision activity and – and review how the trustee was doing that on an ongoing basis as part of our regular supervision activity.

And in the course of that supervision activity, the supervisor might also come to a view that it was possible that a responsible person was not fit and proper?---That is possible.

And if that was to occur, what would happen?---The first step that we would take would be to engage with the RSE licensee to ask them how they had determined that the individual was fit and proper and what was the criteria and the decision-making process and documentation of that process. And that may satisfy us that an appropriate process and criteria had been followed. If it had not, then we would probably recommend or, again, require, depending on the circumstances, that the RSE licensee, perhaps, consider undertaking another assessment looking at other factors, and reassess its view.

What if APRA formed the view that somebody was not fit and proper? What would happen then?---I think our first recourse would be to engage with the RSE licensee to endeavour to get them to take action to determine whether the person really was fit and proper or not. If we were not satisfied with that outcome, then, again, ultimately, we may want to pursue other avenues to – to address that.

One of the problems, one might think, with engaging with the licensee about whether somebody is fit and proper is that the person you are engaging with at the licensee is

the person that you think isn't fit and proper. Do you agree?---Very hard to generalise about that, and there are a number of people that fit and proper assessments are relevant to. We would – you know, obviously engage with a different individual in respect of the assessment and the issues rather than the individual concerned. So, you know, if it's one of the directors, we would engage with the chair of the board. If it's the CEO, we would engage with the – with the chair of the board. If it's the chair of the board, we would probably engage with the deputy chair, so – or if it's another responsible person in management we would engage with whoever we felt was the appropriate person to have that engagement with.

And if, after you've engaged and engaged, there is not an adequate response from the RSE licensee, what is the next step for APRA?---Assuming we were contemplating taking more formal action, we would likely issue a show cause notice as to why we shouldn't take that particular action and set out in that show cause notice what our concerns were, and what we thought the appropriate action to be taken was in response to those concerns.

And a show cause notice, is that a formal document under the Act?---It is.

And what happens if you get a response back which says, "we think this person is fit and proper" or "we're just not going to change"?---Ultimately if we're talking about a fit and proper, then we would need to apply to the court. So the show cause notice in a fit and proper where we felt that someone was not fit and proper and should be removed would be to have that person disqualified, I think, would be the ultimate action and then we would need to apply to the court to have that action pursued.

And you've only had to apply to the court since 2008?---That's correct.

Before 2008, between, I think, February 2003 and 2008, you were able to administratively disqualify somebody on the basis they weren't fit and proper?---That's correct.

And during that five-year period, APRA administratively disqualified – was it 133 - - -?---It was around about that number, yes.

- - - people as not being fit and proper?---Mmm.

And since 2008, when it has been necessary to apply to the court, APRA has applied once to the court to disqualify somebody?---That's correct.

And that was one of the directors of Trio Capital?---That's correct.

And that was resolved by an enforceable undertaking being given by that person - - -?---That's correct.

- - - not to continue to be a responsible person?---That's correct.

And there were another 12 in addition to that one director – I think there are another 12 directors or people associated with Trio Capital that gave enforceable undertakings?---That's correct.

And are there other enforceable undertakings that APRA has obtained since 2008 from - - -?---Not in relation to superannuation, as I understand it.

Okay?---I think, if I can just add some context to the – to the pre and post 2008 change, a significant proportion of those 130 disqualifications were part of an exercise we undertook when changes to the law were introduced in 2004 that required relicensing of all superannuation entities, and we undertook what we called the lost and lazy program where if we were unable to get a response from the trustees in relation to a superannuation entity and could not get them to satisfactorily complete the relicensing process, then we disqualified them through that administrative process. So that was a large portion of those administrative decisions.

I understand. Are you aware of whether APRA has turned its mind in the last, let's say, three years, to the question of whether any particular individual is a fit and proper person at an RSE licensee?---There have been a number of matters that have been raised with particular entities and individuals at those entities around some behaviour that we were not happy with, which leads to discussions internally about the nature of the behaviour and the concern, the seriousness of it, and what the appropriate action is. I – in general terms, that does raise questions about, you know, considerations of fitness and propriety. I – so, I guess, we would have turned our minds to that in a general sense in some cases.

Is one of the concerns that APRA has about having to apply to the court for a disqualification order the cost involved in that?---That is a consideration. I think our primary consideration, and – and certainly when we're considering enforceable undertakings versus disqualification proceedings, firstly, the outcome that we're seeking to achieve, particularly specifically in the case of fit and proper actions, is ultimately the removal of the industry – the removal of the industry – individual from a responsible person role in the industry for a period that we think is appropriate. And we can typically use enforceable undertakings to achieve that outcome in a more cost efficient and timely way with more certainty than would be the case with going through a court proceeding.

Other than in the case of the Trio Capital directors have you sought an enforceable undertaking from an individual in the last 10 years that would, if they had agreed to give it, have prevented them from acting as a responsible person?---As far as I am aware, no. But we have had individuals – the RSE licensee themselves have taken steps to remove individuals at APRAs instigation in that period which has achieved the outcome that we were trying to seek or would have sought through an enforceable undertaking, if needed.

If we go to page 45 of your statement, paragraph 298?---Yes.

You set out there, or you're considering there – I might just wait, I'm sorry, Ms Rowell, until it comes up on the screen. There we go. You were asked a question by the Commission to explain any practical limitations or impediments on APRA seeking disqualification orders pursuant to section 126H of the SIS Act?---Yes.

And at paragraph 298 you're setting out your answer to that?---Yes.

And the first is – the first impediment is:

> *...the resources and expense of gathering sufficient and admissible evidence in the form that would be required by a court.*

?---Yes.

And you make the point:

> *APRA does not have power to recoup costs of an investigation.*

?---Yes.

And then if we go over the page to page 46, the second point you make is about:

> *The legal costs of the court process.*

?---Yes.

And then the third point is about:

> *The length of time involved with court processes.*

?---Yes.

Can I ask you about this: both you and ASIC – when I say "you", I mean APRA – tend to raise as an issue that court processes take a long time. What is the basis of that judgment?---Our previous experience in dealing with matters through relevant tribunals such as the AAT and observation of other court processes that occur in the wider financial sector.

In terms of your experiences in dealing with courts, as far as we understand it, APRA hasn't had any experience with dealing with courts in the last 10 years, has it?---I'm not sure that is strictly correct, but I would need to - - -

In the superannuation space?---In the superannuation space, yes. Obviously there are other APRA industries where we've had different actions and issues.

And when you talk about administrative tribunals, you're talking about a situation where pre-2008 you made an administrative decision to disqualify a person, and then they sought a review of that decision in the AAT?---Yes.

And your observation was it took some period of time for that review to be resolved?---It typically did, yes.

And there were reviews on a number of occasions for a number of decisions, is that right?---And – that's correct, yes.

And is there some comparison that is done internally, based on that now somewhat historical experience, and how long it takes APRA now, in its attempts to, I think – I am going to use the word "harass", I don't mean that in a negative way but to sort of harass the entities to try to make changes by themselves to determine that it's quicker to just keep harassing the entities rather than going to a court?---I – I think our general view would be that – I mean, I don't know that we've done any specific detailed analysis of relative time, etcetera. We make an overall assessment based on a number of factors, of which time is one, cost is one, but, more importantly, what is the outcome that we are seeking to achieve and how best can we achieve that outcome in an efficient and timely manner. And typically when you're talking about fit and proper issues you want the person removed from their role as quickly as possible.

The other thing I want to suggest to you in relation to removing somebody on the basis that they're not fit and proper is that that would be, really, the most extreme step that you could take in relation to the regulation of an entity?---That's correct. I mean, there are – there's disqualification, there's replacement of trustees, there's removal of licence. I mean, they're all quite extreme. The hurdles for taking those actions are really quite high and also we have to have a demonstrable and clear proof that there has been a contravention of the law, rather than a view that there may be or could be a contravention of the law.

And I should be more clear about this: what I mean is if you approach things on the basis of the regulatory pyramid - - -?---Yes.

- - - which many regulators would use, disqualification of a person would be at the very peak of the pyramid?---That's correct.

That would be regarded as a form of incapacitating an entity or a person?---Correct.

And so you would expect that it would not be frequent that APRA would seek to apply to disqualify somebody?---That's correct.

Now, if we consider another standard, which is the conflicts of interest standard?---Yes.

And you've also exhibited that to your statement. If we go again to exhibit HR1-3, page – it's APRA.0007.0005.0281?---Yes.

And this is a standard, the essence of which is embodied just in the objectives that are set out in the grey box on the front, for RSE licensees to establish processes and policies in relation to managing conflicts of interest?---That's correct.

And the standard requires them to have a conflicts management policy?---Yes.

And that that be approved by the board?---Yes.

And that they make sure they identify all the relevant duties and relevant interests?---Yes.

And that they have registers where they record what their duties and interests are?---That's correct.

And are those what APRA would regard as the principles that then have to be applied by the entity?---Yes, although there is a little bit more detail set out in the standard itself about what we would expect to be taken into account in establishing those policies and identifying the interests and duties.

And it seems as if an RSE licensee can comply with this standard by making sure it has a detailed policy and making sure it has a detailed register, and that in that register it's identified all of the interests. Is that right?---In broad terms, yes, although we would also expect there to be – we would have a view as to whether a policy or a process and the identification of interests and duties was sufficient or adequate in order to meet the intent of the legislation.

Yes. Again, that's talking about what is the adequacy of the process or policy that is recorded?---Yes.

That is distinct from the application of the process and the outcome of the process?---Well, both are relevant.

To assessing whether the original process is adequate or not?---Yes.

And if you think about AMP, are you familiar at all with the processes in relation to AMP?---Not in detail, no.

All right. Let me ask you some questions and we will see whether or not this can – we can usefully explore this or not. Do you know whether AMPs processes and policies are regarded as adequate by APRA?---I believe we have undertaken some reviews of those policies, in fact – yes, we have undertaken reviews and we have made observations about where those policies and processes could be strengthened.

I think if we bring up APRA.0004.0001.4034?---Is that a document that's in my pack? No.

No, it's not, Ms Rowell. So this is an email dated 30 January 2018, and it has an attachment to it which we bring up as well which is APRA.0004.0001.4038. So on the right-hand side of the screen we have the letter from APRA to the senior manager of trustee governance at the two AMP trustees dated 30 January 2017, which is concerned with a review of the business monitoring model?---Yes.

And I'm assuming you probably don't know exactly what the business monitoring model - - -?---I have a general understanding of – of the fact that that model is used by AMP. I don't know the model in detail.

And there are some comments that APRA has made about the adequacy of the BMM model back in the beginning of 2017?---Yes.

And then if you look on the left-hand side?---Yes.

We see there's an email back from Ms Sultana, trustee governance, indicating how it is that AMP has responded to those review items, and then you see the response from APRA on 30 January 2018 is:

> *Please find attached a letter confirming that APRA effectively considers these items closed.*

?---Yes.

And what I'm trying to understand is there is a policy that AMP has in place that APRA seems to be now content with, but at a more fundamental level, the trustee has entirely handed over control of the trust to other AMP Group entities. Are you aware of that?---I am – I'm not sure that our understanding of the way the relationship between the trustee and the AMP Group works is – would be appropriately characterised in that way.

What do you mean by that? What is your understanding of how the group works?---So there is a trustee board, there is a – an office of the trustee, and they are charged with oversighting the operations of the RSE licensee. They outsource a number of the services and activities to the AMP Group, and that there are processes in place to manage those relationships and review and monitor those relationships. There will always be a question as to how robust those processes are and how effective they're operating in practice. We would continually review our satisfaction or otherwise with those processes as new information comes to light. And so this particular correspondence, I'm assuming, relates to some specific issues that were identified as part of a review activity looking at a particular number of aspects of that process, and agreeing that those specific recommendations had been addressed rather than, necessarily, expressing an overall view that the – the model and the process

was adequate and would remain adequate into the future. So our assessment is always evolving based on the information that is coming to hand.

And how does APRA assess, if at all, what's going on with the outsource providers?---So we would take a – a number of supervision activities with any individual entity – and I'm not talking about any specific entity here. We would engage with the board to ask them and – and review the material that goes to the board about how – what is the information they receive, is it adequate, does it – is it comprehensive enough, how do they review and challenge what's being provided to them, what other sources of information do they get. We would engage with the senior management on a regular basis to understand the relationship, for example, between, say, an office of the trustee and the business and what monitoring and oversight and challenge. So through, you know, regular engagement, review of material, engagement with the board, deep dive reviews into particular aspects of the operation of – of the entity to try and get a sense of what are the policies and frameworks and how effectively are those policies and frameworks embedded in practice.

And what is the ultimate outcome that APRA is seeking to achieve?---The – prudent and robust management of the trust under the RSE licensee in the best interests of members.

If you look at – so if we bring up your statement on page 3?---Yes.

And this, perhaps, then ties us into the second part of APRAs regulatory approach which is the risk-based approach?---Yes.

And so the principles are then concerned with – or are then implemented or reviewed as part of this risk-based approach?---Yes.

And the risk-based approach is designed to identify and assess those areas of greatest risk to a regulated entity, or to the financial system as a whole and then apply APRAs supervisory resources and attention to these risks in a targeted and cost effective manner?---Yes.

And then you see in paragraph 26 you say:

> *Overall, as the prudential regulator, APRA seeks to promote financial system safety and stability by ensuring that regulated entities are prepared to, and demonstrate their commitment to, operate and manage their risks and assets prudently, so as to be able to meet their financial promises to (in the superannuation context) their members.*

?---Yes.

Now, on its face, what that seems to suggest is that APRA is concerned with the stability of the system and the entities within the system as its primary focus. Do you

agree with that?---That's not our – our view. I mean, I can see why that might be an interpretation, but I think ultimately, the – the objective is that last set of words which is about "in the superannuation context" meeting financial promises to members. If you don't have a prudently well-managed institution such as a trustee with its RSEs, then they're not going to be able to meet their promises and their obligations to members.

Can we take an example. APRA, as we understand it, regards NULIS, the NAB trustee, as a well-functioning trustee?---I would say we would have a view that – that they have operated reasonably soundly on – in a general sense.

You're aware there is some evidence that has been given during the Royal Commission that a NAB entity – I'm sorry, I should go back – that pre-1 July 2016, a predecessor trustee, MLC Nominees, invested all of the assets of the trust into investment-linked insurance policies issued by another MLC entity?---I'm generally aware of that.

And that's a typical structure that is used by superannuation trustees as part of a group with a life insurance company?---It's common for those sorts of arrangements to exist in retail trustees, yes. Retail group trustees.

And what it seems had occurred in relation to the MySuper product was that the insurance company was then using another related party to manage the assets or the investment of the assets, and the insurance company was maintaining its profit at the expense of providing sufficient funds to the investment manager to be able to invest in unlisted assets?---I don't have sufficient familiarity with the details of those arrangements to be able to respond to that.

What I wonder is, is there any prospect that that would be something that APRA is interested in?---Yes. And – and, indeed, as I indicated a little while ago, as we become aware of new information about how arrangements are operating in practice, we will undertake activities to better understand that and – and reassess our view as to whether there are any matters of concern.

And that is something that we do on an ongoing basis through our own supervision activity, but also monitoring what is happening more broadly in – in terms of information that becomes available.

But that – I understand you say you don't have sufficient information to be able to know about that issue. Assume it is as I have described it. What is it that APRA could do about it?---The first step would be APRA would need to understand the actual details of the arrangements that you're referring to and form a view as to whether there were concerns and the degree of those concerns, and then we would, again, have to form a view about what the most appropriate action would be. It could be to engage with the trustee to get them to revisit and review those arrangements, or – it's very hard to make a general statement or response to that without having a complete understanding of the details.

If the issue didn't present any risk to the stability of the fund and it didn't present any risk to the ability of the trustee to meet its financial promises to the members, because the trustee isn't promising a high return on the basis of investment in unlisted assets, would APRA have any interest in it?---Yes, we would. We have undertaken a lot of work, particularly recently, to understand the outcomes that are being delivered by trustees to members, and whether those outcomes are reasonable and in the best interests of members over the medium to long term. So if we felt that, relative to alternative arrangements that could be in place, members were being particularly disadvantaged by a set of arrangements, then we would take an interest and we would look to seek some form of change to address the concerns.

If we go to page 26 of your statement?---Yes.

You have a chart at paragraph 172 - - -?---Yes.

- - - which illustrates that all MySuper single investment strategy products have met their return target in the four years to December 2017?---Yes.

But as we can see, there's a significant difference in what their return targets are?---Yes.

And as we understand it, almost invariably the return target for a MySuper single investment strategy will be a CPI plus target?---That's correct.

And so CPI is, of course, common for everyone. That's not changing. So that just means that every one of these funds is selecting a different return target over CPI?---Yes.

For a single diversified strategy?---Yes, relevant to the specific characteristics of the members – membership of their MySuper product.

Where the balance will be between growth and defensive assets?---In broad terms.

And for the single diversified strategy, they're all going to be within a particular band of the split between growth and defensive assets?---That's often the way these are described, but there's, you know, obviously different ways in which asset portfolios are constructed within that for different reasons.

People might, for example, describe – one entity might describe something as growth, which another entity might consider a defensive asset?---Yes.

And so even just taking the split on its face might not necessarily tell you how comparable the two types of products are?---That's correct. You need to look a little bit deeper than that, yes.

And for a member of the public, it's impossible, isn't it, to look a little bit deeper at that?---It's not impossible. It does require them to seek further information than may be disclosed at a high level, yes.

When it comes to the split between defensive and growth assets, is that something that APRA records and publishes?---We – we do publish information on the asset allocation of MySuper products. We don't typically group it just into growth and defensive. We actually publish more granular asset classes, so, you know, domestic and international equities, property, infrastructure, etcetera.

And so if a member of a particular fund wanted to figure out how to compare growth and defensive assets between two different funds, could they use that asset allocation information to do so?---They could do so, although the primary purpose of APRAs publications is not necessarily for direct to consumer, it is for other industry stakeholders. I think the trustee needs to publish disclosure for members and there is information available through ASICs MoneySmart website as well, I believe. But we do publish that information but its primary purpose is not for individual members.

So if members are setting out to compare the performance of two MySuper products, do you agree the primary things they're going to be able to look at, based on the dashboards that are published, are the return achieved, the return target, and the fees charged?---They're the core elements of the dashboards, yes.

And we understand the point you're making with this chart is the investment performance of MySuper to date is at least satisfactory, if not good, because the return target is hit?---I – I think the general point I'm trying to make in this section of my statement is that in assessing the performance of trustees in delivering outcomes for members, you need to look at performance in a range of different ways, not just in terms of peer performance, but also relative to return targets, looking at net returns, expenses, and a number of other dimensions. So this is just an illustration of a – a measure that can inform an assessment of performance, but it's not the only measure that would say that the trustee is – is delivering good outcomes for members.

Let us take another example. Over the last few years, not for the single investment strategy product but for the – also for the single investment strategy product but for the lifecycle stages that AMP has issued, it has been decreasing its target return. Are you aware of that?---Not specifically, no.

And that decrease in return happens at the level of investment manager and life insurance company and is then reported to the trustee. Is that, from APRAs perspective, an adequate arrangement?---Ultimately, it is the trustee's responsibility to make the decision about the investment strategy and the return targets that underpin that strategy and whether that is appropriate.

And if a trustee didn't have contractual rights to be able to refuse to accept that target or to insist that an investment manager have a different target, does that mean that

there is a problem for the trustee?---We would see that as – as unsatisfactory, and – and not enabling the trustee to fulfil their obligations under the SIS Act.

And if the trustee, even if it had contractual rights, there is no realistic prospect that it would ever step in to the relationship between the related parties, is that an inadequate situation from APRAs perspective?---I would believe that would be the case.

And in that case, would it mean that the trustee, from APRAs perspective, is not acting in the best interests of members?---Again, it's – it's very hard to give a general – a specific answer to a general set of circumstances. We – we would certainly seek to understand the nature of the arrangement and the trustee's actions and whether there was a need for there to be a change in those to ensure that the trustee was acting in the best interests of members.

Have there been situations in the last three years where APRA has formed the view that a trustee, the RSE licensee, is not acting in the best interests of members?---I wouldn't say we have actually formed that view specifically. There have certainly been a number of review work and situation – and situations in the last few years where we have looked at the practices and the arrangements of trustees and required changes to those arrangements and practices so that it – the trustee was acting in the best interests of members and addressing the concerns that we had identified.

If APRA formed the view that a trustee was not acting in the best interests of members, what would its approach be to dealing with that problem?---Again, that's a very broad question. Our process in a nutshell is – is fairly consistent. We seek to understand the issue, we then form a view of what the outcome is that we think might address the concern, and then we seek to work with the trustee to achieve that outcome, which could be through our supervisory actions. It could be through requiring a special purpose investigation to which the trustee had to respond. It could ultimately be an exit from the industry or a change of trustee, and there are examples that we have provided of – of cases of those in our submissions to the Commission.

Would it ever commence litigation?---That is a potential action that we could take if we could not otherwise get the outcomes that were – that we're seeking to achieve through getting changes to practice, or even negotiating an enforceable undertaking, for example.

You know one of the criticisms that has been made by the Productivity Commission in its draft report of APRA is that the behind closed doors nature of its activities is not effective for achieving what I will call general deterrence?---That is an observation that has been made.

By the Productivity Commission?---By the Productivity Commission.

And that's an observation that APRA disagrees with?---We do disagree with that observation.

Do you agree that the characterisation of your activities as behind closed doors?---No.

And do you agree with this proposition: that what APRA does publicly does not identify specific conduct of specific entities?---In general, that would be the case. The exception would be, for example, enforceable undertakings which would ultimately become public – which do ultimately become public.

Yes, but in the case of superannuation, no corporate trustee has been required to give an enforceable undertaking, at least in the last 10 years?---Well, the Trio examples were 2013.

That wasn't a corporate trustee?---No.

Those were individual - - -?---Individuals.

- - - directors?---Yes.

So if we go back to my question: no corporate trustee has been required to give an enforceable undertaking in relation to superannuation in the last 10 years?---That's correct.

And, in fact, in total how many corporate trustees have ever been required to give an enforceable undertaking in relation - - -?---I don't know.

- - - to superannuation?---I don't believe - - -

Not many. At most a handful?---Yes.

So enforceable undertakings, if they were to occur, they would be public?---Yes.

But they don't occur. So what other public conduct does APRA engage in which would identify specific trustees and specific conduct of those trustees?---None. However, we would say that deterrence is not only determined – or deterrence effect is not only achieved by disclosure of issues with individual entities. What is more important is to have the industry aware of the practices and issues that are of concern to APRA, the areas that we are focusing on and want to see changed and improved across the industry. And that that is widely communicated across the industry and we do that through a number of ways.

Such as the thematic reviews?---Thematic review reports and letters, general industry letters on specific issues, speeches, industry engagement, insight articles, and the like.

And these things are directed, can I suggest, to trying to ensure the stability of the trustees and improve the stability of the trustees?---No, that is not their only purpose. Our – our purpose is to ensure that the practices of the trustees operating in the superannuation industry are sound and delivering good outcomes to members over the long term.

Do you agree with me that commencing public enforcement action would be destabilising for an individual trustee?---There is a risk that public action against an individual trustee may cause reputation and other issues that would potentially make the problem that we were trying to address worse, which would be destabilising for that trustee, but ultimately, the impact we would be concerned about would be the impact on the members of that fund. So the reason we take the behind the screens approach is to try to get the issue addressed, and, if needs be, those members move to a different fund and entity without having that in the public domain and causing more adverse impact on those members.

And the adverse impact on the members where there's public attention is what, from APRAs perspective?---Well, typically what you would expect to occur, if there was an issue raised in the public domain with a particular entity, would be that that would cause members and employers that were participating in that entity to have concerns, review their arrangements, seek to withdraw their funds, which would then cause the realisation of assets in a – in a manner that might create liquidity and asset valuation issues that would then ultimately damage the value of the trust and therefore lead to members getting less outcome – less value for their superannuation entitlements.

Under the SIS Act, there's a time period within which a trustee is obliged to redeem a member's interest in the superannuation fund if they roll over to another fund?---Yes, generally speaking there's a three day timeframe for that unless there are specific circumstances that warrant a longer timeframe or they get dispensation for a different time period.

And so the point you're making is if a substantial number of members of a fund reviewed their arrangements as a consequence of adverse publicity, they might all seek to switch to a better fund and that would be destabilising for the fund that is subject of the adverse publicity?---That's correct.

And it's possible that ultimately that might result in worse member outcomes, because the fund was illiquid or unable to sufficiently quickly liquidate its assets in order to move them to a different - - -?---Or you need to liquidate the assets at a value that is lower than their actual value.

Yes. And that would be a concern for APRA?---Yes.

And it would be inconsistent with maintaining the stability of the system?---It would also be inconsistent with delivering good outcomes for the members concerned.

And is that consideration something that APRA takes into account, or has taken into account, in deciding whether to commence public enforcement action?---Yes.

And do you think that that is a consideration that other conduct regulators take into account in deciding whether to commence public enforcement action?---I don't think I'm able to speak on behalf of other conduct regulators and their considerations.

I'm sorry, I said other conduct regulators. I think in fact you very specifically make the point in your statement that you are not a conduct regulator, you are a prudential regulator?---Yes.

And you distinguish between those two types of regulators?---To a degree. I mean, I think – there is an element of conduct regulation in all regulators because ultimately what is delivered in a prudential sense come back to the behaviours and practices of the individuals that are running the entities. But prudential regulators typically do have concerns about protecting the value of the assets and the – yes, and particularly when you're talking about pension trusts or superannuation trusts, that is a – a general concern of prudential regulators in undertaking their roles.

I want to return to this topic, but deal with something else first. In relation to the sole purpose test, that is a civil penalty provision under the SIS Act?---Yes.

That is something which APRA, in respect of which APRA could commence a civil penalty proceeding?---Yes.

APRA has never commenced a civil penalty proceeding in relation to the sole purpose test?---No.

And as we understand it from your statement, APRA hasn't seen a situation which it considers sufficiently clear to be a contravention of the sole purpose test?---Or sufficiently, yes, serious enough to warrant that action, or unable to be addressed in an alternate way.

Do you know whether APRA has considered this question: if a trustee is automatically or regularly debiting money from members' accounts and paying it to advisers who are not providing a service to the members, is that consistent with the sole purpose test?---I think I would need to consider that more fully to give a specific answer. I mean, we – we don't typically look specifically at individual commission or other arrangements, but prima facie it would seem unsatisfactory from a member's perspective to be paying fees for which they're getting no service.

Do you say it would be unsatisfactory?---Unsatisfactory, yes.

As you know, this has been an ongoing area of investigation - - -?---Yes.

- - - for ASIC. ASIC put out a report in October of 2016 - - -?---Yes.

- - - raising what it called the fees for no service issue?---Yes.

You know that in many cases these fees were being deducted from superannuation accounts?---Yes.

Are you saying in the subsequent almost two-year period, APRA has never considered whether that might have contravened the sole purpose test?---I'm not specifically saying that. I'm – in that specific example, we have been engaging and following ASICs work in this area, and ASIC is taking steps to address that issue and ensure that the relevant members are being appropriately remediated. We are monitoring that and we, given that that work is in train, we have not specifically considered what further action, if any, by APRA may be needed. That's not to say we won't form that view but at the moment ASIC is dealing with that matter and ensuring that members are being remediated. And so we do not want to intervene in ASICs process.

Is there a limitation period on commencing a civil penalty proceeding for a breach of the sole purpose test?---I don't know.

Is there some suggestion that you've had from ASIC that ASIC will commence public enforcement action in relation to fees for no service?---I – I don't know the answer to that question.

Is it satisfactory, from the perspective of APRA as a matter of general deterrence, that no proceeding has ever been commenced against a trustee on the basis of a contravention of the sole purpose test where the trustee is deducting money from members' accounts and paying it to related party advisers who are not providing a service?---I think it's too early to form that conclusion because that work is ongoing and APRA has not made any final decisions about what action it may or may not take ultimately in relation to that matter.

APRA – I'm sorry, ASICs responsibility, though, is not for the sole purpose test and the trustees. Do you agree?---I believe that's correct.

APRAs – I'm sorry, ASICs responsibility is in relation to potential contraventions of the Corporations Act for the provision of financial advice or potential contraventions under the ASIC Act for retaining money for services for financial advice which aren't provided?---I believe that's correct.

APRAs responsibility is for regulating trustees' compliance with the sole purpose test?---Yes.

So it can't be that the management of this issue is something that should be left to ASIC?---I am not suggesting that we are leaving it to ASIC. I am saying that we are allowing ASIC to complete its work and review, and ensure that the remediation occurs. At an appropriate point APRA will consider whether there is any further action that we need to take.

Is there some position that APRA has taken as to when in the future will be an appropriate point to consider this issue?---Not at this stage, as far as I'm aware.

So when you say APRA is waiting to see what ASIC will do, has there been any consideration at all within APRA in relation to this issue to date?---There has been discussions with individual entities and – on the matter and seeking to get a complete understanding of the issues as they pertain to the individual entities. There would be general discussions occurring at APRAs internal committees about, you know, what the issue was and what was being done to address it, and – and those sorts of things. As I said, I don't believe that we have made any conclusions at this stage as to what further action, if any, we might wish to take.

What about the question of the adequacy of trustee systems for monitoring whether advice services are provided in exchange for the fees that the trustees are debiting from the members' accounts? Is that something that APRA considers?---APRA would look at a range of systems and processes that trustees have in place to monitor particular arrangements. I am not sure that we would necessarily look specifically at advice arrangements. It may be something that we talk with some trustees about as part of our regular supervision activity. It wouldn't be something that we would necessarily look at in all cases.

Do you have a view as to whether a trustee could be acting in the best interests of its members if it does not have adequate systems in place to monitor whether advice services have been provided in exchange for the fees that the trustee is debiting from the members' accounts?---I – I think as a general proposition, we would have concerns if a trustee didn't have appropriate monitoring arrangements in place for a – a number – in fact all – all of the operations of – of the trustee of which that particular one would be – would be one.

Can I suggest to you a particularly acute problem for a trustee in deducting – I'm sorry, a superannuation trustee in deducting money from members' accounts and paying it to financial advisers for financial advice, is that the financial advice must only relate to superannuation. Do you agree with that?---Again, it is important to understand what the nature of the advice arrangements are and where the costs for that advice are being borne as to where the boundaries are in relation to the sole purpose test and – in superannuation, yes.

I think we're agreeing, but - - -?---Yes.

Let me just - - -?---I think we are agreeing.

- - - go back. Because of the sole purpose test, a member's account can't be debited to pay for financial advice that doesn't relate to superannuation?---I believe that's the case.

And so for a trustee who is properly complying or seeking to comply with the sole purpose test, they need to have systems in place, don't they, to make sure that the fees that are debited are being provided for advice related to superannuation?---Yes.

And so it would be a point of concern, presumably, for APRA if they didn't have adequate systems in place to do that?---Yes.

And if they were deducting money from members' accounts and paying it to advisers who were not providing any services, that would show very clearly that they don't have adequate systems in place?---Following all those assumptions, I guess that would be the case. Again, we would need to look at the specifics, yes.

But we know the last thing is happening. Do you agree – or has happened?---I understand so, yes.

And I'm just trying to understand whether APRA has taken any active steps to try to deal with the relevant trustees about their conduct, insofar as it might breach the sole purpose test, or about their future behaviour, insofar as it might concern the way in which they're carrying out monitoring in the future?---So, as I said earlier, the supervisors that have responsibility for the individual entities that have been identified through ASICs work have been engaging with those institutions to understand the nature and extent of the issues and how the trustee and the group, as relevant, are responding to those issues that have been raised by ASIC.

All right. So you – as you understand it, the supervisors are dealing with and taking those issues up with ASIC?---On an entity by entity basis.

Can we go to paragraph 239 of your statement, which is on page 36?---Yes.

This is a paragraph that relates to a paper that is either finalised or not finalised that APRA and ASIC are drafting?---Yes.

Is it finalised?---It was finalised on 3 August.

All right. Has it been published on APRA and ASICs websites?---Yes.

And I think you haven't exhibited the paper, but it has been exhibited by Mr Kell?---Yes.

And I will just bring that up. Can we bring up ASIC.0880.0011.3343. When was it published on your websites?---I believe it was on 3 August.

I see. It's exhibit PK-7 to Mr Kell's statement, if that assists. Would it help if I said the document ID again. It's ASIC.0800.0011.3343. Did you know when you signed your statement on 3 August that it had been finalised?---No, I knew it was in the process of being finalised but it wasn't clear that it was actually going to be finalised on that day and published on that day.

Thank you. So this is the statement?---Yes.

And the purpose of it, as we understand it, is to try to clarify the respective roles of ASIC and APRA in relation to the regulation of superannuation?---That was the intent.

And the essence of it seems to be those first two bullet points there:

> *APRA is primarily responsible for ensuring RSE licensees prudently manage their business operations in a manner consistent with their member best interest obligations and the delivery of quality member outcomes.*

?---Yes.

And:

> *ASIC is primarily responsible for ensuring RSE licensees meet their conduct obligations in their dealings with consumers, including disclosure and advice to members and ensuring members have access to complaints processes.*

?---Yes.

And this distinction of roles between APRA being responsible for prudently managing or ensuring licensees prudently manage their businesses, and ASIC being responsible for RSEs meeting their conduct obligations, is that a distinction that you think accurately reflects the roles of the two regulators?---In broad terms. I think our primary focus is on the overall operations of the trustee and the RSEs under their oversight and the – and the members as a whole, or – or equity between groups of members. Whereas ASIC is more focused on the specific relationship between the trustees and individual consumers.

Where the SIS Act contains conduct obligations, who is responsible for enforcing those?---You need to look at the specific allocation of responsibilities. I think it's in section 6 of the SIS Act as to which particular provisions of the Act are the responsibilities of the specific regulators.

Does this document help the public to understand that, that is, which regulator is responsible for the conduct obligations under the SIS Act?---The – the purpose of the document is to try and, if you like, provide a more plain English summary of those responsibilities, rather than to be a – a detailed and accurate documentation of those specific responsibilities, but we would think that the commentary in the – in the document and the supporting table about the different aspects of operations and which regulator would have primary carriage in each area is intended to help with understanding those different obligations.

If we go to attachment A to the document, which is page .3347. So this is setting out the different aspects of the regulatory responsibilities?---That's correct.

And do you have a hard copy of that document - - -?---I don't, no.

- - - Ms Rowell. Can we get a hard copy for her?---Thank you. Sorry.

If you go to the back of the document it should have the attachment?---The table, yes.

Thank you, Ms Rowell. I just wanted you to help us understand, as this is going through the responsibilities - - -?---Yes.

- - - does it identify who is responsible for ensuring that the trustee acts in the best interests of members?---The table itself probably doesn't explicitly address that point. I think the summary at the beginning does.

The summary being that it's APRA. Is that right?---Yes.

And it's APRA insofar as APRA is concerned with the trustee prudently managing their business operations?---That's correct. Although, I think there would be potentially an indirect best interest obligation that may arise from some of the areas that are ASICs responsibility, for example, in relation to poor disclosure, or the like, that would ultimately end up being not in the best interests of members, arguably.

And if there was conduct that a trustee engaged in that was not in the best interests of members, that would be whose responsibility?---Generally speaking, it would be APRAs, unless it related to specific matters such as disclosure or advice or other elements which are under ASICs responsibility.

And does the document attempting to explain the division of responsibilities explain that?---I think the document is saying, if you look at the – the way or the activities of the trustee, or the – the aspects of the operation of the trustee, it tries to summarise where the responsibility for those particular aspects sit.

I see?---And so taking from that, if there was an issue that arose in any of those particular areas, it tells you who the relevant regulatory agency would be.

You're aware that some evidence was given during the course of this week of the hearings concerning ASICs – I'm sorry, concerning APRAs engagement with Colonial about compliance with section 29WA - - -?---Yes.

- - - of the SIS Act?---Yes.

And 29WA is – well, contravention of 29WA is an offence?---Yes.

And it's an offence of strict liability?---Yes.

And for an offence – or for a contravention of section 29WA, if that was to be prosecuted, how would it be prosecuted?---We would need to apply to the court, I

believe, to issue an infringement notice, or to get the court to – to take action, I believe. I'm not – I'm not 100 per cent sure.

It has never happened that APRA has pursued a contravention of 29WA?---No.

Apart from Colonial, were there any other entities that contravened 29WA?---I believe there may have been some minor issues that involved section 29WA but I don't have the details.

The most significant one was with Colonial?---I believe so, but I'm not sure.

And the issue, as we understand it, is that Colonial between 1 January 2014 and mid-April 2014 contravened 29WA at least 15,000 times?---So the issue was that as – from 1 January 2014, contributions – default contributions needed to be paid into a MySuper product. There was a particular division of the Colonial RSE in which members typically made irregular contributions, their personal plan. Those – there was no MySuper product in that plan, so when contributions were received in respect of those members after 1 January 2014, default contributions, then there was a potential contravention of that provision of the Act.

When you say "potential contravention"?---There was a contravention.

It's a contravention, isn't it?---Yes.

And APRA had warned entities in advance of 1 January 2014 that they had to pay new default contributions into a MySuper product?---There was a reminder letter sent in November 2013.

And APRAs view was a trustee acting properly, and in compliance with its legal obligations, would put in place systems to pay default contributions into a MySuper product after 1 January 2014?---Yes, that was the expectation.

And Colonial notified APRA that it hadn't done that?---Yes.

And there were 15,000 members who received default contributions not into a MySuper product, just in that first three and a half month period of 2014?---That's correct.

And then after that, through until 2016, at least, Colonial continued to contravene the section?---There were smaller groups of members that – for which contributions were received.

Every few months there would be new members - - -?---Yes.

- - - who would have contributions?---Yes.

Is it the case that every contribution – so every time a contribution is received into the fund that is a default contribution and not paid into a MySuper product is a contravention of 29WA?---I believe that would be how the law was to be interpreted, yes.

So when we talk about 15,000 contraventions, that assume - - -?---It may be members, I think. I'm not sure.

You think it might be members?---Yes.

All right?---I'm not sure.

So in any event, though, there were 15,000 members who received – we don't know how many contributions just in that first three and a half month period?---Yes, and I think they would be probably employer contributions for those members.

They would have to be employer contributions if they're default contributions?---Yes. Yes.

And then every few months after that Colonial would give APRA an update to say there have been some more members where there have been contraventions?---So we agreed a remediation process with Colonial after the first notification of the breach as to the process that would be used to address those breaches to ensure that the members were put into the right option, be it a default option or a choice investment option, as quickly as possible, and that any differential in fee was remediated within a short time period whilst CFS took steps to establish the appropriate MySuper product in the – in the personal – or find a way to address that issue.

If we bring up CBA.0001.0451.0184. So this is the letter sent on 14 March 2014 by APRA to Colonial?---Yes.

And then if we go over to page 2, we see what - - -?---Yes.

- - - APRA put forward as an appropriate course would be that:

> *...contributions received after 1 January 2014 without an investment direction being allocated into a MySuper product or Colonial receiving a valid contribution investment direction from an affected member.*

?---Yes.

And was APRA encouraging Colonial to seek out investment directions?---I don't know that we were encouraging that. I think we were just setting out the alternative ways in which the breach could be rectified.

And then you see the second paragraph – I'm sorry the next paragraph:

Whichever solution or combination of solutions is adopted, APRA expects rectification to be completed in the short term.

?---Yes.

And ultimately, when did APRA determine that the issue was closed?---I'm not sure.

I can probably help. If we bring up exhibit – on the other side of the screen, 5.195. It's CBA.0001.0451.2600. So this is a response from APRA on 21 September 2017, where you will see the response is:

We have no further queries and consider this item closed.

?---I can see that.

That's about three and a half years after APRA sent its letter to Ms Elkins on 14 March 2014?---Yes, although I understand that the actual final payment, if you look further down that email, occurred in July 2017, still a period after, yes.

Three and a quarter years?---Yes.

And is that, from APRAs perspective, rectification completed in the short term?---I think what we were satisfied with was that the process that was dealt with each set of contributions and each member as they occurred was dealt with within a relatively short period which I understand was less than six months. So a – a period to seek a direction for the member. If the direction was received, then the contribution went to the investment choice nominated. If the direction was not received, then they went into an appropriate default product and there was, again, an adjustment made for the differential in fees in that intervening period.

That is, you start the clock ticking for the six months from when the first offence occurs in respect of that member?---I believe that was the process that was agreed at the time.

And was there an agreement by APRA that it wouldn't take any enforcement action in respect of these contraventions?---I'm not sure that I would say that that was necessarily an explicit agreement. I think what APRA agreed with CFS was an appropriate way to deal with the issue in a manner that achieved an appropriate outcome for the members that were impacted.

You see the next sentence on the page says:

Failure to rectify the breach satisfactorily may result in APRA taking enforcement action.

?---Yes.

So do we take it this was a satisfactory resolution of the breach?---I think ultimately APRA agreed an appropriate process and was satisfied that the process had been followed.

Now, one of the things that APRA had suggested, after these initial 15,000 contraventions, was that the ADA transition for the other roughly 60,000 members of the FirstChoice Personal Super product over to a MySuper product be accelerated?---I believe that was raised with them, yes.

Well, it wasn't just raised. APRA said, "This is what you should do"?---I wasn't involved in the specific communications.

And one of the reasons that APRA wanted that to occur was that that would then prevent further offences being committed?---Yes, that would be the case.

But Colonial said no?---Colonial communicated a number of issues that would need to be resolved to expedite the transfer.

And you know one of the things that Colonial said was, "We now have processes in place that will prevent any further contraventions of 29WA"?---Is that something that was communicated to us or are you basing that on the - - -

To you?---I'm not - - -

To you. I can bring it up?--- - - - familiar with all the communications between APRA and CFS.

Can we bring up CBA.0001.0451.0267. That's exhibit 5.198. This is an email from Colonial to APRA. Where it is being explained that:

> *The board after careful consideration did not approve bringing it forward.*

The third bullet point is:

> *The low probability of breaching section 29WA in the future given the controls now in place.*

?---I see that, yes.

But, in fact, it did keep breaching it?---That would appear to be the case, yes.

It kept breaching it through until at least August of 2016?---Yes.

And in respect of any of those further contraventions, do you know why APRA didn't take any enforcement action?---I would – not specifically, but I would assume that it was on the same basis, that the – as soon as it was identified, the members

were dealt with appropriately and the process that had been agreed with CFS to deal with those breaches had been implemented within the agreed timeframes.

Just on the members being dealt with appropriately – I'm sorry, Commissioner, I should tender the one email that hasn't gone into evidence. That was CBA.0001.0451.0184. That's the letter to Ms Elkins dated 14 March 2014 from APRA.

THE COMMISSIONER: Letter APRA to CFSIL of 14 March 2014 becomes exhibit 5.299. The ID is CBA.0001.0451.0184.

EXHIBIT #5.299 LETTER APRA TO CFSIL DATED 14/03/2014 (CBA.0001.0451.0184)

MR HODGE: Can we then bring up CBA.0001.0451.0310. You may not be able to help us with this, Ms Rowell. This is the letter from Ernst & Young concerning remediation by Colonial?---I have not - - -

Have you ever looked at this before?---No, I have not.

Okay. You made a comment before, though, about the remediation being based on the difference in fees between the ADA product and the MySuper product?---That's based on a summary update that I've received in the last few days in preparing for this hearing.

All right. I will just tender that document, Commissioner, rather than asking Ms Rowell about it.

THE COMMISSIONER: Letter EY to CFSIL, 13 October '14, CBA.0001.0451.0310, exhibit 5.300.

EXHIBIT #5.300 LETTER EY TO CFSIL DATED 13/10/2014 (CBA.0001.0451.0310)

MR HODGE: Now, you know that the documents that CBA provided to APRA included the call script and letter that it proposed to use?---I believe so.

Have you reviewed that call script and letter in the course of preparing to give evidence today?---No, I have not.

You haven't looked at it?---No.

Can we bring up exhibit 5.189, which is CBA.0001.0451.0217. So this is an email that was sent by Colonial to an employee at APRA. You will see it attaches the final version of the member communication that's proposed to be used?---Is that over the page?

We can bring that up. If we bring up CBA.0001.0451.0218. This is the standard form letter that's going to be sent out to members?---Yes.

And you see what the members are going to be told in the second paragraph is:

> *There has been a recent change to superannuation legislation which requires us to hold an investment direction from you in relation to future contributions paid into FirstChoice Personal Super. If a direction is not held by us, we are unable to accept contributions into your account. For this reason, we would like you to confirm the investment options into which you would like your contributions to be paid.*

?---Yes.

Now, what I want to suggest to you is this letter is going to mislead the recipients into thinking that they need to give an investment direction?---To be a member of this – to remain a member and to have their contributions credited to this particular product would mean that they needed to give an investment choice direction.

Yes. What the letter doesn't explain, can I suggest, is that if there's no investment direction, then what Colonial is required to do is to pay their contributions into a MySuper product?---Well, that is not in that paragraph. I have not seen the full letter. I don't know if there's more to it.

You can assume there's no more to it. Do you know whether somebody within APRA would have reviewed this correspondence before saying that it was okay?---My understanding is that it was considered internally by APRA at the time.

It was considered?---I believe so.

And considered to be acceptable?---My understanding is that is the case but I was not involved in those discussions.

And was the call script also considered?---I believe the call script was provided.

And APRA would have also satisfied itself that the call script was acceptable?---I believe it was looked at. As I said, I was not involved at the time.

Is it acceptable, from APRAs perspective, that Colonial would be making misleading statements to members in order to obtain an investment direction which would then lead to them no longer contravening 29WA?---Making misleading statements would be unacceptable. I don't have enough information to know whether that is the case

here or not. I think certainly complete – more complete communication to the members would have been desirable.

I take it that in the last few days, as you've received briefings about the Royal Commission, nobody has told you or given you any detail about the evidence that was given by Colonial in this respect?---I have had high level updates on it but not in depth detail.

Have you been told about Ms Elkins' evidence in respect of the call script and letter?---I have had updates on some of that evidence.

Have you been told that Ms Elkins acknowledged that some of the statements were misleading?---I'm aware that's what was indicated.

Have you been told why it is, if the statements are misleading, APRA approved them?---I was provided with some general updates as to the context in which this issue occurred and how APRA dealt with it.

Have you inquired as to why APRA would have approved the call script and letter if they were misleading?---Given that this arose in the last few days I have not had the opportunity to require – expect a detailed briefing on that, no.

That's something you're going to inquire into?---There is no doubt that these matters are under discussion with – within APRA.

Can I perhaps just - - -

THE COMMISSIONER: And those discussions could not be brought to an end before you came into the witness box to give evidence. Is that the position?---That's correct.

Go on.

MR HODGE: Can we bring up the call script, which is exhibit 5.203, CBA.0001.0479.0817. Now, this – actually, this is a different call script. This is a call script for a later call-out campaign. But nevertheless, let me ask you about this one while we find the other one. So this is a guide being given to call centre staff at CBA. You see the background is:

> *Changes to super legislation require us to hold an investment direction from all of our clients about how they want their super invested. If we don't have this information, this account balance is defined as an accrued default amount and we have to transfer this balance to a MySuper product.*

?---I can see that is what it says, yes.

And then you see:

What is success? Contacting client, letting them know that a change is coming to their super which may result in an increase to their ongoing annual fees, costs and insurance premiums.

?---I can see those words, yes.

Continuing:

They need to be aware that they can opt out of this transfer and avoid an increase in fees and premiums if they confirm their investment direction with us.

?---Yes, I can see that.

And then if we go over the page, you see what the call centre staff member is going to say is:

There has been a legislative change, which means that some or all of your FirstChoice Employer Super account balance will be transferred to the life stage investment option later this year. If this transfer proceeds, your ongoing fees and costs may increase.

?---Yes.

Was it APRAs understanding at any time that trustees were taking – I'm sorry, I should withdraw that. Retail trustees were taking active steps to try to obtain investment directions, rather than have ADAs transition over to MySuper products?---We were aware that was occurring. That was, in essence, part of the transition process from the previous legislative provisions to the implementation of MySuper was that the transition process was to allow the entities to – where it wasn't – particularly where it wasn't clear, as to whether a member had made a specific investment choice or not, to communicate with those members, tell them about what the changes were, and get them to either make a specific investment choice or move to a default product.

Was APRA aware that, in general, ADAs would have commissions embedded into them whereas MySuper products have no commissions?---I'm not sure that we necessarily were aware of that at the time.

Is APRA aware of that now?---Our – can you repeat the question, please?

Yes. Is APRA aware that – I will frame it more generally – many ADAs have commissions embedded into them?---I'm – I'm not sure that I have an understanding of the extent to which that is the case.

Did APRA have any understanding as to whether it would be in the financial interests of the retail trustees to keep members in ADAs rather than having them

move to the MySuper product?---I think given the differences between the product structures and fees, it is – there are differences in fee structures and – and terms and conditions between the products, which mean that typically fees are higher in choice products than default products. So that would be in the retail RSEs – they would get more fees for having members in choice products.

So the answer to my question is yes, it would be in the interests of the retail trustees to keep members in ADAs rather than moving them to MySuper products?---Yes, but the conclusion from that is not necessarily that that's not in members' best interests.

To pay higher fees?---Yes.

With commissions?---Yes.

Does APRA have a view as to whether the payment of commissions is in the best interests of members?---You need to look at that issue in the context of the overall products and features and terms and conditions, and what the member is getting in that context to form a view about that. You can't look at line items in a – a product or an option individually to form that view.

What can a member possibly get for a commission?---It's the nature of the structure of those products that were established. It was part of the distribution mechanism and the overall cost base of the – of the product. So it was something in the choice context that the members understood at the time. And so you need to look at it in that – in that wider context to form a view.

Well, they weren't choice members when they went into the ADA products, were they?---Some were, some weren't. I understand.

By definition they can't have been because an ADA is a default product where no investment direction has been given?---I – I think part of the issue that existed at the time of that transition was that it – it wasn't necessarily clear as to the – the nature of the members that were in what were called accrued default amounts as to whether they had actually made a choice in being put into those products.

If they hadn't given an investment direction, they were in an ADA?---Yes, but there was some work needed by the retail trustees at the time to determine whether members had in fact given investment directions.

They could only be in an ADA or they could only be deemed to be invested in an ADA if they hadn't given an investment direction?---Ultimately that was the – yes.

To return to the commission issue, just so I understand what you're saying, you're saying it might be possible that it remains in the members' interests to continue to have a commission deducted from their account and paid to a financial adviser where there's no obligation on the part of the financial adviser to provide an ongoing service to the member?---Commissions were originally about the distribution of the

product and were structured at the time as part of the embedded costs and – and features of those products. And if you were transferring that product, then those features would – would continue. And I think you would need to do more analysis to assess whether there was any member interest issue there. You can't look at that in isolation.

Do you mean you need to compare the overall value of the ADA product with the MySuper product?---Yes.

And, therefore, then conclude as to whether or not the member is better off going to the MySuper product?---Yes.

And so if the member is paying lower fees to go to a product with a similar investment strategy, is there a way in which that could, nevertheless, not be in the interests of the member?---There's too many negatives in that question for me. Can you just repeat that again for me, please?

If the member is going to pay lower fees on going into the MySuper product, with a similar investment strategy to the ADA product, is there still some way in which you think that might not be in the best interests of the member?---It's hard to say in the specifics of the case. And, again, you need to look at the overall structure of the arrangements and best interest needs to be assessed at a range of levels, for the RSE as a whole, for different cohorts of members within the – within the RSE and – and form an overall view, part of which is net returns costs and other features but it's also about the ongoing viability and sustainability of the RSE itself.

Did APRA have a concern from 1 July – at any time from 1 July 2014 about whether retail RSE licensees were acting in their own financial interests when they communicated to members who were in ADAs in order to obtain an investment direction from those members?---My understanding of the process that was undertaken by the supervisors at the time was that they were engaging with each of the entities under their – that they were supervising to understand the nature of the arrangements and what processes were being undertaken. I am not in a position to know whether there were any specific concerns that we had at that time.

Has there been any general project undertaken by APRA to evaluate whether retail RSE licensees acted in their own financial interests in relation to the transfer of ADAs to MySuper products?---No, there has not.

Has there been any concern internally at a general level for APRA as to whether retail RSE licensees acted in their own financial interests in relation to the transfer of ADAs to MySuper?---I – I don't believe so. I think as a general proposition, APRA does have concerns about the management and oversight of related party arrangements generally within the retail sector and the not for profit sector and seek to understand those and whether the trustees are exercising their decision-making in the best interests of members. I'm not sure that we have specifically focused on the

ADA process as part of that consideration. We've looked at a range of different arrangements in terms of related party arrangements.

Can we bring up – we found the right exhibit now – exhibit 5.187, which is CBA.0001.0451.0204. This is the call script that was to be used for that first – at this time it was only 14,000. It then turned out it was 15,000 members who were members of FirstChoice Personal Super where there were default contributions being paid into their account after 1 January 2014. You haven't seen this document before?---No, I haven't.

Let me ask you this: do you see in the middle of the page that the script says:

> *We have been receiving contributions into your account and they are currently being invested into the –*

Whatever the investment option is?---Yes.

Continuing:

> *There has been a recent change to legislation which requires us to confirm the investment options into which you would like your superannuation contributions paid. Would you like me to complete this now on your behalf over the phone?*

?---I can see that.

Do you agree that on its face that is misleading?---I agree that it doesn't provide complete information to the member to enable them to make their choice or decision.

And is that an acceptable outcome from APRAs perspective?---It's not desirable or – I would say.

It's not desirable? Surely it's unacceptable from a regulator's perspective?---It would be preferable if there was complete disclosure to the members.

I don't have any further questions for this witness.

THE COMMISSIONER: Ms Rowell, you've spoken of APRA supervising the work of trustees. A part of that work I understand to be to see whether trustees are asking the right questions of other entities in the business of which they form part. Is that right?---That's correct.

And APRA has no capacity to go and interrogate other parts of the entities other than the trustee, does it?---We can do so. Through our outsourcing standard, we have the ability to engage with the material providers of services to the trustee.

And routinely do?---We do.

Yes. The trustee asking the right questions is one thing. If the flow of information to the trustee is controlled by other parts of the business, how can the trustee know what question to ask?---I – I think it's a practical reality that a lot of the information that comes to the trustee necessarily comes from their service providers, and in a retail group they would be related party service providers. I don't think that means that the trustee can't, therefore, ask for different information or more information, or obtain information from other parties, or require independent review of the information that is provided to them in order to – to form and make better decisions. Indeed, our expectation – excuse me, Commissioner.

No, finish?---Would be that trustees would take some of those steps to satisfy themselves that they were getting the right information and asking the right questions.

How can APRA form any judgment about whether the trustee is doing its job properly?---Through our supervision activities and our engagement with the – the trustee and other parties within the operations of the trustee itself and their material service providers, and also through our review of the information that the trustee itself is looking at and our assessment as to whether that is adequate and – and sufficient to enable them to fulfil their duties.

Yes. Is there anything arising, Mr Hodge?

MR HODGE: No, Commissioner, although I would just like to follow on with one other question - - -

THE COMMISSIONER: Yes.

MR HODGE: Or one other set of questions. Can we bring up paragraph 253 of Ms Rowell's statement. That's on page 38?---Yes.

So in this paragraph you're expressing the position of APRA which is it strongly supports certain amendments which are going to expand APRAs powers to be able to give directions to trustees?---That's correct.

And it will be possible, if the Bill passes, for APRA to direct trustees to make changes to the systems, business practices, or operation?---That's correct.

And, indeed, in subparagraph (g):

> *To do, or refrain from doing, anything else in relation to the affairs of the licensee, the funds for which that licensee is the trustee or any subsidiary.*

?---Yes.

And one of the things that that would seemingly permit APRA to do would be to direct a trustee to merge the fund with another trustee?---That would be a possible use of that power, yes.

Is it likely that APRA would ever actually do that?---You couldn't rule it out. Yes, we would do that.

One of the challenges with taking any significant action or making any significant direction like that would presumably be the likelihood that it would be subject to challenge in court?---That – that is always possible.

And for something like that, the likelihood that one of the trustees, at least, would bring a review application in the Federal Court or in the Administrative Appeals Tribunal would be quite high?---That's possible. Hard to judge the likelihood.

And would it be the case that APRA, in deciding whether to exercise this power, would have to consider the likelihood of court challenge?---I mean, that would be a consideration. The primary consideration would be whether the merger was in the best interests of members and the issues at play and the particular seriousness of the issues that were wanting us to direct the merger to occur, as to how we would weigh up those – those different considerations.

There have been some mergers that have fallen – almost occurred but fallen over in the last few years?---Yes.

For example, the potential merger between Equip Super and Energy Super?---Yes.

And the potential merger between Equip Super and Vision Super?---Yes.

And APRA has reviewed those cases?---We're aware of those cases, yes.

Has - - -?---It has engaged with the relevant trustees to understand the rationale for those decisions.

And formed a view that the decisions were not unreasonable?---I'm not sure I would characterise it that way. I think when we look at a merger and the assessment that the trustees have made, we want to – part of the consideration is the – the viability and the outcomes being delivered by the trustee separately, as – and whether there is any concerns that we would have that would suggest that there was a need or an imperative for a merger to occur. That wasn't the case in either of those situations, as I understand it.

Is one of the other things that APRA could conceivably do under these powers, if it had them, be to direct a trustee to unwind some particular structure that it had in place?---That would be a potential use of those directions, yes.

For example, it might be able to direct an entity, which was both the trustee of a superannuation fund and also the responsible entity of a managed investment scheme, to unwind that arrangement?---Yes.

And is that something that, in your view, APRA might consider doing if it had these powers?---Yes.

And that particular type of structure known as a DRE structure, is that a structure of particular concern to APRA?---It is a structure which in our view raises a number of issues around conflicts management that are difficult to effectively manage and hence that does create concerns. And, indeed, we have actually achieved changes in other DRE structures in the past where we were uncomfortable with or unhappy with the management of conflicts and got – got that separation to occur.

It was the structure of Trio, was it?---No, there were other examples as well.

No, no but it was the structure of Trio?---It was the structure of Trio, yes.

You're making the point that with some other entities you've been able to persuade them to unwind that structure?---That's correct.

MR HODGE: Thank you, Commissioner.

THE COMMISSIONER: Yes, Mr Dick.

MR DICK: Nothing in re-examination, Commissioner.

THE COMMISSIONER: Thank you. Thank you very much, Ms Rowell. You may step down. You're excused.

<THE WITNESS WITHDREW [11.36 am]

MR HODGE: Commissioner, the next witness is Mr Glenfield.

THE COMMISSIONER: Yes.

<STEPHEN EDWARD GLENFIELD, AFFIRMED [11.37 am]

<EXAMINATION-IN-CHIEF BY MR DICK

THE COMMISSIONER: Thank you. Do sit down, Mr Glenfield. Yes, Mr Dick.

MR DICK: Thanks, Commissioner. Mr Glenfield is your full name Stephen Edward Glenfield?---Yes, it is.

And your current business address is the APRA offices at 535 Bourke Street in Melbourne?---It is.

Could you tell the Commissioner your current position in APRA?---I'm a general manager of the specialised institutions division.

And have you received a summons to appear at this round of the hearings of the Commission?---I have.

Do you have the summons with you?---I do.

I tender the summons, Commissioner.

THE COMMISSIONER: Exhibit 5.301, summons to Mr Glenfield.

EXHIBIT #5.301 SUMMONS TO MR GLENFIELD

MR DICK: And Mr Glenfield, you've prepared a witness statement dated 14 August 2018 for this round of hearings?---I have, yes.

And do you have that statement with you?---I do.

And are the contents of the statement true and correct to the best of your belief?---They are, yes.

Mr Commissioner, I tender the statement and the exhibit.

THE COMMISSIONER: The statement and exhibits to the statement of Mr Glenfield of 14 August '18 is exhibit 5.302.

EXHIBIT #5.302 STATEMENT AND EXHIBITS TO THE STATEMENT OF MR GLENFIELD DATED 14/08/2018

THE COMMISSIONER: Thank you, Mr Dick. Yes, Mr Hodge.

<CROSS-EXAMINATION BY MR HODGE [11.38 am]

MR HODGE: Thank you, Commissioner.

Mr Glenfield, what I want to ask you some questions about is IOOF. And in your statement you have given some evidence about the dealings between APRA and IOOF?---I have, yes.

And could you just explain your role in relation to the dealings between APRA and IOOF?---Okay. My role was as general manager of south-west region, which is the region covering Melbourne, Adelaide, Perth, which supervise a range of institutions across superannuation, banking, etcetera. One of the institutions within that was IOOF, so we have a supervisory team that supervises IOOF. I'm their general manager.

You're the what, sorry?---Their general manager.

I see?---Sorry.

And this is, as we understand it, an ongoing issue. Is that right?---IOOF?

Yes?---Yes, it is.

Now, you've given some evidence about the issue that arose with respect to Questor and the cash management trust?---I have, yes.

I just want to make sure we're, at least to begin with, in agreement about the relevant background. Questor was – it may still technically be – a subsidiary of IOOF Holdings?---Yes, it was.

And it was both the trustee of a superannuation fund and the responsible entity for at least two managed investment schemes?---A dual regulated entity, yes.

You just need - - -?---Okay, yes, sorry.

So it was the responsible entity for the IDPS-like scheme?---Yes. Correct.

Does that ring a bell for you?---It does, yes.

And it was also the responsible entity for the cash management trust?---It was, yes.

And as the trustee, it invested some of the assets of the superannuation fund in the cash management trust?---It did, yes.

And as the responsible entity of the IDPS-like scheme, it invested some of the assets of that scheme in the cash management trust?---It did, yes.

And there was then an issue which was that an amount of money back in 2009 was incorrectly recorded as income rather than an asset?---That's correct.

And it was then distributed to then members of the cash management trust?---Also correct.

And then at some point in time Questor instituted a process to try to claw back that money that it had incorrectly distributed?---Correct.

And the way in which it went about doing that was from September 2011 it reduced the unit price – I'm sorry, the distribution that was being paid from units in the cash management trust?---Correct.

And in that way, over the course of three years, it sought to effectively claw back the over-distribution?---Correct.

But to do that not from the people to whom it had distributed the money in the first place but rather from the people who were current members or currently invested in the CMT – they may be the same in some cases?---I was about to say it would include some who had had the over-distribution but others who had joined since that weren't part of that.

And when did APRA first become aware of that issue?---APRA, and my – the supervision team identified it during a – I think a review of audit papers or risk and compliance papers in about 2011, I think, or two – 2011/12. I can't recall. It's in – it's in the statement. The date escapes me.

It was in the statement - - -?---It was post the event.

At some stage APRA identified the fact that this had occurred?---Yes.

And you're saying that was done before there was any notification of that fact by IOOF or Questor to APRA?---Correct.

And when did APRA first become – or first take steps then to contact Questor about this?---I'm trying to recall. We – as part of our review, we did an onsite review of IOOF Questor around about early 2016, I think is the review report that goes out, where we've reviewed the actions taken to remediate.

I just want to make sure we're not - - -?---Yes.

- - - losing - - -?---Some time.

Misunderstanding the time. If we bring up your statement in paragraph - - -?---Thank you.

- - - 105. On page 23 - - -?---23, thank you.

- - - of the statement. So there you speak about APRAs 21 December 2015 prudential review report?---Correct.

And then over the page from paragraph 106, you say:

> *APRA wrote to Questor on 23 June 2016 seeking clarity around the cash management trust over-distribution matter.*

?---Correct.

Do you think that APRA was aware of the issue before about mid-2016, or you're not sure?---No. No. We would have identified it shortly before that, but then gone out to see them quickly once we had identified.

So you probably identified the issue in about 2016?---Yes. I would accept that.

And then – and then went and saw them about it?---Mmm.

And then wrote to them?---Wrote to them, yes.

And the issue had further progressed by the time you got to it, because Questor had implemented its remediation approach?---Correct.

And its remediation approach was that it had reached a settlement with the former custodian?---It had, yes.

And it had received, effectively, half of the amount that it needed to compensate members of the trust – I'm sorry, members of the superannuation fund and the IDPS-like scheme from the former custodian?---Correct.

And it used that settlement moneys to fully compensate the members of the IDPS-like scheme?---This is the RE, yes.

And then it used the balance of those settlement moneys plus the general reserve of the superannuation fund to compensate the members of the superannuation fund?---That's correct.

And just so I make sure we agree about this, do we agree that the reserve is an asset of the fund?---We do.

And do we agree that the trustee holds the assets of the fund on trust for the members?---We do.

And do we agree that the general reserve then, although not allocated to any specific member, belongs to the members?---I do.

And there are going to be certain circumstances set out in the relevant policies in which the trustee can use the reserve for certain purposes?---Correct.

And is it fair to say the concern that APRA had on becoming aware of what Questor had done was that rather than using its own funds to compensate the members where it appeared at least arguable that it was at fault, Questor had used the reserve which belonged to the members to compensate the members?---I think – I think APRA had a dual concern. The first was the distribution of the – the compensation from NAS, as it was at the time, in that it had – it had – with its RE hat on, it had distributed 100 per cent for the IDPS-like, and then the remainder to the superannuation fund members, with its RE hat on. Our concern was that it – it may have had an obligation to actually balance the interests of the two in the distribution, so would you give all to the – to the – to the IDPS crew and less to APRA. We were concerned that that was not correct. Then from the position of the trustee, having received compensation that was less than the full amount, we were concerned that they were not, as with their RSEL hat on, looking to action to the RE to get full compensation for the trustee members.

And this issue, once it was identified in 2016, was the third issue of a similar kind that APRA had identified within the space of the last – or the preceding six or seven months?---So there was a – yes, there were two others. One was I think called Pursuit. It was a sweep for an error that had been made and there was one other, yes.

And if we go to exhibit SG1-17, which is APRA.0002.0003.0698. This is an earlier letter sent in December of 2015 to the directors of IOOF Holdings by APRA?---Correct, yes.

And if we go to page – or bring up pages 0703 and 0704 on the screen at the same time. We see in this earlier letter APRA raising a concern about those two earlier incidents, one which was an issue with IIML in relation to the Pursuit redistribution breach?---Yes.

And the other in relation to Questor for the TPS regular investment sweep breach?---Yes.

And the point that is made, if you go over the page to page .0704, is that the non-superannuation members were compensated by the company operator, whereas the superannuation members were compensated from their own moneys via the Operational Risk Financial Reserve?---Correct.

And APRAs point is it is very hard to see how a decision to compensate beneficiaries in this manner aligns with the covenant in section 52(2)(d)?---Correct.

Do you want to just explain to the Commissioner what 52(2)(d) is?---In acting in the best interests of members, I didn't feel that the – the way that they had dealt with it was appropriate.

I think 52(2)(d) relates to conflicts of interest, doesn't it, and preferring the interests of the members – or the absolute obligation to act in the interests of the members?---Correct.

And APRAs point, if I can summarise it, is if the company makes a mistake that causes loss to the members, then it is not in the best interests of the members and not preferring the interests of the members to use the reserve funds, which are part of the trust, to compensate them, rather than having the company pay for its mistake?---To me, I would expect whilst you can possibly use the reserve to put the members back to the position they should be in immediately, you would, nonetheless, follow up the RE for compensation.

Except in this case, the RE is the trustee?---Which is the great challenge, yes.

Which is the what, sorry?---Is the challenge in that – in that structure.

It seems actually like it's not much of a challenge at all, in the sense that if the company is acting properly in accordance with its statutory obligations, it just has to put its hand into its pocket and compensate the members for its mistake?---From a – from an RSEL viewpoint they should be seeking that from the – from the RE.

And this is, as I say, December 2015. The cash management trust issue isn't going to be recorded for another six months or so. But the approach of IOOF remained an ongoing concern, can I suggest, for APRA in the intervening six months?---Yes, I would agree with that.

And I think you referred to having – that there would have been a meeting with IOOF. Can we bring up APRA.0002.0004.6714. So this is APRAs file note of a meeting that was held on 24 March 2016 between APRA and IOOF?---It looks like a file note from the prudential consultation which was held with the board.

And you attended that?---I did, yes.

And do you recall the meeting now?---I do, yes.

And one of the issues which has been identified by this stage, if we look at the fifth bullet point, is the cash management trust. It said:

> *Discussion regarding the CMT, board believes that the compensation from NAB went into the general reserve which then paid both retail and super members. Therefore, there was no inequality. APRA noted that this wasn't so much the issue but rather the rectification plan which saw IIML skim returns of all superannuation members.*

?---I see that, yes.

Now, that probably suggests that at that time both sides may not have fully understood what had occurred, because certainly the payment from NAB, the former custodian, didn't go into the general reserve?---Correct. We've moved on since then.

The general reserve couldn't have been used to pay retail customers because – or retail members because the general reserve is in the super fund?---On the presumption – and I don't know the answer to it – that that general reserve they're referring to is the general reserve of the super fund, that is correct. I don't - - -

I - - -?---I'm not fully - - -

I understand?--- - - - clear if there is a general reserve in the other fund.

In the what, sorry?---I wasn't – to the point I'm not clear if there is a other general reserve in the group named general reserve but if we make the presumption that it is the general reserve in the super fund, then you are correct.

And it wasn't IIML that was skimming the returns of superannuation members, it was Questor?---In terms of skimming .....

Sorry?---In what way skimming?

That's what APRA has recorded:

> *The rectification plan which saw IIML skim returns of all superannuation members.*

?---I haven't written the note so I don't know what that's getting at.

All right. And then if we go over the page to .6717. This is the note of APRAs view of culture?---Correct, yes.

And it is said – we see in the third paragraph:

> *IOOF operate their superannuation business within a silo and appear to be insulated from the rest of the superannuation industry with views which are not consistent with the industry or best practice.*

?---Yes.

And:

> *The board and management have been seen to make decisions which appear to favour shareholders above superannuation members. A legalistic approach to decision-making is often taken with a means to shield IOOF from obligations which may be in members' best interests.*

?---Yes, so - - -

Go on?---At the meeting, part of what we were trying to do was to get the – the board and management of IOOF to be more interactive with APRA in a way that we've generally found with other funds.

And so this is recording what APRA would have said to IOOF at that meeting?---Our EGM, Keith Chapman, led that discussion, yes.

And this reflects your general recollection of what was said to IOOF at the meeting?---It does, yes.

Now, then, as you've noted in your witness statement, then in June there is the letter sent to – from APRA to IOOF concerning the cash management trust issue?---Yes.

I'm sorry, Commissioner, I tender that file note.

THE COMMISSIONER: File note of meeting between APRA and IOOF, 24 March '16, APRA.0002.0004.6714, exhibit 5.303.

EXHIBIT #5.303 FILE NOTE OF MEETING BETWEEN APRA AND IOOF DATED 24/03/2016 (APRA.0002.0004.6714)

MR HODGE: And then in July of 2016 there is a memo that is sent from a principal analyst to you. Can we bring up APRA.0002.0004.5205. Is the analyst the supervisor in relation to IOOF?---That's correct.

Do you receive memos from the supervisors informing you of where things are at?---I think this memo was preparing me for a meeting we had with the board coming up.

I see. And I just want to direct you to – if we go to page .5206, we see paragraph 11:

> *Supervisions assessment is that IOOFs decision to appoint two additional non-executive directors on the board has been done to appease APRA. From the information received to date it appears that IOOF does not intend to engage in genuine and critical consideration as to how it will structure its governance framework going forward to ensure it better delivers upon its obligations to members' beneficiaries.*

?---Yes.

And - - -?---Would you like some context around that?

Sure?---Okay. So we had done – I think there was the previous off-site review, which is the 215. As part of the response to that IOOF had given us a commitment to review their governance frameworks. The team – which we would have expected

was a – a wide ranging governance framework review. The team was concerned that that framework review was not going to be as in depth as we wanted and was more relying on the appointment of two independent directors to meet the governance issues. It's highlighting to me that we would expect them to do more.

And the view of the supervisor that's expressed here, is that a view that you shared?---At the point that came to me, that was the first briefing of where they had got to. This was to go to the meeting with the board to – to discuss what they were actually doing with the framework with a view to pushing them to go further.

In December of 2016 there was a letter that APRA sent to the directors of Questor concerning the CMT issue. And that is exhibit SG-1-39 to your statement, it's APRA.0002.0006.2432. So this is the letter that APRA sends – and I think you're the signatory. If we bring up page .2434?---I am, yes.

And here you are expressing on behalf of APRA the view that:

> *The use of TPS Super Fund general reserve moneys to compensate TPS super fund members for a loss caused by Questor as responsible entity of the CMT is inappropriate.*

?---I agree.

And you said that:

> *Acting in the best interests of the super fund members Questor ought to immediately replenish the general reserves utilising its funds as responsible entity.*

?---Correct.

And you then said:

> *A failure by Questor to appropriately replenish TPS Super Fund's general reserve will escalate APRAs concerns in respect of Questor meeting its prudential, fiduciary and legislative obligations and may lead APRA to further scrutinise Questor's commitment to prioritising the best interests of its superannuation members.*

?---I did, yes.

Was there some enforcement process that was in contemplation by APRA at that time?---So the – the view that I had taken at that point was – I was of the view – and it's the consistent view that I think you've expressed when you were – with IOOF was that they were – that it was member money being used to compensate and I didn't think that was appropriate. We took – I took internal legal advice at the time to confirm my view, which we obtained. So I – on the basis of that, my view was

that if they didn't replenish, that we should consider whether that – whether there was an action that could be taken for them not doing so, yes, which we referred to our enforcement committee to look at.

And what is the action that was under contemplation?---I was open at the point but part of that could have been a range of matters. It could have been a direction, it could have been taking action against individuals. But I was open to saying that we would go to a more forceful set of actions than – than the traditional style – the way that we were supervising it at the time.

If we then go to SG-1-40. This is the letter that you received in response from Mr Kelaher of IOOF?---Correct, yes.

I'm sorry, that's APRA.0007.0002.1765. And IOOF refused to replenish the general reserve funds?---They did, yes.

Out of curiosity, had IOOF been asked to replenish the ORFR in the case of the earlier issues that had been identified?---No, I hadn't at that point.

You hadn't asked them to do that?---No.

And if we go to page .1766. Do you see in the bottom half of the page APRA has made various statements about options that had apparently been considered by a rectification committee?---I do, yes.

Did APRA undertake any investigations to see whether there was any factual basis for these statements?---No, we didn't.

And then if we go to page .1769. We see the conclusion of what Mr Kelaher says is the final and most relevant fact, which is that:

> *At no time has Questor received any demands for compensation or complaint about its remediation and compensation plans from any member of the TPS Super Fund.*

?---I do.

Did you have any reason to think that an ordinary member of the fund would have any idea what had happened?---No, I didn't.

And then Mr Kelaher says:

> *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.*

?---I do. And I didn't support that view. I don't support that view.

You don't think the pub test is in any sense a way of explaining the best interests duty?---No, I think the best interests duty is clear under the – under the relevant Act.

And there was another issue, wasn't there, which was that one of the things that IOOF seemed to not understand was that there wasn't a question of balancing competing interests under the SIS Act. What was required was that they prioritise the interests of the members of the super fund?---And I've written to them on that.

And you wrote to them and pointed that out?---I did, yes.

And this is April of 2017?---Correct.

Then in May of 2017 there's an internal memo to the escalation and enforcement committee. Can we bring that up. That's APRA.0002.0007.3851. You see this is dated 19 May 2017?---I do, yes.

Are you on the escalation and enforcement committee?---No, I'm not.

Do you – or were you aware of this memorandum being sent?---I've seen and reviewed the memo.

In the course of preparing to give evidence, or you saw it at the time?---I saw it after the enforcement committee – no, I – I can't recall if I saw the memo before the enforcement committee meeting or shortly after but I have seen it, yes.

And if we go to page .3852. We see there's Proposed Strategy. And the second paragraph under that heading says:

> *Frontline's current view –*

I should confirm "frontline" means, effectively, the supervisor?---Effectively my team. Yes.

Sorry, did you say "and your team" or - - -?---So effectively my – it is my team – frontline - - -

Your team is frontline?---Yes. Correct. Frontline supervisors.

Continuing:

> *Frontline's current view is that whilst IOOF have established a reasonable conflicts management framework they have yet to properly implement the framework. Consequently, frontline are concerned that a continued failure by IOOF to implement their conflicts management framework will lead to further instances where IOOF prefer the interests of its other entities/shareholders over those of its superannuation members such as took place in the CMT over-distribution matter.*

?---Yes, so that's based on our on-site review. So IOOF had done considerable work around changing their framework in terms of documentation. Our on-site review – we concluded that it wasn't fully bedded down and operating so we retained concerns.

That is, they had recorded in writing a framework that appeared to be satisfactory to APRA?---So I think the framework appeared satisfactory. I think there were conclusions that the – at general level the staff were putting that into play well but we had concerns remaining at the board level.

If we go to page .3854. We see Next Steps which are that there will be a prudential review on 29 and 30 May?---Yes, I do.

And it will then follow that APRA will then – it will look at whether it has sufficient evidence in the – in the event that the use of coercive powers are deemed to be necessary?---I do.

At this point then APRAs view is, "We haven't reached the point where we would use coercive powers"?---No, not yet. I think at this point – so we've had probably two main reviews around – well, around that area in terms of we did a desk review, which was the 2015, which is looking at the policies and procedures, looking at the minutes and reviewing what's there, which in our mind identified concerns which we wrote to the board about and asked them to – to address. We then went out followed that up with the following review which was going on site to confirm whether what they've said they've done is actually playing out, because in – in anything we do, it's one thing to write it down, it's another thing to actually see it playing out and that it's actually being complied with. And we raised concerns from there. At this point, for me, I – having met the board and gone through it – they've had a number of reviews being done by externals which aren't identifying issues to them but our view is that we still see issue. So I'm still looking for a corroborative piece to support APRAs view to give me a very strong case to go forward. And you will – you may well come to it later. Part of that review is Ernst & Young coming in independently to review the operations of the framework. So looking for an external view that supports APRAs view – because remembering, the APRA view is a two or three day review, it's not an extensive there for weeks and weeks, we've got EY coming in to do a very deep dive review. Those two together could well corroborate to give the full extent of the evidence needed.

There's two separate issues, though, here, aren't there? One is I think the issue that you're talking about, which is there is an ongoing concern of APRA about the adequacy of the governance and management frameworks that IOOF has in place?---I agree.

And there's a separate issue, which is has there been some breach of the law in relation to what has happened with the Questor cash management trust issue, the Pursuit breach and the Sweep breach. Do you agree?---I agree.

And at this point in time, what happens to those specific breaches?---Well, the Questor, we – we referred to the enforcement committee, which has got our general counsel, our head of enforcement on it, who took internal legal advice on likelihood of success in pursuing that matter. That came back – the legal advice came back that it was complex, there were a number of – there were a number of matters that made it less than clear-cut. So not to pursue at that point but to bring it into the broader review that we were doing of IOOF at the time.

Do you accept that for most regulators not every case that they will commence in a court will be clear-cut, 90 per cent – 90 per cent certainty of success?---I would accept that, but in this case, the advice was that we didn't have enough to take the case forward. I accepted the legal advice.

Well, one of the things you say in your statement is that you formed the view that the reserve policy permitted Questor to use the money for this purpose?---The Questor policy, as I understood it, allows for payment for compensation. So our – the team that reviewed that concluded that, yes.

Yes. And I think you say this – if we bring up pages 24 and 25 of your statement. I'm sorry, Commissioner, I tender that document.

THE COMMISSIONER: Memo to escalation and enforcement committee, 19 May 2017, APRA.0002.0007.3851, exhibit 5.304.

EXHIBIT #5.304 MEMO TO ESCALATION AND ENFORCEMENT COMMITTEE DATED 19/05/2017 (APRA.0002.0007.3851)

MR HODGE: And if we bring up Mr Glenfield's statement, pages 24 and 25, paragraph 109 across those two pages. So this is where you explain the reasons why you decided not to take action?---These were the reasons that came through the EEC, yes.

One was that APRA didn't have a power to direct that the reserve be replenished?---As advised, yes.

And that's the case, you can't just direct them to do it at the moment?---Correct.

The second is that:

> *Questor's reserves policy permitted the use of the general reserve to compensate members.*

?---Yes.

Do you know whether anybody checked what the version of Questor's reserves policy was at the time that the decision was made?---No, I'm not aware.

We suspect that you might have looked at a reserves policy which – if we bring up the version which is the 19 August 2013 version, so this is IFL.0027.0001.0746. So you see this is the reserves policy as at 19 August 2013?---Yes.

And then if we go to page 5, which is .0750. You see the general reserve which is at the bottom of the page:

> *The general reserve exists to hold capital to pay future administration and operational expenses under the funds' trust deeds that cannot be directly attributed to the members. The reserve may be utilised for any purpose that the trustee deems appropriate and within the parameters disclosed by the funds trust deeds.*

?---I see that.

Have you ever looked at the reserves policy?---Me personally, no.

I tender that version of the reserves policy.

THE COMMISSIONER: Reserves policy as at 19 August '13, IFL.0027.0001.0746, exhibit 5.305.

EXHIBIT #5.305 RESERVES POLICY AS AT 19 AUGUST '13 (IFL.0027.0001.0746)

MR HODGE: Now, you recall that the decision as to – or the decision as to what was done in relation to how the members was compensated was made in 2015?---Yes.

If we bring up IFL.0027.0001.0737. So this is the reserves policy. You will see this is as at 25 May 2017?---I do.

And by this time, Questor has – is no longer operating. So it has fallen off the list?---Mmm.

And then if we go to page .0740. So you see now the general reserve policy has been amended. And I don't know if it would help if we bring up both versions and put one on either side of the screen. It probably would. So can we put that page on the right side of the screen and on the left side of the screen put IFL.0027.0001.0750. And you see whereas as at 2013 there was a reference to the reserve existing to pay future administration and operational expenses under the funds' trust deeds?---I do, yes.

And now when we go over to purpose, it's now said:

> *The purpose of the general reserves is to hold capital that cannot be directly attributed to members which has been set aside for a clearly stated purpose that the trustee deems appropriate as determined by the funds' trust deeds.*

?---I do.

Then if you look at the section which is Use, you see:

> *The reserve may be utilised for the purpose that the trustee deems appropriate and within the parameters disclosed by the funds' trust deeds and relevant regulatory requirements. For example but not limited to –*

And then you see the third bullet point is:

> *The payment of compensation to members.*

?---I do.

And then if we go to page .0745.

THE COMMISSIONER: On the right-hand or left-hand document?

MR HODGE: On the right-hand, Commissioner. We can see this is the document history for the document. And we see that last printed date which is 19 August 2013, which is that original date for the reserves policy?---I do, yes.

And then we see in the revision history, it was in version 3 revised on 25 May 2016 that there was, amongst other things, the inclusion of uses for reserves, including examples?---Yes.

Do you know whether anybody at APRA had detected that the reserve policy had been amended to permit the payment of compensation from the reserve to members after the reserve had already been used to pay compensation to members?---I'm not aware. I would need to ask the people who reviewed.

I tender the later version of the policy, Commissioner.

THE COMMISSIONER: IOOF reserves policy at 25 May '17, IFL.0027.0001.0737, exhibit 5.306.

EXHIBIT #5.306 IOOF RESERVES POLICY AT 25 MAY '17 (IFL.0027.0001.0737)

MR HODGE: And then if we go back to your statement and page 25 of that statement. So we've spoken about the first reason, we've spoken about the second reason. As to the third reason, which is:

> *Whilst TPS was disadvantaged by the use of the general reserve, its members were not directly disadvantaged as affected members were compensated appropriately.*

?---Yes.

Now, that, can I suggest, rather avoids the issue because the issue is that if Questor, as responsible entity of the CMT was responsible for the loss, it should have been paying for that loss, rather than Questor, in its capacity as trustee of the super fund, using the reserve of the super fund to compensate the members?---I think that's a point that I've made to them, but in terms I think of that point is looking at in terms of individuals' accounts it currently has been recompensed to the amount that they should have. For me the issue is that it came from the general reserve, which ultimately is an asset of the fund, rather than them seeking from the RE, consistent with what you're saying.

Yes. They – the members have been disadvantaged, because the general reserve that belongs to them, though is not specifically attributable to any of them, has been depleted?---They are disadvantaged by its depletion but in terms of them gaining access to that money, it's not going to occur in an immediate future. It would likely be on a wind-up or something similar. So at the – at that point, the members have in their account the money they're entitled to. What we're seeking to see is that we can try to – sorry recompense the general reserve for the amount that was taken out of it.

Or a more immediate way in which they would be disadvantaged is that the reserve ought to be used to meet some operational or administrative expenses and it's not available to do that. So instead the trustee imposes some additional fee on the members?---That presumes that such an event takes place, yes.

Yes. But that's – the imposition of additional fees in order to meet unexpected costs, or costs of complying with regulation, is something that retail trustees have done regularly over the last few years, haven't they?---Sorry, can you repeat that for me?

The imposition of some additional fee in order to meet unexpected costs or the costs of complying with some regulatory changes, is something that retail trustees have done regularly over the last few years?---Okay. So my portfolio has minimal retail funds, so I can't speak for that.

All right. Now, did you ever respond to the pub test letter?---I can't recall what we – I think we took that on to our next review. So that – that formed the basis – I did – we didn't accept the response as being correct. We've gone back out and done another review, and I think – I will have to have a look – we will go through it, I am sure – reiterated our position around it. So we've – yes.

Do you think it was a breach of the sole purpose test to use the reserve funds to compensate members rather than look to the company in a different capacity?---Yes, I'm not sure. I would need to take advice on whether it's a breach of the sole purpose, but what I did think it was was not acting in the best interests, and I've continued to pursue that.

And you what, sorry?---We've continued to pursue them.

You didn't, though, did you, you didn't continue to pursue this issue?---In terms of Questor itself - - -

Yes?--- - - - because Questor is gone. But it has been taken into the way we're – the way we're supervising IOOF as a group going forward.

Did you pursue IIML in relation to the Pursuit breach?---No.

If you were going to pursue them by some enforcement strategy, would that require seeking an injunction from the court to compel them to comply with their best interests duty?---I would need to take legal advice to answer that question.

Can we then bring up APRA.0016.0001.0730. So this is another internal memorandum to you?---Yes.

And this is from Ms Lee, who is the supervisor and Mr Davies who is from resolution and enforcement?---Yes.

And they were now together expressing concerns – a multitude of concerns about the governance and conflicts management of IOOF?---If I can see the rest of the minute, please.

Yes, if there's a copy of it then I would be happy for that to be provided to Mr Glenfield?---Okay. Yes, this is a memo preparing me for a board meeting.

A meeting with the board of - - -?---Yes.

- - - IOOF?---This is coming out of the review that's done that we issued the review report on. We were going to see the board to take them through, I was going – I was actually going with Juliette and she and Anthony were briefing me ahead of that for what the issues were they had found.

They were explaining their concerns about a number of issues in relation to governance and conflicts management at IOOF?---Correct.

And they were concerned, for example, if we go to page .0732, that:

> *The IOOF board has a fundamental misunderstanding of its duty to prioritise the duties to and interests of superannuation fund members.*

?---Yes.

That:

IOOF view themselves as an advice business rather than a superannuation trustee business.

?---Yes. Sorry.

If we go over the page:

...IOOF do not see a clear nexus between themselves and the member when it comes to investments.

?---Yes.

That:

IOOF directors have difficulties identifying conflicts and arrangements with related parties.

?---Yes.

If we go over the page to .0734. That:

IOOF directors are at risk of abrogating their obligations on conflicts management via delegation to committee without appropriate oversight.

?---Yes.

That:

The IOOF board does not view compliance and conflicts management as areas that matter.

?---Yes.

That:

Conflicts management considerations are not adequately documented and the board appears resistant to detailed documentation.

?---Yes.

Indeed, if we go over the page, they raised the question of fitness and propriety?---Yes, they did.

I tender that document, Commissioner.

THE COMMISSIONER: Memorandum to Mr Glenfield of 14 June '17 concerning IOOF prudential review, APRA.0016.0001.0730, exhibit 5.307.

EXHIBIT #5.307 MEMORANDUM TO MR GLENFIELD OF 14 JUNE '17 CONCERNING IOOF PRUDENTIAL REVIEW (APRA.0016.0001.0730)

MR HODGE: And you would have met with the board?---I did. We went through this with the board.

And did you form a view as to whether the board understood its obligations?---I think I've made it clear in the letters that I've written that I think they – they understood their obligations as an RE in terms of balance, but they were not fully understanding their fiduciary duty in terms of acting in the best interests of members, and our reviews and meetings with the board were to explain to them our view on that and to drive them towards a better understanding of what they were doing.

And you sent another letter to them, which is exhibit 5.124, IFL.0006.0003.3953?---Correct.

This is a letter sent on 15 August 2017?---It is, correct.

And if we go over the page to page 2, I think we might need to go over to page 3. You then provided them with a report on the prudential review of the IOOF Group?---We did, yes.

And then subsequently, the ANZ transaction was announced?---It was, yes.

And you sent, I believe, a further letter to IOOF when that happened which is exhibit SG-1-23 to Mr Glenfield's statement which is APRA.0002.0007.2874?---Yes, correct.

And then you sent another letter to them in June, which is SG-1-16, which is APRA.0002.0007.3219. And here what was set out – I think this wasn't written by you, this was written by somebody else, was the minimum expectations that APRA was looking for from IOOF?---That's correct, yes.

Which were to split the board?---Correct.

And to do some other things?---Correct.

I'm sorry, I said split the board, to split the RSE licensee and the RE - - -?---The RE – the RE and RSE functions, yes.

And as we understand it, and I assume as you understand it, the IOOF board met on 1 August to discuss this?---I understand they did, yes.

And have they formally communicated to APRA what their position is?---They've written a letter back to the team that now handles IOOF, yes.

I see. Commissioner, I've just been handed a letter which is dated 14 August 2018 from IOOF to APRA, where what's said is that:

APRAs suggested changes numbers 1, 3 and 4 were endorsed.

And in respect of change 2 there are some matters for discussion?---That's as I understand it, yes.

All right. We will get that marked, Commissioner, but it doesn't have a doc ID at the moment and tendered.

THE COMMISSIONER: But if it becomes exhibit 5.308, letter IOOF to APRA, 14 August '18, we will get it into the system.

EXHIBIT #5.308 LETTER IOOF TO APRA DATED 14/08/2018

MR HODGE: Thank you, Commissioner. And you were aware when Mr Kelaher gave evidence that when he was asked:

You don't share the view of APRA that there are legitimate concerns about these structures. It's just ultimately as a matter of practicality, it's easier to make the changes rather than having to keep dealing with the complaints.

His answer was "yes"?---I am aware of that, yes.

And what I wonder about is this: whether APRA regards this as a successful intervention in relation to governance and management of a trustee?---Good question. I regard it as an ongoing matter but in terms of – of what we are trying to achieve with IOOF. So if you think – with IOOF with the – the challenge with the dual hat is, as we've been through, is you're wearing – and you do refer to it which hat am I wearing today – we're wearing a hat of an RE and an RSE. The overriding obligation of the RSEL is to act in the interests of members. We've had concern over time that they weren't fully conversant with that requirement and that's what's appeared in some of those matters like the Pursuit and the Questor type matter. So I've looked at that as being they're – they're symptoms of – to go into a medical style, they're symptoms of a greater illness which was their inability to manage the conflict in their RSE/RE. So we've taken the view to drive them to better practice to get a – to get it into a form whereby they are acting in the interests of members at all time. So that's – to get it into a long-term position that the members of IOOF will be

given priority. So we took – we've taken a number of measures through those reviews to have the conflicts framework improved and bettered. We got the first step of getting two independent directors on to the board who would act purely with a hat for being there for the members. The key point we had was the Ernst & Young review to help look deeper into how they're managing conflict, how they're dealing with the dual hat, and what they need to do to make that work better. Ultimately, however, we reached the conclusion that it wasn't working. So that was the June 2018 letters requiring the splitting of the two. So to my view, if we end up in a position with the RSEL being separated from the RE, with a fully independent board on the RSEL that acts in the interests of the members of the superannuation fund, from a long-term view that's a successful intervention.

Just on the Ernst & Young review, that wasn't, as I recall it, that wasn't able to fully complete the checking of all tests, because it effectively failed at the first or second hurdle?---It hasn't failed at a hurdle, it's an ongoing review.

I'm sorry, it wasn't – at the time the initial report was given, it wasn't able to complete all of the checks. Is that right? Am I – I will check with my junior - - -?---I don't think that's

I'm thinking of a different review?---Yes.

All right. There's an ongoing Ernst & Young review?---Correct.

And the ongoing Ernst & Young review has ultimately, you say, been superseded by - - -?---It hasn't been superseded. It will – it will provide, I hope, some strong recommendations for further improvement around the way they manage, but we've taken the step of requiring the split to get what we think will be in the best interests of the members long term at IOOF.

Do you think – or did you give any consideration to whether had you commenced a court proceeding against IOOF in respect of any of the three breaches that we've spoken about, the cash management trust, the Pursuit breach, the Sweep breach, whether that might have more effectively operated as a deterrent, specifically to IOOF, and generally to all RSE licensees?---Okay. I gave it consideration definitely for IOOF, which is why we ran – we ran it through the EEC. That went through our legal area, our litigation team, and they concluded that I didn't have enough.

But that's for the CMT?---That was for the CMT. So on that basis, I redoubled the efforts towards getting the best structure in place for the long term. In terms of general deterrence across the industry, I didn't turn my mind to that factor.

What about the Pursuit breach and the Sweep breach. Did anyone consider that?---No. Again, I regarded the Pursuit breach sitting back and looking at the work that the team was doing, again, as I said, it's a symptom of the way the structure was working. For me, the most important thing was to get the structure right first for the long term, and we're in a position you can still consider those matters going forward.

But in terms of the long-term outcome for the members of IOOF, the most important thing in my mind was to get the structure right and the governance and conflicts management right.

Commissioner, I don't have any further questions for this witness.

THE COMMISSIONER: Thank you very much.

MR DICK: I have nothing, Commissioner.

THE COMMISSIONER: Thank you very much. You may step down. You are excused.

<THE WITNESS WITHDREW [12.42 pm]

THE COMMISSIONER: Now, Mr Hodge.

MR HODGE: Commissioner, the next witness is Mr Kell from ASIC. Sorry, I think it's Mr Mullaly from ASIC. I've just received a look which tells me I had it wrong. Would it be convenient if we took a five minute break now to switch around or would you prefer to have lunch now and then come back at 1.45.

THE COMMISSIONER: How much time have we got in the afternoon, that is, if we broke now and resumed at 2, are we going to finish comfortably, or not?

MR HODGE: We will finish.

THE COMMISSIONER: Thank you so much for that vote of confidence. I think then we will resume at quarter to 2.

MR HODGE: Thank you, Commissioner.

ADJOURNED [12.43 pm]

RESUMED [1.45 pm]

THE COMMISSIONER: Yes, Mr Hodge.

MR HODGE: Commissioner, the next witness is Mr Mullaly from ASIC.

<TIMOTHY PETER MULLALY, RECALLED AND RE-AFFIRMED

[1.46 pm]

<EXAMINATION-IN-CHIEF BY MR COLLINSON

THE COMMISSIONER: Thank you, Mr Mullaly. Do sit down. Yes, Mr Collinson.

MR COLLINSON: Mr Mullaly, your full name is Timothy Peter Mullaly?---It is.

Your position with ASIC is senior executive leader of the ASIC financial services enforcement team?---It is.

Your business address is level 7, 120 Collins Street, Melbourne?---That's correct.

You should have there, Mr Mullaly, a copy of your summons to appear before the Commission, dated 6 August 2018?---I do.

I will tender that, if your Honour pleases.

THE COMMISSIONER: Exhibit 5.309 the summons to Mr Mullaly.

EXHIBIT #5.309 SUMMONS TO MR MULLALY

MR COLLINSON: And secondly, Mr Mullaly, have you got a copy of your witness statement, dated 3 August 2018?---I do.

And is that witness statement true and correct?---It is.

I tender that, Commissioner.

THE COMMISSIONER: The statement of Mr Mullaly, 3 August '18, exhibit 5.310.

EXHIBIT #5.310 STATEMENT OF MR MULLALY DATED 03/08/2018

THE COMMISSIONER: Yes. Yes, Mr Hodge.

<CROSS-EXAMINATION BY MR HODGE [1.47 pm]

MR HODGE: Thank you. Mr Mullaly, you've, in your witness statements, addressed some issues in relation to the obtaining of enforceable undertakings from ANZ and CBA?---I do.

And your evidence concerns the process by which those enforceable undertakings are obtained?---It does. It concerns the discussions and negotiations that led to those enforceable undertakings, that's correct.

And so that we can attempt to understand what the process is by which conduct of concern is addressed by ASIC, each of ANZ, CBA and Westpac were identified as having, in different ways, gone about selling a superannuation product to consumers?---That's correct.

And they were selling that product not through financial advisers but through either call centre staff or front-facing bank staff?---That's correct.

And the issue with respect to Westpac concerned call centre staff?---That's correct.

And it's presently the subject of a reserved decision in the Federal Court?---That's correct.

So I'm not going to ask you any questions about that specifically, except insofar as it concerns what happened in relation to ANZ and CBA. In relation to ANZ and CBA, their conduct was concerned with bank tellers or staff members within a bank branch selling the superannuation products to consumers who came into the branches?---That's correct.

And each of them had a similar method by which that occurred, or one way in which it occurred, which was that the staff member would administer some sort of questionnaire to the consumer?---That's correct.

And in the case of CBA, it was referred to as the financial health check?---That's right.

And in the case of ANZ it was referred to as the A to Z review?---That's correct.

And at the end of the carrying out of that questionnaire, the staff member would or might try to suggest other bank products other than superannuation to the consumer?---It – they might do, yes. That's my understanding.

And then the staff member was supposed to make a statement which I think is sometimes referred to as a de-linking statement before talking about the superannuation product?---That's correct. So the de-linking – I think in the ANZ matter, they refer to it as de-linking. CBA, I'm not sure that they use that term. At that point in the process, there was a general advice warning given.

But in any event, what has occurred sequentially is that the questionnaire is administered, the general advice warning is given, and then the consumer is told about the superannuation product?---It's raised with them. That's my understanding, yes.

And is ASICs present view that if the process had been followed exactly as I have just described it, which is administering the questionnaire, and then having the general advice warning, and then just stating facts about the superannuation product without doing anything else, that there would not be an issue with that?---No. We were concerned about that conduct.

You would still be concerned about that?---Yes.

And could you explain to the Commissioner then, so that he can understand ASICs view on this, what the concern is if the process is followed properly?---Well, our concern is that the branch staff would be giving personal financial advice in circumstances where they neither had the training to do so, and were not authorised to do so.

And are they giving personal financial advice merely by recommending the superannuation product?---No, it's the – well, it's the whole process. So by taking into account or if a reasonable person might think that they were taking into account the information that they had gathered through the A to Z or the financial health check.

So the point is questions had been asked about the personal financial situation of the consumer and the de-linking statement, or the personal advice – I'm sorry, the general advice warning, is not enough, from ASICs perspective, to separate the personal questions from the recommendation of the superannuation product?---That was our concern, yes.

And in that way, it would be personal financial advice?---We were concerned that it would be, yes.

Now, as we understand it, in 2012 and 2013 CBA came to ASIC and gave presentations to ASIC where it said that this is what it was going to do?---I understand that there were presentations made to ASIC. I wasn't part of that process. So I can't comment on – on what those presentations were.

Has ASIC retained copies of the presentations?---I – I would presume we have, yes.

When you were running the enforcement process in relation to CBA and ANZ, did you go back to look at what it was that CBA had originally told ASIC it was going to do?---Our investigation team did look at that issue, yes.

And it was the case, wasn't it, that CBA had said one of the ways in which we are going to create interest for this product – or an interest, I think, is by using the

financial health check?---I – I understand that to be the case, but I'm a little bit reluctant to be too certain of that because I wasn't part of those discussions, and – and for the purpose of our investigation, we didn't really consider it relevant.

Was it the case, though, that ASICs view as to whether it was possible to have one of these questionnaires and then a general advice warning and then a recommendation of a superannuation product is something that has changed over time?---I'm not aware of it changing. As part of our investigation, I'm not aware that it was raised with us internally that this was a change in position.

I see. And in 2014 ASIC first becomes aware or commences an investigation in relation to this type of conduct?---In 2014 we commenced a surveillance in relation to this conduct, and that was a more thematic surveillance undertaken in relation to the sales processes in relation to all the banks and two other entities, I believe.

And how did ASIC become aware of the conduct?---There was a complaint that was made and received by ASIC. The exact details of that complaint I'm uncertain of. I understand it was concerning pressure sales within Commonwealth Bank.

I see. But in any event, I think what you say in your statement is ASIC first became aware of the issue in May of 2014?---I think that's correct, yes.

And commenced a surveillance in June of 2014?---That's correct.

And then I think at the end of 2014, ASIC received a good governance notification from CBA?---I believe that's correct, yes.

Prompted by – CBA had completed a number of rounds of mystery shopping in order to check whether its processes were being followed?---That's right.

And then you've explained that ASIC ended up issuing 42 notices in relation to the conduct?---I – it was something along that line. In relation, I think, to both CBA and ANZ.

CBA and ANZ, yes?---And they would have been more in relation to the other banks.

And conducted 13 examinations?---I think that's in relation to CBA as opposed to in total.

I see?---I think there was more in total.

More in total, did you say?---Well, in relation to – I think it's in my statement. So 13 in relation to CBA and seven in relation to ANZ.

And within ASIC, there is something referred to as the Wealth Management Project?---That's correct.

And the issue in relation to selling practices was being taken up to and reported to the members or the committee in relation to the Wealth Management Project?---It became part of the Wealth Management Project, that's correct.

And, for example, if we can bring up ASIC.0015.0010.0837. This should be, if it's going to come up, the notes for the Wealth Management Project board meeting on 24 April 2015. We might just have hard copies provided to Mr Mullaly, Commissioner, rather than – while that's coming, rather than slowing it down. Commissioner, just give me one moment. If the document turns up we will show it to you, Mr Mullaly, otherwise I will just ask you some things and see how we go. The nominal start date of the project was 11 September 2014?---Of the Wealth Management Project.

Of the project in relation to what's referred to as the mis-selling of MySuper products?---That sounds about right, yes.

And do you recall that in April of 2015 ASIC had a target date for outcome which was to issue proceedings by end October 2015 in at least one of three possible matters against CBA, ANZ or Westpac?---That might be right. I – I wouldn't dispute that.

Would you have been – at that stage the manager was Marita Hogan?---That's right.

Does Marita Hogan report to you?---She did – she did. And whether she was at that time, I'm – I would have to sort of go back. So just perhaps a little bit of explanation, there was some surveillance undertaken and that surveillance was undertaken really within our stakeholder team, the financial adviser stakeholder team. Notwithstanding it was within that team, it was still funded out of the Wealth Management Project and still reported through that line of reporting. I – my recollection is that by around that time, Marita would have been reporting to me.

Now, Commissioner, what I will do, I think, is rather than slowing us down now, I will tender some board meeting documents and then at some stage they will – somebody will produce a copy and give them to you. Do you want me to give you the name of the document now so I can indicate what I'm tendering.

THE COMMISSIONER: Yes.

MR HODGE: It is the Wealth Management Project board meeting papers for the meeting dated 24 April 2015.

THE COMMISSIONER: The doc ID.

MR HODGE: Commissioner, the doc ID is ASIC.0015.0010.0837.

THE COMMISSIONER: That will become exhibit 5.311.

EXHIBIT #5.311 WEALTH MANAGEMENT PROJECT BOARD MEETING PAPERS FOR MEETING 24 APRIL 2015 (ASIC.0015.0010.0837)

MR HODGE: The Wealth Management Project would have a meeting every month?---It did, yes. The board had a meeting every month, yes.

The board for the Wealth Management Project?---That's correct, yes.

And I want to suggest it met again on 20 May 2015?---That's quite possible, yes.

And at that time the target date for outcome in relation to this mis-selling of MySuper products was to issue civil penalty proceedings by 20 October 2015?---I don't doubt that that's what's on the report.

And I will tender that document as well, Commissioner, and again it will come up at some stage. It is ASIC.0015.0010.1324. It is the papers for the Wealth Management Project board meeting of 20 May 2015.

THE COMMISSIONER: That will become exhibit 5.312.

EXHIBIT #5.312 PAPERS FOR THE WEALTH MANAGEMENT PROJECT BOARD MEETING OF 20 MAY 2015 (ASIC.0015.0010.1324)

MR HODGE: And do you know whether or not ASIC managed to institute any proceeding by 30 October 2015?---No, it didn't.

Do you know why not?---The matters were still under investigation. We needed to continue to do work in relation to those matters to get the evidence that we needed, to get the advice that we needed. The wealth management team was looking at a whole range of matters, many of which have been agitated through the course of these Royal Commission, so we were looking at fees for no service, we were looking at conduct by advisers, we were looking at poor advice matters. There was a fair bit of work that the team was doing and they were working their way through it.

If the view of ASIC was that administering the health check or A to Z review and then making an offer of a superannuation product was a contravention of the Corporations Act because it was personal financial advice, what was the evidence that needed to be gathered?---Well, we needed to, I suppose, understand exactly what the process that was being gone – going through by the relevant banks. So we were collecting evidence in relation to the interaction between bank branch staff and evidence from the customers themselves. So we were doing section 19s to get that information in evidence. We were seeking information from the banks about their processes, about what had been put in place to mitigate any risk. Just – it's the usual sort of investigation where you need to understand properly the evidence. And by

the time – and I think, again, it's in my statement – some time prior to October 2015 we sought advice from senior counsel. And we – we take guidance from counsel in relation to the sort of evidence that we might need to be able to get a case in court.

But just, if you think this through, you're obviously at least experienced in conducting investigations in relation to matters that might potentially go to court?---Yes.

You know that the allegations that you are outlining to us here are that the process that each of ANZ and CBA admit that they used, which was a financial health check or A to Z review, followed by a general advice warning or de-linking statement, followed by an offer of superannuation, is something that you think contravened the Act?---We certainly were concerned about that. They – the banks admitted to the conduct, in terms of the steps that they were taking.

Yes?---They certainly didn't admit that they were breaching the law. And, in fact, they've never admitted it.

No, that's right. But, you see, the facts they admit, do you agree?---They admit the facts, yes.

And then you need to go to a court to determine whether, as a matter of law, it is a contravention?---Yes, and we've gone to court.

Well, you've gone to court in relation to Westpac?---Yes.

Where Westpac is doing something slightly different over the phone?---Slightly different, yes.

And I just want to make sure I've understood, though. Your view, that is, the view of ASIC since at least 2015, I assume, is that the questionnaire, followed by an offer of superannuation, even though there's some interposed de-linking statement or personal – or general advice warning, is not sufficient to transform that conduct from general advice to personal advice?---That's correct, yes.

And, therefore, that every time the banks do that, they are breaching the law?---Well, not – no, not necessarily every time, because each particular circumstance, each time a bank branch staff member undertakes the questionnaire and has the interaction with the customer, it – it may or may not be in breach. It's not – it's not – we didn't take the view, in a sense, that each case would end up as being personal advice. We – we took the view that we needed to understand some individual cases to make the call about whether or not, in fact, there was personal advice being given. This is a matter that has not been tested at all, whether or not – or the differentiation between personal and general advice. These were complex matters. They were matters that we did get advice on prior to contemplating the issuing of proceedings, and that advice was to the effect that there was some significant risk.

Yes, but you're the regulator?---Yes.

And you have a view about what the law is?---Yes.

And there's always going to be a risk, and sometimes - - -?---Yes.

- - - it will significant and sometimes insignificant?---Yes.

That when you go to court, a court will not agree with you?---Yes.

Surely, the fact that there is a risk that the court will not agree with you is not a reason to not go to court?---No. And we have many matters before the courts where we're concerned about whether or not the court will agree with us, and we had a matter – we took a matter to the court in relation to this particular issue, about the provision of general or personal advice. And we had that matter there. It was a test case. It is a test case. As you've indicated, decision is reserved on it. You know, we've taken that matter.

It's a test case, though, that doesn't involve the administration of a questionnaire, followed by the selling of superannuation?---No, but it – the principle we see is being tested, which is whether or not in the circumstances of these sorts of sales there's general advice or personal advice given.

And so that I can understand what your evidence now seems to be, you recall at the beginning of your evidence you seemed to agree with me, I thought, that ASIC believed that administering the questionnaire and then offering superannuation, even if there was a general advice warning and de-linking statement in the middle, was still personal financial advice?---That was our concern, and – and still is, and what we were trying to achieve and what we did achieve was the conduct stopped.

But - - -?---And we have a matter before the courts where we can test the proposition.

But you don't have a matter before the courts where you can test the proposition, because the matter before the courts doesn't have anything to do with administering this questionnaire?---Yes. I understand what you're saying, and if – if we took the proposition that each small difference, or difference where the principle is the same but a different attempt to get to that same end, that we needed to test every single one of them through the courts, we would be clogging up the courts forever and a day.

So in about August – I'm sorry, in about July of 2015, the target date for the issue of civil penalty proceedings gets pushed back to 30 November 2015?---I – I don't doubt that that's on the report.

Commissioner, I will tender ASIC.0015.0004.0682, which is the papers for the Wealth Management Project board meeting of 2 July 2015.

THE COMMISSIONER: That document will be 5.313.

EXHIBIT #5.313 PAPERS FOR THE WEALTH MANAGEMENT PROJECT BOARD MEETING OF 2 JULY 2015 (ASIC.0015.0004.0682)

MR HODGE: And eventually, ASIC commences a proceeding against Westpac, when?---I think it was December 2016, I believe.

I see?---It's about 18 months ago.

And then at the beginning of 2017, ASIC is continuing an engagement with ANZ and CBA?---So I think in December 2016 in relation to both ANZ and CBA we put a position paper to them.

Where ASIC said, "We consider your conduct to involve various contraventions of the law."?---That's correct.

And at least in the case of ANZ, ASIC had a concise statement drafted?---So some time after then, I think about April or May of 2017.

And a concise statement is the document that is drafted in support of an originating application to be filed in the Federal Court?---That's correct.

So at that stage, in the first half of 2017, ASIC is at least at the point of commencing a proceeding against ANZ?---Yes, I think it was about 10 May.

And what about against CBA?---I'm not aware that a concise statement was drafted for CBA, but around about that time we were coming to similar conclusions – well, no, I retract that. Our concern in relation to ANZ is the response that we received from them in relation to our position paper was, essentially, a denial. And there was no movement. And at that point we thought we needed to say to them, you know, "Unless we're able to sort of move this, we will proceed with court action." I think in relation to CBA, there was more movement by CBA in relation to the concerns that we had.

CBA were willing for ASIC to put out a media release?---I think – well, they may have been. My recollection is that they made some form of offer which may have included issuing – ASIC issuing a media release in relation to it, but we didn't consider that that offer was satisfactory.

And ultimately, they indicated they were prepared to enter into an enforceable undertaking?---Both ANZ and CBA indicated that.

Can I suggest to you that as at about January of 2017, or early February 2017, ANZ – I'm sorry, ASIC was looking to settle a statement of claim against ANZ in the

following month, that is, in February - - -?---Early – yes, I can't dispute that. I'm – that might be right.

In February of 2017 it's looking to settle a statement of claim in March of 2017?---Yes. That might be right.

And then ultimately, that becomes a concise statement, and when did you think that was ready?---My recollection is some time late April, May of 2017. I had thought that there was correspondence on about 10 May 2017.

Sorry, I am just getting the folder I need. And just so I understand then, you've drafted a concise statement, and have you drafted a concise statement with the intention of commencing the court proceeding?---The intention was to ensure that ANZ were aware that if we weren't able to resolve the matter outside of court, that we would go to court.

Had you drafted the concise statement with the intention of commencing a proceeding?---If it was necessary, we would have commenced the proceeding, yes.

And I feel like I'm not understanding ASICs processes. When you say "if it was necessary", what was the alternative to commencing a proceeding?---To resolving the matter outside of court with ANZ.

By an enforceable undertaking?---By a court enforceable undertaking, yes, if that was possible.

So the drafting of the court proceeding is a negotiating tactic to try to get ANZ to move towards an enforceable undertaking?---It was part of the process that we undertook, yes. We saw it as a – a tactic that we could use. And it was not a false threat.

That is, if they really refused to give an enforceable undertaking - - -?---We would have filed.

- - - you would have commenced?---Yes.

Was there any time limit on that?---I think we said within 24 hours.

If they didn't indicate that they were willing to give you an enforceable undertaking - - -?---That's correct, yes.

- - - that you would then commence within - - -?---I think – I think it was 24. I'm sure you've got the document or detail there.

I feel like we might be at cross-purposes. Can we bring up ASIC.0041.0001.7093, which is exhibit number 6 to Mr Mullaly's statement. So this is an email sent from ASIC to ANZ on 10 May 2017?---Yes.

And it's attaching the concise statement?---Yes. I understand.

Draft concise statement?---Yes.

And the statement made in the email is:

> *ASIC intends to commence proceedings on Monday, 15 May 2017. We note that ANZ and ASIC have been in discussions regarding this matter since September 2016. If ANZ is prepared to make admissions regarding the contraventions set out in the concise statement, please inform us by return email by close of business on Friday, 12 May.*

?---Yes. Yes.

And then it also asks:

> *Please also provide us with details of solicitors ANZ has appointed to act in this matter and confirm whether they hold instructions to accept service.*

?---Yes.

And this was a bluff, was it, in the sense that you weren't actually going to commence proceedings if they would agree to give you an enforceable undertaking?---Well, if we could get an agreed court-enforceable undertaking from ANZ we thought that that was going to be a better outcome than commencing proceedings, yes.

What you told them was you're going to commence proceedings. Do you agree?---Well, I think that's what – well, the email. It's – yes, but ASIC did say that, yes.

And presumably by then, the ASIC – the Commission or the enforcement committee, somebody must have resolved that we are going to commence proceedings?---I think the Commission would have – or the appropriate committee would have agreed that if it was necessary, we would commence proceedings, yes.

And what you asked ANZ to do was to say whether it was prepared to make admissions on the contraventions set out in the concise statement?---Yes.

But what you're saying to the Royal Commission is you weren't actually looking for admissions, you were just looking for them to say they will provide an enforceable undertaking?---This is – if they had have wanted to fight this matter in court, we would have gone to court. If they wanted to make admissions prior to us filing or after we filed, that was up to them. We also considered that it was a matter where if we could resolve by way of non-court outcome, that was in the best interests of consumers, in particular, and it was a way – an appropriate way to resolve the matter.

And this was - - -?---This is – this is part of a process where we need to ensure that ANZ understood – and they did understand – that we were serious.

Do you think that financial institutions might take ASIC more seriously if when it drafts a concise statement, says it's going to file it, it actually follows through and does it?---Well, we do that all the time.

But your point is here, when you did it you didn't actually mean it?---No, we would have filed if we hadn't had the response that we wanted, and we got the response that we wanted.

You got a response on 12 May 2017 from ANZ, which is ASIC.0041.0001.7107. That's exhibit TM-8 to Mr Mullaly's letter – to Mr Mullaly's statement. So this is the letter that you got in response?---I understand, yes. Yes.

It came to you?---Well, there was two letters, I think. There was an open letter and a without prejudice letter.

I see. And the open letter didn't – I'm sorry, the without prejudice letter didn't offer an enforceable undertaking?---No, it didn't.

It complained that ANZ was surprised and disappointed to be informed in a telephone call on 10 May 2017 that ASIC was no longer proposing to complete the process in the way that had been contemplated?---It does do that, yes.

And it then proposed that there be a mediation to try to facilitate agreement?---A meeting.

Yes. And then you see in the last paragraph:

> *We think that might best be facilitated by involving a mediator.*

?---There was a mediator, yes.

And the open letter talked about a mediator?---It may have done, yes. I will have to - - -

So on 12 May the deadline that ASIC had imposed on ANZ, there wasn't an agreement to provide an enforceable undertaking?---No.

And then on the morning of 15 May you received an email from the group general counsel of ANZ?---I believe so, yes.

That's ASIC.0041.0001.6002. This is an email from Mr Santamaria to you?---That's correct.

And you already knew Mr Santamaria?---Yes, I do.

And how did you know Mr Santamaria?---I had dealt with Mr Santamaria in relation to investigation of Opus Prime, the collapse of Opus Prime and had quite substantial dealings with him during that period of time. And subsequent to that had kept in touch.

And he said:

> *I can well imagine the many pressures on you with such cases but can I add my own request to that from Lawrance that we get a chance for one final chat before ASIC commences the proposed prosecution.*

?---Yes.

I tender that email, Commissioner.

THE COMMISSIONER: Email from Mr Santamaria to Mr Mullaly, 15 May '17, concerning Smart Choice, ASIC.0041.0001.6002, exhibit 5.314.

EXHIBIT #5.314 EMAIL FROM MR SANTAMARIA TO MR MULLALY DATED 15/05/2017 (ASIC.0041.0001.6002)

MR HODGE: Now, so that I understand, at this stage ASIC has said in writing to ANZ we're going to commence a proceeding on 15 May 2017?---Yes.

It hasn't been qualified or conditional in any way, the statement that was made to ANZ?---Not that I'm aware of, no.

You're saying what ASIC was actually looking for was for ANZ to say, "We're prepared to give an enforceable undertaking"?---We're looking for a response from ANZ, and I think it shows that when the group general counsel starts engaging in the process, we've got their attention.

You've got their attention. Is that honestly what you regard as a successful application of the regulatory process?---I'm not sure what you mean.

Having told them that you were going to commence on 15 May 2017, you then didn't commence on 15 May 2017?---No, we haven't commenced at all against ANZ.

And why did you not commence on 15 May, as you had said you would?---Because we had been contacted by ANZ who indicated they wanted to engage in the process of resolving the matter, and – at the – at the very – I mean, the focus of this was to stop the conduct. We wanted the conduct to stop. And that's what happened. We were able to achieve that. We were able to achieve it in a very timely way without having to go to court.

On 18 May 2017 there was a meeting between ASIC and ANZ?---That's correct.

I'm sorry, can I just go back – did you just say in a timely way?---That's correct.

You had a proceeding drafted in May of 2017?---That's correct.

You entered into an enforceable undertaking with ANZ at the end of July 2018?---That's correct.

You had begun investigating this in June of 2014?---That's correct.

Surely you don't believe that that is a timely resolution?---What I'm saying is – and I certainly concede that we need to do things quicker, however, there was no guarantee that if we had have gone to court in May 2017 that we would be anywhere near resolving the matter. And, you know, it's of no – and I mean absolutely no disrespect to the court at all. These matters take time through the court. They take time. And the experience of the Westpac matter, again, no disrespect to it – to the court, is that it takes time.

Well, you commenced it in December of 2016. You had a trial in February of 2018 and judgment is presently reserved?---That's correct.

And you also said, I think, the conduct has now stopped?---Well, there's some period of time after the signing of the EU to allow ANZ to put in place the proper processes that they need to to ensure that they're – they're able to stop the conduct. Now, there was, in our view, we needed to give some amount of time for those processes to be in place, otherwise they would have been in breach of the EU from day one.

You think - - -?---That's not pragmatic.

THE COMMISSIONER: And if the court made an order, would there be any time to give effect to it except at once?---It – that might be the case, Commissioner, that the court might say it must stop there and then. The court may also make an order that it allows some time.

Go on.

MR HODGE: You could have, presumably, commenced a proceeding and sought an interlocutory injunction to prevent them engaging in the conduct pending the outcome of the trial?---We could have, and we gave serious consideration to that. We sought advice in respect of that. And the advice and our consideration was that it was futile. We wouldn't have got that order. It would – the balance of convenience would have been in favour of the bank.

You spoke to – I'm sorry, ASIC spoke to ANZ on 18 May 2017?---There was a meeting. I wasn't present at that meeting.

You've seen the file note of it?---I have, yes.

And on 18 May 2017, ANZs position was that they don't believe that they have behaved in contravention of the regulations or the law?---ANZ have held that view all the way through.

They continue to hold that view, as far as you know?---I don't think that they've ever admitted that they're in breach of the law. They acknowledge that our views are well founded and that's as far as they're prepared to go.

That your view – you have a reasonable concern?---Yes.

So nobody has ever resolved whether this conduct is or is not unlawful?---No. There is a matter before the courts, though with a decision reserved.

About different conduct?---Slightly different, yes.

All right. And then when does ANZ say to you that they're prepared to accept an enforceable undertaking?---I would have to refresh my memory on the exact date. Some time after 18 May.

I think it's – if you have a look at exhibit TM-11 to your statement. It looks like it's in a without prejudice letter dated 26 May 2017?---Yes.

And as we understand it under the guidelines that ASIC publishes, it will only accept an enforceable undertaking in certain circumstances?---That's correct.

And those circumstances have to be that ASIC is satisfied that it can achieve some better or additional outcome from an enforceable undertaking as compared to what it could achieve in a court?---That's right. Essentially.

Sorry?---Essentially, that's right, yes.

And in this case, what was the better outcome that ASIC thought that it could achieve?---Well, we thought that we could get the conduct to stop. We could get the conduct to be – or agree with ANZ in a sense that they take two steps back from the line rather than just behind the line, in terms of what was general advice and what was personal advice. So we're able to do that through an EU which was not necessarily what could be achieved through a court process, and we could do it in a more timely way.

Just so we can make sure we understand, we agree that if you had gone to court, run the proceeding, and succeeded, the end outcome would be that you would get an injunction to stop the court, almost certainly?---Well - - -

Or at least the conduct will stop?---Yes, yes.

And you also would have been able to obtain a civil penalty against ANZ?---Most likely, yes.

And that would act as a deterrent to them and to others from engaging in the conduct?---Yes.

And so the reasons why you preferred an enforceable undertaking were because you thought you could stop the conduct in a more timely way?---That's one of the reasons, yes.

And sorry, what was the other reason?---That we could agree with them what it is that was acceptable or not acceptable behaviour. So we could be more prescriptive in the EU than we might otherwise have got through a court process. So, for example, if the court had made declarations that there was a contravention, the bank or others might set up a process that's just somewhat slightly different from the manner in which this conduct was occurring, and we might then be in a situation where we have to go through a process of understanding whether that new conduct was in breach of the law or not, and we – we determined that the better outcome was to say, "You cannot do this. You cannot have a – some form of questionnaire, financial health guide, or financial health questionnaire, or an A to Z guide, etcetera." And we stopped that.

If the reason that there was a contravention of the prohibition on personal financial – prohibition on ANZs bank staff giving personal financial advice is because the recommendation of the superannuation product happened in conjunction with the questionnaire, then that would all be stopped by the court proceeding, wouldn't it?---That specific conduct would be. That would be declared to be in breach if we were successful.

Yes?---But I think what we learnt through the whole of this investigation is that all the banks were trying to find ways in which they thought they could continue to do the health check or the A to Z, still have a discussion about superannuation in a way that they hoped we would say wasn't in breach of the law. And we continued to have those – they were making changes to their processes along the way, which is one of the reasons this was more complex than it perhaps sounds, and we – we wanted to stop that completely, and we did.

Again, you still haven't stopped it completely?---Well, at the end of the period of time, I think it was – I'm not sure whether it's two weeks for CBA and 45 days, I think, for ANZ, it will be stopped.

And one of the things that both banks did was to try to make sure that the way in which the enforceable undertaking was framed was very specific about what conduct they were agreeing to stop?---Yes. I think – you know, the whole process and negotiation, again which is one of the reasons why it took such a long period of time, was they were trying to have included in the – in various versions of the EU or draft

EUs, you know, us agreeing to what they could do, and we were trying to push back on that, and we did.

So the end result is enforceable undertakings that are very specific about what is prohibited?---That's - - -

Would you – yes, go on?---Well, that's correct. Yes, I was going to say that's correct.

Wouldn't that be exactly the same outcome that you would expect from a court?---It's – well, our judgment was that there was risk involved in going down that – that process.

So on 26 May 2017, ANZ makes a proposal to you that they would accept an enforceable undertaking or they would enter into an enforceable undertaking?---That's correct.

And you responded to them on 27 July 2017?---That's correct. It seems, yes.

You would describe that as timely?---No, I think that's – it takes too long but I would need to understand what happened in between.

It's your letter, Mr Mullaly, that you send back on 27 July 2017?---I don't – I'm not disagreeing that it's my letter. What happened between those two dates, I don't know. I suspect that we would have had to have internal consultation about the specifics of the offer that was made by ANZ. We would have had to talk to the right people within ASIC, including the wealth management board and potentially the enforcement committee to get, in a sense, approval as to what the response should be. I don't doubt it, I understand what you're saying is it's we need to do better, we need to be quicker.

And then you exchange – I'm sorry, ANZ writes back on 7 August 2017?---That's correct.

And then ASIC writes back on 15 August 2017?---Yes.

And then I think this might or might not be missing from your exhibits but in any event there's then a letter that ANZ sends back on 18 August 2017?---18 August, yes.

And then you write back on 14 September 2017?---I don't have that, but yes.

I will tender that letter, Commissioner. It's a letter of 14 September 2017 from ASIC to ANZ. It's ANZ.800.973.0466.

THE COMMISSIONER: That document is exhibit 5.315.

EXHIBIT #5.315 LETTER FROM ASIC TO ANZ DATED 14/09/2017 (ANZ.800.973.0466)

MR HODGE: Then in October of 2017, you send a draft enforceable undertaking to ANZ?---I think that's correct, yes.

And - - -

THE COMMISSIONER: And is that the first draft proffered by ASIC?---I believe so, yes. Well, it is, yes, Commissioner.

So it's taken from the outset of negotiations until this point for ASIC to say to ANZ, "Here is what we want"?---That's correct.

Why? Surely you begin these negotiations with an understanding of what ASIC wants?---We – we have certainly an understanding of what we want in the broad term.

And you get a proper understanding of what you want by writing it down in the form of a draft undertaking, don't you?---The process that we took was to set out, I suppose, in letter form the high level matters that we wanted them to agree to. What ended up – and it is, as I said before, one of the complexities of this particular matter is it turns on some clauses or expressions, such as, you know, there was concerns about whether something was in conjunction with something and, you know, we were having discussions with and negotiations with ANZ, and, indeed, I think with CBA at the same time.

Is it - - -?---Along those lines.

Is it not an essential first step for the regulator to determine what it wants from the particular member of the regulated community?---Well, I think we did set that out to them, that we did it in letter form.

You said at a high level?---Yes.

Yes. Go on, Mr Hodge.

MR HODGE: Thank you, Commissioner. And one thing you did try to do initially was to frame the enforceable undertaking a little bit more widely so that it would prohibit a needs-based discussion which was defined to be in the first draft by ASIC:

> *Any discussion with a customer which involves the customer providing information about one or more of the customer's objectives, financial situation, and needs, otherwise than for the purpose of compliance with the Anti-Money Laundering Act or with regulations.*

?---I assume since you're reading that, that's what's in the document.

That was - - -?---Yes, I'm not disagreeing.

Originally, what ASIC was looking to do to try to achieve something was to prohibit the conjunction of any needs-based assessment with the selling of superannuation?---Yes.

And then ANZ pushed back and said, "We don't agree to that. We will only agree to something that is similar functionally to the A to Z review"?---There was a lot of negotiations in relation to this EU. I don't doubt what you're saying. But I – I would have to be taken to the correspondence and communications.

Well, let's look at how it started. If we bring up ANZ.800.973.0589 on one side of the screen. And on the other side of the screen, ANZ.800.973.0590. Do you want the doc ID again? I will just read out what it says and we will tender the document. In the draft sent by ASIC on 3 October 2017, it defined needs-based discussion to mean:

> *Any discussion with a customer which involves the customer providing information about one or more of the customer's objectives, financial situation and needs otherwise than for the purpose of compliance with the Anti-Money Laundering and Counter-Terrorism Financing Act 2006 or with regulations or AML/CTF Rules under that Act.*

?---I can see that. So that's in TM-26, I think.

ANZ pushed back on that. And if we bring up the final version of the undertaking which is exhibit TM-27 to your statement. It's ASIC.0041.0001.3343. And go to the second page, we see by the end ANZ had managed to get a definition which was:

> *Needs-based discussion means any discussion with a retail client regarding their financial situation and needs which is similar in substance to an A to Z review.*

?---That's correct.

And can you say that your view is you managed to obtain something in this enforceable undertaking that went beyond what you would have obtained if you got an injunction at the end of a court proceeding?---Well, we believe that we have, yes. We've had the conduct stop, we've indicated what it is that they cannot do. So we've – we've stopped that conduct. And to the extent that they've got any other sort of process in place that they want to undertake similar conduct, we've got a monitoring process to ensure that it complies with the law.

How much was the community benefit payment that they finally agreed to?---They made very early on an offer of $1 million, and they also offered to pay ASICs costs

of $250,000, costs of investigation. We don't accept and can't accept costs of investigation when we accept EUs. We combined the amounts and that was the amount that was agreed.

That is, they agreed to make a community benefit payment of $1.25 million?---That's correct.

And do you recall or are you aware that one of the things – one of the things that ASIC tried to do was to have some factual contextual information included in the enforceable undertaking so that people would know what the value of funds were - - -?---Yes, that's correct.

- - - that were invested. And they provided a draft at one stage of the undertaking that included that information?---And included it for a period of time, yes.

I'm sorry, what?---I think it was limited to a particular period. It might not have been for the whole – the whole of the time that they were engaged in the conduct up to that point of time of the EU. For some reason I think it was for a smaller period of time. I think it was in excess of $583 million at that point.

Yes. For a particular period of time the funds under management that ANZ had managed to get via the conduct was close to $600 million?---That's correct.

And ANZ said we won't agree to that fact going in?---I understand, yes.

And so ASIC took it out?---That's correct.

And letters went back and forth between the parties through until June of 2018?---That's correct.

And then finally, the enforceable undertaking was signed at the beginning of July 2018?---That's correct.

And with CBA – CBA, did it try to call Mr Kell, do you know, to see whether they could get a media release rather than enforceable undertaking?---If – I think there was a meeting in early November 2017, at which time the – sorry, CBA were indicating that they didn't want to resolve the matter by way of an EU, yes.

They – you recall at some time CBA wanted to resolve it by media release?---I think that was earlier, but – yes.

And then do you recall that at some stage CBA tried to get ASIC to agree to postpone the EU until after the Westpac case was decided?---That's correct.

But you wouldn't agree to that?---No.

But nevertheless, the negotiations over the EU took through until, again, July of 2018?---That's correct.

And what was the community benefit payment that CBA agreed to?---The same, 1.25 million.

Do you have any idea what sort of civil penalty you might have obtained had you gone to court?---We hadn't got advice in relation to that. You know, our view is that the civil penalty – depending on the case that we brought, wouldn't have been particularly significant. You know, it wouldn't have been, for instance, in the, you know, hundreds of millions of dollars or tens of millions of dollars.

And - - -?---I should add, for us this wasn't a penalty case. It was about stopping the conduct, and we stopped the conduct.

Would it have been worthwhile to ASIC, and perhaps to the entire community, to know whether a court thought that offering superannuation in conjunction with administering a questionnaire about a person's financial situation amounted to personal financial advice?---We – we consider that the general deterrence outcome of the EUs – you know, that met the general deterrence. It's – it's indicated that ASIC has said that this is not conduct that is acceptable. And, as I say, we have a matter before the courts that's testing out the proposition of where is the line between general and personal advice, and that will give us, you know, the court – the court's view. This is a matter that's untested but we now have a test case.

But testing out a different part of the line?---Well, you know, and as I indicated before, there's all different bits of conduct. Every time we look at matters that come to us for investigation, they can be different. And taking each and every one of those to court to test propositions is not effective regulation. It's not effective.

Do you know whether any assessment was made of whether a consumer – whether there was consumer harm as a consequence of members being switched into ANZ or CBAs superannuation product?---We did do some work in relation to that, and – well, I should say, first of all, our concern and the reason that we wanted this to stop is that we were concerned that there could be significant consumer harm. In particular, in relation to customers or consumers that rolled over superannuation. And in that sense, they may have rolled into – from a low fee fund into a higher fee fund, or they may have had some loss of insurance. So that was the real concern for us and why we wanted this conduct to – to stop. We did do some assessment, as part of our preparation for proceedings, to try and ascertain whether in fact there was real prejudice, real harm, and the results of that were relatively equivocal. You know, it wasn't clear that there was harm. Some people, in fact, had gone into a lower fee-paying fund than they were in previously. We looked at a lot of complaints data – I think from one of the banks, and I can't recall which one – which indicated that a lot of people were concerned that they were over-insured, that they didn't want this insurance that they were now getting and that, in itself, you know, may raise concerns. We were concerned about what the causation of any particular harm or

prejudice might be. What we found is that some people's decisions were made well after – to roll into the fund – were made well after they had opened the actual superannuation account. So that all those issues arose through our work, and, you know, we – we were concerned but we weren't able to point to a significant sort of body of harm, or body of loss, let's say.

Do you agree with me that in order to know whether there would be a significant body of loss, it would be necessary to do a lot of further work and analysis?---Yes, and – and it's – analysis and work that might take years and years and years because some of it might not eventuate until well down the track. We were certainly alive to that, which was – I don't want to say it again, but it's why we wanted it stopped.

So in your enforceable undertaking, there's no requirement on either ANZ or CBA to undertake that analysis?---No, that wasn't – that wasn't the focus. Remediation wasn't the focus in this particular project. As you know, remediation is a focus in a range of other Wealth Management Project matters.

Do you think that superannuation is a product that should be sold in bank branches?---Me personally?

You have a role at ASIC in relation to the sale of financial products. Do you think - - -?---I – I have never turned my mind to it. I think a product such as that could be available in a bank. We need to have people engaged in superannuation. There's a role to be played. It just needs to be done in a manner that is in accordance with the law, and it doesn't lead people to think that the bank is taking into account their personal needs and objectives and circumstances before they make some form of recommendation or mention a fund. So, yes, I think it can be done. I think it can be done. But a lot of care needs to be taken.

I don't have any further - - -?---I was going to say engagement in super is a very important thing and ASIC promotes that constantly.

I don't have any further questions.

THE COMMISSIONER: Are the documents of 3 October '17 in evidence already?

MR HODGE: No, Commissioner, I tender those documents.

THE COMMISSIONER: The email of 3 October '17, ANZ.800.973.0589 and accompanying draft enforceable undertaking, ANZ.800.973.0590, together are exhibit 5.316.

EXHIBIT #5.316 EMAIL OF 3 OCTOBER '17 AND ACCOMPANYING DRAFT ENFORCEABLE UNDERTAKING (ANZ.800.973.0589 & ANZ.800.973.0590)

MR HODGE: Thank you, Commissioner.

THE COMMISSIONER: Thank you, Mr Hodge. Yes, Mr Collinson.

MR COLLINSON: Just one matter, if the Commissioner pleases.

<RE-EXAMINATION BY MR COLLINSON [2.57 pm]

MR COLLINSON: Mr Mullaly, the hypothesis, as I understand it, that was being put to you by Counsel Assisting was to draw a comparison between the position ASIC might be in if instead of entering into an enforceable undertaking with ANZ, it had commenced a court proceeding against ANZ in May 2017?---Yes.

Do you recall those questions?---Yes.

Now, the Westpac proceeding involved similar sorts of issues, doesn't it? It's a similar sized case.

MS NESKOVCIN: Commissioner - - -

THE COMMISSIONER: Just a moment.

MS NESKOVCIN: I have leave to appear on behalf of Westpac.

THE COMMISSIONER: Yes, Ms Neskovcin

MS NESKOVCIN: I want to make a pre-emptive objection. I'm not sure where my learned friend intends to go with this but in terms of asking Mr Mullaly any questions that ask him to opine upon circumstances that differ between the CBA and ANZ proceeding and the Westpac proceeding you're reminded that the matter is the subject of a reserve decision and asking Mr Mullaly these questions which would in some way prejudge the issue may not be the appropriate form today.

THE COMMISSIONER: I don't need much persuasion that it would not be appropriate to prejudge the matter. I have not understood the question as doing more than inviting comparison between size of one actual piece of litigation and size of a hypothetical piece of litigation. Now, if the question is understood in that way, is there a difficulty about it, Ms Neskovcin?

MS NESKOVCIN: No, Commissioner.

MR COLLINSON: Yes - - -

THE COMMISSIONER: Now, have I got the idea right?

MR COLLINSON: You certainly have, Commissioner.

THE COMMISSIONER: Yes.

MR COLLINSON: I think you may have answered, Mr Mullaly, but I was simply asking you whether this hypothetical ANZ proceeding – did I misspeak somewhere there – this hypothetical ANZ proceeding was of a similar scope and scale to the actual Westpac proceeding?---Yes.

And it certainly involved similar legal issues?---Yes, we believe so.

Now, that proceeding, as you gave evidence, was commenced in December 2016?---That's correct.

I'm told the trial was February 2018?---That's correct.

And as of today, there's judgment reserved?---That's correct.

Which is August 2018. Counting forward from that, I get 20 months if one looks at the Westpac proceeding, to a position where as at today there is no resolution of ASICs concerns in relation to the conduct of Westpac?---What I would say is there's no court determination. I just hesitate to say that I – I'm not sure exactly what Westpac are doing right at the moment, so - - -

Thank you for that?---They may well have taken their own counsel on that.

Yes. Now, if we assumed a roughly similar order of events, if you had simply been the tough guy and decided not to engage with ANZ, then roughly speaking, one might think that the court proceeding against ANZ would have commenced in May 2017, there would have been a trial in about July 2018, and by January 2019 which we haven't arrived at yet, one would be in a position of an unreserved judgment. I want to ask you - - -

THE COMMISSIONER: Do we get to a question, Mr Collinson, after your speech?

MR COLLINSON: Well, it might be in a submission, your Honour, so I think it's fair to put to the witness.

I just wanted to ask you, what would you regard as the more satisfactory position to be in as at today if one compares what you achieved at ASIC with ANZ, that is, an enforceable undertaking in July 2018 versus a reserved judgment in a case against ANZ as at January 2019?---Well, certainly, we prefer to have – and we think it's better for consumers that the matter is resolved and we think it's better for general deterrence.

Now, Counsel Assisting sought to characterise your May 2017 communication to ANZ about ASICs intention to issue proceedings as a bluff. You might have

responded to that but just for clarity, what – do you disagree or agree with that characterisation?---It's part of our negotiations but we would have commenced the proceeding if we hadn't had the response.

And is it the case that the enforcement committee within ASIC had authorised the institution of proceedings against ANZ?---I – I believe so.

No further questions.

THE COMMISSIONER: Yes, thank you. Is there anything arising, Mr Hodge.

MR HODGE: Nothing arising thank you, Commissioner.

THE COMMISSIONER: Thank you very much, Mr Mullaly, you may step down. You are excused.

<THE WITNESS WITHDREW [3.02 pm]

MR HODGE: The next witness is Mr Kell.

<PETER RICHARD KELL, RECALLED AND RE-AFFIRMED [3.02 pm]

<EXAMINATION-IN-CHIEF BY MR COLLINSON

THE COMMISSIONER: Thank you very much, Mr Kell. Do sit down. Yes, Mr Collinson.

MR COLLINSON: If the Commissioner pleases. Your full name is Peter Kell?---Yes.

Your position is Deputy Chair of ASIC?---Yes.

And would you give the Commission your – well, I think your work business address is 100 Market Street, Sydney, New South Wales?---Yes. Yes, it is.

And you have there, I believe, a summons to appear before the Commission dated 6 August 2018?---I do.

I tender that, if the Commissioner pleases.

THE COMMISSIONER: Summons to Mr Kell, exhibit 5.317.

EXHIBIT #5.317 SUMMONS TO MR KELL

MR COLLINSON: Now, Mr Kell, do you also have with you a copy of your witness statement?---Yes.

Could I take you, please, to paragraph 37?---Yes.

You will see in the last line the words "due to be released soon"?---Yes.

Referring to this relationship statement. Should that correctly read "now published on ASICs website"?---Yes.

Could you handwrite that in, please, and delete the words "due to be released soon" and then initial your change?---Yes.

And one last change, paragraph 195 on page 54?---Yes.

It's really the same point?---Yes.

In line 4 do you see the words "are releasing"?---Yes.

That's, again, referring to the same document. Should it correctly read "have released"?---"Have released", yes.

So if you make that change, adding those words and deleting the words "are releasing" and initial that?---Yes.

With those changes, Mr Kell, is your witness statement true and correct?---Yes.

I tender that.

THE COMMISSIONER: Exhibit 5.318, the witness statement of Mr Kell.

EXHIBIT #5.318 WITNESS STATEMENT OF MR KELL

THE COMMISSIONER: Yes, thank you, Mr Collinson. Yes, Mr Hodge.

<CROSS-EXAMINATION BY MR HODGE [3.05 pm]

MR HODGE: Thank you, Commissioner.

Mr Kell, I want to just start by understanding a few particular factual matters that you explain in your witness statement in relation to particular entities. If we go to page 22 of your statement. That's ASIC.0800.0013.0022?---Yes.

You are dealing there with some steps that you took in relation to NAB and NULIS?---Yes.

And you make the point that in 2017, ASIC imposed additional licence conditions on NULIS following ASICs inquiries into several breach reports that had been lodged by NABs Wealth entities?---That's right.

And those breach reports relate to two things. One is the charging of plan service fees to members of the MKPS and MKBS where there was no linked adviser?---Yes.

And the second thing is some changes that were made to TPD insurance?---That's correct.

And as a consequence of those things, ASIC was concerned and had sought from NULIS and NAB either an enforceable undertaking or, alternatively, a change to licence conditions?---That's correct.

And it had originally sought that in about July of 2016?---Around that time. Yes, I don't have the exact date but around that time.

And ASICs position was that it would be – its preference was for an enforceable undertaking?---I think that was the starting position but I don't think there was a strong preference for an enforceable undertaking or a licence condition. I would say in this instance they are very similar in terms of what they would achieve.

You understood that a licence condition was regarded as being less serious than an enforceable undertaking?---No. In fact, in a range of other instances, it's generally put to us that a licence condition is – can be a stronger outcome than an enforceable undertaking. To give you an example of that, when there was concern around the issues that had arisen with Commonwealth Financial Planning's enforceable undertaking and the way in which there had been failures to comply with aspects of that enforceable undertaking, ASIC took the step of imposing licence conditions to address the failures that had arisen with the enforceable undertaking. So licence conditions may, in some circumstances, be – be more onerous. In this instance, I would have to say that the sort of outcome that was being aimed for was relatively similar. You had a public outcome, you had a range of requirements for the licensee to undertake and implement. You had a third party expert who had to oversee that and report on it, and so on. So reasonably similar in terms of the outcome, but certainly I don't think we have a hierarchy that says licence conditions above – sorry, EUs above licence conditions or, indeed, necessarily vice versa.

Your view is they will achieve a similar sort of outcome?---In – in this case, yes. In other cases, licence conditions may indeed be more onerous. My understanding is

that in some – in some cases the imposition of licence conditions requires wider reporting requirements by the entity to other regulators. So in those circumstances, licence conditions can actually represent a potentially more onerous outcome.

Can we bring up ASIC.0036.0002.0927. This is a letter of 23 August 2016 from ASIC to Ms Smith, the chair of NULIS and Mr Hagger, the chair of National Wealth Management Services Limited?---Yes, yes.

And if we go to page 3 of that document. You see at the top of paragraph – the top of the page, paragraph 8, ASIC is rejecting a proposal that has put forward by NAB and NULIS for negotiated commitments?---Mmm.

And it says:

> *Finally, ASIC does not consider that negotiated commitments are an appropriate way to resolve its regulatory concerns for the following reasons.*

?---Sure. Yes.

Continuing:

> *(a) We again point to the number and nature of breaches and their recurrence which suggest that a stronger and enforceable response is required.*

?---Yes.

Continuing:

> *(b) An enforceable undertaking is an appropriate regulatory outcome in the circumstances of our concerns.*

?---Yes.

Continuing:

> *(c) An EU is an administrative settlement and the mechanism we would ordinarily use to resolve serious compliance concerns, even in circumstances where a regulated entity has complied with its statutory obligations to report any breaches, has cooperated and has been prepared to acknowledge ASICs concerns.*

?---Yes.

And is that subparagraph (c) factually accurate? Does that reflect ASICs position?---What it reflects, I think, is that we typically obtain enforceable undertakings more regularly than licence conditions in these circumstances, but that is not a reflection, as I said, on licence conditions or enforceable undertakings,

indeed, being one or above the other. It's a – simply a reflection of the reality, in terms of the outcomes that we often take in – in these cases. I mean, if you look at 9, you have the note that:

...*licence conditions reflecting similar obligations are an alternative option*

Yes, 9 says:

> *The alternative basis upon which ASIC is prepared to resolve its concerns without enforcement action is for NULIS to consent to licence conditions reflecting similar obligations as under an EU.*

?---Yes.

And taken together what those paragraphs seem to suggest about ASICs position at least as at August 2016 is that (a) an enforceable undertaking and a change to licence conditions are not regarded as enforcement action?---No, no, the – they are within the spectrum of enforcement action. They are not court-based enforcement action but they are in the spectrum of enforcement action. And I think that's sort of set out in my – my statement.

And (b), that an EU is the mechanism that would ordinarily be used to resolve serious compliance concerns?---EUs are – court-enforceable undertakings are used more commonly when we're not looking to take a court-based approach but we do use licence conditions. I've just described an instance where we've done so. And in many cases they can achieve essentially the same sort of result, the same outcome that we're aiming for.

Is the starting point for ASIC, when it has identified conduct that it considers to breach the law, that it will commence a proceeding?---That has to be considered in these matters. I think one of the points that perhaps didn't come through in the previous discussion is that we will only consider an enforceable undertaking in circumstances where if it wasn't offered or if it wasn't offered to – in a way that was satisfactory to us, we would be able to and prepared to commence proceedings. And with licence conditions, that we would seek to impose a licence condition. I mean, last financial year, as an example, we – we had, I think, around 30 civil cases and around 25 enforceable undertakings, but for those enforceable undertakings, a sort of a threshold test – and the same issued applied when I was a commissioner at the Australian Competition and Consumer Commission – you would not seek an enforceable undertaking unless you were prepared to take the next step should it be knocked back or should negotiations fall – fall over. Otherwise, your enforceable undertaking tool would not, over the longer term, have credibility. And I think that's recognised more broadly within regulators.

You see, what you just said was:

I think one of the points that perhaps didn't come through in the previous discussion is that we will only consider an enforceable undertaking in circumstances where if it wasn't offered or if it wasn't offered to in a way that was satisfactory to us, we would be able to and prepared to commence proceedings.

?---Yes. I don't want to suggest that in each and every case that we had worked up proceedings but that is – that is something that ASIC – and as I said, in my time at the ACCC – is – is one of the basic sort of considerations that you have in place when you're looking at whether an enforceable undertaking is the right approach. It may offer better alternatives for a range of reasons, but if – if you don't obtain that undertaking, you have to understand that you would be prepared to take alternative action.

I'm just trying to understand how this view of enforceable undertakings fits with ASICs regulatory guide, which says:

We consider that enforceable undertaking can sometimes offer a more effective regulatory outcome than could otherwise be achieved through other available enforcement remedies, namely, civil or administrative action. We will not enter into an enforceable undertaking that does not offer a more effective regulatory outcome.

Is that how ASIC approaches enforceable undertakings?---That is part of the decision making process. But I'm not quite sure what – what you're getting at here, Mr Hodge.

Do you see that there are two different ways that you might approach an enforceable undertaking? One way is what you say in your regulatory guide, which is if we've decided that we're in a position to commence a court action but we think that we could obtain something more with an enforceable undertaking, then we would be prepared to consider an enforceable undertaking. That is one way?---Yes.

The other way is to say an enforceable undertaking is something that we would look to as a matter of course but we would only look to it if they wouldn't agree to it we would be willing to commence a court proceeding?---I'm not sure that the two are entirely inconsistent, if that's what you're getting at, but the – you will – we will generally be looking to enter into enforceable undertakings when they do offer the right sort of outcome and, in general, a sort of outcome that provides some potential additional or positive or alternatives to – to going to court. But, as I said, part of the threshold test is if, ultimately, the entity that we're negotiating with knocks it back, we have to be prepared to take the next step.

In the case of NULIS, NAB and NULIS said that they would prefer to have licence conditions?---I think that's ultimately what was conveyed, yes.

And negotiations then commenced over the terms of the licence conditions?---Yes.

And in October of 2016, ASIC released its fees for no service report?---Our first fees for no service report, that's right.

You've released updates since then?---Numerous updates, yes.

And in the first report, the amount of fees for no service or the quantum that was referred to in the case of MLC Nominees, which is the – one of the NAB trustees, was $12.6 million?---That's correct, yes.

And then after the report was released on 3 November 2016, representatives of NAB Wealth came and gave a presentation to ASIC?---Yes, I understand that's correct. Though I wasn't at that presentation, but yes.

One of the people who was at that presentation for ASIC was Andrew Mitchell?---Mmm.

Is that right? And that was, as you understand it, the first time that ASIC was told that, in fact, the quantum of the plan service fees was about $34 million?---That's right. 34, 35. Around that amount, yes.

But it was at that presentation that ASIC was told that for the first time?---That is my understanding.

And if we bring up ASIC.0061.0001.0001. This is an internal email from Mr Mitchell to Mr Tanzer and a couple of other – three others – two others, I'm sorry?---Yes. Yes.

Mr Tanzer was then a commissioner?---Mr Tanzer was, at that stage, a commissioner and the commissioner responsible for superannuation at that stage.

And we see Mr Mitchell's update back to ASIC, about halfway down the page:

> *Today, ASIC was informed that the estimate for compensation for the new notices is approximately $21.7 million, which when added to the previously announced figures for the PSF breach total $34.6 million.*

?---Yes.

And at the bottom of the page under the heading Next Steps:

> *Today's update radically revises the previous compensation estimates to a total of $34 million including interest.*

?---Yes.

And it said – the opinion is expressed by Mr Mitchell:

The revised figure is concerning because the company has known about the events for approximately 11 months and has only just presented the figures in a meeting today. No formal letter and just a hard copy PowerPoint presentation. We are questioning whether the imposition of licence conditions is sufficient in this situation.

?---Yes.

I tender that email, Commissioner.

THE COMMISSIONER: Email Mitchell to Mr Tanzer and others 3 November '16, ASIC.0061.0001.0001, exhibit 5.319.

EXHIBIT #5.319 EMAIL MITCHELL TO MR TANZER AND OTHERS DATED 03/11/2016 (ASIC.0061.0001.0001)

MR HODGE: Nevertheless, there was a negotiation over licence conditions with NULIS – or the negotiation continued?---Yes.

And do you know whether there was any internal questioning of whether there should be a change in strategy in relation to NAB or NULIS at this time?---I was not party to any internal deliberations of that sort.

But in your role now has anybody told you whether there was any internal deliberations about whether or not it was appropriate to continue with negotiating licence conditions, given that information?---My understanding is that the licence conditions were negotiated with NULIS, and then imposed soon after that, very early in 2017. But those – the imposition of those licence conditions did not preclude further investigations into the conduct of NULIS, which were commenced in a formal sense at around that same time that are now very well advanced, and that deal with additional concerns that have arisen in respect of NULIS.

When you say "are now very well advanced", you're talking about are going on at the moment?---Yes.

And that's in relation to both the PSFs and also the adviser service fees?---That is in relation to – now, this is where I will need to make sure I've got the terminology correct – but, yes, in relation to the fees that were the subject of the 34-35 million dollar compensation - - -

That's the PSFs?---Yes. Plus within NULIS, what we called the – the sort of no obligation or the adviser service fees where customers left the corporate super, moved to the personal super plan and were charged fees in a situation where there was no obligation on the part of the adviser to provide the advice and that they weren't properly informed. We also have significant investigations underway and

well advanced in relation to NABs fees for no service across other parts of their business in relation to personal advice, fees for no service.

And that personal advice in relation to fees for no service would include advice where the payment is being debited from the superannuation fund?---I would have to double-check on that but yes, that could well be right, yes.

And the first time that ASIC raised fees for no service issues with NAB was in about mid-2015?---That's about right. Our fees for no service project kicked off at around that time, involving, as I think you're probably aware, NAB, the other three banks and AMP. So it's a very broad-based project, and we contacted all of the major entities around the issue of whether fees had been paid without advice services being provided across their entities, across the different licensees. We've had 27 investigations as part of that project. I think we've collected more than two and a half million documents. You can see that we've obtained hundreds of millions of dollars so far in remediation and – and more – more to – more to come. And so 31 licensees have been part of that project and NAB was certainly very much a key part of that and remains so.

So far no proceedings have been commenced in relation to the fees for no service project?---No, so far – sorry, that is correct. So far no proceedings have commenced. We've had enforceable undertakings, bannings, and the licence condition. I would expect that there is a very high likelihood of proceedings commencing in the – in the near future.

And in terms of the remediation that has occurred so far, that is, the entities agreeing to pay back money that they shouldn't have taken in the first place, plus loss of earnings on that money?---Broadly speaking, yes. It's – it's a work in progress. It's a very, very significant project, the remediation project, and we have given that remediation aspect priority. You only have to look at the amounts involved to get a sense of – as to – to why. So I think so far there has been about 260 million paid back. But if you allow for the estimated compensation and the provisions, you are looking at 850 million. It doesn't give me any pleasure to say this but I wouldn't at all be surprised if it ends up being in excess of a billion dollars.

Just so we can try to - - -?---Yes.

- - - put this in some useful context, this is the return to customers of their money that was first wrongfully taken from them, dating back to 2008 or 2009?---Around that time, that's correct.

And so far, the actual compensation that has been paid is about $260 million?---That's right.

And ultimately, you expect that at some time in the future the total amount will, on the present estimate, be $850 million?---That's right.

So there's only another $790 million to go on the present estimate – sorry there's only another 590 million to go on the present estimate?---You've done the maths well there, yes.

Well, not the first time. And then assuming it gets over a billion dollars, there will be another 150 million or so to be reimbursed to those customers?---There could well be. I base that statement on the assumption that there will be entities that are not necessarily part of the – the big five, so to speak, who may have fees for no service issues. We've already had five or so breach reports from other entities. And it's also the fact that for those large – there's the four largest banks and AMP, that they are still working through the amount they will have to pay back, especially in their related licensees. Typically the work is less advanced in those areas, and that's where there's considerable engagement on – on ASICs – ASICs part.

And has there been any work to assess what profit these entities have made by having deprived customers of their money over this extended period of time?---That's not something that we have sought to do at this point. It's – it's a good question. I think I would like to – well, I am happy to say that ASIC will – will look at that, but I would say up until this point of time it has been a – a very, very resource intensive task to focus on, if you like, the main game, getting money back into the pockets of consumers, and – and that continues.

Because – and I just want to make sure we agree on this – the customers will be paid back the money plus their interest or loss of earnings?---Sure.

But it doesn't follow, and you wouldn't assume, that the earning that the entity is making on that money is the same or less than the earning that the customer would have received?---Yes. Look, I need to give that some more thought but I – maybe I'm drawing a link here that might be going a little far, but to my mind, that's one of the – the points you're making, Mr Hodge, is – is one of the reasons why ASIC has argued, as part of the debate around extending our enforcement power for a disgorgement power so we could look to tackle that more directly: the amount of money that has been made by the entities in relation to the misconduct.

Another way of creating a disincentive to deter entities from engaging in this sort of conduct would be to commence civil penalty proceedings, obtain substantial civil penalties from them that would entirely deprive them of any profit they might have hoped to have made from the conduct. Do you agree?---I agree. And I think you will – that has been obviously one of the key issues that we have been considering as part of investigations in relation to a number of the entities that are within scope for the fees for no service issue. And I think you will expect to see that.

Do you know to what extent limitation periods have already been missed because the initial contraventions occurred more than six years ago?---I can't give you a comprehensive answer on that, but certainly the limitation period issue is something we have firmly in mind as we are – as we sort of plan and prepare for further actions.

When you say you have it firmly in mind, do you mean you know that as every day goes by - - -?---There's a risk. That's right. There's a risk that some of these matters will run into the limitation periods in a significant way, if – if we don't take action soon. We're – we're certainly alert to that issue.

Now, another issue that arose in relation to NAB and NULIS in 2016 was a proposed successor fund transfer where NAB came to ASIC to speak about the continuance of grandfathered commissions?---Yes.

And the outcome was a letter – can we bring up, it's ASIC.0800.0011.3312. I think that's exhibit PK-151 to your statement, Mr Kell?---Yes.

This is a letter that was sent to Ms Debenham of NAB. And it explains that ASIC has been briefed on the proposed approach to the payment of grandfathered commissions following the proposed successor fund transfer?---Yes.

And that NAB have told ASIC that based on its legal advice, it considers that:

> *NULIS should be able to continue to pay grandfathered benefits to advisers.*

?---Yes.

And notes that NAB doesn't propose to seek a no action letter from ASIC?---Yes.

And was that the end of ASICs consideration of this issue?---In relation to, as in this letter, in relation to the grandfathering aspect of that, yes.

And if we go to exhibit PK-150 of your statement, which is ASIC.0800.0012.1761. And this is an internal email. I think the email addresses are cut off but it's an email from Ms Bird to you and Mr Tanzer?---Correct.

And it's explaining that there's this issue that has been raised by NAB?---Yes.

And then it describes what is ASICs proposed response. And you see this about two-thirds of the way down the page:

> *We note that NAB Wealth's letter is unusual because they are effectively letting us know what they plan to do and testing whether we have concerns.*

?---Yes.

And it said:

> *We also note that NAB Wealth may consider our response unhelpful.*

?---It says that, yes.

And said:

> *In the alternative, we could consider whether we think a no action letter is needed. However, we have not done so because (1) NAB have not asked us to do so, (2) the law is clearly uncertain; (3) the only relief we could grant is a no action letter which may be of questionable value to NAB, (4) consideration of whether to grant a no action letter would take some time – the issues have industry-wide implications and raise complex legal and policy issues.*

?---That's correct.

And then when we go over the page, we see that there's an explanation of what is the potentially complicated legal issue about how the platform operator provisions apply?---Yes, that's one of the legal issues, yes.

And so as we understand it, this issue having been squarely raised by NAB where it was going to rely upon these provisions to continue with grandfathering of commission, ASIC didn't go on to figure out what its position was about this?---Not to any greater extent than the – well, the internal deliberations that led to – to this email. That's correct.

And I just want to try to understand that. The grandfathering provisions have come in as part of legislation that has recently been passed in FOFA. FOFA has now been in operation since 1 July 2013 – I think compulsorily since 1 July 2013. It was able to sort of be voluntarily complied with from 1 July 2012. Does that sound about right?---Yes. The grandfathering arrangements apply generally from 2014.

That was - - -?---Yes.

- - - you had to have - - -?---Yes.

- - - an investment made by 1 July 2014?---Yes. Yes.

And there's now a question as to how a particular exception that allows grandfathering applies?---Yes.

And it would seem as if there is an obvious consumer harm issue here, because ASIC believes that commissions are not good for consumers?---Yes.

And rather than taking any steps to investigate this issue and bring a proceeding to determine the law, ASIC didn't do anything?---Well, we obviously gave the issue some consideration, but given that the law allows for changes ..... pretty expansive changes to the parties to an arrangement, or businesses to be onsold. Given that there was a high degree of uncertainty, I think the view, as you can see at that stage, was that we simply, in effect, note NABs view and that they've taken legal advice and that it was not seen as a matter where – this was not seen as a matter where testing the law, if you like, would be productive. I mean, that – I'm summing it up. I'm not

saying those were the exact words used but that – that's – I think where things landed at that time.

And why would it not be productive?---I think the view from our internal legal unit was that it was – there was a degree of – a considerable degree of uncertainty, and – plus a view that given what the grandfathering provisions allowed by way of continuing commission payments in the case of changes to arrangements and changes to ownership, and so on, that this was not a matter where it would be likely to warrant further investigation. I wasn't involved in the details of the discussion at that stage, I have to say. I know an email had been sent to me, but I – I think it's – I'm very much prepared to say I accepted the views of our financial advisers team and our legal team at that stage.

You say in your statement that ASIC contacted APRA on 27 July 2016 and spoke to the APRA supervisor dealing with the comprehensive triannual review by NULIS Nominees?---Yes.

And you've exhibited a note of the contact. It doesn't appear as if you raised with APRA this grandfathering of commissions?---I - - -

I appreciate it's not you personally?---I don't know that we did but no, I accept that. I have no knowledge that we did.

With the benefit of hindsight do you regard this as an acceptable outcome from ASICs position?---With the benefit of hindsight I think the question that the Royal Commission has raised here around whether continuing grandfathered commissions satisfies a best interests test, effectively – that's sort of part B of your questions to me – I think, with the benefit of hindsight, we should have considered that issue. And we should have raised it with APRA as well, and it's an issue which I would say that we will consider, we should have considered, and we will consider it. I – I heard the evidence over the last few days from the relevant witnesses from NAB and NULIS about that aspect of this matter. I wouldn't want to suggest that I have formed a view on it, but I didn't find some of the reasons put forward as to why grandfathering should continue and might be in the best interests to be particularly persuasive, but I think that's something that we would need to consider. I think there's also a bigger issue here. And indulge me for a moment, Mr Hodge, I would like to make this point. Leaving aside the legal test, grandfathering – the entire provision is not in the interests of consumers. The Parliament has, in effect, put in place a provision that enables the continuing payment of commissions that generate conflicts of interest and unnecessary costs widely across the financial system. It was pictured as – depicted as a transition issue of a relatively modest or limited nature. It's actually an extremely expansive provision, both in terms of the circumstances under which grandfathering is allowed to continue, and the time period over which it may continue into the future. We can and should look at individual cases, but I think for the interests of consumers in the financial system as a whole, it would be highly desirable to have this dealt with at a policy level.

Now, accepting that's your view, one of the things you presumably could have done in 2016, consistent with that view, is to challenge this proposition that the trustee of a superannuation fund is a platform operator and on that basis able to grandfather commissions?---Yes, that would be a – a – obviously, a very technical argument. With the benefit of hindsight, I wonder whether the best interests issue would have been a more productive way into the matter.

It might well be that that is a simpler way to - - -?---Yes, and as I said, we didn't consider that at all. We should have.

Now, one of the – I want to move then to another part of your statement where you talk about some investigations that ASIC has been undertaking in relation to the transition of ADAs to MySuper?---Yes.

And you deal with this commencing at page 26 which is ASIC.0800.0013.0026?---Yes.

And you say at page .0030 at paragraph 110:

> *On the basis of material reviewed at this stage, ASIC is of the view that there does not appear to be a systemic issue with the default transfer process, including disclosure.*

?---That is on the basis of the material that we looked at as part of the project that's described in the preceding few pages. I would have to say, given the evidence I've heard in the last few days, I think more broadly there is a systemic issue, but the work we undertook was to look at the transition to MySuper through the prism of adviser behaviour, based on a – an anonymous complaint that we had received, looking at it through the extent to which authorised representatives, as in advisers, and advisory firms, had potentially engaged in conduct to avoid transitioning their clients across. We have certainly identified a series of cases there where we are taking follow-up action, including, potentially, banning action, but we did not find, as part of that project, that – through the – looking directly at the advisers, that there were large numbers of advisers who were engaging in – in practices that were problematic in – in this context. I accept that that prism is not the broader prism around how trustees and wealth management firms were communicating it, and so I – I would just say that's the context of that comment in 110.

Could we then move to another topic which is general deterrence, and you express some views about how ASIC regards general deterrence, and if we go to page 43 which is .0043?---Yes. Yes.

You make a point at paragraph 154 that:

> *ASICs view is that with large money flows involved in superannuation and the financial futures of so many Australians linked to the outcome of their*

superannuation, it is most important that misconduct and/or poor practices are broadly deterred.

Does that mean deterred through enforcement action in the nature of civil litigation, or do you mean something – do you mean other types of deterrence?---Certainly civil or other litigation is a critical part of general deterrence. But in that statement I'm expressing it broadly. Deterrence can also be achieved through other enforcement mechanisms, through administrative mechanisms, through licence conditions as well. But I would very much agree that civil litigation is a key component of general deterrence.

At paragraph 201 of your statement which is page .0055, you say:

When ASIC is provided with the right enforcement tool kit, it can use that tool kit where appropriate to achieve a deterrent effect in respect of others in the industry.

And then at paragraph 203 over the page:

If ASIC were to have a greater role as a conduct regulator for RSE licensees, then it would need to be provided with powers that enable it to carry out appropriate public enforcement action and have appropriate sanctions imposed.

I wonder if you can help us with this. As it stands, ASIC may not have very many explicit powers or any real explicit powers under the SIS Act to bring civil penalty proceedings but under the Corporations Act and the ASIC Act, it can bring civil penalty proceedings for false or misleading representations that are made by entities in relation to financial services. And that would presumably include where a trustee or a wealth management group makes false or misleading representations to members concerning their superannuation. Do you agree?---Yes.

And it has powers to commence civil penalty proceedings in respect of directors' duties?---Mmm.

That's right?---Yes. Yes.

And do you agree that presumably the directors of a corporate trustee fundamentally need to ensure that the trustee complies with its obligations to act in the best interests of members?---Well, ultimately, yes. Yes.

And if the directors of the trustee fail to exercise due care and diligence so as to ensure the trustee acted in the best interests of members, ASIC could commence a civil penalty proceeding for that?---Yes.

And ASIC has the power under the ASIC Act to commence a proceeding for unconscionable conduct?---Yes, obviously.

And conduct of a corporate trustee or a wealth management company associated with a corporate trustee in relation to a superannuation product issued by the corporate trustee would presumably be conduct that, if unconscionable, would be caught within the ambit of the ASIC Act?---I would expect so.

And that would be another basis upon which ASIC could commence a proceeding for unconscionable conduct?---Yes.

And has ASIC commenced any proceedings against corporate trustees for either false or misleading representations or unconscionable conduct?---I do not know that we've done it for unconscionable conduct. And I would have to check on false and misleading but I – if we have, not many actions.

And has it commenced any proceedings for contraventions of the director obligations – I think that's part 2.7 of the Corporations Act but I might be wrong about that, but in any event, sections 180 and onwards, has it commenced any proceedings seeking civil penalties against directors in relation to their conduct of corporate trustees in the last five years?---I don't believe so in the last five years, but, again, I would have to - - -

In the last 10 years?---Yes, I would have to check.

Were there any proceedings commenced against the directors of Trio?---I think there were, yes.

That may have been - - -?---Yes.

All right. And so what I wonder is when you say ASIC would need to have more powers to have a greater role as a conduct regulator, is that a statement that you see as being easily reconcilable with the fact that ASIC already has a number of powers which it doesn't exercise?---I think that paragraph is a reference to the powers or provisions under the SIS Act. And there is an issue here as well around giving you, for want of a better phrase, the frontline legislation, where ASIC only has a relatively limited set of powers. There would, perhaps, be – it would perhaps be desirable to clarify how and where you would expect conduct regulation to be most appropriately housed. I think we would want to – we are wanting to undertake further, but having said that we are wanting to undertake further enforcement action in this area. We've recently received additional funding to do so. It's part of our plan to expand our approach to the regulation of the super sector.

Do you think on the – I'm sorry, I said part 2.7. I think it's actually part 2D.1 - - -?---Yes.

- - - in relation to the directors' duties. Do you think that the way in which ASIC has gone about commencing or not commencing civil penalty proceedings in relation to, say, the adviser service fees issue, or the plan service fees issue, gives confidence that ASIC would, if it had expanded powers under the SIS Act, exercise those

powers in a way that would deter misconduct?---I would point to the fact that we've already had some outcomes against the entities, that we have significant investigations underway which are likely to lead to litigation, and that we've obtained hundreds of millions of dollars in compensation to date as an indication that we take these issues very seriously. I would also point to the fact that we have a more expansive track record of litigation in relation to those parts of the – broader superannuation sector where we are the sole regulator or the frontline regulator. So to give you an example, the actions that we've taken in relation to financial advisers who advise on superannuation or, indeed, licensees in that space. The National Sterling Group, the first case we took to court under the new best interests provisions against NSG, effectively involved a model whereby the advisers in that firm were inappropriately rolling people over into expensive or inappropriate superannuation products, selling inappropriate insurance which was then coming out of that superannuation – their superannuation. So within those areas where we have been the sole regulator, much of our work relates directly to people's superannuation and how that is impacted through poor advice or misleading or deceptive conduct.

You don't think, though, do you, that the reason that ASIC has not commenced – there's a lot of negatives. Let me put it a different way. Are you suggesting that a reason why ASIC has been reluctant to commence civil penalty proceedings in relation to the conduct of RSE licensees is because of some confusion about its role because APRA has primary responsibility under the SIS Act?---No, no, it's – it's – I'm simply pointing out that there are provisions under SIS that we are not responsible for that would potentially provide the ability to take those sorts of actions. I'm not – I'm not saying it's because of a confusion around that issue.

Do you mean if you had a power to commence a civil penalty proceeding for a failure to comply with the best interests duty, you might do so?---Or the sole purpose test I had in mind.

That's something that APRA presently has the power in relation to, the sole purpose test?---Yes.

So if you were able to do it, then you might do it?---Look, it – that's a potential example.

Commissioner, I don't have any further questions for this witness.

THE COMMISSIONER: Mr Kell, you've spoken a lot about civil penalty proceedings. Do you regard civil penalty proceedings as the best ultimate means of achieving public denunciation of misconduct?---I think they can be a very effective means, but it will, Commissioner, it would depend on the circumstances. It might be that criminal proceedings are in some cases an appropriate tool. It might be that in other circumstances banning someone for life from the industry in which they're working sends a very, very powerful message as well. But certainly, I would say that civil penalty proceedings are a very important part of the – the deterrence tool kit.

If criminal proceedings were to be launched, that would have to be by the Commonwealth DPP, would it not?---That's correct.

And the process would entail ASIC submitting a brief to Commonwealth DPP for consideration by the director of whether the circumstances are fit for prosecution?---Indeed.

And do not answer this if the answer would embarrass current considerations, but has ASIC, in the last five years, given consideration to submitting a brief to Commonwealth DPP in respect of any aspect of the fees for no service matter?---Yes.

Yes. Mr Hodge.

MR HODGE: Nothing from that, Commissioner.

THE COMMISSIONER: Yes. Mr Collinson.

MR COLLINSON: No questions.

THE COMMISSIONER: Yes. Thank you very much, Mr Kell. You may step down?---Thank you.

You're excused.

<THE WITNESS WITHDREW [4.04 pm]

THE COMMISSIONER: Mr Hodge.

MR HODGE: Commissioner, I have some very brief closing observations.

THE COMMISSIONER: Well, you announced at the beginning of this round that it was proposed to deal with closing submissions somewhat differently this time.

MR HODGE: Yes.

THE COMMISSIONER: Yes.

MR HODGE: So the way that we propose to deal with it is that by Friday of next week, Counsel Assisting will provide written submissions to you which will constitute the full closing submissions from Counsel Assisting. And that will include the specific findings that Counsel Assisting says may be open to you, Commissioner, with respect to the evidence that you've heard in respect of particular entities. And we will also, in some detail, address or outline the particular policy issues for consideration, both by parties granted leave to appear and also for other members of

the public who wish to make public submissions. I am in your hands but I think you were the one who were going to tell us about what process you would like to use for the receipt of submissions. I don't want to presuppose anything.

THE COMMISSIONER: Well, my understanding is that Counsel Assisting will make written closing submissions which are to be published on the Commission's website by 5 pm next Friday, 24 August 2018. Those submissions will include submissions about the particular case studies that have been undertaken. Those submissions will also include the identification of what Counsel Assisting see as issues or questions of principle that arise. So far so good, Mr Hodge?

MR HODGE: Yes, thank you, Commissioner.

THE COMMISSIONER: What is then proposed is that parties having leave to appear would have until 5 pm on Friday, 31 August – so a further seven days – to file written submissions not exceeding 20 pages in relation to each case study. And those written submissions not exceeding 20 pages per case study would relate to the findings said to be available with respect to the particular case studies. I probably garbled that but in effect the idea is that parties having leave to appear should deal with the case studies in writing limited to 20 pages by 5 pm Friday, 31 August. So they will have the full week after Counsel Assisting have published their submissions.

Now, the Commission has already announced that written submissions will be invited both from parties having leave to appear and from the public more generally in relation to the policy issues that are identified in this round of hearings, and the proposal is that parties with leave and members of the public may make written submissions in relation to those policy issues, that they have until 5 pm Friday, 21 September '18 to make those submissions. I have given some thought to what page limit I should impose on the policy submissions. My wish is that the submissions be as concise as the subject matter will permit, but the issues are issues that do not admit of being dealt with in half a page, I suspect. So I propose that the page limit should be 50 pages.

But as with all page limits, that's the outer limit, not the necessary extent. And the proposal is that all of those submissions about policy should be lodged with the Commission through the Commission's website. The website will be set up in a way that will permit the public to make their written submissions but so, too, parties should make their written submissions through the website so that we are getting all the policy papers in through the one portal and we're not ending up having to double-handle everything. So to back up, written closing submissions from Counsel Assisting by 5 pm Friday, 24 August.

Parties with leave to appear, written submissions about the case studies not exceeding 20 pages 5 pm, Friday 31 August. Written submissions about policy issues not exceeding 50 pages, 5 pm Friday, 21 September. The last set of submissions all to be channelled through the Commission website.

MR HODGE: Thank you, Commissioner.

THE COMMISSIONER: Now, Mr Hodge.

MR HODGE: Commissioner, I have a list of additional tender documents, which is – it runs to 41 documents.

THE COMMISSIONER: Which you are not going to require me to read out but you are going to make available to the transcript writer or you're going to read out, Mr Hodge, which?

MR HODGE: I certainly didn't propose to read it out myself, Commissioner. I would be quite happy to hand it to the transcript operator. I should indicate it is primarily witness statements in relation to either case studies that we haven't heard evidence in relation to or some – in some cases, additional witness statements for case studies that you have heard evidence in relation to. There are also some additional documents that have been referred to in the course of the hearings or which parties given leave to appear have asked us to tender, and we will publish the list on the website as well.

THE COMMISSIONER: Yes.

MR HODGE: So if you're content with that, Commissioner, I have told you that. Otherwise I won't take that any further. What I proposed, Commissioner, was, consistent with what we promised at about 10 am two weeks ago, that I would very briefly outline at the conclusion of this two round of hearings some of the questions that we consider may arise and some other procedural matters. So long as you're content with me doing that, Commissioner, I will proceed to do that. Perhaps if I start with these observations: over the course of the past two weeks, you've heard evidence, Commissioner, by our count, from seven directors of trustees, including four chairs and one deputy chair, two CEOs, and nine other officers from within trustees or their service providers.

And cumulatively, the trustees that have been covered in oral evidence are responsible for more than $627 billion worth of funds under management, which is more than 38 per cent of the total funds held in regulated super funds in Australia as at 30 June 2017. And those trustees are also responsible for $228 billion of MySuper assets. In the documents that have been tendered, there are some statements related to two case studies that we had initially proposed to deal with and have now elected not to deal with orally, and I should just indicate what those are. In addition to CBUS which we spoke about on the opening, the other two entities are Sunsuper and Mercer.

In relation to Sunsuper, investigations continued in relation to it last week, and we concluded that the issue that was raised there was of insufficient general application to warrant consideration orally. And in relation to Mercer, the issue ultimately we determined didn't go beyond something that had already been addressed publicly in a

news report and shortly before the commencement of the hearings we received a submission from Mercer acknowledging that the conduct or some aspects of the conduct may fall below community standards and expectations.

What the evidence as a whole suggests is that it may well be the case that you will conclude that some RSE licensees are not, as they are obliged to do, prioritising the interests of their members over the interests of others, including themselves and the groups of which they are parties. And there are certain types of decisions that seem to particularly raise matters of concern. The decision to charge or allow others to charge members' fees which are then paid to financial advisers in circumstances where the member doesn't receive or could not have been receiving the services in respect of which the service was provided, and in some cases, they would also be not the financial adviser, him or herself, but rather some other company within the group that was supposed to be providing services.

Another decision of concern are decisions to charge or maintain grandfathered trailing commissions and other forms of conflicted remuneration. Another decision of concern is the decision to delay, or at the very least not expedite the transition of accrued default amounts to a MySuper product with, it would seem, one apparent effect being to entrench members for a longer period of time in legacy products with trailing commissions. A fourth decision is the potential failure to become aware and intervene to prevent the charging of fees by a related party where those fees result in negative returns to members.

And a fifth type of decision is the potential failure to exercise proper oversight over the distribution channels of a trustee's superannuation products by related parties. And those decisions, as we say, may be ones which do not demonstrate a sufficient prioritisation, or any prioritisation, of the interests of the members over the interests of the trustee or parties related to the trustee. It may also be conduct which is in contravention of the best interests duty and other legal obligations. There was also evidence, Commissioner, that you may ultimately conclude suggests that some trustees may have failed to exercise their discretions independently of other influences or third parties.

And it would seem to follow from the fiduciary obligations of the trustees that this ought not have occurred. One particular example is the outsourcing of services which are required to administer a trust. That is not something that is prohibited. But outsourcing does not absolve the trustee of ultimate responsibility for what occurs in relation to the use and application of trust money. A third issue that you may consider, Commissioner, is that there was evidence that suggests that there may have been problems with the ways in which some trustees communicated to members, information that was provided to members that had the potential to confuse or to mislead them, and some examples of things that we looked at over the course of the week included disclosure about service fees, disclosure about tax surpluses, statements about the reasons, consequences or effects of the transition from accrued default amounts to MySuper, statements about the reasons why compensation was

now being paid, or information provided to members about commissions and other forms of conflicted remuneration.

These things that we have observed, Commissioner, go to this: members of superannuation funds, like most beneficiaries, are vulnerable, and in respect of superannuation, many are disengaged and disadvantaged by a lack of financial literacy. They are readily able to be taken advantage of. And the evidence, you may conclude, Commissioner, suggests that this has occurred in some cases. In most industries, the forces of competition can be relied upon to minimise improper conduct and effective regulation can be expected to address breaches of the law when breaches occur.

However, for superannuation, the disengagement of members, amongst other things, may limit the effectiveness of competition, and there are also questions, Commissioner, as is apparent, about the effectiveness of regulation in relation to superannuation. Those things combined mean, as we said in the opening, that there is a particular importance for members of the RSE licensees complying with their fiduciary obligations. Now, against these overarching issues, there are some specific questions that we will identify now to assist the parties in preparing for their general written submissions, and further questions will be expanded upon in the written closing next week.

The first question is this: are there structures that raise inherent problems for a superannuation trustee being able to comply with its fiduciary duties. For example, where a trustee is a DRE, that would seem to raise an inherent conflict of interest, or the potential of a conflict of interest, but are there other structures such as investment of funds in insurance policies issued by related party insurers or the integration of a superannuation trustee into an advice business that also raise inherent problems. Second, if these structures do raise inherent problems, is structural change of entities, mandated by legislation or otherwise, something that is desirable.

There are obvious and very significant challenges with mandating structures or structural changes and an important question is can it be really said with any confidence that conflicts that arise from structures are so unmanageable as to warrant legislative intervention where one would think that ordinarily the very strong preference should be away from any form of legislative intervention in particular corporate structures. Third, apart from structural arrangements, are there other types of relationships that present obvious challenges to a trustee in discharging its duties, or where the benefits to the member of those relationships are limited or non-existent.

If so, would it be appropriate to make legislative interventions to eliminate those temptations and difficulties for trustees. For example, would it be desirable to prohibit all commissions payable from superannuation products and end grandfathering, at least in relation to superannuation products. Might it also be desirable to prohibit ongoing advice fees being deducted by trustees from superannuation accounts. To do so, would mean that financial advisers could only be

paid from a member's superannuation account for one-off advice to a member in relation to superannuation.

A consumer could still enter into an arrangement to make ongoing payments from the consumer's bank account to a financial adviser if the consumer wished to pay for and commit to paying for ongoing advice. A consumer would likely be aware of ongoing direct debits from the consumer's bank account. Or a consumer would have to authorise a specific payment for one-off advice where the payment is coming from the consumer's superannuation account. Such a payment could, in accordance with the sole purpose test, only be in respect of advice relating to superannuation.

In this way, the risk of a consumer's superannuation balance being depleted by ongoing advice fees dripping out of the account would be removed. Such a change might act to nudge a consumer to consider more carefully what financial advice she or he wishes to obtain and what she or he wishes to pay for it. It would also remove the risk of a trustee making deductions from a superannuation account to make ongoing payments to a financial adviser or to some other entity for services that were not provided or not provided adequately. It would thereby protect both the member and the trustee. But would it have a detrimental effect on the provision of financial advice to consumers so as to harm their financial interests.

Fourth, is it necessary to strengthen existing laws prohibiting misconduct so as to address misconduct identified during the course of the hearings or potential misconduct identified during the course of the hearings, or is it simply necessary to enforce existing laws. Perhaps there are small changes that are required. For example, should there be harsher penalties for directors who breach their covenants imposed under the SIS Act. Should there be civil penalties for failing to act in the best interests of members. Should there be greater civil penalties for breaches of the sole purpose test.

Fifth, what can be done to encourage the regulators to act promptly on misconduct or potential misconduct and is the present allocation of regulatory roles appropriate to achieve specific and general deterrence from misconduct. Given that what we are fundamentally concerned with is conduct that in subtle but ongoing ways negatively affects the retirement outcomes of consumers, are either of the regulators best placed to carry the responsibility to protect consumers should the balance between them be restructured or significantly altered.

Sixth, and finally, are there further structural tweaks necessary to make it more likely that consumer interests will be best served in the superannuation industry, and, Commissioner, we offer two examples that might assist to remove or mitigate temptations for trustees. The first is stapling. Meaning, consumers are attached to a single superannuation account and do not end up with new accounts each time they change jobs, which might reduce the incentive for superannuation trustees to wish to maintain low balance members. Second, would it be desirable to impose obligations on the shareholders of trustees to exercise powers under their constitution, or when

otherwise acting in relation to the trustee, to do so in the best interests of the members.

Commissioner, those are all the things that we wish to say now. The various questions and issues which we have raised will be refined and developed further in our written submissions. And subject to anything further you may wish to say, Commissioner, that concludes the oral round of hearings.

THE COMMISSIONER: Thank you. Thank you, Mr Hodge. The Commission will adjourn until 10 September next at 9.45.

MATTER ADJOURNED at 4.28 pm UNTIL MONDAY, 10 SEPTEMBER 2018

Index of Witness Events

Index of Exhibits and MFIs