# Senate Select Committee on Superannuation and Financial Services

## Main Inquiry
## Reference (a)

**Submission No. 101**
(Supplementary to Submission No. 96)

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**SUPPLEMENTARY SUBMISSION.**

**A. Focus on Delays by APRA/ASIC – HIH Case. Predicting Success or Failure.**

Since completion of my submission only days ago, there has been considerable publicity in relation to delays by the Regulators concerning HIH. Again APRA has made admissions relating to its long running knowledge of difficulties of HIH. Again there have been explanations given on behalf of APRA where APRA has admitted having been aware of difficulties in HIH over a long period (Since September 2000 at least). Publicity has been given to the extension of time allowed, "grace periods" and other concessions extended to HIH. (HIH without announcement to APRA seemingly appointed the Provisional Liquidator before APRA allowed time had expired!). This highlights an absolutely basic flaw in the "Corporate Management System" of APRA.
There are many management and other analytical models available for "Predicting Success or Failure". Many studies with empirical evidence available for different business classes exist. "Failed Banks and US Railroad companies" are examples. (Unfortunately there is seemingly case study material now developing for "Failed APRA/ASIC Supervised Financial Institutions).
The circumstances and the explanations highlight a severe deficiency in the "professionalism" of APRA/ASIC.
There seems to be no actuarial assessments undertaken, but that the "soft" and "toothless" regulatory approach seems to be the model!
Given the indicators available in relation to CNAL and HIH, and the fact that BOTH have failed to rectify or renovate the organizations seem to give a very high FAILURE RATE in the discretionary systems of APRA/ASIC. It would be interesting (though probably not "discoverable" due to the "Old Fashioned

Secrecy" provisions) to see just how many other SUCCESSFUL "soft line" cases have occurred. How many other Financial Institutions have "come back" after allowing the Soft Line Approach? More so, how many are still in the APRA/ASIC "pipeline" of "Overdue, Grace Period, Pending" and other classifications which will result in FAILURE?
Failed insurance companies do not seem to have the same existing statutory "Safety Net" for which there is provision under the SIS Act for funds to be supported by the Minister. However there seems to already be cries from the public and those affected to attribute blame to APRA/ASIC for its flawed regulatory performance.
While it is important for the SIS Act Funds to be able to distinguish the existing statutory protection available for Superannuation and the special place that Superannuation and its protection must enjoy, it can be expected that further appeals for support will now be forthcoming from policy holders, and claimants who seem now to be in line also to suffer unexpected losses due to the failure of HIH and APRA/ASIC! There is even the unfortunate connection of HIH as an insurer of CNAL it seems up to 29.6.2000! The impact of this failure and connection was mentioned in my earlier submission but now takes on an even more acute profile.
**The failure to professionally administer the existing laws must now be redressed by the Government critically correcting the failures of the agencies and quickly restoring through the existing statutory mechanisms the damage done by the failures.**

**B. Zero Tolerance Policy.**

A Zero Tolerance Policy has been advocated and implemented in some other areas, particularly "drug" related law enforcement.
While there has been public disquiet in that area and nonacceptance as a deterrent, there seems to be a much stronger case for advocating "Zero Tolerance" in relation to many aspects of the prudential supervision of Financial Institutions, particularly the Non-bank institutions regulated by APRA (and ASIC) and certainly more in relation to Superannuation (and now possibly Insurance). In the absence of "Zero Tolerance", the Softer approach must now demand a process which can include a more transparent and robust process for asking for and giving reasons capable of assessment by the "market" and researches and not just the regulators, whenever the prescribed provisions have not been strictly complied with by the Trustees (and Insurers). The public and the market will probably prove to be much better judges of the prospects for success or failure than the Regulators! However they need to have the information that is "knowable" and is capable of being provided to the public and the financial advisers to enable informed decisions to be made. Concealing the information under "secrecy" merely delivers the "worst of both worlds". Protection for the wrongdoers, exposure to the innocent! The price of any concessions granted to bring supervised prudential organizations into compliance surely has to be more transparency of the information. The risk attaching to failure to comply surely has to be revealing of the fact that there has been a failure to comply to the investing public! Where justified, appropriate enforcement action also needs to be taken before disasters are allowed to accumulate and have such devastating effects on the "investing" public as has occurred through the regulatory failures in the case of CNAL (and now HIH!) All within the same time frame – the last twelve months! **This can only be corrected by the Government recognizing the failures of its agencies, taking appropriate corrective action (but also encouraging the Agencies to be self assessing/critical on a continuing basis) and using existing statutory provisions to correct the effects!**

## C. Update of the Memorandum of Understanding between APRA/ASIC

The MOU of 12.10.98 seems to be one of the most ineffective documents ever written!
A close examination of the MOU will reveal a serious lack of structure and recognition of the many problems and issues faced by the Regulators. A much more comprehensive and structured process is required.
There are many deficiencies and failures in the systems, communication, consultation processes outside of the parties being regulated. There is the need for closer liaison with the financial services industry in a more structured and representative manner, with some accountability also attributable to the other "players" in the industry. Practical measures such as exchange arrangements between officers of each organization, secondments from the private sector and other law enforcement agencies seems to be necessary. This can be achieved through a thorough governance and management review process. With (mutual) exchanges, there need be no additional cost!
Perhaps people skilled in "Joint Venture" and results oriented organizations could help overcome what

seems to be one of the most unsuccessful "partnerships" or joint ventures ever attempted, whether in the public service or private sector.
A corporate "Scorecard" with "Key Performance Indicators" (KPIs) needs to be introduced to evaluate the performance of the "cooperation" effort. It seems to me it would be ZZZ. Are Targets Set, are they met, do they achieve "Threshold", "Underperformance", (ever Over Performance"?). Some fairly simple processes could be introduced to improve an absolutely failed "Joint Venture". As to financial performance, budget targeting and measurement of success or failure, I shudder to think just how badly APRA/ASIC MOU inspired performance assessment would fare.
The failures now identified should also be followed up through a "Post Implementation Review" (Internal Audit) process, not only within each organization, but as to the effectiveness of the "Joint" arrangement. The gaps are "gaping" and seem to be getting "wider". They need to be closed off completely and create a culture of acceptance of responsibility rather than being able to point to where "things fell through the cracks/wide gaps!" A shrug of the shoulders and "Well it is not our fault!" **The real perpetrators of course cannot be excused, CNAL, its directors, managers, auditors and advisers. So far as the public is concerned however, it is clearly a matter of fault on the part of the two agencies entrusted to administer very important statutory laws in the Corporations Law, the SIS Act and related matters!**

## D. Council of Members – Beneficiaries Consultation – Comparison to Shareholder Rights

This point arises following discussion with a Press reporter. Surely, there is a process to compare the status of Superannuation Fund members with that of "shareholders" in a company. There seems to be a complete lack of understanding by the Trustee in the case of CNAL and maybe it is widespread, of the very high duty to as as a Trustee, not as some sort of opportunistic business preying on the vulnerabilities of the people to whom they owe such a high duty as a Trustee!
Other than through the mechanism of the respective Trust Deeds, there is indeed no equivalent of "Shareholders" Rights such as an Annual General Meeting type process where Trustees should be forced to present accounts and to account for their performance annually and "publicly" to their "Members". Trust Deeds are generally very private in nature. There is now room for improvement to compel Trustees to report Annually, not only to the Regulators, (which they have been so easily able to avoid), but also to report within the strict reporting periods required for Public Companies, to do so in a similar manner to all "Members", and where acting for many Funds collectively to all funds, where monies are "invested". There may also be some additional protection at very little cost to have a process for the election of a "Council of Members" which also could exercise some supervisory power over Trustees on behalf of Members. These could be aggregated to ensure quality and efficiency. The "Secrecy" which confines the information to the Trustee, the Auditors, and the Regulators, without any actual publications in relation to important aspects (such as the ECMT) provides a recipe and invitation for incompetence and long lasting concealment ("mushroom") tactics! Only more disclosure requirements and compulsory dialogue can relieve the ineffective regulators of pressure and responsibility. There must be clear prohibitions against the making of certain investments, rather than to rely on "Guidelines". (The older system of having only nominated authorised Trust Investments was apparently found to be too restrictive.)

**Every APRA Approved Trustee should therefore be required to report to a Council of Members (and Financial Advisers) at least annually with full disclosure of accounts and records similar to that of a public company.**

## E. Risk and Risk Management by APRA/ASIC, the Government and the Public.

It is rather ironic that APRA/ASIC whilst engaged in supervision and regulation of "Risk Takers", in Financial Institutions, Companies and the business community, have not managed or perhaps even recognized the extent of "Risk Taking" and Risk Management and Acceptance, that they are expected to exercise in their own affairs. If there is a culture that they have no accountability or are immune from the consequences of error or mistake in performance of their functions, then the Government and the Public can expect an inferior performance from these very important regulators. If they do not "deliver" the degree of protection expected, then there is a case for not having Regulators at all! Failure to Regulate and deliver satisfactory results must result in just criticism and in our society to pay for the mistakes clearly made. There cannot be "All Care taken but no responsibility". On a fair assessment of the damage done in the two most recent cases of Regulator Failure (as well as the Corporate and business failure of the Trustee and the Insurer), there may well be a case for the appointment of "Managers/Receivers/Liquidators" so to speak of the Regulators themselves! By effectively concealing weaknesses that might otherwise be exposed in an "open market" the regulators have clear responsibility. The delays cannot be excused with such regularatory as they are occurring. Unfortunately where the Government has committed through legislation and policy to allow "Approved" Trustees who have the commitment and support through legislation to

operate under such patronage, then the Government (as the shareholder) must also support the failings of the Regulators.
The "floodgates": argument now is an addition one to address. If there is to be a procession of failures, then the tendency is always to try to "stem the flow".
However, if the failures can now be limited, and if they are in fact limited to one APRA Approved Trustee, where there is provision for Government support, then surely that risk must be accepted and the Minister motivated to quickly correct the deficiencies.
**In the case of a major failed Insurer, this should not be allowed to adversely affect, but in fact should influence the Government to quickly correct the correctable situation. In the process, the Government also must address the systemic failure of the Regulators to properly assess and manage the manageable risks of regulatory efficiency.**

## F. The Superannuation "Investors" Dilemma.

Superannuation is advocated as the vehicle for providing for one's own retirement. There is an assumption almost everywhere that Superannuation can really only accumulate! This is a fair assumption. (Market conditions can of course and will always affect some classes of investment.) Much concern is often shown as to the differing "rates of return" achieved by the various funds and competition exists in relation to maximising of returns. The "risk/ return relationships is well known". However when funds intended for "low risk" return are converted to "high risk" by failures in the systems, a serious situation exists. CNAL apparently had no "low risk" "safe" system for its beneficiaries monies.(Though when fully analysed the law may be able to distinguish and separate where CNAL APRA, ASIC, Investigators, Liquidators and others cannot), ASIC/APRA and auditors failed to detect irregularities and have them corrected! They were capable of being corrected by reasonable yet decisive action on the part of the regulators, the ones with the power to do so.
Information was concealed from the ASIC licensed financial advisers! The ASIC licensed financial advisers were unable (or ill equipped) to ascertain the "knowable" information and bring about management of the Approved Trustee from the consumer viewpoint. The consumer was prevented by the solid wall of "secrecy". Even after the "freeze" from my very first inquiry, APRA was still assuring me that CNAL was a registered and complying Approved Trustee! At the same time, ASIC was using its powers to warn and threaten against implying any irregularity on the part of CNAL! Fortunately this attitude changed, but when it was too late, and yet after the time when both agencies were in full knowledge of the events for some time which has brought about such devastation!
The performance of all licensed operators is always expected to vary. Some are better than others. But with a prudential and purported supervisory system in the "sacred" area of superannuation, the expectation is that within the known and accepted risk areas, there should in fact be an elimination of the risk of complete failure to the extent exhibited in relation to CNAL.

**It is a function of the Agencies, and when they fail the Government, where there is already statutory power to do so, to ensure that the protection professed is delivered. When information is held and "Investors" given the information which could assist them to avoid flawed Trustees (and Insurers), then and only then can there be any refuge for the Regulators and the Government in the event of failure. Unfortunately in the case of CNAL the regulators until forced to act belatedly have in fact been the agents of CNAL (not the consumers)! This can now be corrected by the Minister.**