FEDERAL COURT OF AUSTRALIA

Australian Prudential Regulation Authority v Kelaher [2019] FCA 1521

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| File number: | NSD 2274 of 2018 |
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| Judge: | **JAGOT J** |
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| Date of judgment: | 20 September 2019 |
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| Catchwords: | **SUPERANNUATION** – whether two entities and their directors contravened s 52 and s 52A of the *Superannuation Industry (Supervision) Act 1993* (Cth) (**SIS Act**)– trustee’s duties – duties of trustee directors – alleged contraventions of statutory covenants – care, skill and diligence – best interests of the beneficiaries – conflicts of interest – whether the governing rules of the trusts exclude liability for the alleged contraventions – prudent person and prudent superannuation trustee standards of care – inadequate proof of contraventions – application dismissed |
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| Legislation: | *Corporations Act* *2001* (Cth) s 601FB(2), Pt 2D.1  *Evidence Act 1995* (Cth) s 140  Explanatory Memorandum, *Superannuation Legislation Amendment Trustee Obligations and Prudential Standards) Bill 2012* (Cth)  *Superannuation (prudential standard) determination No. 1 of 2012* (*Operational Risk Financial Requirement SPS 114*)  *Superannuation (prudential standard) determination No. 7 of 2012 (Prudential Standard SPS 521)* cll 8, 10, 11, 16  *Superannuation Industry (Supervision) Act 1993* (Cth) ss 3, 7, 10(1), 51, 51A, 52, 52(a), 52(b), 52(2)(b), 52(2)(c), 52(2)(d), 52(d)(i), 52(2)(d)(iv), 52(4), 52(8), 52(8)(a), 52A, 52A(d)(i), 52A(2)(b), 52A(2)(c), 52A(2)(d), 52A(2)(f), 52A(3), 54B(1), 54B(2), 55, 55(1), 55(3), 56, 56(1), 56(1)(a), 56(2), 56(2)(a)(1), 56(2)(a)(ii), 56(2A), 57, 57(2), 60A, 115  *Superannuation Legislation Amendment (Trustee Obligations and Prudential Standards) Act 2012* (Cth)  *Treasury Laws Amendment (Improving Accountability and Member Outcomes in Superannuation Measures No. 1) Act 2019* (Cth) |
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| Cases cited: | *Apostolovski v Total Risk Management* [2010] NSWSC 1451; (2010) 79 NSWLR 432  *Australian Securities Commission v AS Nominees* (1995) 62 FCR 504  *Australian Securities and Investments Commission v Drake (No 2)* [2016] FCA 1552; (2016) 340 ALR 75  *Australian Securities and Investments Commission v Healey* [2011] FCA 717; (2011) 196 FCR 291  *Australian Securities and Investment Commission v Letten (No 17)* [2011] FCA 1420; (2011) 286 ALR 346  *Briginshaw v Briginshaw* [1938] HCA 34; (1938) 60 CLR 336  *Commonwealth Bank Officers Superannuation Corporation Pty Ltd v Beck & Anor* [2016] NSWCA 218  *Cowan v Scargill* [1985] 1 Ch 270  *Daniels v Anderson* (1995) 37 NSWLR 438  *Dovuro Pty Ltd v Wilkins* [2003] HCA 51; (2003) 215 CLR 317  *Elder’s Trustee and Executor Co Ltd v Higgins* (1963) 113 CLR 426  *Finch v Telstra Super Pty Ltd* [2010] HCA 36; (2010) 242 CLR 254  *HIH Insurance Limited (in prov liq) v Adler* [2002] NSWSC 171; (2002) 41 ACSR 72  *In re Chapman* [1896] 2 Ch 763  *Karger v Paul* [1984] VR 161  *Manglicmont v Commonwealth Bank Officers Superannuation Corporation Pty Ltd* [2010] NSWSC 363; (2010) 239 FLR 159  *Manglicmot v Commonwealth Bank Officers Superannuation Corporation Pty Ltd* [2011] NSWCA 204; (2011) 282 ALR 167  *Mercer Superannuation (Australia) Limited v Billinghurst* [2017] FCAFC 201; (2017) 255 FCR 144  *Morley v ASIC* [2010] NSWCA 331; (2010) 81 ACSR 285  *Nestle v National Westminster Bank* [1993] 1 WLR 1260  *Saker Re; Great Southern Managers Australia Ltd (recs and mgrs. apptd) (in liq) (No 2)* [2011] FCA 958; (2011) 85 ACSR 211 |
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| Date of hearing: | 1 - 3, 10 - 12, 15 - 17 July 2019 |
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| Category: | Catchwords |
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ORDERS

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|  | | NSD 2274 of 2018 |
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| BETWEEN: | AUSTRALIAN PRUDENTIAL REGULATION AUTHORITY  Applicant | |
| AND: | CHRISTOPHER FRANCIS KELAHER  First Respondent  GEORGE VENARDOS  Second Respondent  DAVID COULTER (and others named in the Schedule)  Third Respondent | |

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| JUDGE: | JAGOT j |
| DATE OF ORDER: | 20 September 2019 |

THE COURT ORDERS THAT:

1. The amended originating application be dismissed.

2. The applicant pay the respondents’ costs as agreed or taxed.

Note: Entry of orders is dealt with in Rule 39.32 of the *Federal Court Rules 2011*.

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JAGOT J:

##### 1. THE PROCEEDING

1 The applicant, the Australian Prudential Regulation Authority, (**APRA**), alleged that two entities within the IOOF Group of companies, referred to as IIML (the sixth respondent) and Questor (the seventh respondent), and two of their directors, Mr Kelaher (the first respondent) and Mr Venardos (the second respondent), contravened ss 52 and 52A of the *Superannuation Industry (Supervision) Act 1993* (Cth) (the **SIS Act**). APRA sought disqualification orders against the directors and three responsible officers of the entities, Mr Coulter (the third respondent), Mr Vine (the fourth respondent) and Mr Riordan (the fifth respondent). The issue of potential disqualifications was deferred for hearing and determination at a later time. These reasons for judgment concern only the alleged contraventions.

2 IIML was the trustee and licensee of the IOOF Portfolio Superannuation Fund (**IPS Super**). Questor was the trustee and licensee of The Portfolio Service Retirement Fund (**TPS Super**) until June 2016 when the beneficiaries and assets of TPS Super were transferred by a successor fund transfer to IPS Super. IPS Super and TPS Super were “registrable superannuation entities” for the purpose of the SIS Act: APRA’s amended statement of claim or **ASOC** [5]-[6], as admitted in Defences [5]-[6].

3 APRA contended that the respondents (excluding the third, fourth and fifth respondents who were not subject to these obligations) contravened various covenants imposed on them by the SIS Act, in effect, to exercise the requisite degree of care, skill and diligence, to act in the best interests of the beneficiaries of the super funds, and to give priority to the interests of the beneficiaries in the event of a conflict of interest. These contraventions were said to have occurred in the course of five incidents affecting the super funds known as CMT, Pursuit, Sweep, Bendigo and Optus.

4 APRA sought to prove its case relying solely on documents brought into existence by the respondents in connection with the incidents. As a result, there was no dispute about the primary facts. Both parties recorded the salient aspects of the facts on which they sought to rely in their written submissions. I have relied on the factual summaries of the parties as indicated in the reasons below. As will become apparent APRA relied on the IOOF documents as containing admissions against interest by the respondents including, as I would understand it, admissions of contravention of the statutory covenants. For a number of reasons I have found APRA’s approach unpersuasive. The documents were all produced with the benefit of hindsight. Apart from the opinions or conclusions expressed as to breach of the statutory covenants, the documents are expressed at a high level of generality, assuming knowledge on the part of the reader as to IOOF’s systems, policies and procedures (which remained unproved by other evidence). I also do not accept that there can be an effective admission of a legal conclusion, which is a matter for the Court based on the whole of the evidence. Even if such a statement could constitute an admission I would not be persuaded as to its reliability. It was for APRA to prove its case of contraventions by such evidence as it saw fit. The fact that it has chosen to run a purely documentary case means that it must take the documents as it finds them – as documents brought into existence for specific purposes, mostly by authors whose qualifications and experience are unknown, using the benefit of hindsight, often expressed at a high level of generality, and assuming otherwise unproven knowledge of IOOF’s systems, policies and procedures.

5 Another related, systemic weakness in APRA’s case is that it has asserted contravention of the covenants and, in so doing, has alleged defaults and inadequacies in IOOF’s systems, policies and procedures, without descending into the detail of proving the actual systems, policies and procedures in play in respect of the incidents in question. Instead it has relied on IOOF’s documents as described above which do not themselves identify those systems, policies and procedures. As one of the respondents put it, a critical plank in APRA’s case is that alleged defaults gave rise to causes of action or reasonably arguable causes of action for recovery against IOOF entities, the claims being in the nature of claims for contractual negligence, but APRA has given no attention to the kind of factors which would necessarily inform the foundation of any such claims such as the details of the actual system in existence, the nature of the default or flaw in the system, the reasonable foreseeability of that default or flaw, the reasonable availability of any alternative that might have avoided the default or flaw, and the materiality of the potential consequences of the default or flaw. Without expressly saying so APRA’s approach involved reliance on the doctrine of *res ipsa loquitur* when the one thing that is clear is that the facts of the incidents in question in this case by no means speak for themselves.

6 As will also become apparent, in treating the facts as if they automatically bespeak liability, APRA has effectively cast the trustees in the role of insurer to the beneficiaries, which is contrary to principle. APRA has also sought to extend legal principle by applying the kind of requirements to which a trustee is subject in deciding whether or not a beneficiary is entitled to a payment out of the trust, a circumstance in which the trustee is bound to give proper consideration to the relevant information and if necessary obtain relevant information to fulfil its trust duty, to the day-to-day decisions which a trustee of a large fund must make in the administration of the trust. APRA has not explained why this extension of legal principle is warranted and, as explained below, I am unpersuaded that it is warranted.

7 For these reasons, and as explained in more detail below, I have decided that none of APRA’s claims of contraventions of the SIS Act against the respondents are sustainable with the consequence that there is no foundation for the making of any disqualification orders and the further amended originating application should be dismissed.

##### 2. SECTIONS 52, 55, 56 AND 57 OF THE SIS ACT

8 There is a preliminary dispute between APRA and the respondents which is fundamental to their competing cases. In short, APRA contended that despite their governing rules IIML and Questor could not be exempted from liability for contraventions of the s 52 covenants and could not indemnify themselves from the assets of the trusts in respect of liability for such contraventions. The respondents contended that the governing rules of the trusts, in conformity with the SIS Act, excluded liability for the alleged contraventions of the s 52 covenants and enabled IIML and Questor to indemnify themselves from the assets of the trusts in respect of any such liability.

9 The relevant provisions of the SIS Act include s 3, which provides that the main object of the Act is to make provision for the prudent management of, relevantly, superannuation funds.

10 Section 7 provides that:

This Act applies to a superannuation entity despite any provision in the governing rules of the entity, including any provision that purports to substitute, or has the effect of substituting, the provisions of the law of a State or Territory or of a foreign country for all or any of the provisions of this Act.

11 The “governing rules” are defined in s 10(1) to mean in relation to a fund, scheme or trust,:

(a) any rules contained in a trust instrument, other document or legislation, or combination of them; or

(b) any unwritten rules;

governing the establishment or operation of the fund, scheme or trust.

12 Part 6 contains ss 51 to 60A of the SIS Act. Section 51 provides that the object of the Part is to set out rules about the content of the governing rules of superannuation entities. Section 51A confirms that the covenants taken to be contained in the governing rules of a superannuation entity are cumulative. Section 52 contains the covenants by the trustee taken to be contained in the governing rules of a superannuation entity. Section 52A contains the covenants by the directors of a corporate trustee taken to be contained in the governing rules of a superannuation entity. Section 55 concerned the consequences of the contravention of covenants. In this regard, it should be noted that s 55(1) was repealed by the *Treasury Laws Amendment (Improving Accountability and Member Outcomes in Superannuation Measures No. 1) Act 2019* (Cth) and replaced by ss 54B(1) and (2) to the same material effect. As the relevant conduct pre-dates this amendment it is the form of the Act before this amendment which is relevant.

13 Section 55 included the following provisions:

(1) A person must not contravene a covenant contained, or taken to be contained, in the governing rules of a superannuation entity.

(2) A contravention of subsection (1) is not an offence and a contravention of that subsection does no result in the invalidity of a transaction.

(3) Subject to subsection (4A), a person who suffers loss or damage as a result of conduct of another person that was engaged in in contravention of subsection (1) may recover the amount of the loss or damage by action against the other person or against any person involved in the contravention.

(4) Unless an action under subsection (3) is of a kind dealt with in subsections (4A) to (4D), it may be begun at any time within 6 years after the day on which the cause of action arose.

(4A) If:

(a) the person who is alleged to have contravened subsection (1) is or was a director of a corporate trustee of a registrable superannuation entity; and

(b) it is alleged that the contravention is of a covenant that is contained, or taken to be contained, in the governing rules of the entity, and is:

(i) a covenant of the kind mentioned in subsection 52A(2); or

(ii) a covenant prescribed under section 54A that relates to the conduct of the director of a corporate trustee of a registrable superannuation entity;

an action under subsection (3) may be brought only with the leave of the court.

(4B) A person may, within 6 years after the day on which the cause of action arose, seek the leave of the court to bring such an action.

(4C) In deciding whether to grant an application for leave to bring such an action, the court must take into account whether:

(a) the applicant is acting in good faith; and

(b) there is a serious question to be tried.

(4D) The court may, in granting leave to bring such an action, specify a period within which the action may be brought.

(5) It is a defence to an action for loss or damage suffered by a person as a result of the making of an investment by or on behalf of a trustee of a superannuation entity if the defendant establishes that the defendant has complied with all of the covenants referred to in sections 52 to 53 and prescribed under section 54A, and all of the obligations referred to in sections 29VN and 29VO, that apply to the defendant in relation to each act, or failure to act, that resulted in the loss or damage.

(6) It is a defence to an action for loss or damage suffered by a person as a result of the management of any reserves by a trustee of a superannuation entity if the defendant establishes that the defendant has complied with all of the covenants referred to in sections 52 to 53 and prescribed under section 54A, and all of the obligations referred to in sections 29VN and 29VO, that apply to the defendant in relation to each act, or failure to act, that resulted in the loss or damage.

(7) Subsections (5) and (6) apply to an action for loss or damage, whether brought under subsection (3), section 29VP or otherwise.

14 Section 56 is relevantly in these terms:

(1) Subject to subsections (2) and (2A), a provision in the governing rules of a superannuation entity is void if:

(a) it purports to preclude a trustee of the entity from being indemnified out of the assets of the entity in respect of any liability incurred while acting as trustee of the entity; or

(b) it limits the amount of such an indemnity.

(2) A provision in the governing rules of a superannuation entity is void in so far as it would have the effect of exempting a trustee of the entity from, or indemnifying a trustee of the entity against:

(a) liability for breach of trust if the trustee:

(i) fails to act honestly in a matter concerning the entity; or

(ii) intentionally or recklessly fails to exercise, in relation to a matter affecting the entity, the degree of care and diligence that the trustee was required to exercise; or

(b) liability for a monetary penalty under a civil penalty order; or

(c) the payment of any amount payable under an infringement notice; or

(d) liability for the costs of undertaking a course of education in compliance with an education direction; or

(e) liability for an administrative penalty imposed by section 166.

15 Section 57 is relevantly in these terms:

(1) Subject to subsection (2), the governing rules of a superannuation entity may provide for a director of the trustee to be indemnified out of the assets of the entity in respect of a liability incurred while acting as a director of the trustee.

(2) A provision of the governing rules of a superannuation entity is void in so far as it would have the effect of indemnifying a director of the trustee against:

(a) a liability that arises because the director:

(i) fails to act honestly in a matter concerning the entity; or

(ii) intentionally or recklessly fails to exercise, in relation to a matter affecting the entity, the degree of care and diligence that the director is required to exercise; or

(b) liability for a monetary penalty under a civil penalty order; or

(c) the payment of any amount payable under an infringement notice; or

(d) liability for the costs of undertaking a course of education in compliance with an education direction; or

(e) liability for an administrative penalty imposed by section 166.

(3) A director of the trustee of a superannuation entity may be indemnified out of the assets of the entity in accordance with provisions of the entity's governing rules that comply with this section.

16 The governing rules of the TPS trust included these provisions:

Cl 15.4: The Trustee is only liable for its acts or omissions which are dishonest or constitute an intentional or reckless failure to exercise the degree of care and diligence required of it.

Cl 15.5: the Trustee may recover from the Fund any loss or expense incurred in relation to the Fund unless:

(a) it results from the Trustee’s dishonesty or intentional or reckless  
failure to exercise the degree of care and diligence required of it; or

(b) the law prevents it.

17 The governing rules of the IPS trust included these provisions:

Cl 11.5: No Trustee or director of the Trustee shall be liable under any personal liability in respect of any loss or breach of trust in respect of the Fund or the benefits of a Member unless the same shall have been due to:

11.5.1 its own failure to act honestly in a matter concerning the Fund;

11.5.2 intentional or reckless failure to exercise, in relation to a matter affecting the Fund, the degree of care and diligence that the Trustee or director was required to exercise.”

…

Cl 11.7: The Trustee and the directors of the Trustee shall be indemnified out of the assets of the Fund against all liabilities and expenses incurred by them in the execution of their duties hereunder and shall have a lien on the Fund for such indemnity.

18 In support of its contentions, APRA submitted that:

(1) s 55 does not provide that it is a defence to liability to rely on an exemption or indemnity in a trust instrument;

(2) s 55 cannot be modified or excluded by a trust instrument. If it were otherwise, s 55 would not apply according to its terms as provided for in s 7;

(3) the object in s 3 reinforces this approach to the construction of s 55;

(4) s 56 preserves a trustee’s general right of indemnity out of the trust assets for liabilities incurred in the proper performance of its duties or exercise of its powers;

(5) ss 56(2) and 57(2) do not specify the universe of limitations on the provisions of a trust instrument; and

(6) the terms of the provisions, in the overall context of the SIS Act, mean that no provision of a trust instrument can purport to exclude or modify liability under s 55(3).

19 The respondents submitted that:

(1) s 56(1)(a) refers to “any liability” which is of the broadest scope and would include s 55(3) liability;

(2) s 56(1) leaves open to a trustee to agree governing rules that provide for the trustee to be indemnified for any liability, subject only to ss 56(2) and (2A);

(3) s 55(3) liability is not identified in ss 56(2) or 57(2) as a liability which cannot be excluded by a trust instrument;

(4) s 56(2) includes liability for breach of trust and thus liability to beneficiaries;

(5) the exclusion in s 56(2)(a)(1) overlaps entirely with the covenant in s 52(a) and the exclusion in s 56(2)(a)(ii) overlaps in part with the covenant in s 52(b) which demonstrates the permitted scope of an exemption from liability arising under s 55(3);

(6) if it were right that no s 55(3) liabilities could be excluded or the subject of an indemnity it would follow from s 55(1) that contravention of any covenant, not just the s 52 covenants, would be protected thereby prohibiting the ordinary right of a trustee and beneficiaries to agree to exclude a trustee’s liability for breaches of covenants contained in the trust deed; and

(7) it is wrong to say that the respondents’ construction leaves trustees free to contravene the s 52 covenants. Remedies such as an injunction may be granted to prevent or retrain a breach of a covenant.

20 I do not find resolution of this aspect of the dispute straightforward. There are what appears to be anomalies on both approaches to construction. On balance, however, I consider that APRA’s approach better reflects the provisions construed in the context of the SIS Act as a whole. This is because I consider s 7 of the SIS Act to be of fundamental importance to the resolution of this aspect of the dispute. By s 7 the SIS Act applies despite any provisions in the governing rules. Section 55(3) provided for a statutory cause of action, with its own limitation period and its own defences, which included compliance with all of the covenants in ss 52 to 53 (amongst others). If, by governing rules, a trustee may exclude liability under s 55(3) then it cannot be said that the SIS Act is being applied despite anything in the governing rules. Similarly, if, by governing rules, a trustee may indemnify itself out of the trust assets then it cannot be said that the SIS Act, specifically the statutory cause of action and limited defences, are being applied.

21 It may be accepted that s 56(1) uses the words “any liability”, but the section is to be read in harmony with ss 7 and 55. Section 56(1) is also about provisions in the governing rules which are void because they purport to preclude or limit the trustee’s right of indemnity in respect of any liability from the assets of the entity. The liability with which s 55 is concerned is that provided for in s 55(3). Section 56(1) is not purporting to operate on s 55(3). As such, it is not trespassing on the code which s 55 has created. Section 56(2), in contrast, is not a code of any kind. It is identifying some kinds of provisions of governing rules which will be void. The fact that liability under s 55(3) does not appear in the list of void provisions is immaterial. Section 55 operates according to its terms and, by s 7, despite any provision in the governing rules of a trust.

22 For these reasons, to the extent that the respondents’ defences depended on the proposition that IIML and Questor could never have been liable under s 55(3) and would have had a right of indemnity under the trust instruments for any such liability, I do not accept those defences. If my conclusion is incorrect then, as the respondents submitted, APRA’s case must fail. There is no allegation of dishonesty or an intentional or reckless failure to exercise the required degree of care, skill and diligence.

##### 3. THE STATUTORY COVENANTS

###### 3.1 The legislation

23 The conduct in issue spans the period from 2007 to 2018. Accordingly, the covenants in their form before and after 1 July 2013, when the *Superannuation Legislation Amendment (Trustee Obligations and Prudential Standards) Act 2012* (Cth) came into force, are relevant.

24 APRA conveniently summarised the pre and post 1 July 2013 covenants by the trustee of a registrable superannuation entity (or **RSE**) as follows:

During the relevant period, the s 52 covenants [which are covenants by each trustee of a registrable superannuation entity] relevantly included covenants:

(a) **s 52(2)(b) (due care, skill and diligence covenant)** ASOC [25(a)], [26], [38], [39]:

**[Pre-1 July 2013]**: “to exercise, in relation to all matters affecting the entity, the same degree of care, skill and diligence as an ordinary prudent person would exercise in dealing with property of another for whom the person felt morally bound to provide”;

**[Post 1 July 2013]**: “to exercise, in relation to all matters affecting the entity, the same degree of care, skill and diligence as a prudent superannuation trustee would exercise in relation to an entity of which it is trustee and on behalf of the beneficiaries of which it makes investments”.

(b) **s 52(2)(c) (best interests covenant)** ASOC, [27], [39];

**[Pre- 1 July 2013]**: “to ensure that the trustee’s duties and powers are performed and exercised in the best interests of the beneficiaries”

**[Post 1 July 2013]**: “to perform the trustee’s duties and exercise the trustee’s powers in the best interests of the beneficiaries”.

(c) **s 52(2)(d) (conflicts covenant) [post 1 July 2013 only]** ASOC [27], [39]:1

“where there is a conflict between the duties of the trustee to the beneficiaries, or the interests of the beneficiaries, and the duties of the trustee to any other person or the interests of the trustee or an associate of the trustee:

(i) to give priority to the duties to and interests of the beneficiaries over the duties to and interests of other persons; and

(ii) to ensure that the duties to the beneficiaries are met despite the conflict; and

(iii) to ensure that the interests of the beneficiaries are not adversely affected by the conflict; and

(iv) to comply with the prudential standards in relation to conflicts”.

25 Before 1 July 2013, there was only one covenant by a director of a trustee of a registrable superannuation entity in s 52(8) requiring the director to exercise a reasonable degree of care and diligence for the purposes of ensuring that the trustee carried out its s 52 covenants.

26 After 1 July 2013, s 52A was inserted into the SIS Act which provided for covenants from each director of a corporate trustee of the entity including:

s 52A(2)(b): to exercise, in relation to all matters affecting the entity, the same degree of care, skill and diligence as a prudent superannuation entity director would exercise in relation to an entity where he or she is a director of the trustee of the entity and that trustee makes investments on behalf of the entity's beneficiaries;

s 52A(2)(c): to perform the director's duties and exercise the director's powers as director of the corporate trustee in the best interests of the beneficiaries;

s 52A(2)(d): where there is a conflict between the duties of the director to the beneficiaries, or the interests of the beneficiaries, and the duties of the director to any other person or the interests of the director, the corporate trustee or an associate of the director or corporate trustee:

(i) to give priority to the duties to and interests of the beneficiaries over the duties to and interests of other persons; and

(ii) to ensure that the duties to the beneficiaries are met despite the conflict; and

(iii) to ensure that the interests of the beneficiaries are not adversely affected by the conflict; and

(iv) to comply with the prudential standards in relation to conflicts;

s 52A(2)(f): to exercise a reasonable degree of care and diligence for the purposes of ensuring that the corporate trustee carries out the covenants referred to in section 52.

###### 3.2 Care, skill and diligence covenant, s 52(2)(b) and s 52A(2)(b)

27 APRA submitted that IIML and Questor were professional trustees and held themselves out as such with the consequence that they should be held to a higher standard of care than that of an ordinary prudent person (that is, before 1 July 2013). APRA referred to *Australian Securities Commission v* ***AS Nominees*** (1995) 62 FCR 504 in which Finn J said at 516 – 517 that:

It is old and accepted law that in managing a trust business the trustee should exercise the same care as an ordinary, prudent business person would exercise in conducting that business as if it were his or her own: *Speight v Gaunt* (1883) 9 App Cas 1; *Learoyd v Whiteley* (1887) 12 App Cas 727; *Knox v Mackinnon* (1888) 13 App Cas 753. There is an equally well-accepted gloss on (or adjunct to) this in relation to trustee investments which is aptly described in *Scott on Trusts*, par 227.3 as the "requirement of caution".

…

Where the trustee is itself a company the requirements of care and caution are in no way diminished. And here, unlike with companies in general, these requirements have a flow-on effect into the duties and liabilities of the directors of such a company. It was established early - largely it would seem from case law on charitable and municipal corporations - that at least when, and to the extent that, directors of a trustee company are themselves "concerned in" the breaches of trust of their company, they are liable to the company according to the same standard of care and caution as is expected of the company itself: *Charitable Corporation v Sutton* (1742) 2 Atk 400; 26 ER 642; *Attorney General v Wilson* (1840) 10 LJ Ch 53; *Joint Stock Discount Co v Brown* (1869) LR 8 Eq 381; *Fouche v Superannuation Fund Board* (1952) 88 CLR 609.

To affirm such a limited coalescence in the standard of care of directors and trustees in the case of directors of trust companies is not to reignite the arid debate on whether directors are trustees: cf *Re International Vending Machines Pty Ltd* at 473; L S Sealy, "The Director as Trustee" [1967] Camb LJ 83. It is merely to say that in this context the duties of trusteeship of the company can give form and direction to the common law and statutory duties of care and diligence imposed on directors, where the directors themselves have caused their company's breach of trust: on the duty of care of directors generally, see *Daniels v Anderson*; *Permanent Building Society v Wheeler* (1994) 11 WAR 187; see also *Superannuation Industry (Supervision) Act 1993* (Cth), s 52(8), (9).

28 At 517-518 Finn J concluded that if it were necessary to do so he would hold the trustee in that case to a higher standard of care than the ordinary prudent businessperson on the basis that the trustee was a professional trustee company holding itself out as having special or particular knowledge, skill and experience which invited “reliance upon themselves by members of the public in virtue of the knowledge, etc, they appear so to have”.

29 Further, APRA noted that in *Australian Securities and Investments Commission v Drake (No 2)* [2016] FCA 1552; (2016) 340 ALR 75 at [273] Edelman J agreed with Finn J’s observations in *AS Nominees* at 517-518. His Honour said at [276] that:

…any holding out by a trustee of a special or particular knowledge, skill and experience reflects an assumption of that special degree of responsibility. Again, the question is an objective one which is based upon the circumstances of the trust deed or declaration of trust and the acceptance of the obligation by the trustee.

30 APRA also referred to ***Finch v Telstra*** *Super Pty Ltd* [2010] HCA 36; (2010) 242 CLR 254 in which the principles in ***Karger v Paul*** [1984] VR 161 were considered. At [28] French CJ, Gummow, Heydon, Crennan and Bell JJ identified *Karger v Paul* as a case involving a trustee’s discretion under a will. At [29] they contrasted that kind of power with the case at hand in which the trustee was bound to consider whether to reach opinions which determined eligibility for a benefit to be paid from the trust. While the consideration involved factors “difficult to weigh, impressions to be formed, and judgments to be made” the trustee was not exercising a discretion. Accordingly, forming the required opinion “was not a matter of discretionary power to think one thing or the other; it was an ingredient in the performance of a trust duty”: at [30]. At [66] their Honours said:

There is no doubt that under *Karger v Paul* principles, particularly as they have been applied to superannuation funds, the decision of a trustee may be reviewable for want of “properly informed consideration”[*Kerr v British Leyland (Staff) Trustees Ltd* [2001] WTLR 1071 at 1079; *Stannard v Fisons Pension Trust Ltd* [1992] IRLR 27 at 31.]. If the consideration is not properly informed, it is not genuine. The duty of trustees properly to inform themselves is more intense in superannuation trusts in the form of the Deed than in trusts of the *Karger v Paul* type. It is extremely important to the beneficiaries of superannuation trusts that where they are entitled to benefits, those benefits be paid. Here, for example, the applicant was claiming a Total and Permanent Invalidity benefit to support himself for the rest of his life. His claim depended on the formation of an opinion by the Trustee about the likelihood that he would ever engage in “gainful Work”: that was not a mere discretionary decision. In the Deed there was a power to take into account “information, evidence and advice the Trustee may consider relevant”, and that power was coupled with a duty to do so. It would be bizarre if knowingly to exclude relevant information from consideration were not a breach of duty. And failure to seek relevant information in order to resolve conflicting bodies of material, as here, is also a breach of duty. The Scheme is a strict trust. A beneficiary is entitled as of right to a benefit provided the beneficiary satisfies any necessary condition of the benefit

31 As noted above, a consistent theme of APRA’s case is its attempts to draw an analogy between the kind of decision with which *Finch v Telstra* was concerned and the kinds of decisions which the trustees were making in the present case. As will become apparent, I am not persuaded that the analogy is sustainable.

32 APRA also noted *Apostolovski v Total Risk Management* [2010] NSWSC 1451; (2010) 79 NSWLR 432 in which Gzell J said:

21 A trustee’s duties under a superannuation deed were limited by McLelland J to those applicable to the exercise by a trustee of discretionary powers in *Rapa v Patience*, NSWSC, unreported, 4 April 1985. His Honour adopted what had been said by McGarvie J in *Karger v Paul* [1984] VR 161 about the challenge to a trustee’s exercise of discretionary power.

22 In *Karger* a testatrix left her entire estate to her husband during his lifetime with power in her trustees in their absolute and unfettered discretion, upon the request of the husband, to pay or transfer the whole or part of the capital of the estate to the husband for his own use absolutely. Upon the death of the husband the trustees were to pay the residue to the plaintiff for her own use absolutely. The husband and the testatrix’s solicitor were the trustees. The husband made a written request to pay the entire capital of the estate to him and he and his co-trustee acceded to the request.

23 At 164 McGarvie J said that the issues examinable by the court were limited to whether there had been a failure to exercise the discretion in good faith, upon real and genuine consideration and in accordance with the purposes for which the discretion was conferred. In short, the court examines whether the discretion was exercised but does not examine how it was exercised.

24 In *Rapa*, McLelland J adopted this approach with respect to a claim by an employee for breach of duty by the trustee of a superannuation fund for failing to allow his claim for total and permanent disablement. His Honour said:

“The grounds on which the performance by trustees of functions such as these may be successfully challenged are those applicable generally to the exercise by trustees of discretionary powers, helpfully discussed by McGarvie J in *Karger v Paul* (1984) VR 161. As encapsulated by his Honour in that case there are three such grounds and in some circumstances a fourth. They are, first, that the discretion was not exercised by the trustees in good faith, second, that the discretion was not exercised upon real and genuine consideration (which includes consideration of the wrong question - see Scott on Trusts 3rd ed. Vol. 3, para. 187.3), third, that the discretion was not exercised in accordance with the purposes for which it was conferred and, fourth, where the trustees have disclosed (otherwise than in the course of the proceedings in which the discretion is challenged) the reasons for the exercise of their discretion that those reasons are not sound.”

25 As Ormiston JA remarked in *Telstra Super Pty Ltd v Flegeltaub* [2000] VSCA 180; (2000) 2 VR 276 at 278 [6] it seems to have been assumed since the decision in *Rapa* that similar restrictions to those discussed in *Karger* apply to the formation of opinions as to the qualification of a beneficiary for benefit under a superannuation trust deed.

26 Judicial dissatisfaction with such limitations has been expressed from time to time (*Vidovic v Email Superannuation Pty Ltd*, NSWSC, unreported, 3 March 1995; *Flegeltaub* at 277 [4], 283 [25] and 284-285 [33]; *Jeffrey Guy Baker v Local Government Superannuation Scheme Pty Ltd* [2007] NSWSC 1173 at [8]; *John Gilberg v Stevedoring Employees Retirement Fund Pty Ltd* [2008] NSWSC 1318 at [18]; *Kowalski v MMAL Staff Superannuation Fund Pty Ltd (No 3)* [2009] FCA 53 at [25]; *Tuftevski v Total Risk Management Pty Ltd* [2009] NSWSC 315 at [128]).

27 In *Finch v Telstra Super Pty Ltd* [2010] HCA 36; (2010) 84 ALJR 726 the High Court recently held that a decision that a person was entitled to payment out of a superannuation fund for total and permanent invalidity was not a discretionary decision in the sense used in *Karger*. A decision whether a member of such a fund was unlikely ever to engage in gainful work was an ingredient in the performance of a trust duty.

…

28 Here the fault was not to fail to take relevant information into account: it was to fail to act with reasonable dispatch. But, in my view, that also is a breach of fiduciary duty by Total Risk as trustee of the Fund.

29 In *Finch* there was no discussion of an award of damages against the trustee. But a trustee must bring to his or her office the same degree of care, skill and diligence as an ordinary prudent person would exercise in performing the duties of a trustee and to fail or exercise that degree of care, skill and diligence constitutes a breach of fiduciary duty.

30 In *Government Employees Superannuation Board v Martin* (1997) 19 WAR 224 at 273 Ipp J said as much:

“It was the duty of the Board to preserve the trust property (the fund) and observe the terms of the trust. In managing the fund, the Board was required to exercise the same diligence and prudence as an ordinary prudent man of business would exercise in conducting that business if it were his own: see *Austin v Austin* (1906) 3 CLR 516; *Fouche v Superannuation Fund Board* (1952) 88 CLR 609 at 641. The duty so imposed is an equitable one: see *Permanent Building Society v Wheeler* (1994) 11 WAR 187 at 237.”

31 In *Austin* the High Court held that it was the duty of a trustee, in managing the trust affairs, to take those precautions which an ordinary man of business would take in managing similar affairs of his own. In *Fouche* at 641 the Court said that the duty of a trustee of a superannuation fund was a duty of reasonable care – care which an ordinary prudent man of business would take.

32 In my view, by at least 7 September 2007 Total Risk as trustee, through its servants or agents managing the Fund, had failed to exercise that degree of care, skill and diligence that an ordinary prudent person would exercise in the circumstances.

33 APRA said that the equivalent duty of directors to exercise due care, skill and diligence is analogous to that of directors of corporations to “take reasonable steps to place themselves in a position to guide and monitor the management of the company”. A director cannot necessarily avoid liability merely by relying on conduct of officers of the corporation: *Daniels v Anderson* (1995) 37 NSWLR 438 at 501-503. Further, as Finn J explained in *AS Nominees* at [517], the duties of trusteeship can give form and direction to the common law and statutory duties of care and diligence imposed on directors. APRA said that this duty may be heightened where there is a conflict of interest, referring to the statement of Santow J in ***HIH Insurance*** *Limited (in prov liq) v Adler* [2002] NSWSC 171; (2002) 41 ASCR 72 at [372(14)] that:

Where there is a transaction involving the potential for conflict between interest and duty, as here arose, the duty of care and diligence falls to be exercised in a context requiring special vigilance, calling for scrupulous concern on the part of those officers who become aware of that transaction to ensure that any necessary corporate approvals are obtained and safeguards put in place. While the primary responsibility will fall on the director or officer proposing to enter into the transaction, this does not excuse other directors or officers who become aware of the transaction.

34 APRA referred also to *Australian Securities and Investments Commission v* ***Healey*** [2011] FCA 717; (2011) 196 FCR 291 where Middleton J said:

18 A board should be established which enjoys the varied wisdom, experience and expertise of persons drawn from different commercial backgrounds. Even so, a director, whatever his or her background, has a duty greater than that of simply representing a particular field of experience or expertise. A director is not relieved of the duty to pay attention to the company’s affairs which might reasonably be expected to attract inquiry, even outside the area of the director’s expertise.

19 The words of Pollock J in the case of *Francis v United Jersey Bank* (1981) 432 A 2d 814 (1981), quoted with approval by Clarke and Sheller JJA in *Daniels v Anderson* (1995) 37 NSWLR 438, make it clear that more than a mere ‘going through the paces’ is required for directors. As Pollock J noted, a director is not an ornament, but an essential component of corporate governance.

…

170 …In *Vines v Australian Securities and Investments Commission* (2007) 62 ACSR 1, Santow JA (who dissented on the facts but not on principle) clarified the position as follows (at [731]):

The degree of an officer’s permissible reliance on others will turn on similar considerations as those that determine the overall standard of care for an individual director. They focus particularly on the characteristics of the company, the skills and experience of the officer concerned and the delegate, and the reasonably anticipated risks entailed in so doing. What is expected here is a level of scrutiny as befits supervision, not the detailed direct involvement that is associated with operational responsibility. Where there is no cause for suspicion nor circumstances demanding critical and detailed attention, it is reasonable for an officer to rely on advice, without independently verifying the information or scrutinising the data or circumstances upon which that advice is based: see *Re HIH Insurance Ltd (in prov liq); ASIC v Adler* (2002) 168 FLR 253; 41 ACSR 72; [2002] NSWSC 171 at [372].

171 The position of non-executive directors (as distinct from directors in general) has also been the subject of judicial consideration. In *ASIC v Macdonald*, Gzell J noted at [255] that:

While Clarke and Sheller JJA in *Daniels* rejected the test propounded by Rogers CJ Comm Div for the limit of a director’s entitlement to rely on management, they did recognise that the role of a non-executive director was to guide and monitor the management of the company rather than to be involved at an operational level.

172 It is clear that an objective standard of care is applicable to both executive and non-executive directors.

173 This approach to the standard of care has been adopted by the case law. An example of such is found in *Gamble v Hoffman* (1997) 24 ACSR 369. The court refused to subjectify the standard of care to (namely, in that case) the standard of a person who “left school at the age of 14 years, has no tertiary qualifications and has spent his life…essentially as a fruit and vegetable market gardener”. The court, at [373], rejected the assertion that:

[S]ubjective considerations of that nature and extent should affect the minimum content of the duty or standard of care required of the respondents in this matter…

…

[T]he ambit of the duty and the standard of care depend on particular circumstances. However, the test is essentially objective that is did the officer exercise the degree of care and diligence that a reasonable person in a like position in a corporation would exercise in the corporation’s circumstances? I doubt whether the factors which Mr Bates advanced would justify a lower standard of care.

174 In this proceeding, the directors’ responsibilities and duties were outside the realm of operational responsibility. ASIC does not contend that the directors needed to be involved at “an operational level”. This is not a case concerning the need to verify information or scrutinise data of a type outside each director’s own knowledge. The salient feature here is that each director armed with the information available to him was expected to focus on matters brought before him and to seriously consider such matters and take appropriate action. This task demands critical and detailed attention, and not just ‘going through the motions’ or sole reliance on others, no matter how competent or trustworthy they may appear to be.

175 Directors cannot substitute reliance upon the advice of management for their own attention and examination of an important matter that falls specifically within the Board’s responsibilities as with the reporting obligations. The Act places upon the Board and each director the specific task of approving the financial statements. Consequently, each member of the board was charged with the responsibility of attending to and focusing on these accounts and, under these circumstances, could not delegate or ‘abdicate’ that responsibility to others.

35 APRA submitted that:

(1) “Under s 52A, as with s 180(1) of the *Corporations Act* [*2001* (Cth)], directors cannot substitute reliance upon the advice of management for their own attention and examination of an important matter that falls specifically within the directors' responsibilities, such as a compensation plan for beneficiaries: cf *ASIC v Healey* at [170], [171] and [175]”.

(2) “…the Court would not accept that blind reliance on management could discharge [a director’s] duties under s 52(8) (prior to 1 July 2013) and s 52A in circumstances where, to [the director’s] knowledge, those very executives and lawyers had a conflict of interest or duty and the decision in question concerned one of the core functions of the trustee, namely, protecting the trust estate from being dissipated”.

(3) “…the issue of the appropriate approach to rectification of breaches and the use of beneficiaries’ reserves were matters that should have ‘attract[ed] inquiry’ of Kelaher and Venardos”.

(4) “It is relevant to observe that neither Kelaher nor Venardos has chosen to give evidence in these proceedings. To make out a defence based on reasonable reliance on management the Court would need to make factual findings as to the state of mind of those directors. The Court should be cautious in making such findings in the absence of evidence and in circumstances where the one person who could give that evidence had deliberately chosen not to do so.”

36 The respondents submitted that the higher standard of care of a prudent superannuation trustee was introduced only by the 1 July 2013 amendments to the SIS Act. Before those amendments the statutory standard of care was the ordinary prudent person. Accordingly, care must be taken to ensure that the higher standard of care is not imposed on conduct occurring before 1 July 2013. They referred to ***Manglicmot*** *v Commonwealth Bank Officers Superannuation Corporation Pty Ltd* [2011] NSWCA 204; (2011) 282 ALR 167 at [120] in which the New South Wales Court of Appeal held that the pre-1 July 2013 statutory formula did not “materially add to… [the] general law duty to exercise reasonable care”.

37 I agree that in the face of the clear words of the SIS Act before and after 1 July 2013 it would be wrong to impose any standard on conduct which occurred before 1 July 2013 other than the ordinary prudent person standard. The higher standard of the prudent superannuation trustee applies only to conduct after 1 July 2013.

38 The respondents submitted that the circumstances of each alleged breach are critical. The question will always be whether what was done satisfied the relevant standard of care, skill and diligence in the particular circumstances. This question is to be answered prospectively and without the benefit of hindsight: *Elder’s Trustee and Executor Co Ltd v Higgins* (1963) 113 CLR 426 at 448. I agree also with this submission. It is the particular circumstances of the conduct which will be determinative. For example, it is not possible to characterise the issue of a “compensation plan” as a non-operational matter divorced from the particular circumstances as they existed at the relevant time.

39 The respondents referred to the fact, which I accept, that a trustee’s duty does not amount to a duty to avoid all loss and that an ordinary prudent person (and for that matter prudent superannuation trustee) can commit errors of judgement without being liable: *In re Chapman* [1896] 2 Ch 763 at 765; *Jacobs’ Law of Trusts in Australia* (8th ed, 2016), at [17]-18].

40 The respondents said, and I accept, that the post-1 July 2013 higher standard of care does not convert a superannuation trustee into a surety of no loss and does not involve strict liability.

41 I accept also that APRA’s submission that “[i]t is no longer the law that directors can rely upon officers without verification” goes too far. As the first respondent submitted there are many circumstances in which a director is entitled to rely on management provided that there are not circumstances from which the director knew or ought reasonably to have known that such reliance was misplaced: *Healey* at [37], [170] and [174]. As the second respondent submitted:

In *Re HIH Insurance; ASIC v Adler* (2002) 41 ACSR 72, Santow J observed at 167 that “at general law, a director is entitled to rely without verification on the judgment, information and advice of management and other officers appropriately so entrusted” unless “the directors know, or by the exercise of ordinary care should have known, any facts that would deny reliance on others.” Similarly, in *ASIC v Healey* (2011) 196 FCR 291, Middleton J noted that “[w]hile directors are required to take reasonable steps to place themselves in a position to guide and monitor the management of the company, they are entitled to rely upon others, at least except where they know, or by the exercise of ordinary care should know, facts that would deny reliance” (at [167]).

Further, in *Morley v ASIC* (2010) 81 ACSR 285, the NSW Court of Appeal recognised at [807] that a “non-executive director may be reliant on management and other officers to a greater extent than an executive director.”

42 I do not accept APRA’s attempt to label “compensation plans” as matters uniquely within the sphere of responsibility of the directors. As the second respondent submitted:

This is a mischaracterisation of *Healey*, which was concerned with the particular responsibility directors have for a company’s financial reports. The relevant extract of the judgment on which APRA seeks to rely states that directors could not substitute reliance upon others:

“…for their own attention and examination of an important matter that falls specifically within the Board’s responsibilities as with the reporting obligations. The Act places upon the Board and each director the specific task of approving the financial statements. Consequently, each member of the Board was charged with the responsibility of attending to and focusing on these accounts and, under these circumstances, could not delegate or ‘abdicate’ responsibility to others.”

That this obligation is a matter that falls specifically within the Board’s responsibilities is expressly provided for in s 295(4) of the Corporations Act.

The compensation plans in these proceedings are not “matters that fall specifically within the Board’s responsibilities as with the reporting obligations.” There is no provision in the SIS Act, analogous to s 295(4) of the Corporations Act, which provides that the compensation plans are specifically the responsibility of the board.

43 It may be accepted that, as APRA said, “IOOF’s Delegated Authority Policy (CB F6/84A,   
p. 1703\_0011) provided that officers only had delegated authority to approve a compensation plan of up to $500,000 without recourse to the Board. Other than the [so-called] Bendigo Failure, all of the compensation plans in issue in these proceedings were for amounts greater than $500,000”. But this does not mean that the directors were disentitled from relying on the information that the management provided to them in respect of the compensation plans. As was submitted for Mr Venardos:

APRA has neither alleged, nor proved, that IOOF’s management was dishonest or incompetent. Nor has APRA alleged or proved that the legal advice given by Mr Riordan and Mr Vine as to the ability of the companies to access the reserves or pursue other sources of compensation was wrong or given in bad faith. Furthermore, as officers and employees of IOOF Service Co, each of Mr Riordan and Mr Vine assisted the trustee companies to give primacy to the interests of beneficiaries. There was nothing to suggest they were not familiar with that responsibility or to suggest to the board that they were acting in dereliction of their duties.

There is also no evidence that Mr Venardos knew facts or ought to have known facts which would deny reliance on management. To the contrary, the evidence is that each of Mr Coulter, Mr Riordan and Mr Vine were skilled and experienced in their respective fields, as were the members of the Rectifications Committee:

(a) Mr Coulter was appointed the Chief Financial Officer of IOOF in 2009. He has over 25 years’ experience having worked at JP Morgan, ANZ, Colonial and PwC.

(b) Mr Riordan is the Group General Counsel. In that role, he is responsible for, among other things, the provision of internal and external legal, risk and compliance services across the IOOF Group. This includes the provision of internal and external legal advice, ensuring that IOOF’s business practices are both legally enforceable and defensible, and ensuring the Board is informed of “significant regulatory contact”. Mr Riordan has more than 25 years’ experience in financial services, trustee services and governance. Prior to joining IOOF in 2009, he was a partner at the law firms Holding Redlich and Cornwall Stodart.

(c) Mr Vine is the Group General Manager of Legal, Risk and Compliance and reports to Mr Riordan. Among other duties, Mr Vine is responsible for the provision of legal advice and for ensuring IOOF and its subsidiaries comply with its obligations. Mr Vine has more than 20 years’ experience and prior to joining the IOOF Group in August 2014, he held in-house legal and governance roles at AXA, Bell Potter and Telstra.

(d) The Rectifications Committee was a management committee formed in the first half of 2015. It comprised key management stakeholders and management experts from the Compliance, Fund Accounting, Operations and Tax teams, with the stated purpose of facilitating the payment of compensation to affected members and investors.

44 The first respondent submitted that “the assessment of what was required of the trustee and the directors to discharge their obligation to act with due care, skill and diligence necessarily must also take account of the scale of the superannuation trusts and the relevantly immaterial amounts at issue, and the other tasks to which IIML, Questor and their directors had to attend in managing the superannuation trusts”. I accept that all relevant circumstances must be taken into account and that the materiality of the amounts involved is one such consideration. As the first respondent submitted:

In the present case, the assessment of what was required of the trustee and the directors to discharge their obligation to act with due care, skill and diligence necessarily must also take account of the scale of the superannuation trusts and the relevantly immaterial amounts at issue, and the other tasks to which IIML, Questor and their directors had to attend in managing the superannuation trusts. APRA does not do this; instead, it invites the Court to review the decisions in a vacuum. That is a legally wrong approach.

For example, as at 30 June 2015, the size of the IPS Super fund was approximately $5.15 billion, and its ORFR reserve was approximately $10.17 million. It was in these circumstances that, on 27 May 2015, the Board of IIML considered the recommendation of management to pay compensation to superannuation members in connection with the Pursuit incident in an amount of $696,436.06, representing 0.00014% of the total fund and less than 7% of the ORFR. While superannuation trustees are doubtless required to exercise due care, skill and diligence in relation to all trust monies, it is uncommercial, unreasonable and unrealistic to suggest that a prudent superannuation trustee or its directors would engage in lengthy and detailed investigation, deliberation and cogitation where the amounts at issue were relevantly immaterial to the proper and sound functioning of the superannuation trust as a whole.

45 This is not to say that the content of the duty of due care, skill and diligence is to be assessed by merely comparing the amounts in issue with the amounts in the fund as a whole. Nevertheless, the size of the fund and the size of the losses, which APRA alleges beneficiaries had to be compensated for, is a critical part of the relevant context. Given that APRA’s case depends on the existence of reasonably arguable causes of action for liability on the part of the trustees and IOOF Service Co, by analogy, the full range of considerations which would inform a case in negligence would be relevant to any evaluation of the existence of the putative causes of action. APRA’s case, however, eschews any such detail, instead relying on the fact of an event and loss, along with the purported admissions, to make good its proof. As will become apparent, this approach is insufficient.

46 For these reasons while I do not accept the first respondent’s submission that I should be slow to conclude that any respondent fell below the relevant standard of care merely because APRA did not call expert evidence to this effect, expert evidence not being essential, there does need to be proof of facts from which a rational conclusion may be drawn that there has been a failure to measure up to the standard of care required. APRA’s case, as will be explained, fails at the hurdle of proof.

###### 3.3 Bests interests of beneficiaries, s 52(2)(c) and s 52A(2)(c)

47 APRA referred to *Manglicmot* at [121] where Giles JA (with whom Young JA and Whealy JA agreed) said:

Nor in my opinion does s 52(2)(c) materially add to breach by the respondent of its general law duty to act in the best interests of members of the Fund. The respondent's general law obligation could be expressed, in the language of s 52(2)(c), as an obligation to perform and exercise its duties and powers in the best interests of the beneficiaries. The words "to ensure" add nothing; an obligation is an obligation. Again, the respondent was exercising a discretionary power, and "to ensure" does not turn the question of exercise of a discretionary power into one of strict liability. There is liability if the discretionary power is exercised improperly, but otherwise there is not.

48 APRA observed that while *Finch v Telstra* did not concern the best interests covenant the High Court “was emphatic that the superannuation context is relevant to the construction of a trustee’s duties and obligations”, saying:

33 Another aspect of the factual context is that the Deed is dealing with the superannuation of employees. For some people, superannuation is their greatest asset apart from their houses; for others it is even more valuable. Different criteria might be thought to apply to the operation of a superannuation fund from those which apply to discretionary decisions made by a trustee holding a power of appointment under a non-superannuation trust. Employer superannuation is part of the remuneration of employees. Membership of the employee superannuation fund may be compulsory. Superannuation, unsurprisingly, is a matter of trade union interest. The question of superannuation entitlements may form the subject of an industrial dispute within the meaning of s 51(xxxv) of the Constitution. Superannuation is not a matter of mere bounty, or potential enjoyment of another's benefaction. It is something for which, in large measure, employees have exchanged value – their work and their contributions. It is "deferred pay". These are propositions which are not falsified by arguments advanced by the Trustee to the effect that the Death and Total and Permanent Invalidity benefits under the Deed involve in part an element of bounty. Superannuation is a method of attracting labour. The legitimate expectations which beneficiaries of superannuation funds have that decisions about benefit will be soundly taken are thus high. So is the general public importance of them being sound.

34 A further factor is the public significance of superannuation. The federal government has attempted to reduce outflows by reducing the dependence of retired persons on the old-age pension funded out of general revenue. The taxation concessions now provided pursuant to Pt 3-30 of the *Income Tax Assessment Act 1997* (Cth) are designed to encourage citizens to make provision for their retirement by investing in superannuation and to encourage their employers to create superannuation funds in their favour. The Parliament also has required employers to contribute a certain percentage of the employee's salary for these purposes. Partly as a result, large amounts of assets are administered by the trustees of superannuation funds.

49 I accept APRA’s submission that this context informs the application of the best interest covenant. APRA said:

…the application of the requirement that the trustee “do the best they can for the benefit of their beneficiaries and not merely avoid harming them”: *Cowan v Scargill* [1985] Ch 270 at 295, referred to with approval by Byrne J in *Invensys Australia* *Superannuation Fund Pty Ltd v Austrac Investments Ltd* [2006] VSC 112; 198 FLR 302 at [107]. The “best interests” are those of present and future beneficiaries, and the trustee is required to hold “the scales impartially between different classes of beneficiaries”: *Cowan v Scargill* at 286-287. As Megarry V-C observed, “When the purpose of the trust is to provide financial benefits for the beneficiaries, as is usually the case, the best interests of the beneficiaries are normally their best financial interests”: at 287. Consequently, applied to a power of investment (which was the subject matter of *Cowan v Scargill*), the power was required to be “exercised so as to yield the best return for the beneficiaries, judged in relation to the risks of the investments in question; and the prospects of the yield of income and capital appreciation both have to be considered in judging the return from the investment”.

By parity of reasoning, the trustee’s best interests obligation when applied to the duty to get in the trust property and to protect and vindicate the rights attaching to it (*CGU Insurance Limited v One.Tel Ltd (in liq)* (2010) 242 CLR 174 at [36]; *Fischer v Nemeske Pty Ltd* (2016) 257 CLR 615 at [11]) requires, in the superannuation context, that the trustee seek to achieve the best outcome for the capital of the fund, judged in relation to the risks of particular action and the prospects that it might provide a partial or complete recovery of funds for the trust.

50 APRA submitted that the trustee’s duty to inform itself properly is also relevant, citing *Commonwealth Bank Officers Superannuation Corporation Pty Ltd v Beck & Anor* [2016] NSWCA 218 at [137] - [140]. At [137] Bathurst CJ said:

137. In *Finch*, the Court left open the application of *Karger v Paul* principles to superannuation funds: at [64]. However, it emphasised that so far as they may apply, the decision may be reviewable for want of properly informed consideration: at [66]. The importance of this matter in the context of superannuation funds was explained by Nettle JA in *Alcoa of Australia Retirement Plan Pty Ltd v Frost* [2012] VSCA 238; 36 VR 618 at [59] in the following terms (Redlich JA and Davies AJA agreeing):

“With respect, I entirely agree with his Honour. As the decision in Finch has enabled us better to understand, trustees of superannuation funds are no longer to be conceived of in the same way as custodians of charitable or family settlements through the exercise of whose absolute discretion settlors have chosen to channel their beneficence. The economic, industrial and ultimately social imperatives which inform the advent of the superannuation industry, not to mention that beneficiaries of the kind with which we are concerned in one way or the other invariably purchase their entitlements, are productive of legitimate expectations which the law will enforce. Superannuation fund trustees are bound to give properly informed consideration to applications for entitlements and, if that necessitates further inquiries, then they must make them.”

51 On this basis APRA submitted that:

In *Finch v Telstra* the High Court stated that that duty “is more intense in superannuation trusts” than in trusts of the type discussed in *Karger v Paul* [1984] VR 161: at [66]. If the consideration is not “properly informed, it is not genuine”: at [66]. Knowingly to exclude relevant information from consideration is a breach; so too is a failure to seek relevant information in order to resolve conflicting bodies of material: at [66]. By parity of reasoning to *Cowan v Scargill*, the trustee’s best interests obligation when applied to the duty of trustees properly to inform themselves requires the trustee properly to inform itself of all relevant information affecting the financial interests of members in the preservation and maximisation of the capital of the trust, and where it is not available, to seek it.

52 In other words, APRA sought to extend the principle applying to decisions about entitlements to any and all matters potentially affecting the capital of the trust. There must be a myriad of decisions taken every day by trustees of large superannuation funds which potentially affect the fund both materially and immaterially. The extension of the principle which APRA proposes appears onerous in the extreme and highly impractical.

53 APRA said this principle answered a submission that there will be no breach of the best interests covenant if the “act or omission can be objectively supported, no matter that the subjective decision-making process of the trustee was defective”. I disagree. A decision which is taken to ensure and is objectively in the best interests of beneficiaries at the time it is made does not lose that character because, at that time, more information could have been obtained.

54 APRA said that it “may be that the contravention of the best interests covenant, and hence   
s 55(1) of the Act, does not also sound in loss sufficient to accrue a statutory cause of action for members and a liability of the trustee to compensate such persons for loss or damage, but that is a different thing from whether it founds a contravention by a superannuation trustee of its statutory obligation in s 55(1) of the Act”. As APRA put it:

There will be a breach of the obligation if the exercise of the power in issue or performance of a duty, or the failure to exercise a power or perform the duty, could not reasonably be regarded as in the best interests of beneficiaries. This is not to suggest that there is, in every case, only one possible course of action that is in members’ “best interests”. APRA agrees with the submission made by the 4-7th R OS [25], there will often be more than one course of action that could be regarded as being in the “best interests of members”, and in some cases, a decision “either way” might be capable of being regarded as “objectively right” (citing *Nestle v National Westminster Bank* [1993] 1 WLR 1260 at 1270. That is why the focus of the inquiry, and how APRA has framed its case, is always on whether the decisions actually made by the trustees, their directors and their responsible officers “could not reasonably be regarded as in the best interests of members”…

55 This much may be accepted. It will frequently be the case that there is more than one course of action which may be regarded as being in the best interests of the beneficiaries. The test is objective and is to be applied prospectively, that is, from the position of the trustee at the time of the decision, without impermissible hindsight.

56 APRA also cited the first instance decision of Rein J in *Manglicmont v Commonwealth Bank Officers Superannuation Corporation Pty Ltd* [2010] NSWSC 363; (2010) 239 FLR 159 at [51] that:

I do not accept that the trustee is made liable for any outcome which turns out to be unbeneficial to members, even if the original decision which led to that outcome was taken with the best interests of all members in mind. Another way of describing this approach is to say that s 52(2) is concerned with process, not outcome.

57 APRA noted the observations of the New South Wales Court of Appeal in *Manglicmont* at [104]-[105] and ***Mercer*** *Superannuation (Australia) Limited v Billinghurst* [2017] FCAFC 201; (2017) 255 FCR 144 at [38] in support of its submission that the distinction between “process” and “outcome” is apt to distract from the core question. As APRA put it:

A course of conduct that later turns out to have been unbeneficial to members’ interests is not a breach of s 52(2)(c) because of how events in fact play out. The converse is also true: a course of conduct that, assessed by reference to the time it was made, involved conduct that was not in the best interests of beneficiaries is not rendered otherwise because of how events in fact play out. Section 52(2)(c) is agnostic in both cases to hindsight developments; it focuses on whether the conduct or course of conduct was or was not capable of being described, at the time it was done or engaged in, as “in the best interests of beneficiaries”.

58 Again, so much may be accepted, but this does not mean that the mere fact further information could have been obtained at the time of the impugned decision necessarily means that the trustee has breached the best interests covenant.

59 APRA also relied on *Mercer* per Flick and Kerr JJ at [62] to support the submission that “this Court has recognised that s 52(2)(c) requires trustees to make enquiries and, even in cases where liability is not clear-cut, to seek to obtain through negotiation an outcome in the best interests of beneficiaries having regard to the possibility that a third party has an exposure to contribute monies to the assets of the fund”. I am unable to draw the same principle from *Mercer*. As far as I am aware, there is no authority that supports this proposition as some form of rigid principle which is to be applied irrespective of the circumstances of the particular case.

60 The fourth to seventh respondents described APRA’s submissions about the best interests covenant as “incoherent” noting that in some respects the submissions were orthodox and in others sought to expand the scope of the covenant, particularly in relation to the concept of the alleged duty of the trustee to properly inform itself. This submissions accords with the views I have expressed above, in particular relating to APRA’s approach to the principles in *Finch v Telstra*.

61 The fourth to seventh respondents also disputed APRA’s approach to the decision-making of a trustee citing ***Cowan v Scargill*** [1985] 1 Ch 270 at 294 that:

If trustees make a decision upon wholly wrong grounds, and yet it appears, from matters which they did not express or refer to, that there are in fact good and sufficient reasons for supporting their decision, then I do not think that they would incur any liability for having decided the matter upon erroneous grounds; for the decision itself was right.

62 As the fourth to seventh respondents put it (my emphasis):

Once it is appreciated that the power or duty in relation to which the “best interests” obligation arises is the obligation to vindicate the rights attaching to trust property, it is clear that the relevant question can only be whether the trustees’ decisions to pursue alternative sources of compensation are **objectively capable** of being supported. APRA’s attempts to convert the inquiry mandated by the “best interests” obligation into one concerned with “process”, rather than “action”, should be rejected.

The observations in the cases to which APRA refers in its submissions at [51]-[52] reinforce, rather than undermine this point. Indeed, the point being made in *Mercer Superannuation (Australia) Ltd v Billinghurst* (2007) 255 FCR 144 at [38] was that flaws in the decision-making process were only relevant to the extent that they produced a flawed decision.

63 Subject to one matter I find the respondents’ submissions in this regard persuasive. I would not, however, exclude from breach of the best interests covenant a case in which it is proved that the trustee’s subjective purpose or object in acting was contrary to the best interests of the beneficiaries.

64 It will also be apparent that the reference in *Cowan v Scargill* is to the existence of circumstances at the time of the decision to which the decision-maker had no apparent regard. The reference does not suggest that a decision which was in breach of the duty by reference to existing circumstances can be transformed into a decision not in breach of the duty by subsequent events. The “good and sufficient reasons” in support of the decision must exist at the time the decision is made. One aspect of APRA’s submission, consistent with the reasoning in *Cowan v Scargill*, is that the best interests of beneficiaries is to be assessed by reference to the circumstances as they exist when the decision is made and not by reference to subsequent unforeseen events. Another aspect of its submission put orally, however, is inconsistent with *Cowan v Scargill*. APRA proposed that the **only** relevant matter was the respondent’s state of mind at the time of the decision. I disagree. In my view, a decision which is not reasonably justifiable as in the best interests of the beneficiaries, assessed objectively by reference to the circumstances as they in fact existed at the time, will be in breach of the covenant. Equally, subject to the exception I have noted, a decision which is reasonably justifiable as in the best interests of the beneficiaries, assessed objectively by reference to the circumstances as they in fact existed at the time, will not be in breach of the covenant.

65 I also accept the further submissions of the fourth to seventh respondents, citing G Thomas, “[t]he duty to trustees to act in the ‘best interests of their beneficiaries’” (2008) 2 *Journal of Equity* 177, that (1) a standard of perfection is not imposed on trustees; (2) in cases where the purpose of the trust is to provide financial benefits for the beneficiaries, “the best interests of the beneficiaries are normally their best financial interests”: *Cowan v Scargill* [1985] 1 Ch 270 at 287, 289: (3) acting in the best interest of the beneficiaries is in effect synonymous with a trustee’s obligation to promote and act consistently with the purpose for which the trust was established; (4) in relation to discretionary powers, there will be “liability” pursuant to s 52(2)(c) “if the discretionary power is exercised improperly, but otherwise there is not”: *Manglicmot* at [121]; (5) the duty applies when the power is exercised; (6) there may be cases where an issue is so finely balanced that “a decision either way can be regarded as objectively right”: *Nestle v National Westminster Bank* [1993] 1 WLR 1260 at 1270; and (7) the relevant question is whether the course of action that was taken was one of the courses of action that may be described as being in the best interests of the beneficiaries.

###### 3.4 No conflicts, s 52(2)(d) and 52A(2)(d)

66 Sections 52(2)(d) and 52A(2)(d) came into force on 1 July 2013, by amendments introduced by the *Superannuation Legislation Amendment (Trustee Obligations and Prudential Standards) Act 2012* (Cth).

67 According to APRA, the terms of the statutory text are clear and unambiguous so that the suffering of loss by beneficiaries is not a necessary ingredient for contravention, and in many cases will be irrelevant. APRA said its case was one in which the respondents did not acknowledge the conflicts that existed and did not give priority to the interest of the beneficiaries over other interests but that APRA did not need to go further and prove that the respondents were actually motivated by a competing interest in their decision-making. APRA also emphasised that the covenants bind each director individually, including the obligation to “comply with prudential standards in relation to conflicts”, relevantly, Superannuation (prudential standard) determination No. 7 of 2012 (Prudential Standard SPS 521) (**SPS 521**) which came into force on 1 July 2013.

68 SPS 521, as APRA submitted, provides that:

(a) a trustee must have a conflicts management framework, approved by the Board, to ensure that the trustee identifies all potential and actual conflicts in its business operations and takes all reasonably practicable actions to ensure that they are avoided or prudently managed (para 8);

(b) the Board is ultimately responsible for the development and maintenance of the conflicts management framework (para 10);

(c) the Board must take all reasonable steps to ensure that all responsible persons and other employees of the trustee clearly understand the need to identify conflicts, the content and purpose of the conflict management framework, and their obligations as a responsible person of a superannuation trustee (para 11);

(d) the trustee must have a conflicts management policy approved by the Board that includes certain minimum requirements including, most relevantly, recording in the minutes of the Board, board committee and other relevant meetings details of each conflict identified and the action taken to avoid or manage the conflict (para 10).

69 APRA acknowledged that at all relevant times Questor and IIML had a Conflicts of Interest Policy in place which required:

(a) all matters affecting the beneficiaries of the relevant trusts to be addressed at subsidiary company board level;

(b) disclosure of conflicts of interest as a standing item on the agenda for meetings of the boards of each company;

(c) the Board to affirm at the conclusion of each RSE Licensee (superannuation trustee) meeting that all directors of the meeting have acted in the capacity as trustee, that all matters have been considered in that capacity, and that priority has been given to the duties to and interests of, beneficiaries in all situations where there is a conflict of interest, as required under sections 52(2)(d) and 52A(2)(d) of the SIS Act;

(d) The priority given to beneficiaries’ interests as part of the decision making must be demonstrated in the minutes in respect of trustee decisions that present a potential conflict.

70 APRA contended that the requirements of this policy had not been met, noting that at the relevant meetings the boards did not make the declaration referred to in paragraph (c) and there is nothing in the minutes to demonstrate the decision-making process referred to in paragraph (d). As to (c), there is no requirement that the affirmation appear in the minutes of the meeting. Accordingly, it would not be inferred from the minutes alone (as APRA assumed) that the affirmation in (c) did not occur. Further, (d) applies only if in the objective circumstances there was in fact a potential conflict. In any event, compliance or otherwise with the policy does not of itself establish any contravention of the no conflicts covenant.

71 The fourth to seventh respondents pointed out that the no conflicts covenant is not equivalent to the general law obligation of a fiduciary not to act when in a position of conflict. This must be accepted as the statute contemplates that the trustee and its directors will continue to act where there is a conflict and in so acting will comply with the covenants. They also cited   
R Sackville, “Duties of Superannuation Trustees: From Equity to Statute” in M S Donald and   
L B Beatty (eds), *The evolving role of trust in superannuation* (2017) at p 320, in support of the proposition, which I accept, that the covenant applies to conflicts which have actually arisen rather than mere possible future conflicts. They also pointed out that SPS 521 in cl 16 states that:

…A relevant duty or a relevant interest is one that might reasonably be considered to have the potential to have a **significant impact** on the capacity of the RSE licensee, the associate of the RSE licensee or the responsible person with the relevant duty or holding the relevant interest, to act in a manner that is consistent with the best interests of beneficiaries.

72 The fourth to seventh respondents also submitted that the fact that by s 52(4) and s 52A(3) the no conflicts covenant expressly overrides any duties owed by the trustee and directors and officers pursuant to Pt 2D.1 of the *Corporations Act* *2001* (Cth) is important. Sections 52(4) and 52A(3) resolve any such conflict by providing that the duty of the trustee and director “override” any conflicting obligations they have under Pt 2D.1 of the *Corporations Act 2001* (Cth), being the general statutory duties and powers of officers and employees of corporations. As the fourth to seventh respondents put it, at law, there is no conflict between these obligations because the potential inconsistency between the various statutory duties has been resolved by the operation of s 52(4) and s 52A(3) of the SIS Act.

73 The first respondent also made a number of salient points about the no conflicts covenant. In particular, the first respondent submitted that:

The first point to be made in relation to the Conflicts Covenant is that it only operates “where there is a conflict between the duties of the trustee to the beneficiaries… and the duties of the trustee to any other person” …(ss 52(2)(d), 52A(2)(d)). In other words, the covenant only has work to do where, as a matter of objective reality, a conflict exists. The covenant does not operate where a conflict is hypothetical or so insubstantial as to be unreal. Thus, before the Court can find that the Conflicts Covenant was engaged, it must be satisfied that a real conflict objectively existed.

74 I agree. This submission is consistent with the statutory text.

75 The first respondent also said:

Next, a point should be made regarding the relationship of the Conflicts Covenant to the Best Interests Covenant. The Conflicts Covenant requires the trustee, in case of conflict, to do four things:

a) to give priority to the duties to and interests of the beneficiaries over the duties to and interests of other persons (ss 52(2)(d)(i)), 52A(2)(d)(i));

b) to ensure that the duties to beneficiaries are met despite the conflict (ss 52(2)(d)(ii)), 52A(2)(d)(ii));

c) to ensure that the interests of beneficiaries are not adversely affected by the conflict (ss 52(2)(d)(iii)), 52A(2)(d)(iii)); and

d) to comply with prudential standards in relation to conflicts (ss 52(2)(d)(iv)), 52A(2)(d)(iv)).

The first three of these requirements overlap in substance with the Best Interests Covenant. A trustee will not have acted in the best interests of beneficiaries if it fails to do any one of these three things. The converse is also true — a trustee who, in fact, acts in the beneficiaries’ best interests will not have failed to meet any of the first three requirements of the Conflicts Covenant.

It is for this reason that APRA’s conflicts of interest case adds nothing as a matter of substance to its Best Interests Covenant case. Despite APRA’s colourful references to “an environment ripe for conflict” (ACS [6], [123]), APRA’s case based on the Conflicts Covenant largely rises and falls on its Best Interests Covenant Case. The only qualification to that proposition is that it is possible, at least, that the Conflicts Covenant might be contravened by reason of a failure to comply with the prudential standards (ss 52(2)(d)(iv)), 52A(2)(d)(iv)), notwithstanding that the best interests of the beneficiaries were met. In such circumstances, however, the transgression would have been so inconsequential that the Court would properly deny even declaratory relief and there would be no rational basis for disqualification orders.

76 I agree with these submissions. This is not to say the no conflicts covenant is otiose. It is to recognise that in the circumstances of this case it adds little to APRA’s arsenal unless APRA’s real concern is a mere failure of documentation (that is, a failure to record the existence of conflicts, assuming any existed). APRA’s oral submissions came close to acknowledging that its real concern was the lack of documentation but, as the first respondent submitted, if that was the scope of the problem, relief would be denied in the exercise of discretion.

77 Further, it may be accepted that ss 52(4) and 52A(3) of the SIS Act provide a legal resolution of any conflict of interest between the obligations of a trustee and a director under the SIS Act and the obligations they have under Pt 2D.1 of the Corporations Act. By law, there is no conflict as the former obligations override the latter. This does not mean, however, that the trustee or director is taken to have complied automatically with the statutory override. The trustee or director who does not give priority to the interests of the beneficiaries over the interest of the other person will not have complied with the covenant whether or not the other person is a corporation to which obligations under Pt 2D.1 are owed. The trustee or director who fails to give such priority because of a Pt 2D.1 obligation will have contravened the covenant. Putting it another way, a conflict that is resolved by the statute because of the statutory override may nevertheless be a conflict the subject of the obligations in ss 52(2)(d) and 52A(2)(d). For this reason I do not accept the proposition advanced by a number of the respondents that there could never be a conflict between the interests of IIML and Questor in their capacities as trustee and the interests of beneficiaries or that any such conflict is necessarily “at best theoretical because the statute addresses that issue”. The statutory override is necessary to avoid an otherwise untenable position of inconsistent statutory obligations but the override does not mean that in fact a trustee or director may never be in a position of actual conflict, still less that the trustee or director may never in fact prefer the interests of the other persons despite the statutory override.

78 In my view, the no conflicts covenant goes further than the best interests covenant. The requirement in s 52(d)(i) and s 52A(d)(i) to give priority to the duties to and interests of the beneficiaries over the duties to and interests of other persons involves both a subjective and objective element. These provisions are concerned with and require that in the   
decision-making process actual (not merely theoretical or potential) conflicts are recognised (including conflicts that are subject to the statutory override) and that priority is given to the interests of beneficiaries over the interests of other persons.

79 This said, it must be recalled that the no conflicts covenant is not about avoiding conflicts of interest. Conflicts of interest are inevitable. It is about managing conflicts of interest. And the conflicts which need to be managed are actual conflicts which have the capacity to significantly impact on the duty to act in the best interests of beneficiaries. Potential or theoretical conflicts of interest are not to the point.

80 APRA’s contentions about conflicts of interest remained at the level of theory. That is, as will become apparent, APRA has not established the necessary factual foundation to support the conclusion that any actual conflict of interest existed. Nor does it grapple with the fact that to be relevant under SP 521 the posited conflict must be capable of having a significant impact on the capacity of the responsible person to act in the best interests of beneficiaries. Nowhere does APRA attempt to confront this standard. Its case on the no conflicts covenant exists at a level of generality and theory which is inapt to make the case it apparently wants to make.

81 I accept also the submissions for the second respondent as follows:

The gravamen of APRA’s complaint in relation to the minutes is that there was no identification of the conflict it asserts existed and no setting out of the process by which the asserted conflict was managed. Each of the relevant minutes includes a declaration that there was no conflict. That would be true if each director was observing the covenant to give primacy to the interests of beneficiaries regardless of whether or not absent that primacy there might otherwise have been thought to be a conflict. Thus, the real complaint is not the failure to properly document the matter, but an alleged failure to come to a conclusion of conflict. That is an invitation to the court to second guess the views on that issue not only of the current respondents but also the absent directors. That minds may or may not differ on this issue is not the test. It is not appropriate for APRA to assert that the honest assessment of the board as to absence of conflict should be disregarded. There is no allegation that the directors dishonestly believed there was no conflict. That should be the end of that issue. That declaration in the minutes is also evidence that no director was preferring the interests of the company over the interests of beneficiaries on any issue raised at a meeting.

##### 4. CORPORATE STRUCTURE

82 APRA described the corporate structure of the IOOF Group as a “conflicted one”.

83 The diagrams in Annexure A show that the IOOF Group resulted from the merger in 2009 of AWM Ltd and IOOF Holdings Ltd, referred to as IOOF Hold Co. The post-merger structure, and relevant directors, officers and employees are shown on p 2 and p 3 of Annexure A.   
Page 4 of Annexure A shows the different capacities in which the various entities in the IOOF Group acted and the locations within the structure where the alleged contraventions arise.

84 It will be apparent from the diagram on p 4 of Annexure A that IIML and Questor were trustees and licensees of registrable superannuation entities (or **RSEs**) including IPS Super and TPS Super. IIML and Questor were also the responsible entities (or **REs**) of managed investment schemes (**MISs**). The funds of the superannuation entities overseen by IIML and Questor were invested in the managed investment schemes of which IIML and Questor, or another entity in the IOOF Group, were the REs. IIML was also the platform administrator of an investment platform known as “Pursuit”.

85 APRA, in addition to describing the structure as “conflicted”, identified it as vertically integrated, thereby allowing for the generation of revenue at all levels. A client could obtain advice from IOOF advisers (generating advice fees), invest in an IOOF superannuation platform (generating platform fees), which in turn invests in IOOF investment products (generating investment management fees) and may be marketed ancillary services such as estate planning (generating trustee service fees). So much may be accepted, but it goes nowhere in the case.

86 APRA submitted and I accept that:

(c) the governance structure for the group involved substantial (sometimes even complete) commonality of directors and officers, and the Boards of IIML and Questor did not have their own Risk and Compliance Committee or hold separate meetings when acting as trustee of a superannuation entity as distinct from when acting as RE of a Managed Investment Scheme or in its own corporate capacity: ASOC [68], [94]-[95], [96]-[97].

87 As APRA said it is apparent from Annexure A and other material that:

(a) The “executive officers” of IIML and Questor (including each of Kelaher, Coulter, Vine and Riordan) were the senior executives of IOOF Hold Co and the IOOF Group including IOOF Service Co: ASOC [68]; admitted by IIML and Questor Defence [68].

(b) Each of Kelaher, Venardos, Riordan, Coulter and Vine were, at all relevant times a “responsible officer” of IIML or Questor in its capacity as the trustee, of IPS Super or TPS Super. Kelaher, Riordan, Coulter and Vine were also officers of IOOF Service Co.

(c) There was substantial overlap of directors between the IOOF Group’s entities in other ways too, including Kelaher and Venardos: ASOC [94]-[95]; IIML and Questor Defence [95].

(d) The Boards of IIML and Questor did not have their own Risk and Compliance Committee: ASOC [96] – [97]; admitted by IIML and Questor Defence [96] - [97].

(e) The Boards of IIML and Questor did not hold separate meetings when acting as trustee of a superannuation entity as distinct from when acting as RE of a Managed Investment Scheme or in its own corporate capacity: ASOC [96] – [97]; admitted by IIML and Questor Defence [96]-[97].

88 APRA stressed that it did not allege that the structure of the IOOF Group itself involved any contraventions of the SIS Act. Rather, its case was that the corporate and governance structures of the IOOF Group meant conflicts of interest would arise and that, in the particular instances alleged, the conflicts of interest which arose were not managed and founded breaches of the statutory obligations. According to APRA, the corporate and governance structures of the IOOF Group gave rise to potential conflicts between:

the interests of beneficiaries and the obligations to beneficiaries of each of IIML and Questor in its capacity as trustee and licensee of the relevant superannuation entity; and (ii) the interests of other entities in the IOOF Group, or of individuals within it, or the obligations of IIML, Questor and their responsible officers to other persons.

89 The fourth to seventh respondents, in contrast, submitted that:

…the “commonality of directors and officers” in the governance structure of the IOOF Group, is a structure that operates such that the duties towards beneficiaries are constantly in effect and binding the same entities and the same officers. Similarly, the shared services, which APRA criticises at paragraphs [108]-[120] of their closing submissions, operate to the same effect (that is, by reason of IOOF Service Co’s contractual obligations, its officers and employees are likewise already obliged to prioritise the best interests of beneficiaries over the interests of IOOF Service Co).

The common and overlapping structure that APRA takes issue with thus in fact has the effect of reinforcing the obligation to prioritise the interests of beneficiaries and sharpen – rather than dilute – its prominence. To put it differently, the very fact that the trustee functions of IIML and Questor are not siloed or isolated, gives prominence to the duties of those entities as trustee.

In this way it can be seen that the law by operation of s 52(4) of the SIS Act, the common corporate structure and the contractual obligations by which IOOF Service Co employees operate in the context of overarching SIS Act responsibilities are each aligned in promoting the paramount duties of IIML and Questor with respect to beneficiaries.

##### 5. THE SERVICES ARRANGEMENTS

90 The IOOF Group operated under a “shared services” model. Before the 2009 merger the AWM group had its own related service provider, Australian Wealth Management Service Co Pty Ltd, which provided its services to the AWM Group, including Questor, pursuant to a Services and Resources Support Deed dated 19 July 2005. After the merger this company was renamed **IOOF Service Co**. This internal service company employed all staff and was responsible for providing many of the services and IT resources to IIML and Questor in their various roles as trustees of superannuation entities and REs of managed investment schemes. It provided these services pursuant to a supplemental deed executed in 2009 which supplemented the services and resources support deed.

91 As APRA pointed out, pursuant to the new service arrangements from 1 July 2009, IOOF Service Co’s contractual obligations to IIML, Questor and the IOOF Group included that it:

(a) “have adequate audit, monitoring and assessment procedures in respect of the Services” (cl 3.3, p. 72);

(b) provide all computer software (or software modifications) “free from defects, errors or impairment, subject to normal wear and tear” (cl 6.1, p. 74);

(c) provide only resources that are “fit for purpose and use or intended use” (cl 6.2, p. 74);

(d) “engage suitably qualified and experienced Personnel to perform the Services and maintain competency and capacity to perform the Services and its obligations” (cl 8.1(a), p 74);

(e) “exercise due care, skill and diligence in the performance of the Services” (cl 8.1(b), p. 75);

(f) “perform the Services under this deed so that the Services, when performed, shall (i) be fit for their stated purpose; (ii) comply with all the requirements of this deed and legislative requirements” (cl 8.1(d), p. 75);

(g) “perform its functions and obligations to the standard that the Recipient would be required to perform, if performing the obligations itself” (cl 8.1(f), p. 75);

(h) indemnify IIML, Questor, their officers and employees as relevant “against all direct loss and damage which [IIML/Questor etc] suffers in connection with” (cl 11, pp. 77-78):

(i) “a breach by [IOOF Service Co] or any of its officers, employees or agents or subcontractors of any obligation imposed under this Deed”;

(ii) “the dishonest, fraudulent, intentional or reckless misconduct of the first party or any of its officers, employees, or agents; or”

(iii) “the negligence act or omission of the first party or any of its officers, employees or agents”.

92 Further, APRA said:

The dispute resolution provisions (cl 17, p. 80) contemplated that litigation would be a last resort. It contemplated that there be (i) written notice first, (ii) then negotiation “in good faith to resolve the dispute for 10 Business days or such longer period as is agreed by the parties”, (iii) failing that, the involvement of the CEOs in negotiations to assist in a resolution, (iv) failing that, referral of the matter to directors for consideration; and (v) if necessary, referral by either party to an “independent and suitably qualified mediator” whose decision was to be “conclusive and binding on the parties, in the absence of manifest error”.

Finally, the Deed required that all parties obtain and maintain professional indemnity insurance “for such amount as a prudent person in the position of Service Company would obtain”: cl 23.1(b).

93 In 2013 these contractual arrangements were replaced by a new services and resources support deed dated 1 April 2013 to which IOOF Service Co, Questor and IIML were parties, containing materially identical arrangements.

94 As APRA submitted:

In 2014, these arrangements were amended by a Deed of Variation dated 30 June 2014 for the purposes of incorporating “certain provisions required by the APRA Prudential Standards SPS 231 – Outsourcing”: CB 5/46, p. 1205. The relevant amendments included: a revised cl 17 (dispute resolution) to materially similar effect: CB 5/46,   
p. 1210; a new cl 27 – which mandated that Service Company perform all of the Services provided to an APRA-regulated institution with the due care, skill and diligence expected of a service provider to such institutions “objectively measured against prevailing industry standards”: CB 5/46, p. 1206; and a replacement Schedule G (“Fees”) with a clause providing greater detail for the allocation of IOOF Service Co’s fees amongst different recipients in the IOOF Group. The new Schedule G expressly acknowledged that “shared service departments” provided by IOOF Service Co included all of “Finance, Company Secretarial, Human Resources, Legal, Risk and Compliance, Information Technology, Operations and Customer Service, and Distribution Management”: CB 5/46, p. 1211-12.

The 2014 variation also included a new Schedule H (“Service Level Agreements”) providing that Service Company would provide:

(a) [relevant to the Pursuit and Sweep failures] “Asset Transaction” services, including “Investment into products”, at a minimum every 2 days: CB 5/46, p. 1219. It also recorded that the expected service levels for the processing of “Bulk Client Routines”, which included “Automatic Investment Process” and “Month End Processing” would be provided by IOOF Service Co: CB 5/46,   
p. 1220-21;

(b) [relevant to the Bendigo failures] “Manual buys” and “Manual sells” which were to take 2 days to load, and 5-10 days to finalise: CB 5/46, p. 1219.

95 APRA submitted, and I accept that:

In substance, virtually all of the service requirements and responsibilities of IIML and Questor were outsourced to IOOF Service Company. That is the overwhelming inference from the terms of the service contracts themselves and the Schedules of Service Levels included in them. Further, it was not just the operational staff that were provided by IOOF Service Co to IIML and Questor. All of their “responsible persons” (other than non-executive directors) were employed by IOOF Service Co: CB 26B.

96 The fourth to seventh respondents provided a more detailed summary of the service arrangements. In their submissions it was noted that:

In relation to Questor, the following deeds and agreements applied during the Relevant Period (being 1 May 2009 to 6 December 2018):

(a) a Services and Resources Support Deed dated 19 July 2005 between IOOF Service Co and various entities in the AWM corporate group, including Questor (2005 Deed);

(b) a Services and Resources Support Deed dated 1 April 2013 between IOOF Service Co and various IOOF Group entities, including IIML and Questor (2013 Agreement), which arguably had the legal effect of discharging the parties of their obligations under the 2005 Deed; and

(c) an IOOF Group Services Agreement dated 5 July 2017 between IOOF Service Co and various entities in the IOOF Group, including Questor but not including IIML (2017 Agreement).

In relation to IIML, the following deeds and agreements applied during the Relevant Period:

(a) a Services Agreement dated 30 November 2007 between IIML and Deregistered Service Co (2007 Deregistered Service Co Agreement);

(b) from 1 July 2009, the 2005 Deed; and

(c) the 2013 Agreement.

Each of the Service Agreements are in a similar form and relevantly include terms to substantially similar effect.

97 The fourth to seventh respondents’ summary of the deeds may also be adopted. Accordingly, the deeds required IOOF Service Co to provide the “Services” and “Resources” to each of the Recipients. IOOF Service Co was required to provide Services to the Recipients “from time to time, and in accordance with the reasonable lawful instructions and direction of the Recipient”. The Services comprised three categories: “Personnel Services”, “Further Services” and “Administration Services”. The Personnel Services were the provision of services of IOOF Service Co’s employees and sub-contractors as required by the recipient to carry on its business, the Further Services were defined as the services listed in Schedule B and comprised the provision of training and education to IOOF Service Co employees and the provision of “additional services in connection” with the training and education services, and the Administration Services were defined as the services listed in Schedule A, which included, for example, IT, asset management, finance, financial planning, legal, marketing and research services. That is to say, the Personnel Services involved the provision of labour.

98 The fourth to seventh respondents also observed that the deeds imposed a range of reciprocal and overlapping obligations upon both IOOF Service Co and the recipients (relevantly including IIML and Questor) in relation to the performance of the services. They thus identified that under cl 3 and cl 8 of the 2005 deed, IOOF Service Co was required, amongst other things:

(a) to adequately supervise its Employees and Contractors, and have adequate audit, monitoring, and assessment procedures in respect of the Services   
(cl 3.3(b)) (defined in the ASOC as the Service Co Procedures Obligation);

(b) to provide premises, equipment and facilities for its Employees and Subcontractors (cl 3.3(a)); and

(c) to the best of its ability, engage and retain suitably qualified and experienced personnel (cl 8.1(c));

(d) to the best of its ability, exercise due care, skill and diligence in the performance of the Services (cl 8.1(b)) (this is the first limb of the “Service Co Standard of Care Obligation” defined in APRA’s Statement of Claim);

(e) to the best of its ability, perform the Services so that the Services, when performed, would be “fit for their stated purpose” and comply with all requirements of the deed and “legislative requirements” (cl 8.1(d) (second limb of the “Service Co Standard of Care Obligation” pleaded by APRA);

(f) to the best of its ability, perform its functions and obligations to the standard that the Recipient would be required to perform, if performing the obligations itself (third limb of the Service Co Standard of Care Obligation pleaded by APRA) (cl 8.1(f)); and

(g) to the best of its ability, ensure its Employees and Subcontractors abide by any policies or procedures of IIML notified to IOOF Service Co (cl 8.1(e)).

99 Clause 9 of the 2005 deed required the recipients of the services from IOOF Service Co to the best of their ability:

(a) to provide IOOF Service Co’s Employees and Subcontractors with proper lawful instructions or directions to act (whether or not they were acting under the Recipient control or supervision) (cl 9.1(a));

(b) to ensure that IOOF Service Co’s Employees and Subcontractors abide by any policies or procedures of IIML (cl 9.1(e));

(c) to ensure that IOOF Service Co’s Employees and Subcontractors complied with all requirements of the agreements and legislative requirements (whether or not they were acting under IIML’s control or supervision) (cl 9.1(d)); and

(d) to exercise due care, skill and diligence towards IOOF Service Co or its Employees and Subcontractors (cl 9.1(c));

(e) to maintain clean and adequate premises (including computers, software and any other ancillary property or services) for IOOF Service Company’s employees and Subcontractors to carry out their duties (cl 9.1(b));

(f) to keep adequate systems, procedures and processes, including recording systems, compliance and monitoring systems or processes, to ensure IOOF Service Co or its Employees or Subcontractors were able to carry out their duties (cl 9.1(g)); and

(g) to promptly as practicable notify IOOF Service Co of any material matter that was likely to cause IOOF Service Co or its Employees or Subcontractors to not be able to carry out their duties and obligations under the agreements (cl 9(h)).

100 Further, cl 8.1(l) of the 2005 deed provided that IOOF Service Co would carry out its duties “in reliance of [sic] the duties of the Recipient under clause 9 of [the 2005 Deed]”.

101 Clause 11 of the 2005 deed provided for mutual indemnities in these terms:

11.1 A party (“first party”) will indemnify the other party, its officers and employees as relevant, against all direct loss and damage which that party suffers in connection with:

(a) a breach by the first party or any of its officers, employees or agents or subcontractor of any obligation imposed under this deed;

(b) the dishonest, fraudulent, intentional or reckless misconduct of the first party or any of its officers, employees or agents; or

(c) the negligent act or omission of the first party or any of its officers, employees or agents.”

11.2 No party is liable to another for indirect or consequential loss.

102 Clause 6.1 provided that:

All of the Resources comprising electronic equipment, computers, computer software (or software modifications) shall be free from defects, errors or impairment, subject to normal wear and tear (defined in APRA’s Statement of Claim as the Service Co Resources Obligation).

103 Because of the definition of Resources this obligation applied only to items of the kind referred to in Schedule F, which were owned by IOOF Service Co.

104 The fourth to seventh respondents referred also to the pleaded Service Co Compliance Obligation which appeared in cl 16.1 in these terms:

The parties acknowledge that several obligations are or will be imposed on the Recipient where it acts as trustee of a superannuation fund under the Superannuation Industry (Supervision) Act 1993, and that the outsourcing by the Recipient under this deed may be an outsourcing agreement to which regulation 4.16 of the Superannuation Industry (Supervision) Regulations 1994 applies. The parties must do all such other acts and things as are necessary to ensure that the Recipient complies with its statutory obligations under this legislation.

105 They also referred to cl 12.2 as follows:

Each party will:

(a) use reasonable endeavours to build and maintain a co-operative working relationship with a view to ensuring that the Services to be performed are provided in an efficient manner; and

(b) provide reasonable assistance to each other as is necessary or is desirable for the other party to perform its obligations under this deed.

106 Based on these provisions, the fourth to seventh respondents submitted that:

A striking feature of the Services Agreement is that, although they are notionally ones under which IOOF Service Co provides the Services to the Recipients, they in fact impose a range of reciprocal and overlapping obligations upon both IOOF Service Co and the Recipients (relevantly including IIML and Questor) in relation to the performance of those Services.

107 They also referred to the mutual indemnities and their scope as follows:

Importantly, the indemnities given by each party under clause 11.1 were limited to “direct loss and damage”. Similarly, clause 11.2 provided that no party would be liable to the other for “indirect or consequential loss”.

There is no settled meaning of the terms ‘indirect’ or ‘consequential’ loss. The trend of recent Australian authority is away from the assumption that consequential loss refers to the second limb of *Hadley v Baxendale* in favour of construing the clause objectively according to what a reasonable and ordinary business person would consider the word meant in light of contract as a whole and its commercial purpose. In *Environmental Systems Pty Ltd v Peerless Holdings Pty Ltd* (2008) 19 VR 358, Nettle JA (at [93] and with whom Ashley and Dodds-Streeton JJA agreed) expressed the view that a reasonable business person would consider a reference to ‘consequential loss’ in a contract to mean everything beyond the normal measure of damages. He recognised the importance, however of construing the contract as a whole and giving due weight to the context in which the clause appears, including the nature and object of the contract. The approach was followed by Bleby J in *Alstom v Yokogawa Australian (No 7)* [2012] SASC 49 (at [269]-[292] in rejecting the English approach and holding that ‘consequential loss’ was a term capable of wide meaning and could extend to all damages suffered as a consequence of a breach of contract, unless qualified by the context. In *Macmahon Mining Services Pty Ltd v Cobar Management Pty Ltd* [2014] NSWSC 731 McDougall J (at [16]-[17]) favoured an approach that looks to the causal relationship between the breach and the damage.

The context of clause 11.2 supports a wide meaning of the phrase “indirect or consequential loss”. The parties are related entities. The obligations are overlapping and interdependent. In those circumstances it is readily understandable why the parties may be taken to have intended that clause 11.2 impose a real and significant restriction on liability.

108 APRA maintained, however, that:

Clauses excluding liability for “indirect or consequential loss” are notoriously difficult to construe: *Macmahon Mining Services v Cobar Management* [2014] NSWSC 731 at [13] per McDougall J. The suggestion, therefore, that Questor could and should have formed the view (without legal advice) that IOOF Service Co clearly had no liability is, even at this level, difficult to accept. In any case, the authorities establish the following principles which indicate that the better view is that the loss in question was not indirect or consequential:

(a) An exclusion clause must be given its natural and ordinary meaning within the context of the contract as a whole: *Darlington Futures Ltd v Delco Australia Pty Ltd* (1986) 161 CLR 500.

(b) The ordinary distinction being made by such a clause is “between ‘normal loss’, which is loss that every plaintiff in a like situation will suffer, and ‘consequential losses’, which are anything beyond the normal measure, such as profits lost or expenses incurred through breach”: *Environmental Systems Pty Ltd v Peerless Holdings Pty Ltd* (2008) 19 VR 358; [2008] VSCA 26 at [87] per Nettle JA.

(c) The statement of principle in Peerless, however, is not to be taken to have created a “rigid new construction principle for limitation clauses” that lost profits or expenses are always indirect or consequential loss: Regional Power Corporation v Pacific Hydro (No 2) (2013) 46 WAR 281; [2013] WASC 356 at [95]-[96].

(d) Rather, having regard to the contract in question, the focus is on the causal relationship between the breach and damage, so that “[d]irect damage is that which flows naturally from the breach without other intervening cause and independently of special circumstances, while indirect damage does not so flow”: *Macmahon* at [16]-[17], citing *Saint Line Ltd v Richardsons, Westgarth & Co Ltd* [1940] 2 KB 99 at 103 per Atkinson J;

(e) For a breach constituting a failure to act in accordance with a contract which required an investment to be made in a particular way, the direct damage flowing from that breach was the difference in the actual value of the investment portfolio and the value that it would have had the contract had been performed in accordance with its terms. In those circumstances, the loss is direct as there is no intermediate step between the breach and the loss, and the loss does not depend on any investment decision by the client: *Patersons Securities Ltd v Financial Ombudsman Service Ltd* [2015] WASC 321; 108 ACSR 48 at [145]-[150].

109 The relevant point for present purposes is that much of APRA’s case is based on the existence of reasonably arguable existence of causes of action for loss against IOOF Service Co. The respondents’ proposition is that confronted by the reciprocity and mutuality of the obligations and indemnities in the deeds regulating the services provided by IOOF Service Co, any such causes of action would have been beset by obvious practical and legal difficulties including the exclusion of liability for consequential and indirect losses. That exclusion would be yet another legal hurdle that would have to be met in the formulation or prosecution of any claim for liability against IOOF Service Co. I accept the respondents’ submissions. The mutual and reciprocal obligations of IOOF Service Co and the trustees means that proving a breach of contract by IOOF Service Co would have been far from straightforward. APRA’s apparent assumptions to the contrary are divorced from the reality of the contractual arrangements.

110 As the fourth to seventh respondents put it (and as I accept given the terms of the deeds):

…the very nature of the Service Engagements, providing as they did for a series of reciprocal and overlapping obligations and contemplating such a high degree of cooperation and shared responsibility for the performance of the Services, would have made it inherently difficult to isolate and attribute liability to IOOF Service Co for any perceived deficiencies in the Services, especially in respect of events occurring up to seven years earlier and where there had been a supervening merger in 2009.

111 The fourth to seventh respondents submitted, and I also accept, that in every case on which APRA relied the following problems would arise:

First, an immediate difficulty which any of the proposed claims would have invariably confronted is the need to establish in each case a proper factual basis as to why the relevant failure:

(a) should be regarded as having been caused by IOOF Service Co’s failure to “adequately supervise Employees and Contractors” rather than a failure on the part of IIML/Questor to provide the Employees and Subcontractors with proper lawful instructions or directions to act;

(b) should be regarded as having been caused by IOOF Service Co’s failure to “have adequate audit, monitoring and assessment procedures in respect of the Services” rather than a failure on the part of IIML/Questor to have “kept adequate systems, procedures and processes”;

(c) should be regarded as having been caused by IOOF Service Co’s failure to “exercise due care, skill and diligence in the performance of the Services” rather than a failure on the part of IIML/Questor to exercise due care, skill and diligence towards IOOF Service Co’s Employees;

(d) should be regarded as having been caused by IOOF Service Co’s failure to the best of its ability to ensure the Services complied with the agreements and legislative requirements rather than a failure on the part of IIML/Questor to the best of its ability to ensure that IOOF Service Co’s Employees complied with the agreements and legislative requirements; and

(e) should be regarded as having been caused by a failure of IOOF Service Co, rather than IIML, to “do all such other acts and things as are necessary” to ensure that IIML/Questor complied with its statutory obligations (assuming there was in fact a breach of IIML’s statutory obligations, which is denied).

In other words, the nature of the contractual obligations is such as to make it inherently difficult to assign responsibility as between the parties to the contract.

Secondly, these difficulties are compounded by questions of attribution. Given the overlapping obligations and the fact that employees acted in multiple capacities for both IOOF Service Co and IIML/Questor difficult questions arise as to whether the relevant act or omission of an employee is to be attributed to IOOF Service Co or IIML/Questor. Without an understanding of the acts or omissions of the individual employees involved and the capacity in which they were acting at any particular time, it is difficult to determine whether:

(a) the employee was providing services to IIML/Questor on behalf of Service Co; or

(b) the employee was providing services on behalf of IIML/Questor (their labour having been provided to IIML/Questor as a Personnel Service under the Service Engagements).

Thirdly, in circumstances where a particular issue can be traced back to before July 2009, difficult questions of attribution and fault as between IOOF Service Co and Deregistered Service Co, and IIML and Questor, would arise.

Fourthly, more specific difficulties would also arise in relation to the “Service Co Standard of Care Obligation” and the “Service Co Procedures Obligation” which APRA alleges have been breached in this case. Each of these were qualified, rather than absolute obligations insofar as they required IOOF Service Co to perform particular acts to a particular standard (that is, “to the best of its ability exercise due care, skill and diligence” in relation to the Standard of Care Obligation and to have “adequate audit, monitoring and assessment procedures” in relation to the Service Co Procedures Obligation) rather than making IOOF Service Co strictly liable for the achievement of a particular outcome. A breach of these obligations could thus only be established by proof of a failure on the part of IOOF Service Co to meet the requisite standard of care. The onus of doing so rests with APRA.

Fifth, even if the above difficulties could be overcome, it would then fall to be determined whether the identified loss was in substance to be characterised as consequential loss under clause 11.2. Important considerations in that regard will be whether the identified loss is to be seen as the result of some other anterior or intervening operative cause or whether the loss to IIML/Questor only arises as a consequence of a loss to particular beneficiaries. Relevant to the latter issue will also be the effect of any ‘loss’ on any initial compensation sourced from reserves.

112 These observations need to be kept in mind when confronted by APRA’s assertions of the existence of reasonably arguable causes of action against IOOF Service Co and the alleged lack of any practical difficulty in making a claim to recover losses from IOOF Service Co.

##### 6. RESERVES

###### 6.1 The ORFR

113 Section 52(8) of the SIS Act provides that:

The covenants referred to in subsection (1) include the following covenants by each trustee of the entity:

(a) to formulate, review regularly and give effect to a risk management strategy that relates to:

(i) the activities, or proposed activities, of the trustee, to the extent that they are relevant to the exercise of the trustee's powers, or the performance of the trustee's duties and functions, as trustee of the entity; and

(ii) the risks that arise in operating the entity;

(b) to maintain and manage in accordance with the prudential standards financial resources (whether capital of the trustee, a reserve of the entity or both) to cover the operational risk that relates to the entity.

114 Section 115 of the SIS Act provides that:

(1) The trustee of a superannuation entity may maintain a reserve of the entity for a particular purpose, unless the governing rules of the entity prohibit the maintenance of a reserve for that purpose

(2) The governing rules of a registrable superannuation entity must not prohibit the maintenance of a reserve to cover the operational risk relating to the entity.

(3) If the governing rules of a registrable superannuation entity are inconsistent with subsection (2):

(a) subsection (2) prevails; and

(b) the governing rules are invalid, to the extent of the inconsistency.

115 APRA submitted that:

The Operational Risk Financial Requirement (**ORFR**) is a statutorily mandated financial resource target that superannuation funds are required to meet to protect beneficiaries from operational risk. It may be held as trustee capital or reserves within the trust fund. At all times, Questor and IIML met their ORFR target by holding reserves within TPS Super and IPS Super, and accordingly the reserves were trust money. The ORFR was only available to address operational risk that occurred within the superannuation entity and not where the risk occurred in a MIS for which Questor or IIML was the responsible entity.

116 According to APRA:

(1) “First, the purpose of the ORFR is not to excuse trustees or their related entities from liability. The requirement to have in place financial resources for the ORFR arises from s 52(8)(b) of the SIS Act. The Explanatory Memorandum that accompanied the introduction of this section into the Act made clear that the operational risks to which the new reserve requirements were directed were the risks arising when there was no insurance or third party liability that could meet the loss such that the only recourse of the trustee was to the assets of the fund pursuant to the trustee's indemnity: EM, Superannuation Legislation Amendment Trustee Obligations and Prudential Standards) Bill 2012, p. 25 [1.99].”

(2) “Second, the requirement to meet the ORFR is governed by the *Superannuation (prudential standard) determination No. 1 of 2012* (*SPS 114 Operational Risk Financial Requirement*) (**SPS 114**): CB Part H, tab 14, pages 397 - 40. SPS 114 relevantly provides that:

(a) an ‘operational risk’ is ‘the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events’ (para 6);

(b) a superannuation trustee must have a strategy, approved by the Board, for meeting the ORFR target amount and the Board is ultimately responsible for ensuring the implementation of the trustee's ORFR strategy (para 18);

(c) the trustee’s ORFR strategy must describe:

(d) the process for determining when and how the financial resources held to meet the ORFR target amount can be called upon (para 19(f)); and

(e) the process for implementing a replenishment plan in accordance with paragraph 20 (replenishment plan) (para 19(g)).”

(3) “In accordance with the requirements of SPS 114, at the relevant times Questor and IIML had an ORFR policy in place: CB 4/33, p. 630. That policy included a section on ‘Payments from the ORFR’. Relevantly for present purposes, it required the trustee to gather minimum information prior to approval of payment from the ORFR including “Sources of compensation available to the Trustee”. This is a recognition by Questor and IIML, at least in their policies, that the ORFR is only to be used in combination with a proper assessment of other sources of compensation, including insurance or third party liability.”

(4) “Third, in determining whether to use the ORFR, the trustee and its directors remain bound by ss 52 and 52A. It is APRA’s case that a decision to use the ORFR is a decision that must be made in the best interests of beneficiaries and that cannot be the case where there are other sources of compensation available, outside of the trust fund, that are not being considered and pursued.”

117 Proposition (1) is not borne out by the Explanatory Memorandum. It may be accepted that IOOF’s ORFR policy contemplated that alternative sources of compensation would be considered before recourse to the ORFR. Proposition (4) is too absolute. Whether or not alternative sources of compensation must be pursued would depend on the trustee’s evaluation of a wide range of factors but most particularly the prospects of success and the exposure to legal costs.

118 The fourth to seventh respondents noted that the governing rules of IIML and Questor provide for reserves. As they put it:

The TPS Trust Deed provides that:

(a) the Trustee must maintain a Reserve Account for each Employer sub-plan, and record various proceeds, contributions and amounts in that reserve account as specified (clause 10.10);

(b) the Trustee must apply amounts held in the Reserve Accounts for one or more of a number of specified purposes which include meeting losses or expenses, and any other purpose which the trustee determines (clause 10.11).

The IPS Trust Deed simply provides that the Trustee shall keep a Reserve Account showing various amounts credited to that account.

The IOOF Group also had a ‘Reserves Policy’, which made provision in relation to the maintenance and operation of various different reserves.

The Australian Master Superannuation Guide notes that:

“The terms “reserves” is not defined in the SIS legislation….A reserve is commonly understood to be an account held within a superannuation fund that holds amounts that have not been allocated to a particular member.”

That Guide goes on to note that “Reserves in large APRA funds are, for example, intended to spread potential costs across different generations of members”. This is consistent with APRA’s SPG 222 (Management of Reserves), which states that reserves are typically regarded as monies forming part of the net assets of the RSE; are set aside for a clearly stated purpose; are largely concerned with contingent events; and are monies that have not been allocated to members. In the SPG, APRA notes some reserves are intended to spread potential costs arising from contingent events across different “generations” of members.

119 The respondents argued that against this background the notion that the reserves comprised “members’ money” was apt to mislead if used as an analytical tool. The interest of members in the funds is not the same as their interest in their individual accounts, a proposition which may be accepted. Members’ interest in the funds is as part of the reserve, a proposition which may also be accepted. The fourth to seventh respondents also submitted, and I accept, that:

Whether the reserves are permitted to be used otherwise than as a last resort is a question to be answered by reference to a careful and precise analysis of the relevant legislative, regulatory and policy documents, considered in the context of a particular set of circumstances...

120 The fourth to seventh respondents submitted that:

(a) From 1 July 2013, the SIS Act has required an RSE licensee to maintain an operational risk reserve. In particular, s 52(8)(b) deems there to be a covenant contained within a fund's governing rules requiring the trustee *“to maintain and manage in accordance with the prudential standards financial resources (whether capital of the trustee, a reserve of the entity or both) to cover the operational risk that relates to the entity”*.

(b) APRA Prudential Standard SPS 114, “*Operational Risk Financial Requirement*” (SPS 114) was introduced at the same time, along with APRA Prudential Practice Guide, SPG 114, ‘Operational Risk Financial Requirement’ (SPG 114). Those publications provide further detail and guidance as to the requirements of s 52(8)(b).

(c) SPS 114 includes the following:

(i) An “operational risk” is defined as *“the risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events”* (SPS 114 at [6]).

(ii) An “operational risk event” is defined to mean an “operational risk that has (a) materialized and (b) caused one or more beneficiaries in an RSE to sustain a loss, or to be deprived of a gain to which they otherwise would have been entitled” (SPS 114 at [7]).

(iii) An RSE licensee must “determine a target amount of financial resources to address the operational risks of the RSE licensee's business operation” (SPS 114 at [8]).

(iv) An RSE licensee must also “determine a tolerance limit below the ORFR target amount that reflects the level below which the RSE licensee must take action to replenish financial resources held to meet the ORFR target amount” (SPS 114 at [10]).

(v) The financial resources held to meet the ORFR target amount must be held either as an operational risk reserve held within an RSE, as operational risk trustee capital held by the RSE licensee, or a combination of both (SPS 114 at [14]).

(vi) An RSE licensee must “build the financial resources to meet the ORFR target amount within three years of the effective date [1 July 2013] in a manner that ensures that the RSE licensee acts fairly in dealing with beneficiaries” (SPS 114 at [28]).

(vii) An RSE licensee must have a strategy in relation to the ORFR which must include, inter alia, “the process for determining when and how the financial resources held to meet the ORFR target amount can be called upon” and “the process for implementing a replenishment plan” (SPS 114 at [18], [19](f) and (g)).

(viii) An RSE licensee may only use funds held to meet the ORFR for specified purposes, including “to make a payment to address an operational risk event” (SPS 114 at [17]).

(ix) If the level of financial resources held to meet the ORFR target amount falls below a certain amount, the “RSE licensee must implement a replenishment plan” which “must seek to replenish the level of financial resources held to meet the ORFR target amount within a reasonable period in a manner that ensures that the RSE licensee acts fairly in dealing with beneficiaries” (SPS 114 at [20]).

(d) SPG 114 includes the following:

(i) APRA “does not endorse any particular approach for determining the ORFR target amount”, save that it expects that the target amount will be “at least 0.25 per cent of funds under management” (SPG 114 at [7], [9]).

(ii) The purpose of the “tolerance limit” is to “enable an RSE licensee to manage immaterial fluctuations below the ORFR target amount without the need for a replenishment plan”, and “APRA envisages that immaterial fluctuations may arise from a small payment or payments out of the financial resources held to meet the ORFR target amount” (SPG 114 at [13], [14]).

(iii) APRA recognises that an “RSE licensee may enter into arrangements that could provide it with a compensation payment to address the cost of an operational risk event” and that “compensation arrangements may play an important role in replenishing the financial resources held to meet the ORFR target amount after it has been used” (SPG 114 at [15], [16]).

(iv) APRA considered that “there is likely to be a level of uncertainty as to the timing, coverage and availability of compensation payments” and thus they “do not influence the ORFR target amount but can reduce the prospect that members bear the cost of replenishing the financial resources held to meet the ORFR target amount” (SPG 114 at [16]).

(v) An RSE licensee “may only make a transfer out of an operational risk reserve in accordance with the provisions on the use of the financial resources held to meet the ORFR target amount in SPS 114” (SPG 114 at [34]).

(vi) An RSE licensee “may call upon the financial resources held to meet the ORFR target amount to address an operational risk event. This definition is based on losses sustained by, or gains deprived from, beneficiaries and not costs to correct the cause of the event” (SPG 114 at [40]).

(vii) APRA envisages that “a payment to address an operational risk event may include a transaction or other process-related cost(s) when an RSE licensee is able to justify that the cost has only materialized as a result of the operational risk event and payment of the cost in a timely manner is essential to ensure that the loss is properly addressed and members do not incur large one off expenses” (SPG 114 at [42]).”

(e) IOOF’s Reserves Policy (Reserves Policy), which constitutes the “ORFR strategy” referred to in SPS 114 at [18], includes the following provisions which are of particular relevance for present purposes:

(i) The ORFR target amount was 0.25% of funds under management (p 465).

(ii) The lower “tolerance limit” was 80% of the ORFR target amount (p 466).

(iii) The ORFR funds were determined to be held as a reserve within the fund, rather than as trustee capital (p 466).

(iv) It was provided that the *“financial resources within the ORFR can only be accessed to rectify a loss arising from an operational risk event”* (p 467).

(v) It was provided that *“if accessing the ORFR will result in a breach in the tolerance limit set, the Trustee will investigate the circumstances leading to the operational loss, the impact on the financial resources within the ORFR, any right to receive compensation from third party service providers or recover losses from the insurer and the strategy to replenish the financial resources within the ORFR in order to meet the Target Amount as per the replenishment plan”* (p 467).

(f) Under the heading “Payments from the ORFR” it said (p 468):

*The ORFR is to be used to fund losses resulting from operational risk events, accordingly these losses translate to paying current members or former members for losses incurred and/or restoring current members back to the position they would have been in had the operational risks had not occurred.*

Minimum information to be gathered prior to approval of payment from the ORFR is as follows:

* Amount of loss suffered, impact on the Fund as a whole;
* Number of members affected;
* Impact of individual members;
* Confirmation that loss was caused by an operational risk event; and
* Sources of compensation available to the Trustee.

121 As a result the fourth to seventh respondents said that the purpose of the ORFR was to “require financial resources to be held from which any losses suffered by beneficiaries could be compensated (Explanatory Memorandum at [1.112]-[1.115])”. They contended that these parts of the Explanatory Memorandum are concerned with the potential incongruity of a trustee indemnifying itself from the assets of the trust for loss caused by an operational risk which would defeat the purpose of the ORFR which was designed to protect current members from bearing the full brunt of the operational risk loss. This is a different object from compensating members. The object is to ensure that operational risk losses are not borne solely by the current members. I should record that I do not see this as supporting the proposition that the legislative response was to provide for the ORFR rather than to remove the trustee’s capacity to indemnify itself for breach of the s 52 and s 52A covenants. The Explanatory Memorandum is not dealing with s 52 or s 52A in these paragraphs.

122 This said, I agree that APRA’s submission that “the operational risks to which the new reserve requirements were directed were the risks arising when there was no insurance or third party liability that could meet the loss such that the only recourse of the trustee was to the assets of the fund pursuant to the trustee’s indemnity” goes too far. SPS 114 does not impose any such requirement. The closest express provision to that requirement is IOOF’s Reserves Policy requiring that the minimum information to be gathered before any payment from the reserves included sources of compensation available to the trustee. Otherwise SPS 114 contemplates that the ORFR is available for all operational risk events and not just those where there was no insurance or third party liability. This concept of the ORFR being a last resort only is a construct of APRA’s. It is based on a number of factors including the s 52 and s 52A covenants, as well as the IOOF Group’s internal risk management strategy for the purposes of s 52(8)(a) of the SIS Act which identified that two important controls they had in place to prevent or minimise this risk were professional indemnity insurance and arrangements with IOOF Service Co. Accordingly, as APRA put it:

IIML’s “Risk Management Strategy” (July 2013) (CB 3/23E) provided:

(a) “IIML is able to enforce its rights under the [Group Resources Deed] to a supply of resources if required by APRA”: IIML “Risk Management Strategy” (July 2013):

(b) The “controls” in place to address “operational risk” and “insurance risk” included ensuring the trustees had adequate insurance coverage and outsourced service providers were regularly monitored (p. 403\_0065-67).

123 APRA’s case, as a result, was that the ORFR “should only be used where the superannuation entity’s primary controls had failed to avoid the impact of the operational risk on beneficiaries, that is, where the trustee could not compensate the beneficiaries from moneys other than reserve moneys by making a claim on its insurance policy or enforcing its contractual rights against service providers”. APRA said:

APRA accepts that s 56(2A) requires the ORFR to be exhausted before the trustee can rely upon its right of indemnity as against any other part of the trust property. This does not, however, convert the ORFR into a fund that can be used to immunise the trustee from liability where it had no right to call on the indemnity (e.g. where insurance would have responded or the liability arose under s 55 of the SIS Act). Nor is the ORFR available or to shield related parties from liability to the trust.

This analysis is not affected by the fact that the ORFR may be held as trustee capital rather than as a reserve. Where the ORFR is held as trustee capital, it is still a financial resource that is statutorily required to be held for a particular purpose for beneficiaries’ benefit. The use of this resource without exhausting other means of risk management is not in beneficiaries’ best interests either.

124 These statements are not supported by anything in the statutory scheme and go too far. It is not the case that the use of the ORFR without “exhausting other means of risk management” is necessarily not in the best interest of beneficiaries. This proposition appears to be central to APRA’s case yet it is not founded in the statutory scheme or any principle of trust law which APRA has identified. It is a manifestation of APRA’s construct that there is a duty rather than a discretion to make claims against potentially liable entities for loss. I do not accept the construct as a matter of principle. To the contrary, I accept the submissions of the respondents including, in particular, that of the first respondent that APRA’s approach to the ORFR is misconceived.

125 The first respondent submitted that:

The requirement that trustees maintain financial assets to cover “operational risk” is found in s 52(8)(b) of the SIS Act. This Operational Risk Financial Requirement (ORFR) was introduced by the 2012 Amendments with effect from 1 July 2013.

The phrase “operational risk” is not defined in the SIS Act, but its meaning is explained in the Explanatory Memorandum to the 2012 Amendments (2012 EM):

Operational risk is the risk that a superannuation fund may suffer loss due to inadequate or failed internal processes, people and systems or from external events. It does not include the investment or market risk that superannuation fund investments are subject to. Examples of operational risk include: miscalculation of member benefits such as unit pricing errors; inadequate trustee insurance; damage to member records; computer or software failure; fraud, negligence or misconduct; and loss of key staff.

This definition of ‘operational risk’ includes, in terms, risks arising from the “inadequate or failed internal processes, people and systems” of the trustee.

Section 52(8) is (and was at all times) relevantly in the following terms:

(8) The covenants referred to in subsection (1) include the following covenants by each trustee of the entity:

(a) …

(b) to maintain and manage in accordance with the prudential standards financial resources (whether capital of the trustee, a reserve of the entity or both) to cover the operational risk that relates to the entity.

Section 52(8)(b) makes specific reference to the circumstance that the ORFR is to be maintained and managed “in accordance with the prudential standards”. The relevant prudential standard in that regard is Prudential Standard SPS 114: Operational Risk Financial Requirement (**ORFR Standard**).

The ORFR Standard imposes certain requirements on RSE licensees with respect to the ORFR:

a) First, it echoes the language of s 58(2)(b) of the SIS Act by providing that the ORFR must be held as either an operational risk reserve held within an RSE, as capital held by the RSE licensee, or a combination of both;

b) Secondly, it provides that the ORFR must “be separately identifiable from member accounts and reserves held in the RSE for other purposes”;

c) Thirdly, it requires RSE licensees to have set an ORFR target amount and adopt a strategy for meeting that amount;

d) Fourthly, the ORFR Standard required that the ORFR target amount had to be met within three years of 1 July 2013;

e) Fifthly, the ORFR Standard requires that an RSE licensee determine a tolerance limit, below which the trustee must take action to replenish the financial resources held to meet the ORFR target amount; and

f) Sixthly, it provides that amounts held for purposes of satisfying the ORFR can only be used “to make a payment to address an operational risk” event and for certain other purposes ancillary to satisfying the ORFR, the consequence being that the ORFR fund could not simply be handed over to members or used for purposes unconnected with operational risks.

126 Based on these matters the first respondent submitted that:

Nothing in either the SIS Act or the ORFR Standard prevents the ORFR fund from being used to compensate members for losses incurred by reason of operational risks caused by the actions of the trustee, its directors or related bodies corporate of the trustees. Nor is there any provision of the SIS Act or the ORFR Standard that requires that, where an operational risk event occurs as a result of the actions of a trustee, its directors or its related bodies corporate, the trustee is obliged to replenish the ORFR fund from its own monies. The ORFR Standard provides that the ORFR fund must be replenished when it falls below the specified tolerance limit for the ORFR fund as specified by the trustee, but does not otherwise control the manner or timing of such replenishment. APRA does not allege that any of the uses made of the ORFR at issue in these proceedings would have reduced, or in fact reduced, the ORFR funds of either IPS Super or TPS Super below the specified tolerance limits for those funds such that replenishment was required.

Indeed, the entire purpose of the ORFR is to compensate members for operational risk events, including those arising from the actions of the trustee. So much is clear from the 2012 EM [1.104]:

These changes will provide current RSE members with enhanced protection from losses due to operational risk. They will reduce the chances of a particular cohort of members, who happen to be members of the RSE when an operational risk related loss is identified, bearing an unfair proportion of the loss. This is because the reserve or capital used to meet the loss will have built up over time.

The entire rationale for the ORFR is to ensure that there is a fund available to pay compensation to members who suffer operational risk related loss, including in circumstances where that loss is the result of the actions of the trustee. The fund was not to protect members from having ultimately to pay the costs associated with an operational risk related loss, but rather to spread the burden of that loss so that it was borne by all members over time, rather than at the time the loss crystallised. As the passage quoted above makes clear, the Legislature envisaged that members would ultimately meet the costs of the operational risk related loss in any event, but saw benefit in spreading that loss over time so that it was borne by a wider membership pool.

Contrary to the foregoing submissions, APRA submits that the 2012 EM (ACS [89]):

made clear that the operational risks to which the new reserve requirements were directed were the risks arising when there was no insurance or third party liability that could meet the loss such that the only recourse of the trustee was to the assets of the fund pursuant to the trustee’s indemnity.

The only citation given for the proposition is paragraph 1.99 of the 2012 EM which is quoted in its entirety in paragraph 44 above. That paragraph does not stand for the proposition for which APRA cites it. APRA’s submission should be rejected.

In this context, it is misconceived and a complete mischaracterisation to describe the ORFR as “members’ money” (as was said in opening) (T9.13; T59.28; T88.33). It is money in a dedicated fund, held in accordance with the provisions of the SIS Act, for the express purpose of paying compensation to members for losses arising from operational risk, including risks arising from the trustee’s conduct. Using that fund to compensate members in such circumstances does not involve compensating members with their own money in any relevant sense; rather, it is to use the fund for the very purpose for which it was created.

There is no obligation on a trustee to itself replenish the ORFR fund to account for funds used to compensate members for losses arising from operational risks arising from the trustee’s conduct. Again, there is no provision in the SIS Act or the ORFR Standard to that effect, and there is nothing in the 2012 EM to suggest that that was intended. To the contrary, the 2012 EM contemplates that the cost of the ORFR is to be met by members, albeit that that cost would be spread across members over time.

This construction of the ORFR is confirmed when one has regard to the terms of s 52(8)(b). That provides that the ORFR can be satisfied from the “capital of the trustee, a reserve of the entity or both”. Where a trustee elects to establish the ORFR as capital on its own balance sheet, there could be no suggestion that the trustee was acting in breach of trust by paying some of that fund as compensation to members for an operational risk associated loss arising from the trustee’s own actions. Similarly, provided that such compensation did not reduce the ORFR below the relevant tolerance level, such a trustee would have no obligation to replenish the ORFR under the SIS Act or the ORFR Standard.

If the trustee elected to establish the ORFR using both capital on its own balance sheet and a reserve in the trust, the position would be the same. If members suffered an operational risk related loss, the trustee would be free to compensate such loss from either the ORFR capital on its balance sheet or the ORFR reserve in the trust. It would be absurd to suggest that the former was the trustee’s money but the latter was “members’ money”; they are simply alternative ways of establishing the fund required by the SIS Act. Similarly, it could not sensibly be suggested that, if the operational risk related loss stemmed from the trustee’s own actions, the trustee would be acting in breach of its obligations under s 52 of the SIS Act if it used the ORFR reserve in the trust because that was “members’ money”, but that it could validly use the ORFR capital on its own balance sheet in such circumstances.

These examples demonstrate that where and how the ORFR fund is held does not affect the trustee’s rights, powers and obligations relating to how that fund is used. Other consequences may flow, such as how the ORFR is dealt with on a winding up of the superannuation entity or a change of trustee, but the ORFR can be used in the same manner and for the same purposes, regardless of whether it is held as capital of the trustee, a reserve of the trust or both.

To describe an ORFR reserve in a superannuation trust as “members’ money” is a lawyer’s artifice. Other than on a winding up, an ORFR fund held as a reserve in a trust is no more “members’ money” than is an ORFR fund held on the trustee’s balance sheet.

127 These submissions are persuasive and undermine APRA’s case about the use of the ORFR. APRA has sought to put a gloss on the use which may be made of the ORFR to the effect that it is available to reimburse members for losses but only when consideration of all other potential avenues for redress have been exhausted. Further, in oral submissions APRA said that any use of the ORFR or the general reserve to reimburse members could not be considered to be “compensation” of the members for loss because they were being given their own money. For the reasons set out above that construct is artificial. The propriety of the use of the ORFR (and any reserve) is to be determined by the statutory scheme and the instruments and policies which regulate the use of the reserve. APRA’s construct is not founded on anything in those documents and must be rejected. This undermines a large swathe of APRA’s case, founded as it is on the impropriety of the respondents’ conduct in proposing the use of or using the ORFR to reimburse members for certain losses.

###### 6.2 The general reserve

128 Section 115 of the SIS Act facilitates but does not mandate the existence of other reserves.

129 IOOF’s Reserves Policy provides that the general reserve exists to hold capital to pay future administration and operational expenses under the 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 trust deeds. The general reserve is made up of such funds as contributions to the fund which, at year-end, are yet to be allocated to members (and therefore do not yet form part of members’ benefits), unallocated bank or ATO interest, frozen investments from redemption of members through financial hardship claims, and interest earned on the General Reserve's assets each month.

130 The fourth to seventh respondents said that the General Reserves Policy had been amended a number of times since 2013, and in May 2016 it was amended to make “express reference to ‘the payment of compensation’ as one of the permitted applications of the reserve. However, given the breadth of the Trusts Deeds and the working of the previous policy, this was always a permitted use of the reserve but was made express by the amendment”.

131 While it was common ground that the money in reserves formed part of the trust so that the members had a beneficial interest in the reserves, there was again a dispute as to whether the reserves should be characterised as members’ money or not. APRA noted that the respondents’ approach, that the reserves could not be characterised as members’ money, was inconsistent with the fact that the money formed part of the assets of the trust. APRA said further:

(1) The ORFR Policy explicitly provided for the distribution to beneficiaries of any excess financial resources held in the ORFR Reserve: CB F3/25, p. 467.

(2) The reference in the Reserves Policy to the general reserve “generally” not being distributed was subject to the explicit caveat that the trustee may decide to distribute part of the general reserve where “it considers its fiduciary and equitable obligations require it to do so”: CB F3/25, p. 455. This would include where the amounts held in the reserve were excess to requirements.

(3) In February 2018, Mr Coulter endorsed a paper that went to the IIML Board which considered whether to distribute any excess amounts held in the IPS General Reserve to beneficiaries: CB F15/386, p. 5559. The papers records that the Audit Committee had raised a query as to whether the reserve “was at a sufficiently high level, such that an amount considered excess to the requirements of the fund should be distributed to members”.

(4) The reserves are therefore “members’ money” in the sense that (1) they are money that is subject to the trust, in which beneficiaries’ have a beneficial interest; and (2) in relation to which beneficiaries have a very real prospect of sharing. The unnecessary depletion of those reserves is therefore to the beneficiaries’ detriment.

132 However, none of this means that the reserves cannot be used for purposes for which they were established and are maintained including the compensation of members. It is also not to say that the respondents are wrong to point out, as the first respondent did, three things about the general reserve.

a) First, those reserves do not comprise or include amounts in individual members’ superannuation accounts, but are rather made up of felicitous amounts flowing incidentally as a result of accounting, tax and timing matters;

b) Secondly, the Reserves Policy contemplates the widest possible range of uses for funds in the general reserve (“for any purpose that the Trustee deems appropriate and within the parameters disclosed by the Funds’ Trust Deeds”); and

c) Thirdly, members can have no expectation to any amounts in the general reserve (save on a winding up), as the policy makes clear that the general reserve will not generally be allocated to members.

133 I also accept the first respondent’s submission that the legal analysis is not assisted by characterising the reserves as “members’ money”. As the first respondent put it:

The correct question is whether, having regard to the trustee’s broad powers with respect to the general reserve and the unlikelihood of members’ ever sharing in that fund, the use of that fund to compensate members in relation to the CMT episode was consistent with the trustee’s obligations under the trust deeds and the SIS Act.

##### 7. ADDITIONAL PRELIMINARY MATTERS

###### 7.1 The use of IOOF documents as admissions

134 As noted APRA’s principal evidence comprised IOOF documents brought into existence for the purpose of internal investigations and self-reporting. APRA said that it relied on these documents as admissions. It did so, however, without identifying the specific parts of the documents said to constitute admissions and failed to distinguish between their use as against the corporate and individual respondents. In short, the documents cannot constitute any form of admission by the first and second respondents.

135 The fourth to seventh respondents addressed this use of the IOOF documents in detail. They submitted as follows:

To the extent that a document records a fact, then describing the document as an “admission” does not give it any different or greater status than it already has by virtue of being a business record. Indeed, APRA’s desire to characterise these documents as “admissions” indicates the need for especial caution in identifying the relevant “fact” said to be contained within it. Frequently, it is apparent that APRA seeks to rely not on the record of a “fact”, but on the expression of an opinion, being a conclusion which depends on the application of a legal standard, or other evaluative judgment.

To the extent that it is a factual opinion upon which APRA relies, then before the Court could treat it as evidence of the truth of the opinion, an exception to the opinion rule would need to be made out: *Lithgow City Council v Jackson* (2011) 244 CLR 352. APRA has not proved that the authors of any of the documents upon which it relies have the expertise to render their opinions admissible as expert opinions, and nor has it demonstrated that the requirements of s 78 of the *Evidence Act 1995* (Cth) have been met.

A further point should be noted concerning so-called “admissions” of fact (or factual opinions). As is explained below, whether there has been a breach of a covenant is an inquiry that is prospective in nature. That is to say, it must proceed without the benefit of hindsight, and solely on the basis of the knowledge that existed at the time. All of the documents that APRA relies on as “admissions”, were created after the events in question, during or following an investigation into circumstances that were not previously known. In those circumstances, the probative weight of the documents relied upon by APRA is virtually nil.

To the extent that the documents contain an opinion involving the application of a legal standard to particular facts, or a bare opinion concerning the law, APRA appears to accept that the documents it relies upon are not probative of whether or not there was a contravention of any covenant or other legal standard. So much, in any event, was made clear in the decision of Gummow J in *Dovuro Pty Ltd v Wilkins* (2003) 215 CLR 317 at [69]-[70].

…

Finally, to the extent that the documents are relevant, the weight to be given to the matters recorded in them needs to be assessed in light of the role and qualifications of the person creating them, as well as the regulatory context in which the respondents were operating. That is to say, the fact that there was an institutional willingness to investigate and notify regulators of issues, through the structure of breach reporting, would ordinarily be regarded as reflecting well on a regulated entity. The fact that APRA now seeks to deploy those communications against an entity it regulates may well prompt a more careful analysis of whether an “incident” should be characterised as a “breach” requiring reporting in the future. But, for present purposes, in assessing the weight to be given to these reports, the context in which, the purpose for which, and the spirit in which they were given, needs to be taken into account.

136 I agree with these submissions. To the extent that APRA relied on statements involving a conclusion of law (such as to the effect that one or more of the respondents had breached one or more of the statutory covenants) I do not consider these statements to constitute admissions. But even if they did constitute admissions I would not give them weight in the overall analysis because the issue is one which I must determine based on the evidence and consistent with principle. What will also become apparent is that the documents which form the core of APRA’s evidentiary case are not only the product of hindsight analysis but also are expressed at an unhelpfully high level of abstraction. They appear to assume the knowledge of what must be detailed and intricate systems for management and thus provide no information about those systems when assessing, with hindsight, the cause of a particular incident. As such, I consider the documents incapable of taking the weight which APRA seeks to place on them, in effect, as proof of its case.

###### 7.2 The use of APRA opinions

137 The fourth to seventh respondents submitted that:

APRA also appears to rely heavily on its own expressions of opinion: either by reason of it communicating its views directly to the respondents, or to the world at large by means of policy publications.

Once more, the fact that such opinions were expressed is irrelevant. If APRA correctly described the law, or the required course of action in particular circumstances, then it must prove that in these proceedings by means other than its own prior statements. Unless there is an obligation backed by legislation to comply with a command or recommendation of APRA, or to consider its opinions, then the fact that APRA has spoken does not shed any light at all on the issues to be determined in these proceedings.

Equally, on the case pleaded by APRA, the fact that a particular person was aware of APRA’s opinion is not relevant to the existence of any of the asserted contraventions.

Overall, in the fourth to seventh respondents’ submission, the very heavy reliance by APRA on asserted “admissions” by the respondents, and its own “opinions”, merely serves to demonstrate the fundamental weakness of APRA’s case.

138 I agree with these submissions including, as will become apparent, that APRA’s reliance on these matters is indicative of the weakness of its case. APRA has not realistically confronted the need for reliable evidence of the particular factual circumstances said to give rise to the breaches of the statutory covenants. For example, it has eschewed proof of the existing systems and procedures and instead appears to rely on the bare facts of error and asserted loss as evidence which necessarily bespeaks contraventions of the due care covenant. I do not consider it open to proceed in this way. APRA treats the trustee as an effective insurer against all loss when this is not the law. It gives no attention to the kind of evaluative and nuanced analysis that would be required to decide whether any particular conduct failed to measure up to the requisite standard of care. There is an evidentiary vacuum when it comes to the existing systems and procedures making it impossible to perform the kind of analysis that would be required for APRA to make good its claims.

139 APRA’s approach to proof of its contentions is of particular significance given that I also accept the submissions for Mr Venardos that these proceedings are for a penalty in the form of a banning order so that the relevant standard to be applied is the ***Briginshaw*** standard (*Briginshaw v Briginshaw* [1938] HCA 34; (1938) 60 CLR 336), embodied in s 140 of the *Evidence Act 1995* (Cth). As Mr Venardos’ submissions put it:

Insofar as APRA’s case *“rests on inferences from primary facts”*, satisfaction as to a “reasonable and definite inference” is required; *“it is not enough for the circumstances to give rise to conflicting inferences of equal degrees of probability.”* [*ASIC v Healey* (2011) 196 FCR 291 at [103] per Middleton J citing the principle expounded by the High Court in *Bradshaw v McEwans Pty Ltd* (1951) 217 ALR 1 at [5]].

140 The fact that none of the respondents gave evidence in these circumstances is immaterial. It was for APRA to prove the primary facts on which its allegations of contraventions depended. The way in which it sought to do so was fundamentally inadequate.

###### 7.3 The Group’s alleged profit motive

141 As the submissions for Mr Venardos also pointed out, to the extent that APRA’s case was that conduct was driven by the relevant companies saving expenditure on reimbursing beneficiaries for losses, the case theory is tenuous in the extreme. As the submissions pointed out, in 2015 at the time the compensation plans were considered by the boards:

IOOF Hold Co was an ASX 100 company with more than $123.6 billion in funds under management, administration, advice and supervision and more than 600,000 customers around Australia. For the year ended 30 June 2015, the group earned revenue of approximately $938 million.

…

The losses of the super funds to which the plans were directed were as follows:

(a) Pursuit: the total members’ funds in IPS Super as at 30 June 2015 was $18.04 billion. The total approved compensation of approximately $696,436.06 to superannuation members represented 0.0039% of the total members’ funds in IPS Super as at 30 June 2015.

(b) Sweep: the total members’ funds in TPS Super as at 30 June 2015 was $6.36 billion. The total approved compensation to superannuation members of $1,027,129.98 represented 0.016% of the total members’ funds in TPS Super as at 30 June 2015.

(c) Bendigo: the total members’ funds in IPS Super (of which the Bendigo Plan was a sub-plan) as at 30 June 2015 was $18.04 billion. The total approved compensation of approximately $114,000 represented 0.00062% of the total members’ funds in IPS Super as at 30 June 2015.

(d) CMT: The total members’ funds in TPS Super as at 30 June 2015 was $6.36 billion. Accordingly, the total approved compensation to be sourced from the general reserve of $1.616 million represented 0.0254% of the total members’ funds in TPS Super as at 30 June 2015.

###### 7.4 APRA’s use of the minutes of board meetings

142 As the second respondent also submitted APRA relied on the minutes of the meetings of the various boards, all of which recorded no conflict of interest, to support its case of breaches of the no conflicts covenant. However, as the second respondent put it, the minutes of a meeting are not required to record everything that was said. I agree with the submissions for the second respondent as follows:

The Courts have consistently recognised that while minutes of board meetings should record decisions and resolutions made by the board, minutes are not expected to be complete transcripts of words spoken at the meeting and nor do they need to record arguments for or against resolutions:

(a) In *August Investments Pty Ltd v Poseidon Ltd (*1971) 2 SASR 60, Zelling J noted at 62:

*“… I think the word “minutes” as it appears in ordinary usage in company law means the record of resolutions and matters ancillary thereto and not a complete transcript of every word used in the course of a meeting. If I am wrong in this, I think that a company has a discretion as to how it keeps its minutes and provided it faithfully records all that is required to be recorded, namely, how the business of the meeting was conducted and what resolutions were passed…”*

(b) In *Whitlam v Insurance Australia Group Limited* (2005) 52 ACSR 470, Einstein J stated at [181] “it would be unreal to expect every single matter discussed at a board meeting to be reflected in the minutes.”

(c) In *John J Starr (Real Estate) Pty Ltd v Robert R Andrew (A’Asia) Pty Ltd and Others* (1991) 6 ACSR 63, Young J relevantly noted the following points in relation to the contents of company minutes at [89]-[90]:

*“4. Minutes must be as concise as circumstances permit. Thus reasons for resolutions etc are seldom recorded.*

*…*

*6. A minute is not a report. Therefore speeches and arguments normally do not appear in minutes.*

*…*

*12. Reports of committees etc are not summarised in the minutes. A copy should be initialled or otherwise identified by the chairman and copy may be circulated with the minutes and/or attached to the original minutes.”*

It follows that the absence in the minutes of a detailed record of discussion or consideration about matters before the board does not support the conclusion that such discussion or consideration did not occur.

##### 8. THE PLEADING DISPUTE

###### 8.1 Introduction

143 It is a feature of this case that the respondents each contended, in a multiplicity of ways, that APRA’s case as advocated in its opening and closing submissions departed from APRA’s case as pleaded and that because forensic decisions (such as not calling witnesses) had been made on the basis of the case as pleaded, APRA should be held to its case as pleaded and not permitted to stray therefrom. APRA denied that it had strayed from its pleading and provided a table, a copy of which is Annexure B, showing the paragraphs of its amended statement of claim (**ASOC**) in which it had pleaded the facts upon which it sought to rely.

144 If APRA has materially departed from the pleading then it should not be permitted to do so. I accept that the respondents made forensic decisions on the basis of the case as pleaded. They ought not to have to deal with an unpleaded case.

###### 8.2 Consideration

145 Many of the respondents make the same or similar complaints about APRA having run a case which was not pleaded. Where the issue is the same or similar I deal with it once only by reference to the first of the respondents to have raised the issue.

146 The first respondent said (as is the fact) that a “repeated refrain in APRA’s closing submissions is that IIML and Questor were obliged to pursue claims against themselves and third parties in connection with the Pursuit, Sweep, CMT and Bendigo matters as an incident of ‘the fundamental obligation on trustees to get the trust property in, protect it and vindicate the rights attaching to it’ (ACS [198], [362]; see also [45], [200], [203], [364], [366], [367])”. However, according to the first respondent:

There is no allegation anywhere in the pleading that IIML or Questor breached any obligation at general law to get in the trust property. The proposition appeared for the first time in APRA’s closing submissions and APRA should not be permitted to pursue it. Given that there is a short answer to the point, however, it is convenient to explain why the new case is meritless.

147 The short answer that the first respondent gave is that (my emphasis):

The reliance on the duty to get in the trust property is misconceived and misunderstands basic principles of trust law. As a matter of the general law of trusts, the content of the duty is simple. As the authors of *Jacobs’ Law of Trusts in Australia* (8th ed, 2016) explain (at [17-02]):

The trustees, by virtue of their office, have an ‘obligation to get the trust property in, protect it, and vindicate the rights attaching to it. Thus, on assuming office, the trustees should get in all trust property, so the title to it is, if not in their names, at least in their control…. If the trust property consists in whole or in part in shares, they should procure the registration of the shares in their names. If notice is required to be given in order to perfect an imperfectly assigned debt, that notice should be given.

**In the case of a chose in action, a trustee does not need to actually pursue that chose in action to “get it in” in the relevant sense. Once the chose in action is vested in the trustee it is relevantly “in”. The trustee may have an obligation to pursue a chose in action, but much will depend on the circumstances.**

**The true position is explained in *Lewin on Trusts* (19th ed, 2015) at [34-022]:**

**The trustees’ legal ownership enables them to bring common law proceedings against third parties as representing the beneficiaries… [I]f it is the fact, or there are reasonable grounds for believing, that legal steps, if taken, would produce no useful result, the trustee (or an executor) is not liable; the trustees may take into account the position of the debtor, the amount of the debt and the probability of the proceedings being successful.**

It was presumably for this reason that APRA pleaded that the alleged claims against IOOF Service Co were “reasonably arguable”. IIML and Questor had no duty to pursue any claim falling short of that standard.

APRA now incorrectly attempts to synonymise the duty to “get in the trust property” with one to pursue any potential chose in action the trustee may have, no matter how speculative, costly or uneconomical. Such a duty would wreak havoc upon the law of trusts. It would oblige trustees to whittle away trust funds by pursuing spurious claims for fear they may otherwise breach their duties.

The consequences of this error for APRA’s closing submissions is profound. In many respects, the entire architecture of APRA’s new case regarding the Pursuit, Sweep, CMT and Bendigo matters depends on the correctness of its assertion that pursuing choses in action is an incident of the trustee’s duty to get in trust property. The rejection of the proposition leaves those cases without any clear basis in legal principle.

148 Before dealing with the pleading issue I should record that I agree with this submission. It is apparent that, contrary to APRA’s contention, the only “pattern” in the present matter is not connected with the conduct of the respondents. The “pattern” is that reflected in APRA’s case. Its case consisted of identifying an apparent error by the trustee which may or may not have occasioned loss to the beneficiaries, asserting that the error gave rise to reasonably arguable causes of action against the trustee and IOOF Service Co, relying on IOOF documents as constituting admissions (including purported admissions as to legal conclusions), and then treating the mere fact of error and loss as a form of *res ipsa loquitur* sufficient to establish that the relevant respondents breached their statutory covenants. This case theory is then overlaid with a principle, the source of which is never explained, to the effect that a trustee must “exhaust” consideration of all potential claims against the trustee and IOOF Service Co, irrespective of the legal or practical difficulties which such claims would confront and the time and expense that would be involved in “exhausting” consideration, because of the duty to get in and vindicate property of the trust.

149 Accordingly, as the first respondent submitted, APRA has sought to graft onto the duty of a trustee to get in trust property the notion that this duty extends to pursuing to the point of “exhaustion” every possible claim, regardless of its legal or practical complexity or its prospects of success. I agree with the first respondent that:

The consequences of this error for APRA’s closing submissions is profound. In many respects, the entire architecture of APRA’s new case regarding the Pursuit, Sweep, CMT and Bendigo matters depends on the correctness of its assertion that pursuing choses in action is an incident of the trustee’s duty to get in trust property. The rejection of the proposition leaves those cases without any clear basis in legal principle.

150 APRA said that it pleaded this duty to get in trust property in ASOC [74](a)(ii)(iv) and (v) and as an integer of the conflicts pleaded at [74] - [77]. The problem for APRA is that the paragraphs on which it relies are concerned only with the alleged conflicted structure of the IOOF Group. Nowhere does APRA plead that the relevant respondents breached their statutory covenants by failing to get in and vindicate the trust property via “exhausting” any choses in action they might have. The case it is seeking to run in this regard was not pleaded. The respondents’ complaints in this regard are justified. The fact that the first respondent has provided a complete answer to APRA’s case suggests that there may be a lack of prejudice arising from APRA running the unpleaded case but this is merely fortuitous as I concur with the first respondents’ submissions. If I had reached a different view then there may well be prejudice as it is not difficult to envisage that different forensic decisions could have been made if the respondents knew they were dealing with an asserted duty to get in trust property as an adjunct to a purported duty to exhaust consideration of all choses of action to recover potential losses in order not to contravene the statutory covenants.

151 The first respondent said that another new argument deployed for the first time by APRA in its submissions was its submission based on the High Court’s decision in *Finch v Telstra*. The first respondent noted that:

There are two aspects to APRA’s *Finch* submissions. The first is that the superannuation context matters and that the obligations on trustees in that context may be different, having regard to the nature of the trusts involved, to the obligations of private trusts and the like. So much may be accepted. That observation, however, is not instructive as to how the provisions of the SIS Act or the trust deeds ought be construed.

The second aspect of APRA’s submission based on *Finch* is a submission to the effect that a decision by a superannuation trustee to not pursue a claim against a person having some possible liability to the trust is not a “discretionary decision”, but a “duty” that a trustee must exercise, which duty includes an obligation to positively form an opinion about that matter (ACS [200]).

152 The first respondent submitted in response that:

The nature of the discretionary decision/duty dualism at issue in *Finch* is explained in *Jacobs’ Law of Trusts in Australia* (8th ed, 2016) (at [16-06]):

Under the heading of pure powers may be grouped those acts which trustees may do if they think fit – namely, those acts in respect of which they have a discretion whether to do them or not…. In the case of duties, the trustees are bound to do the thing prescribed, whether in their view it is wise to do it or not. If they fail to perform the duty, the court will compel them to do so, or will do so for them. In the case of powers, they are bound to exercise their judgment actively and honestly, as to whether they should do or refrain from doing something and then act accordingly…

The essential difference between powers or discretions and duties properly so-called, lies not in the nature of the trustees’ obligation but in the nature of the act the trustee is obliged to do. Thus, if a trustee is directed by the trust instrument to pay the income from the trust fund to A, the direction is a duty. The trustee’s failure to make the payment constitutes a breach of trust and is actionable by A. But if the trustee has a mere power to apply the income for A’s maintenance and honestly decides, after taking into account only material considerations, to make no payment to A, the court will not interfere.

The issue arose in *Finch* because it was argued in that case that a decision by a superannuation trustee as to a beneficiary’s entitlement to “total and permanent invalidity” benefits was a discretionary decision in the relevant sense. The High Court held it was not because the trustee was required by the terms of trust to form the relevant decision — that is, the trustee had a duty to do make the relevant decision and, in doing so, to consider whether the relevant preconditions for payment of the benefits were met: (2010) 242 CLR 254 at [29]-[30]. In that sense, a failure to consider relevant matters in making the required decision could constitute a breach of trust: (2010) 242 CLR 254 at [66].

APRA strains in the present case to draw an analogy with *Finch*. It contends that, particularly having regard to the superannuation context, IIML and Questor’s trust duties extended to require them to properly consider the claims that the trusts had against IIML, Questor or third parties, and that a failure properly to consider those matters constituted a breach of the trustees’ obligations under the general law and the SIS Act.

153 The first respondent explained why these arguments should be rejected in these terms:

These arguments should be rejected for four reasons:

a) First, the analogy does not work. The decision at issue in *Finch* concerned the fundamental and central obligation of a superannuation trustee to pay out benefits to qualifying members. The High Court emphasised that superannuation benefits were “deferred pay”, and that beneficiaries had legitimate expectations that decisions about those benefits would be “soundly taken”: (2010) 242 CLR 254 at [33]. By contrast, the decisions at issue in the present case are far removed from decisions relating to members’ entitlements to benefits. They relate to the ordinary day-to-day operations of superannuation trusts. *Finch* does not stand for the proposition that every decision made by a trustee in the administration of a superannuation trust is converted to a trust duty. That would be a remarkable proposition. The reality is that the proper administration of superannuation trusts require judgments every day by the trustee regarding how best to serve the interests of beneficiaries. That does not convert each such decision into the product of a duty, nor render each such decision susceptible to challenge as a breach of trust.

b) Secondly, even if IIML and Questor were under a duty in the sense described in *Finch* to make decisions about pursuing claims on behalf of the trust against themselves and third parties, APRA has not appreciated what the content of that duty would be. The relevant duty is that described …above by reference to the passage from *Lewin on Trust*. The trustee would be entitled to not pursue any such claim on reasonable grounds, including having regard to the legal and factual difficulties in bringing the claims.

c) Thirdly, while the language used by the High Court in *Finch* focuses on the “decision” made by the trustees, and the formation of opinions that were a necessary integer to making that decision (see (2010) 242 CLR 254 at [29]-[30]), it must be recognised that *Finch* was a case where there was no relevant distinction or separation between the trustee’s “decision” and the trustee’s consequent actions. The relevant determination to deny total and permanent invalidity benefits was temporally and practically indistinguishable from the trustee’s actions in subsequently denying those benefits: see (2010) 242 CLR 254 at [4]. It should not be supposed, then, that by focusing upon the trustee’s “decision” in *Finch*, the High Court was intending to endorse the view that a trustee can breach its duty by failing properly to make a “decision” that is never acted upon or which is subsequently changed. *Finch* does not stand for the proposition that if a trustee makes a plan on Monday to take action on Friday which would be in breach of trust, that is itself a breach of trust, even if the trustee changes course on Tuesday, Wednesday or Thursday. The distinction is important in the present case where many of the “decisions” impugned by APRA were changed or not acted upon. Throughout its submissions, APRA appears to contend that *Finch* supports the view that any decision by a trustee, whether acted upon or not, can constitute a breach of trust if not the product of proper consideration. That is incorrect. There is no concept of ‘thoughtcrime’ in the law of trusts. *Finch* does not suggest otherwise.

d) Fourthly, and most critically, insofar as APRA’s new *Finch* argument turns on the question of what matters were actually considered by Mr Kelaher and the other individual respondents in making the relevant decisions, APRA’s failure to raise that case earlier has caused irreparable prejudice. Mr Kelaher could have answered that case by giving evidence as to his thought processes and the matters he considered. He has been denied that opportunity by APRA’s dilatory conduct.

154 Leaving aside the last of these submissions concerning the pleading point and associated prejudice, I should record here that I agree with these submissions. APRA’s case, insofar as it relies on *Finch v Telstra* to suggest that the relevant respondents were making non-discretionary decisions and had to obtain information, such as independent legal advice, before they could make a decision is unpersuasive and not supported by authority. The core trustee duty of determining whether a beneficiary has an entitlement is not analogous to a decision as to whether or not a chose in action, such as the right to make a claim for loss, should or should not be pursued. The latter decision is more akin to an exercise of discretion because it involves a potentially wide range of relevant considerations and an evaluation of all of those considerations including the amount at stake, the prospects of success, the practical and legal issues which will be confronted, and the available alternatives (at the least). Accordingly, I do not accept a fundamental plank in APRA’s case that the alleged existence of causes of action or reasonably arguable causes of action imposed on the trustee a duty to “exhaust” consideration of the potential choses in action and to inquire and obtain further information if any such further information was necessary to enable that exhaustive consideration to be given.

155 In terms of the pleading argument, APRA relied on [125], [131], [161], [167], [206], [247], [253], [270] and [276] of the ASOC as well as [126], [132], [162], [168], [207], [248], [254], [271] and [277] of the ASOC and [119], [158], [239] and [267] of the ASOC. None of these paragraphs assert the existence and breach of the duty by analogy to *Finch v Telstra* on which APRA now seeks to rely. If I had accepted the arguments by analogy to *Finch v Telstra* (which I do not) then it also would have followed that the respondents may well be irreparably prejudiced by the new way in which APRA chose to put its case. In particular, the forensic decision whether or not to call the individual respondents would most likely have been influenced by the lack of any pleading to the effect that the relevant respondents were bound by a duty to give exhaustive consideration to the potential causes of action. These submissions for APRA, which appear throughout its case, are not supported by a pleading. If the submissions were sustainable (when in my view they are not) they should not be permitted given the prejudice to the respondents.

156 The first respondent submitted that APRA had also sought to develop a case that IIML and Questor had acted too slowly in paying compensation. Thus, as the first respondent put it:

…Senior Counsel for APRA asserted that compensation took a long time (T39.19, T42.15, T45.34) and “a very long time” (T42.27). At one point he said it was “dragging on” (T48.16). Indeed, at one point, Senior Counsel for APRA appeared to put the issue of delay at the centre of APRA’s case (T48.30):

[T]he underlying concern with all this is that it’s taking so long… [and] the interests of the members are not being properly addressed through swift action.

This “delay” case is not pleaded. APRA should not be permitted to run it. Apart from anything else, that case is unfair in circumstances where APRA knows very well that the delay of which it complains was principally a function of a lengthy tax ruling process which was in the best interests of beneficiaries. In those circumstances the “delay” case should never have been put.

157 APRA said that the delay in paying compensation was pleaded in relation to the Pursuit matter at ASOC [122]-[124] and [129A]. These paragraphs do not plead that there was any breach of duty by reason of delay. I thus accept the first respondent’s submissions. No such case was pleaded and to the extent that APRA’s submissions involve delay they should be disregarded.

158 The first respondent submitted that:

In his oral opening, Senior Counsel for APRA alleged that APRA would prove that the respondents engaged in “[a] very strong pattern of conduct” (T9.9), whereby “the super trustees and responsible officers… always preferred the interests… of the IOOF Group to the interests of beneficiaries” (T11.9).

That case is, again, not pleaded and Mr Kelaher objects to APRA departing from its pleaded case.

That being said, in a somewhat bizarre twist, APRA’s own case proves that there was no pattern. Of the three relevant episodes involving Mr Kelaher — Pursuit, Sweep and CMT — each had a different outcome. In the case of Pursuit, an insurance claim was made with the proceeds used to substantially replenish the ORFR reserve. In the case of Sweep, Questor ultimately used its own funds to replenish the ORFR. And, in the case of CMT, Questor used funds from a third party (NAB) and the general reserve to compensate beneficiaries. Thus, in none of three cases did the relevant trustee rely only on a reserve to compensate beneficiaries, as opposed to using funds from other sources.

159 As will be apparent from the reasons which follow, I accept this submission. No such case was pleaded and no pattern of conduct is apparent. The incidents which found APRA’s case are all unique involving their own distinct facts and circumstances.

160 The fourth to seventh respondents also contended that APRA had articulated a new case from that which was pleaded. They said that:

To permit APRA to depart from its pleading now would not just be inconsistent with the basis upon which the matter was set down for trial: it would occasion irremediable prejudice to the fourth to seventh respondents. Investigations of factual matters irrelevant to APRA’s pleaded case, but arising on the case now sought to be put, would have been conducted. Different decisions would have been made in relation to the evidence (including, most importantly, oral evidence) to be adduced.

161 They provided an overview of their complaints as follows:

(a) **The “duty to get in trust property, protect it and vindicate the rights attaching to it”**: Part III of the ASOC, entitled “Obligations of Trustees”, pleads in a careful and apparently complete manner the source and content of the various duties and obligations that APRA considered relevant to its case. Nowhere in that section (or anywhere else in the ASOC) is there any reference to an obligation to “get in trust property, protect it and vindicate the rights attaching to it”, yet that duty is mentioned at least 10 times in APRA’s written closing submissions (ACS) (at [45], [198], [200], [203], [230(a)], [240], [362], [364], [366], [367]). It is fair to say that this duty is the bedrock upon which APRA’s case as run is built: but it is not the case that was pleaded. The apparent purpose of this innovation in APRA’s thinking is to convert a discretionary decision (whether to assert a right) into a mandatory duty (to “get in” or “vindicate” trust property). The reasons why that case must fail are dealt with elsewhere in these submissions: but the fact that it has been attempted shows that APRA has recognised that its pleaded case (involving duties in relation to alleged “reasonably arguable” causes of action) cannot succeed.

162 For the reasons given above I accept these submissions. APRA has sought to graft on to the discretionary decision whether or not to make a claim against one or more entities to recover loss of a duty to do so by analogy to the duty to get in trust property. The duty has not been pleaded and APRA should not be permitted to recreate its case in its submissions from the case which it pleaded.

163 The fourth to seventh respondents next identified:

(b) **The “duty not to knowingly exclude relevant information and to seek relevant information in order to resolve conflicting bodies of material”**: Having sought to convert decision-making in relation to the assertion of rights into a duty, APRA then layers another duty on top of it. The relevance of this duty to the facts of the present case is said to be revealed by the High Court’s decision in *Finch v Telstra Super Pty Ltd* (2010) 242 CLR 254 at [66]. The problem is, that, once again, one searches in vain within APRA’s pleading for any reference to a duty of the kind now given such prominence in APRA’s submissions. To take but one obvious example, when APRA pleaded a breach of the “best interests” and “no conflicts” covenants as I.O.O.F Investment Management Limited’s (IIML) Pursuit Compensation Breach (ASOC at [121]), it specifically and exhaustively set out in sub-paragraphs (a) to (e) (with sub-paragraph (a) in turn picking up paragraphs [118] and [119]) the matters relied upon as constituting the alleged contraventions. None of those matters raised, even obliquely, an allegation of the knowing exclusion of relevant information, or a failure to obtain further information to resolve a conflicting body of material. Yet that duty is now central to APRA’s case (see, e.g., ACS at [45]-[46], [366]). Once again, this theory of the case is hopeless, for reasons developed elsewhere in these submissions. But it is also not pleaded. And, if it had been, the likelihood that different evidence would have been called to address it is obvious.

164 Consistently with my conclusions above I agree with this submission. The case is not pleaded. If I had accepted APRA’s case that there was a duty to exhaust consideration of any potential cause of action including a duty to obtain further information such as independent legal advice then the respondents would be exposed to the prejudice of having made forensic decisions on one basis and having to deal with a case on another basis altogether. This should not be permitted.

165 The fourth to seventh respondents also identified as a new case the following:

(c) **“Process” vs “Decision”**: The preceding two examples of APRA’s departure from its pleaded case may be seen as integers in a larger departure. Whereas APRA’s pleaded case was tied squarely to the characteristics of actual decisions, it is apparent now that APRA’s real complaint relates to the process by which those decisions came to be made. That “process” case was not pleaded, and it goes without saying that the evidentiary response of the fourth to seventh respondents would have been very different if it had. To be clear:

(i) In relation to IIML’s Pursuit Compensation Breach, the pleading at ASOC [118]-[121] focused on the objective features of the compensation plan, and located the breach in the alleged objective failure of the plan to serve the best interests of members.

(ii) In relation to Questor Financial Services Pty Ltd’s (Questor) Sweep Compensation Breach, the pleading at ASOC [157]-[160] focused on the objective features of the compensation plan, and located the breach in the alleged objective failure of the plan to serve the best interests of members.

(iii) In relation to IIML’s Bendigo Compensation Breach, the pleading at ASOC [196]-[199] focused on the objective features of the compensation plan, and located the breach in the alleged objective failure of the plan to serve the best interests of members.

(iv) In relation to Questor’s CMT Remediation Breach, the pleading at ASOC [238]-[241] focused on the objective features of the remediation plan, and located the breach in the alleged objective failure of the plan to serve the best interests of members.

(v) In relation to Questor’s CMT Compensation Breach, the pleading at ASOC [266]-[269] focused on the objective features of the compensation plan, and located the breach in the alleged objective failure of the plan to serve the best interests of members.

(vi) In relation to IIML’s CMT Compensation Breach, the pleading at ASOC [282]-[286] focused on the objective features of the compensation plan, and located the breach in the alleged objective failure of the plan to serve the best interests of members.

APRA cannot now change its case to focus on the process by which those decisions were made, and must be confined to a challenge based on the objective features of the decisions taken.

166 APRA said in response:

**Process and outcome in issue**: pleaded at ASOC, [121] (Pursuit), [160] (Sweep), [199] (Bendigo), [239] and [267] (CMT) that IIML/Questor contravened by developing, adopting and approving relevant compensation plans, in light of information pleaded at [119] (Pursuit), [158] (Sweep), [197] (Bendigo), [239] and [267] (CMT).

Pleaded at ASOC, [126], [129], [132], [135] (Pursuit), [162], [165] [168], [171] (Sweep), [207], [210] (Bendigo), [254], [248], [274] and [277] (CMT) that individuals failed to take relevant steps to ensure best interests promoted and conflicts managed (e.g. identify conflicts and seek independent advice).

167 I accept that ASOC, [126], [129], [132], [135] (Pursuit), [162], [165] [168], [171] (Sweep), [207], [210] (Bendigo), [254], [248], [274] and [277] all involve a claim about the process of decision-making. Accordingly, I do not see this aspect of APRA’s case as having departed from the pleadings.

168 The fourth to seventh respondents submitted that:

(d) “**Implementation”**: APRA pleaded a case that various “compensation plans” were “implemented” (see, e.g., ASOC at [121], [160], and [199]). In each case, the plan that was “implemented” was pleaded to be comprised of certain specific steps (see ASOC at [115], [154], [194]). To take the “Sweep Compensation Plan” as an example, it was alleged to be comprised of steps including “paying compensation to superannuation beneficiaries by means of funds taken from the” TPS ORFR and “not compensat[ing] affected beneficiaries of TPS Super from its own funds” (ASOC at [154]). It goes without saying that “implementation” of such a plan could only involve “paying” money from the ORFR, and “not paying” money from Questor’s own funds. Yet in APRA’s Submissions at [482]-[484] APRA puts its “implementation” case on the basis that other actions were taken. But those actions were not pleaded as forming part of the relevant “plan”. APRA cannot now depart from its pleaded formulation of the “plans” that were alleged to be implemented.

169 APRA said the implementation was pleaded and particularised at ASOC [117] and [156]. I accept APRA’s submission.

170 I otherwise consider the pleading points to be adequately addressed by APRA’s responsive document annexed as Annexure B to these reasons for judgment.

##### 9. THE ALLEGED CMT BREACHES

###### 9.1 Step 1 - The CMT Overpayment

9.1.1 The CMT

171 APRA’s contention is that Questor in its capacity as trustee of TPS Super breached its   
Pre-2013 Due Care Covenant and was liable under s 55(3) of the SIS Act to beneficiaries of TPS Super for the loss and damage they suffered due to the CMT Overpayment.

172 The basic facts were not in dispute. As APRA put it, the CMT (sometimes referred to in IOOF documents as the “Cash Management Fund” or “CMF”) was a Managed Investment Scheme (**MIS**) of which Questor was the RE. The CMT invested in short to medium term debt securities or deposits and was focused on “receiving a moderate level of income at around the cash rate”: Product Disclosure Statement (PDS), CB 1/5A, p. 213\_0001. One of the benefits of the CMT, as advertised to investors in the PDS, was that “you will generally receive regular income from your investment in the form of distributions”:(CB 1/5A, p. 213\_0003). However, the PDS also identified that “[s]mall differences in both investment performance and fees and costs can have a substantial impact on your long-term returns”:(CB 1/5A, p. 213\_0004).

173 The CMT was governed by a document titled “The Wholesale Trusts Constitution” (**CMT Constitution**): CB 1/6G. The CMT Constitution relevantly provided that:

(1) The CMT was a unit trust with unitholders holding units that conferred an equal undivided interest in the trust: cl 5.1 (p. 219\_0366).

(2) Questor was required to determine the daily net income of the trust on each business day, and to decide the classification of any item as being on income or capital account in accordance with generally accepted accounting principles: Fifth Schedule, cl 12.1 (p. 219\_0385).

(3) The net daily income of the CMT was required to be distributed to unitholders on specified distribution dates: cl 12.2-12.5 (p. 219\_0386). Questor otherwise had a discretion as to whether to distribute income or capital at any other time: cl 12.7   
(p. 219\_0373).

174 In APRA’s words:

The net effect of these clauses was that unitholders were entitled to all of the income of the CMT and that it was Questor’s responsibility as RE and manager to determine the classification of amounts held as either income or capital in accordance with applicable accounting principles. Pursuant to the CMT Constitution, Questor was also entitled to a management fee of up to 1.5% per annum of the asset value (cl 18.1) as well as additional custody fees (cl 18.2) (p. 219\_0378).

175 As at 2009, in addition to acting as RE, Questor was also the only unitholder of the CMT. It held those units in two different capacities: first, as RE of a Managed Investment Scheme known as The Portfolio Service Plan (**TPS MIS**) into which investors had invested funds and, second, as the trustee and licensee of the superannuation entity, TPS Super. In this latter capacity, it was regulated by APRA. As APRA submitted:

The effect of this arrangement was that beneficiaries of TPS Super and investors in the TPS MIS could direct Questor, as trustee and RE respectively, to invest trust money held on their behalf into the CMT. The units issued in the CMT were then held by Questor on trust for those beneficiaries and investors, providing those investors with exposure to the CMT portfolio and income distributions which Questor as trustee would pass on to their individual accounts (less any tax and applicable fees payable).

176 Further, APRA said:

As RE and manager of the CMT, Questor was required to manage the fund in accordance with the CMT Constitution and its obligations as an RE under the Corporations Act 2001 (Cth). Those obligations included obligations to exercise care and skill, act in the best interests of members, value the scheme property at regular intervals, and ensure that all payments out scheme property are made in accordance with the scheme constitution and the Corporations Act: ss 601FC(1)(b), (c), (j) and (k). Unitholders in the trust (i.e. Questor as TPS Super) had a right to recover loss and damage caused by breach of these provisions pursuant to s 601MA.

While Questor could delegate responsibility for management of aspects of the fund to other service providers, it remained personally liable to members for any acts or omissions by those service providers: s 601FB(2). This provision is also relevant to the application of the indemnity in the CMT Constitution, as discussed further below.

177 APRA referred to the role of NAB in these terms:

The CMT Constitution provided that Questor could appoint a custodian to hold assets and title documents to assets on its behalf: cl 9.8 (p. 219\_0371). As at 2009, NAB provided these services pursuant to a contract known as the “Master Custody Agreement” which had been novated to it from the previous provider on and from 16 September 2003 (the Master Custody Agreement): CB 1/1. Pursuant to the Master Custody Agreement, NAB held all assets of the CMT delivered to it and was required to deal with those assets in accordance with Questor’s authorised instructions: cl 3.1 (p. 20). NAB could only pay out moneys from the Fund in accordance with authorised instructions: cl 3.7 (p. 22).

The Master Custody Agreement obliged NAB to exercise the degree of care and diligence that a prudent person would exercise in NAB’s position (cl 3.17(f)) and to have in place effective internal controls to ensure compliance with applicable laws (cl 3.19(a)) (pp. 26-27).

178 APRA referred to the role of IOOF Service Co as follows:

Questor also relied upon the administration services provided by IOOF Service Co to administer the CMT: ASOC, [214]; admitted IIML/Questor Defence, [214].

Those services were provided pursuant to the Services and Resources Support Deed dated 19 July 2005: CB 1/2, p. 68….

IOOF Service Co also provided employees, services and resources to Questor as trustee of TPS Super. The supply of these employees, services and resources was governed by the Services and Resources Support Deed…

9.1.2 The CMT Overpayment

179 The background facts below reflect APRA’s submissions except where otherwise indicated.

180 In June 2009, NAB incorrectly classified a maturing term deposit as “income” instead of “capital” and proposed to Questor (in its capacity as RE of the CMT) that the capital totalling $6.16 million be distributed as investment income. This created what the contemporaneous documents label as an “overdistribution” to the unitholder (being Questor, in its capacity as RE of the TPS MIS, and Questor in its capacity as trustee and licensee of TPS Super).

181 The approval of the CMT Overpayment by IOOF Service Co is recorded in the email exchange between Mr Edward Youds (acting on behalf of Questor as RE of the CMT) and Mr Michael Toal (of NAB) on 15 June 2009: CB 2/8C. The email records that Mr Youds approved the email less than one hour after receiving the request from Mr Toal.

182 The distribution of capital was made by Questor in its capacity as RE of the CMT to Questor in its capacity as unitholder in the CMT. In turn, Questor in its capacity as RE of the TPS MIS distributed the capital as an income distribution to investors in the TPS MIS, and Questor in its capacity as licensee and trustee of TPS Super distributed the capital as an income distribution to beneficiaries of TPS Super.

183 The CMT Overpayment was not discovered until February 2010 when Questor as RE of the CMT changed custodians from NAB to BNP Paribas, at which time BNP Paribas completed a full reconciliation of the CMT assets and identified that Questor continued to show a   
$6.16 million term deposit asset held within the CMT: CB 2/0010, p. 268. However, the capital this represented, instead of being reinvested, had been distributed.

9.1.3 APRA’s case

184 According to APRA, the CMT Overpayment was caused by NAB’s error as to the calculation of an income distribution but was also the result of failures by Questor and IOOF Service Co to exercise due care, skill and diligence in the operation of the CMT and TPS Super by having adequate controls in place to avoid an unauthorised payment of capital. APRA said that these failures were confirmed by IOOF’s Head of Investment and Accounting Services, Mr Vincent Rossitto, in a detailed report he prepared in October 2013 (some four years later):CB 3/31A,   
p. 620\_0001. After reviewing all of the relevant records and policies, Mr Rossitto concluded (CB3/31A, p. 620\_0002) that the “root cause” of the issue was that:

(1) investment governance, investment compliance and third party outsource monitoring required improvement;

(2) there was a lack of clarity and experience around roles, responsibilities, procedures and process flows; and

(3) there was a poor understanding of source documents and reports supplied by external parties and investigation of reconciling, outstanding and excluding items.

185 APRA said that each of these matters involved a failure by Questor and IOOF Service Co, not NAB. According to APRA these failures caused Questor and IOOF Service Co to fail to detect the CMT Overpayment, in circumstances where a prudent superannuation trustee would have done so, as confirmed by Mr Rossitto in his comments on what would become the CMT Compensation Paper provided to the Questor board. In response to a proposed comment in the paper that:

…it [the CMT Overpayment] was not the result of the administrator or Trustee's failed internal processes at the fund level

Mr Rossitto commented in a so-called “bubble comment” on the draft document:

There was no framework, process or procedure in place to detect the error. A yield analysis of TPS cash account disbursement should have picked this up. Operational staff at the time saw the CMT as part of TPS’s cash account, ie all rolled into the TPS entity

(CB 10/212E)

186 APRA said that:

Despite each of the above facts being recorded in the respondents’ own business records, Questor and IOOF Service Co’s failure to exercise the degree of care, skill and diligence expected of them under s 52, the CMT Constitution and the Services and Resources Support Deed, and their corresponding exposures to liability for the CMT Overpayment, are denied by each of the respondents. This is despite Questor having reported the CMT Overpayment to ASIC as a significant breach of the Corporations Act 2001 (Cth) and its compliance plan in October 2013: CB 2/12, p. 278.

In support of this position, APRA relies upon the documents prepared by Mr Rossitto, including the opinions expressed within it, as an admission: Evidence Act 1995 (Cth), s 81, 82(b). Mr Rossitto was an [sic] senior member of the IOOF Finance team, reporting directly to Coulter: CB 4/32G. The representations were made within the scope of his authority for the purposes of s 87 of the *Evidence Act 1995* (Cth) and are accordingly attributed to Questor. No objection has been taken to the admission of this document into evidence. Indeed, it formed part the documentary tender on behalf of the 4th to 7th respondents.

As against each of the other respondents, APRA relies upon Mr Rossitto’s report as a business record pursuant to s 69 of the *Evidence Act 1995* (Cth). It is admissible as evidence of the facts represented within it which, APRA says, prove Questor and IOOF Service Co’s negligence. APRA notes that it does not allege that any of the individual respondents were involved in the CMT Overpayment, or seek declarations against the individuals with respect to the CMT Overpayment: cf Coulter OS [7].

APRA submits that the evidence overwhelmingly demonstrates that in approving and distributing the CMT Overpayment without a proper investment framework in place and without any degree of oversight of NAB’s calculations, in both its capacity as RE and trustee, Questor did not exercise the degree of care, skill and diligence required by it pursuant to s 601FC(1)(b) of the Corporations Act and s 52(2)(b) of the SIS Act. This failure, in addition to NAB’s error, contributed to CMT Overpayment occurring.

187 According to APRA, the beneficiaries of the trust suffered loss by reason of the CMT Overpayment. APRA characterised the loss as loss of the capital invested in the CMT and the loss of the income stream (from June 2009 until the capital was later reinstated in full) that would have been earned on that capital had it remained invested. APRA detailed this alleged loss as follows:

(a) the loss of earnings on trust money that Questor as trustee had been instructed to invest in the CMT, but which instead had been involuntarily returned, as income, to the beneficiaries’ cash accounts;

(b) liabilities incurred by reason of the erroneous treatment of the unauthorised capital return as income, including liabilities for income tax and deductions for other fees and charges;

(c) losses arising from the resulting unit pricing error for the CMT. As the accounts of the CMT continued to show a $6.16 m asset until corrected, this meant that the price paid by incoming unitholders (including members of TPS) was inflated and the unitholder would have a lower value in the fund than they should have had. In addition, when a unitholder redeemed any units in the fund the amount paid to that unitholder was too high, at the expense of ongoing unitholders (see the Joint ASIC and APRA Unit Pricing: Guide to good practice (August 2008), p. 90: CB 1/6KA).

188 APRA said that its case gave rise to exposures for liability on the part of each of NAB (as service provider to Questor as RE of the CMT), IOOF Service Co (as service provider to Questor as RE of the CMT) and Questor (as RE of the CMT). According to APRA, there was available to Questor reasonably arguable claims for the loss as against NAB, IOOF Service Co and itself.

189 As to NAB’s exposure, APRA noted that the only answer provided by the respondents’ submissions was the lack of any proven loss. Excluding Mr Venardos they otherwise accepted that if there was loss then it was reasonably arguable NAB was liable for the loss. APRA noted that:

NAB, in fact, was the only entity that Questor and its responsible officers were willing (belatedly) to make a claim against and NAB ultimately ended up admitting some liability and contributing about $1.5 m to the compensation payment: CB 7/115,   
p. 1830.

190 As to IOOF Service Co’s exposure, APRA said that it was exposed in its capacity as service provider to the RE of the CMT and that each of the failures in systems and processes identified by Mr Rossitto “were failures in the services provided by IOOF Service Co pursuant to the Services and Resources Support Deed”. APRA said that the losses were direct losses and thus within the scope of IOOF Service Co’s indemnity or, at the least, it was reasonably arguable that the losses were direct rather than indirect or consequential losses.

191 As to Questor as the RE of the CMT, according to APRA:

Questor’s own records demonstrate that it failed to act with care and diligence. Further, the acts and omissions of NAB and IOOF Service Co identified above were directly imputed to Questor by s 601FB(2) of the *Corporations Act 2001* (Cth).

192 APRA acknowledged that the CMT Constitution contained relevant provisions which would have to be considered in respect of any liability of Questor as RE of the CMT, referring to the following matters:

(a) Questor was not liable for any loss suffered in respect of the CMT if it acts in good faith and without default or negligence (cl 16.3, CB 1/0006G   
p. 219\_377).

(b) Questor could take and act upon legal advice or the advice, statements or information of bankers, accountants, auditors, valuers and other experts who are independent of Questor, and would not be liable for anything done, suffered or omitted by it in good faith and on reliance upon such opinion, advice, statement or information (cl 16.4, CB 1/0006G p. 219\_377);

(c) Questor was entitled to be indemnified out of the assets of the trust for any liability incurred by it in performing or exercising its powers or duties in relation to the trust (cl 9.3, CB 1/0006G pp. 219\_0370-0371).

193 APRA said that there was no suggestion that the respondents considered these provisions at the time Questor decided not to make a claim against itself as RE and there was no evidence that “if Questor had turned its mind to this, and sought competent legal advice, that the existence of these clauses would have meant that a claim against Questor was not reasonably arguable”. APRA continued:

In any case, a “careful analysis” of the relevant CMT Constitution together with the MIS provisions of the Corporations Act 2001 reveals that it was highly unlikely that Questor as RE would have had a good defence based on any limit of liability or indemnity for the following reasons:

(a) With respect to the first limitation, it is APRA’s case that Questor did act with default and negligence with respect to the CMT Overpayment and CMT Remediation Plan. It accordingly cannot avail itself of the exemption clause.

(b) With respect to the second limitation, Questor’s liability for the CMT Overpayment did not arise by reason of its reliance on advice or information provided by an expert. It arose because of the failure by Questor to have in place the processes and procedures that a reasonable person would exercise in its position. Further, there is no suggestion in the evidence that NAB provided Questor with any “expert” advice or information on which it relied. The exchange with Mr Youds suggests that NAB simply provided the calculation spreadsheet and Mr Youds, without scrutinizing the calculations, approved the distribution.

(c) With respect to the indemnity, its scope was limited. At all relevant times, s 601GA(2) of the *Corporations Act 2001* (Cth) provided that Questor as RE could only be indemnified where the liability arose from the proper performance of Questor’s duties as RE. Further, in determining whether Questor’s performance of its duties was proper, s 601FB(2) imputed the acts and omissions of Questor’s service providers (namely, NAB and IOOF Service Co) to Questor. A “careful analysis” of the indemnity, in the context of the statutory regime for the regulation of MIS, reveals (and would have revealed to Questor and its responsible officers at the time) that Questor had a real exposure by reason of its own failures and the failures by NAB and IOOF Service Co. The indemnity would not have responded to these failures which did not constituted a proper execution of the duties of an RE.

Perhaps more relevantly, and not averted to by any of the respondents, is the provision in cl 21 of the CMT Constitution that required Questor as RE to promptly respond and seek to resolve any complaint by a unitholder alleging that it had been adversely affected by Questor’s conduct in its management or administration of the CMT (p. 219\_0382). The PDS for the CMT includes provisions to the same effect: CB 1/5A (p. 213\_0008). As set out in further detail below, no such complaint was ever made by Questor in its capacity as unitholder and trustee of TPS Super, despite being adversely affected by Questor’s conduct as RE over a significant period of time.

194 In its reply submissions APRA referred to the observations of Gordon J in *Australian Securities and Investment Commission v Letten (No 17)* [2011] FCA 1420; (2011) 286 ALR 346 at   
[14]-[20] to the effect that “liabilities ‘improperly incurred’ will include conduct of the trustee that is ‘exercised with an absence of the care and diligence that a person of ordinary prudence should exercise’ (at [16], [18])”.

195 APRA also contended that in in its capacity as trustee and licensee of TPS Super when receiving the distribution of capital from Questor in its capacity as RE of the CMT, Questor failed in its obligations under the SIS Act of due care and skill. The failure consisted of not reconciling the CMT Overpayment to the underlying yields, or detecting it promptly so as to mitigate its effects, by appropriately monitoring and supervising the distributions made by the RE of the CMT (i.e itself). As identified above, APRA submitted that Questor’s failure to do so was itself a contravention of the covenant in s 52(2)(b), namely, a failure to exercise the required degree of care, skill and diligence (called Questor’s CMT Overpayment Breach). APRA said it also gave rise to exposure 4 in step 1 of the CMT Diagrams (which are reproduced in Annexure C).

196 In oral submissions APRA emphasised that there was no evidence of the respondents considering any of the complex arguments they now put against the existence of reasonable arguments for the liability of NAB, IOOF Service Co and Questor (in its varying capacities) and thus the relevance of the arguments was questionable. As noted above, I disagree with this submission. The standard of due care, skill and diligence involves an objective measure. If, objectively, circumstances existed which meant that it was not reasonable to pursue the alleged liabilities which APRA has identified then it does not matter if the relevant respondents had those matters in mind at the time or not. There will be no breach of the due care covenant if, objectively, the conduct met the relevant standard of care.

9.1.4 The respondents’ case

197 The respondents submitted that APRA had failed to prove Questor’s breach of Questor’s   
pre-2013 care, skill and diligence covenant. According to the respondents (or one or more of them) APRA has not established the necessary material facts to support the claim. In particular it has not identified the source of the obligation that Questor as RSE, an investor in the CMT, would have to audit or monitor the distributions made to it. Thus, “APRA has not provided the Court with any evidence upon which it could be said that Questor, in its capacity as RSE of TPS Super (which is the only capacity in which it had obligations to comply with SIS Act covenants), failed to exercise the due care, skill and diligence required of a trustee in that position”.

198 Further, it was submitted that for the Court to conclude that Questor as RSE has failed to exercise the degree of care, skill and diligence that an ordinary prudent person would exercise, evidence of at least the following 6 matters would be required:

(1) the services which IOOF Service Co provided to Questor as RSE with respect to the receipt of distributions from the CMT;

(2) the basis upon which Questor as RSE was obliged to conduct audits or assessments or monitoring of the provision of those services, and why it was not entitled to rely upon Questor as RE and/or NAB in relation to the calculation and distribution of income from the CMT, particularly in light of:

(a) the obligations imposed on Questor as RE in relation to the calculation and distribution of income from the CMT by the CMT Constitution;

(b) the obligations imposed on NAB in in relation to the calculation and distribution of income from the CMT by the provisions of the Custody Agreement;

(3) what specific actions it is said that Questor as RSE was required to undertake, by reference to the degree of care, skill and diligence that an ordinary prudent person would exercise in dealing with property of another for whom the person felt morally bound to provide;

(4) the nature of the audit or monitoring system alleged to have been required, and whether it could have detected this kind of error and resulted in the CMT Overpayment being detected before it was made or before it was passed on to superannuation beneficiaries;

(5) practically speaking, how any such system could assess, audit and monitor “the status of capital invested in the CMT” or what precisely that means, or similarly “the composition of distributions made to beneficiaries of TPS Super”; and

(6) what further information would need to be obtained from NAB and the Investment Managers for this purpose, and whether this would require access to any of their computer systems, and whether Questor as RSE would be entitled to obtain that information and access.

199 The respondents said it was “particularly relevant to note Questor as RSE’s very limited role in receiving income distributions from the CMT and crediting the proceeds to members’ Cash Management Accounts from which it follows that any services provided to Questor as RSE by IOOF Service Co would be similarly limited”. The fourth to seventh respondents thus concluded:

In circumstances where there is no primary evidence capable of making out APRA’s claimed lack of due care, skill and diligence, it might have been expected that APRA would lead expert evidence to identify the role and responsibilities of a trustee investor in a product with the features of the CMT. But it chose not to.

In these circumstances, Questor submits that APRA has failed to establish that a prudent superannuation trustee exercising the requisite degree of care, skill and diligence would have devised and implemented an audit and monitoring system to avoid this error.

200 The fourth to seventh respondents noted also that APRA’s submissions failed to focus on the role of Questor as RSE and IOOF Service Co’s provision of services to Questor in that role alone. Further, the documents on which APRA relied “reveal nothing about what IOOF Service Co is actually alleged to have done in relation to the receipt of distributions from the CMT, or as to the ‘appropriate’ control testing and/or auditing, monitoring which it is said Questor as RSE ought to have performed of those service provided to it by IOOF Service Co”. To the extent APRA relied on these documents as containing admissions, the fourth to seventh respondents said that:

To the extent that it is a factual opinion upon which APRA relies, then before the Court could treat it as evidence of the truth of the opinion, an exception to the opinion rule would need to be made out: *Lithgow City Council v Jackson* (2011) 244 CLR 352. APRA has not proved that the authors of any of the documents upon which it relies have the expertise to render their opinions admissible as expert opinions, and nor has it demonstrated that the requirements of s 78 of the *Evidence Act 1995* (Cth) have been met.

201 They also submitted that the documents were created after the event and with the benefit of hindsight following an investigation into the event. As the question of breach is to be answered by reference to the circumstances as they existed at the time of the alleged breach the probative weight of the after the event documents is “virtually nil”. Otherwise, to the extent the “documents contain an opinion involving the application of a legal standard to particular facts, or a bare opinion concerning the law, APRA appears to accept that the documents it relies upon are not probative of whether or not there was a contravention of any covenant or other legal standard. So much, in any event, was made clear in the decision of Gummow J in *Dovuro Pty Ltd v Wilkins* [2003] HCA 51; (2003) 215 CLR 317 at [69]-[70]”. APRA, it was said, appeared to rely on the documents as evidence that opinions were held at the relevant time which raises a question of the relevance of such facts. Finally, they said, to the extent that the documents are relevant, the weight to be given to the matters recorded in them needs to be assessed in light of the role and qualifications of the person creating them, as well as the regulatory context in which the respondents were operating.

202 The respondents submitted that APRA’s case relating to the exposures of NAB, IOOF Service Co and Questor in its capacity as RE and RSE was misconceived. The first respondent’s submissions disclosed the alleged misconceptions and were adopted by the other respondents.

203 In respect of NAB, it was submitted that there was no evidence of loss. As the first respondent’s submissions put it:

If one considers the position immediately following the CMT Overpayment, none of the CMT unitholders had suffered any loss. The beneficiaries of the CMT, TPS MIS and TPS Super had each received part of the capital of the CMT, but they were no worse off for that. The CMT unitholders had gained absolute title to property in which they had previously only held a beneficial interest, but that is itself not a detriment. Indeed, it is fairly described as gain because they have improved their title.

APRA attempts to define these gains as losses (ACS [180]). It does so on three bases:

a) First, it says that there were “lost earnings” because money that was to be invested in the CMT was not so invested. The premise of that submission, however, is the supposition that the overdistributed capital earned less outside the CMT than in it. There is no evidence that that was the case. Indeed, to the extent the CMT was a cash fund, the likelihood is that the overdistributed capital would have earned more outside the CMT.

b) Secondly, APRA says that people would have incurred liabilities by reason of the erroneous treatment of unauthorised capital returns on income. Again, though, whether or not that is correct is a complex matter. To know if that occurred, one would need to know a lot more about the tax position of the relevant individuals, including their income and capital gains positions. There is no evidence of these matters either.

c) Thirdly, APRA says that the overdistribution resulted in a unit pricing error whereby the unit price for the fund was too high because that price reflected a supposition that the $6.16 million in capital was still in the fund. Consequently, anyone purchasing units in the fund would pay too much. As a theoretical matter, that is correct, but there is no evidence that this occurred. More fundamentally, however, this “loss” is not the value of the amount overdistributed. It is not the $6.16 million. This category of loss would have to be calculated by the amounts of any overpayment, which would be considerably less than $6.16 million. There is no evidence of any such overpayments or their amount.

Thus, even assuming contrary to the evidence that a claim against NAB existed in relation to the CMT Overpayment, there is no sound basis upon which the Court could conclude that that claim was of any substance or value. NAB may have caused the overdistribution, but that did not mean it was liable to reinstate the CMT to the value of the overdistributed capital.

204 In respect of IOOF Service Co, as the first respondent put it:

…there is no reliable evidence that there was any failure on the part of IOOF Service Co in relation to the overpayment.

The only evidence that APRA can point to (ACS [174]-[177], [185]) is a single document authored by Mr Rossitto and dated 18 October 2013 (**Rossitto Account**).

205 The following matters were advanced by the first respondent about the Rossitto Account:

(1) the Rossitto Account was produced by Mr Rossitto when he was under investigation in 2013 as part of the whistleblower investigation. Mr Rossitto was required to produce information and was one of the targets of the investigation;

(2) a document of this kind is “an entirely insubstantial basis” to make any findings as to the true cause of the CMT overdistribution as it would not be surprising if Mr Rossitto sought in the Rossitto Account to lay blame on IOOF/Questor’s systems and processes in order to defray any criticism of his own conduct; and

(3) the Court would be “very slow to take at face value Mr Rossitto’s analysis as an objective assessment of who was at fault”, particularly given that “it is not substantiated by any other evidence”.

206 It was also submitted that even if the Rossitto Account was to be accepted “it is by no means clear that the deficiencies in Questor’s systems that Mr Rossitto identified were, in his view, tantamount to breaches of duty by Questor” as:

Ordinary experience is that unexpected events can reveal unforeseen weaknesses in systems and processes. While it would be imprudent not to redress those weaknesses after an issue had arisen, it does not follow that there was any default, negligence or breach of trust in failing to recognise the issue before it occurred.

207 Further, APRA’s case had failed to “grapple with the reciprocal obligations owed by Questor to IOOF Service Co under the AWM Service Deed. For example, Questor’s obligations included that it would keep proper systems, procedures and processes (clause 9.1(g)). Given that obligation, it is by no means clear that IOOF Service Co would be liable for any failure to ‘adequately audit, monitor or assess its procedures’ (cf. ASOC [224(b)(iii)]) or to itself have systems or processes to detect an overdistribution (cf. ASOC [228])”.

208 IOOF Service Co was also not liable for indirect or consequential losses (cl 11.2 of the services deed). In the submissions of the first respondent:

APRA contends that the loss suffered by Questor as RE of the CMT or as trustee of TPS Super might not have met this description but there is little doubt that it would. Again, the immediate effect of the overdistribution was simply to put capital in the hands of Questor as RE of CMT. Questor profited from that. If Questor wished to contend that some further loss resulted, by definition that loss would be indirect and consequential. The same is true of Questor in its capacity as trustee of TPS Super. The overdistribution did not operate to harm Questor in that capacity in any way. Any subsequent harm was therefore necessarily indirect and consequential. The mooted cases are not in the category of cases where it is difficult to draw a line between direct loss and indirect or consequential loss.

209 The respondents submitted that any liability of Questor as trustee of TPS Super would be excluded by the exclusion of liability and rights of indemnity granted under the trust deed but, on my conclusion, the provision would not so operate in respect of any liability under s 55(3) of the SIS Act. However, as the respondents also pointed out the services deed did not distinguish between services provided to Questor as RE and as trustee of TPS Super. The respondents noted that again APRA’s evidence was confined to the Rossitto Account and the fact that Mr Youds, “someone working within the IOOF group, ‘approved’ the distribution in May 2009 and did so ‘within an hour’ of approval being sought by NAB and ‘without scrutinising the calculations’ (T23.21; ACS [166], [192(b)])”. As the first respondent put it:

APRA seeks to have the Court infer that it was Mr Youds’ role to independently verify distributions by NAB and that he was delinquent in that duty but there is no evidence to substantiate those propositions. Indeed, there is no evidence as to what information was available to Mr Youds to verify the distributions from the CMT proposed by NAB or to confirm the correctness of the amounts involved. In circumstances where NAB was the custodian and CUSCAL was the investment manager, it would not be at all surprising if Questor had no visibility with respect to the CMT income from month-to-month, other than the information it received from NAB. The evidence indicates that, even for NAB, it was difficult to detect errors in the calculated level of income at this time because there were major fluctuations in value associated with the Global Financial Crisis. There is therefore no basis to believe that Mr Youds failed to perform his function.

210 The first respondent also noted that Questor as RE was entitled by the CMT Constitution, cl 16.4(b), to take and act upon:

the advice, statements or information from any bankers, accountants, auditors, valuers and other persons consulted by the Manager who are in each case believed by the Manager in good faith at the time of appointment to be expert in relation to the matters upon which they are consulted and who are independent of the Manager …

211 The CMT Constitution itself contained a limitation on liability in cl 16.3 as follows:

Subject to the Corporations Act, if the Manager acts in good faith and without default or negligence it is not responsible to Members for any loss suffered in respect of a Trust. The liability of the Manager in relation to a Trust is in any case limited to the Assets of the Trust.

212 The CMT Constitution also contained an indemnity in cl 9.3 in these terms:

The Manager is entitled to be indemnified out of the Assets of a Trust for any liability incurred by it in performing or exercising any of its powers or duties in relation to that Trust. This indemnity is in addition to any indemnity allowed by law. Nothing in this constitution will prevent the Manager exercising its powers to satisfy any right of indemnity out of the Assets or to exclude or limit its personal liability.

213 As the first respondent put it, there is simply no reliable evidence of any default or negligence by Questor. The first respondent’s submissions included the following:

APRA makes a further submission that the right of indemnity would not be available to Questor as RE of CMT because the actions of IOOF Service Co were imputed to Questor in that capacity by s 601FB(2) of the Corporations Act (ACS [192(c)]). That depends on two suppositions: one being that IOOF Service Co was at fault in relation to the CMT overdistribution (which APRA has not proved); and the other being that the actions of IOOF Service Co were otherwise than “reasonable and honest” and hence outside the description of “proper performance” in s 601GA(2) (which is not pleaded and certainly could not be proved).

214 The second respondent made a number of submissions to the same effect but also said that if Questor as RE had sued NAB or IOOF Service Co or itself it would have been met with the defence that Questor could recover the overpaid amounts from members consistent with the principle that recoupment was a permissible remedy in these circumstances: see *Jacobs Law of Trusts (8th ed)* at [17.37]-[17.38] and the cases cited therein. As the second respondent put it “there could be no loss if the overpayment was recoverable and a failure to exercise the right as trustee to recover an overpayment would have been a complete answer to any claim for loss”.

215 The second respondent also made the “no loss” contention and pointed to the APRA record of a discussion with IOOF representatives about the issue in which this was said:

APRA noted that … investors of the CMT were in a neutral position and had not really benefited from the over-distribution per se. This was on the basis that investors were originally beneficially entitled to the interest in the capital asset, and the erroneous distribution of the capital asset as income meant that they simply received an asset that they were beneficially entitled to.

9.1.5 Discussion – The alleged CMT Overpayment breaches

216 One fundamental problem with APRA’s case is that it assumes that far too much can be inferred from two documents created years after the events in question for a particular purpose (an investigation into the causes of the CMT Overpayment relying on the accumulation of hindsight wisdom over nearly four years) and by a particular person (Mr Rossitto) who was implicated in the error if only by reason of his position as Head of Investment & Accounting Services - Finance.

217 The first document, dated 18 October 2013, prepared by Mr Rossitto and entitled “Response to the Investigating Officer on the Whistleblower Disclosure Report” does say that “our review” concluded the root causes of the error were as APRA identified. But whether these root causes could have been reasonably known about and acted upon in 2009 is entirely unclear on the evidence. Similarly, as to the second document and Mr Rossitto’s comment that a “yield analysis of TPS cash account disbursement should have picked this up”, I do not know whether a yield analysis was routinely performed or not, whether any such analysis was performed and should have disclosed the error but itself contained an error, what a yield analysis involved, or whether it was reasonable in all the circumstances for a yield analysis to have been performed.

218 To continue on this theme, I do not know:

(1) why NAB made the error it did;

(2) if there was any reasonable means by which Questor, in any of its capacities, could have discovered the error at the time it was communicated by NAB. As noted above, while Mr Rossitto in 2015 referred to a yield analysis as a means of detecting the error I do not know what this would have involved, nor whether it was required to be performed or was routinely being performed or was never performed in 2009. What is apparent is that Mr Rossitto’s 2013 root cause analysis does not refer to any failure to perform a yield analysis or suggest that one was routinely performed at this time or should have been performed. I also do not know if Mr Rossitto’s assertion that a yield analysis would have revealed the error is correct. The error was subsequently detected by a full reconciliation of the accounts carried out by the proposed new custodian but there is no way of knowing that a yield analysis as proposed by Mr Rossitto would in fact have detected the error. At its highest, Mr Rossitto believed this to be so but there is nothing in the evidence suggesting the exercise had been done as he proposed and did disclose the error. The evidence is left at the level of an after the event assertion in the form of a comment in passing about one aspect of a draft report to the board more than five years after the event;

(3) what Mr Youds did and did not do, nor what he was required to do and thus I have no idea what IOOF Service Co did for Questor in either of its capacities or what it was required to do;

(4) any of the 6 matters identified by the respondents as crucial to identifying any act of default or negligence by Questor as superannuation trustee as set out above; or

(5) any of the other matters which the respondents identified as the subject of lack of evidence.

219 APRA appears to assume that the many gaps in the evidence are filled by the documents brought into existence years after the event, but this is not so. Characterising statements in the documents as admissions against interest by Questor (and perhaps by IOOF Service Co, that being unclear on APRA’s submissions) is of little assistance. The so-called admissions are nothing more than the result of four years of hindsight made by a person who carried out a review (the details of which are unknown) and had a personal interest in deflecting any criticism from himself in an internal investigation focussing largely on his actions (if such criticism would have been justified, a fact I also do not know anything about). As the respondents submitted, the author, Mr Rossitto, would have had an interest in deflecting responsibility to systems and processes. The relevant systems and processes themselves remain a mystery. It is impossible to ascertain whether Questor as RE or as RSE or IOOF Service Co fell short of the standard of care given these evidentiary gaps. As such, to the extent that the documents contain any admissions against interest they are of little utility. They provide no evidence of the kind that would be expected from a party seeking to establish the existence of reasonably arguable causes of action for liability against NAB, IOOF Service Co and Questor.

220 Aspects of the submissions of the fourth to seventh respondents may be conveniently adopted in this regard:

(1) “First and most significantly, the documents say nothing about the specific matters which APRA must prove to establish the pleaded elements of this breach. In particular, they reveal nothing about what IOOF Service Co is actually alleged to have done in relation to the receipt of distributions from the CMT, or as to the ‘appropriate’ control testing and/or auditing, monitoring which it is said Questor as RSE ought to have performed of those service provided to it by IOOF Service Co.”

(2) “The opinions expressed by Mr Rossitto in his 18 October document, which APRA now seeks to rely upon, are expressed at such a level of generality to be of little assistance to the Court in assessing whether Questor and IOOF Service Co breached their obligations to exercise due care and skill. For example, it is not clear whether the ‘gap’ or ‘root causes’ identified by Mr Rossitto are attributable to Questor as RE, Questor as RSE, IOOF Service Co as a service provider to the RE, IOOF Service Co as a service provider to the RSE, NAB or a combination of these entities. Similarly, it is not apparent from Mr Rossitto’s document how he says that the ‘gap’ or ‘root causes’ caused or contributed in the requisite sense to the CMT Overpayment. Indeed, it is not even clear from Mr Rossitto’s 18 October document what he says was the ‘gap’ in Questor or IIML’s processes.”

(3) “Mr Rossitto’s 18 October document should be treated with caution given that it was prepared by him in response to a whistleblower investigation looking at the appropriateness of his conduct. It is only natural that someone in Mr Rossitto’s position would seek to deflect some of the blame on to operational processes and procedures.”

(4) “At best, Mr Rossitto’s 18 October document represents the views of a manager in IOOF’s Investment and Accounting Services Team. There is no evidence that Mr Rossitto possessed any of the requisite skills, qualifications or experience required to undertake reviews for the purposes of identifying process gaps or root causes of incidents like the CMT Overpayment.”

(5) “Mr Rossitto prepared his 18 October document more than four years after the CMT Overpayment occurred. There is no evidence that Mr Rossitto had any involvement in the events leading up and immediately following the CMT Overpayment. It is a hindsight review, prepared by a person who is not a lawyer, and who was not analysing the issue from the perspective of, and in accordance with the standards applicable to, the legal covenant of due care, skill and diligence.”

(6) “There are obvious limitations on the ‘review’ undertaken by Mr Rossitto. As Mr Rossitto himself records at the bottom of page one of his 18 October document, his conclusions regarding the adequacy of Questor’s processes and the root cause of the overpayment were based on a review of a limited set out documents. It is not clear what information those documents actually contain. None of those documents appear to be in evidence before the Court. Moreover, Mr Rossitto’s opinions were expressed without having spoken to or questioned Mr Youds who authorised the CMT Overpayment. This shortcoming creates obvious deficiencies in Mr Rossitto’s account. For example, it is not clear how Mr Rossitto concluded that the root cause of the overpayment involved a ‘poor understanding of source documents and reports supplied by external parties’ when he had not spoken with the employee involved in authorising the CMT Overpayment. Similarly, it appears (and certainly there is no evidence of this) that Mr Rossitto’s opinions were expressed without reviewing or having any regard to any of the agreements governing the relationships between NAB, the RE, the RSE and its members (that is the Custody Agreement, the CMT Constitution and the Services Agreement, the TPS Trust Deed and the relevant PDSs). These documents define the responsibilities and obligations of the relevant parties. It would be difficult, if not impossible, for Mr Rossitto to reliably express an opinion about the adequacy of Questor’s processes and systems without first understanding what precisely Questor, NAB and IOOF Service Co were required to do in the relevant contractual framework.”

(7) “Mr Rossitto’s claim in his 18 October document that he had identified the ‘root cause’ of the CMT Overpayment was subsequently rejected by Rob Urwin, Head of Risk, who was investigating the whistleblower complaint. In his report dated 20 October 2015, Mr Urwin noted that ‘[m]anagement failed to identify the root cause which led to the incident’.”

221 In respect of Mr Rossitto’s bubble comment on the draft board paper of 16 October, the fourth to seventh respondents said the same limitations applied. Further, as these submissions put it in terms with which I agree:

…it is impossible to know what Mr Rossitto intended to assert by the representation in the second sentence that a yield analysis “should” have detected the error. This opinion raises more questions than it answers. For example, did he mean that a yield analysis was undertaken by Mr Youds, but for some unidentified reason he did not detect the error? Or did he mean that if Mr Youds had undertaken a yield analysis, the error would have been identified? In any event, what was a yield analysis and how might it have detected the error? Was it easy or difficult to perform? Was it an expensive and time-consuming process? These are just some of the unanswered questions raised by Mr Rossitto’s bubble comment relevant to assessing whether Questor had exercised due care and skill. They highlight the dangers of placing any reliance on Mr Rossitto’s bubble comment…

222 The inescapable conclusion is that the evidence on which APRA relied is an insufficient foundation from which to infer anything about liability for the CMT Overpayment except that if the overpayment caused loss to Questor or the beneficiaries of the TPS Super trust there would be a reasonable argument that NAB might be liable to reimburse that loss. I cannot be satisfied as to the existence of a reasonable argument of exposure to liability on the part of IOOF Service Co or Questor in any of its capacities. I am unable to infer from the evidence that, in fact, there would have been any such liability because of the lack of reliable evidence providing the details about who did what when and what they were required to do. The documents involving Mr Rossitto are not a substitute for evidence of the kind that would be required to establish a reasonably arguable exposure to liability on the part of IOOF Service Co and Questor.

223 As to NAB, I accept the respondents’ submissions on the alleged loss. In particular I accept that APRA’s case of loss is again based on a series of assumptions or, at best, mere speculation, none of which find a sufficient or indeed any foundation in the evidence. The evidence, as the respondents put it, does not prove that: (1) the overdistributed capital earned less outside the CMT than in it, (2) any beneficiary in fact incurred liabilities by reason of the overdistributed capital, (3) any person in fact paid too much for their units in the fund, or (4) if any person did suffer this kind of loss by overpayment, the amount of the overpayment. As the respondents said, there is no sound evidentiary basis to conclude that any claim against NAB had substance or value.

224 I otherwise accept the respondents’ submissions that Questor as RE was entitled to rely on the information from NAB as custodian by cl 16.4 of the CMT constitution. Further, there is insufficient evidence from which it would be inferred that Questor committed any default or negligence by relying, as it was entitled to do, on the information which NAB provided. On this basis there was no reasonably arguable case for Questor being liable to members for loss (if loss itself had been proved, which it was not). Accordingly, under cl 16.3 of the CMT constitution, Questor as RE was protected from liability to its members, there being no suggestion that Questor acted other than in good faith. For this reason the deeming provision in s 601FB(2) of the *Corporations Act* *2001* (Cth) is of no assistance to APRA; APRA has not proved any reasonable foundation for its assertion that Questor would not be protected from liability by cl 16.3.

225 I also accept that if Questor as RE had managed to identify any loss worth the effort of a claim against NAB, IOOF Service Co or itself, the available response would have been that the losses could and should be recouped from the overpaid members.

226 In short, to the extent that APRA’s case involved the CMT Overpayment giving rise to reasonably arguable cases for liability on the part of NAB, IOOF Service Co and Questor itself, I disagree. The evidence falls far short of disclosing the existence of such reasonably arguable cases. APRA bore the onus of proving the existence of the reasonably arguable cases for liability but has not discharged that onus. To the contrary, the respondents have proved that any claim against NAB, IOOF Service Co and Questor in respect of the CMT Overpayment would have been complex and fraught with difficulty. It does not matter if the respondents did or did not recognise the complexities and difficulties at the time. The complexities and difficulties existed and, it must be inferred, in all likelihood would have emerged if in 2009 claims had been made.

227 It also follows from the above discussion that I do not accept that APRA has proved that Questor in its capacity as trustee of TPS Super acted in breach of Questor’s Pre-2013 Due Care Covenant (as referred to in [233(b)(i)] of the ASOC) or had any liability for loss and damage pursuant to s 55(3) of the SIS Act (as referred to in [233(b)(ii)] of the ASOC). Using the terms in the ASOC, APRA has failed to prove Questor’s CMT Overpayment Breach.

###### 9.2 Step 2: The CMT Remediation Plan

228 APRA contended that in accepting the CMT Remediation Plan for itself as unitholder, and in considering and deciding to pass on the consequences of that plan to beneficiaries of TPS Super who had invested in the CMT and thereafter implementing that decision, Questor breached its Pre-2013 Best Interests Covenant, Questor’s Best Interests Covenant (post 1 July 2013) and Questor’s Conflicts Covenant.

9.2.1 Background facts

229 The following summary is taken from the submissions of the parties.

230 Questor discovered the CMT overpayment in February 2010. As APRA said:

In September 2011, the Fund Accounting Team (of which Mr Rossitto was the head) determined to resolve the accounting issue at the RE level by writing down the   
$6.16 m asset on its books and “diluting” distributions paid from the CMT (the **CMT Remediation Plan**).

231 As a result, under the direction of Mr Rossitto Questor, in its capacity as RE of the TPS MIS and as licensee and trustee of TPS Super, diluted the quarterly distributions made to investors and beneficiaries in respect of the CMT. These diluted distributions were not only imposed on investors in the TPS MIS and beneficiaries of TPS Super who had received a share of the CMT overpayment, but also investors and beneficiaries who joined after June 2009 and had received no part of the CMT overpayment. The members were not notified of this dilution to their allocations.

232 APRA identified what is known about these actions as follows:

(a) On 7 September 2011, Mr Steven Sorraghan (Fund Accounting Manager) asked BNP Paribas to advise how long it would take to write down a $6m asset from the CMT if the daily yield was reduced by 0.10% (p. 255\_0064);

(b) On the same day, BNP Paribas responded that this would take about 5.5 years (p. 255\_0063);

(c) On 23 September 2011, Mr Sorraghan asked BNP Paribas to commence writing down the asset by $6,000 a day (approx. 0.20% impact on the yield),

(CB 2/8E).

Mr Rossitto later confirmed that the decision to amortise the asset was made by him. He made this without any ratification by any internal committee (CB 2/9A, p. 266\_001) and that he had not sought “sign off” on the decision “[g]iven our flat structures and desire to get on with business” (CB 3/29A, p. 617\_0001). He further indicated that “David C [Coulter] was updated as developments occurred” (CB 3/29A, p. 617\_0001).

233 The plan was thus implemented by Mr Rossitto in September 2011 and continued for a year under his auspices.

234 The first reliable evidence of the plan coming to the notice of one of the individual respondents is dated 17 September 2012, 12 months after the plan had been implemented. On that day, Mr Coulter received a covering paper to the Annual Financial Reports which Mr Coulter was required to endorse which disclosed that:

The Cash Management Fund has in its statement of comprehensive income a amortisation expense of $1.6 million. In May 2009 an over distribution was calculated by National Asset servicing (NAS) [NAB] and approved by Questor Fund Accounting department for $6.3 million.

During the 2012 financial year we have been in lengthy discussions with NAS and BNP Paribas regarding the over distribution, the creation of the asset representing the over distributed amount and the subsequent transfer to BNP in 2010.

As the Portfolio Service (TPS) is the sole investor in the Cash Management Fund, the best course of action was to amortise the asset off over a three year period. This ensures minimum impact on the Cash Management Fund’s daily yields and on TPS’ quarterly cash account distribution to unit holders.

235 On 19 September 2012, Mr Rossitto sent Mr Coulter an email in which, as APRA put it:

(a) Mr Rossitto emailed Coulter and asked him whether “Chris K” (Kelaher) was aware of the issue. Coulter replied: “Chris has no explicit briefing on it other than to say ‘we’re handling it’”: CB 2/9A, p. 266\_001.

(b) Mr Rossitto further explained to Coulter that:

“New investors coming into the TPS get a diluted distribution, we need to cover this issue for TPS RF [Retirement Fund, i.e. TPS Super] and compliance SIS sign off in the coming weeks. It’s likely that these investors would need to be compensated”.

(c) Coulter replied “HOW MUCH?.

(d) Mr Rossitto also told Coulter that he would probably need to speak to NAB as they should pay “a portion” of any compensation “seeing as it was their mistake which QFSL [Questor] signed off on”.

236 Further, on 21 September 2012, Mr Rossitto completed an “Issue Notification Form” concerning the CMT overpayment and CMT Remediation Plan which he reported to IOOF Compliance (copying Mr Coulter): CB, 2/10, p. 267. The notification identified the background to the CMT Overpayment and that it had had “[p]ositive impact on exited clients, negative impact on new investors via a diluted distribution to be assessed for materiality”   
(p. 269). Mr Rossitto also identified that there was potential compensation to be paid to the superannuation beneficiaries which was unquantified at the time. In a separate document, not emailed to Mr Coulter (a fact which APRA overlooks), APRA said that “Rossitto identified that the overdistribution was a breach of Questor’s compliance plan and its obligations under s 601FC(1)(h), 601FC(1)(i) and 912A(1)(b) (p. 271)”. This is an overstatement. Mr Rossitto identified that there was an issue under these provisions but did not express any conclusions about breach.

237 The report to the Questor board for the meeting on 25 September 2012 to approve the annual accounts included the following:

We wish to bring the following note to the Directors attention:

The Cash Management Fund has in its statement of comprehensive income a amortisation expense of $1.6 million. In May 2009 an over distribution was calculated by National Asset Servicing (NAS) and approved by the Questor Fund Accounting department for $6.3 million.

During the 2012 financial year we have been in lengthy discussions with NAS and BNP Paribas regarding the over distribution, the creation of the asset representing the over distributed amount and the subsequent transfer to BNP in 2010.

As the Portfolio Service (TPS) is the sole investor in the Cash Management Fund, the best course of action was to amortise the asset off over a three year period. This ensures minimal impact on the Cash Management Fund’s daily yields and on TPS’s quarterly cash account distribution to unit holders.

238 The Questor board met on 25 September 2012: CB 2/11, p. 275. Mr Kelaher and Mr Venardos attended the meeting (despite the minutes not recording the attendance of Mr Venardos). APRA noted that at the meeting (the principal object of which was to approve the annual financial reports):

(a) The Board noted that Questor’s auditors, KPMG, would be issuing a qualified compliance plan audit opinion because of the CMT Overpayment issue;

(b) Venardos asked the question “who wears the costs associated with this potential breach”.

(c) Coulter responded that “the member would not be impacted and it was a decision between the Custodian and the company who wears the costs”.

(d) Mr Rossitto, however, further clarified that that “the issue is essentially one where an incoming member to TPS post the breach will have received a diluted distribution”.

239 The minutes of the board meeting record (CB 2/11 p. 276):

The Board noted that Thomas Robertson Head of Compliance is currently reviewing the auditor’s position to determine whether the breach highlighted is reportable. The Board queried why this is not reportable. Mr Rossitto stated that Mr Robertson will investigate the impact of the potential breach having occurred in 2009 where the compliance plan controls were different from the current compliance plan requirements. It is therefore arguable that the current compliance plan has been adhered to and the 2009 compliance plan has not.

Mr Venardos asked who wears the costs associated with this potential breach. Mr Coulter advised the member would not be impacted and it was a decision between the Custodian and the company who wears the costs. Mr Coulter advised management is currently undertaking an assessment to establish how many members are adversely affected. This is an extensive data mining exercise. Mr Rossitto added that the issue is essentially one where an incoming member to TPS post the breach will have received a diluted distribution.

240 Questor notified ASIC of the over distribution on 5 October 2012 noting that:

The Fund over distributed to 2 internal unit holders $6.16 Million in May 2009. In February 2010 master custody was transferred from NAB to BNP, transfer completed and signed off by internal and external Parties. Doubts were raised as to the existence of an asset which started the investigation process. The over distribution was authorised by internal fund accounting staff at the time of the error.

241 The description of the licensee’s rectification of the breaches reported referred to a need to determine the nature and extent of any compensation required.

242 In September 2013 IOOF received the whistleblower report which identified that management was “reducing the rate of return in respect of the cash fund of the Questor product in order to recover an earlier over distribution, to the detriment of retail investors who were not members of the fund at the time of the over distribution”. The internal investigation then commenced. Mr Rossitto provided his report of 18 October 2013 in response to this investigation. In this document, in addition to the matters already noted, Mr Rossitto said that:

There is no specific “sign off” form on the decision taken or email, suffice to say that decisions are made every day on current and historical issues, breaches, incidents, staffing, good value claims etc. It is in the best interests of members that we determine appropriate courses of action, taking into account alternative strategies. These strategies were discussed internally amongst Investment and Fund Accounting professionals.

Given the historical nature of the issue and the timeframes required to implement accurate and robust rectification, we felt that it was in the best interests of members that the most appropriate course of action was that as advised to ASIC.

During the course of the investigation the Head of Investment and Accounting Services met with the CEO Bridges and Questor’s legal representative; another alternative was discussed at this meeting. The CFO was updated as developments occurred.

The alternate methods considered are summarised as follows:

* Full write off of the amount was considered when it was confirmed that there was an error in the May 2009 TWT CMT’s distribution. Whilst a full write off may have been appropriate for the TWT CMT, a full write off in TPS would have diluted the cash return by approximately 45% for the quarter. At this point in time the investigation was still ongoing and further discussions were required with NCS. We considered it imprudent and not in the members’ best interests to adjust the distribution as there was still further analysis to be done and a full rectification plan to be put in place.
* A suggestion was made that a charge be made against TPS members, as allowed under the PDS and Trust deed, of the over distributed amount and then pay TPS to offset the full write off amount. This method would not affect TPS cash distribution rates struck or distribution amounts. We did not consider nor pursue this course of action as it was felt not to be in the members’ best interests.
* Have NCS pay the full amount to cover the full write off. This may still be an option however consideration needs to be given to (1) Questor’s approval to distribute (2) roles and responsibilities as they apply to the SLA (3) NCS see TPS as one unit holder, therefore their preferred course of action was to adjust the distribution downwards in the TWT CMT once the error was acknowledged. As TPS was, and remains the major unitholder, the underpayment balanced out the overpayment therefore no compensation would be payable.

The issue remains on NAS’s Risk Register. NAS appear to be open to negotiations on compensation amounts payable to new TPS members entering the fund, on a see through basis, who have received a diluted distribution as detailed in our correspondence to ASIC.

As outlined in the letter to ASIC of 17 January 2013, the preferred approach was to write back the distribution over a three year period ending September 2014. The write off, in percentage terms, amounts to 0.2% per annum on the TPS book’s cash distribution. The methodology adopted was seen as causing minimal disruption to TPS members and the business whilst allowing sufficient time to source and analyse data out of the Pathfinder system, determine how a bulk good value claim could be processed and to determine appropriate communication strategies once the extent of new members entering the fund was known. To act, by way of implementing an immediate full write off, without proper thought to all issues and incomplete analysis on how to best correct the error may have led to erroneous redistribution / recovery without the correction being managed in a planned, controlled and accurate manner. The communication to ASIC stated that we would be assessing the merits of reducing the time horizon. We plan to recommend that the end date be 30 June 2014 being an appropriate financial year end cut-off date. The formula, as outlined in the letter to ASIC, will be used to pay compensation to members who have received a diluted distribution and will be funded by Questor.’ (CB 620\_0003 – 620\_0004).

…

As previously advised there is no specific communication approving the method employed suffice to say that decisions are made every day on current and historical issues, breaches, incidents, staffing, good value claims etc, the most recent being the clearance of 2005/2006 issues from the Questor incident and breach register. Our focus, in any rectification, is to ensure that current and exited members are treated fairly and equitably and any decisions made are in their best interests.

Historical issues are dealt with to the best of our ability and at the least inconvenience and best value to members. (CB 620\_0004).

243 The report from the internal investigation was completed by 20 October 2013 and submitted to Mr Riordan. The report recommended “a further assessment of the impact on members and compensation and if required, reporting to APRA”: CB 3/30A p. 619\_0001.

244 At the Questor board meeting on 28 October 2013 the matter was discussed, the minutes recording as follows (CB3/32A p. 629\_0003):

The Board noted the update on the cash management fund over distribution first reported to the Board in October 2012. The Board noted as set out in the business arising that a whistle blower notification has been investigated by Risk and a report has been finalised and is with the Group General Counsel. The Board noted from the report that at the very least the following action will be required:

a) a further assessment of the impact on members and proposed compensation. This review will be brought forward instead of waiting for the 3 year period to lapse to ensure the right level of exposure is identified which takes into account the entry and exit of members and the amount of compensation;

b) an update to procedures to conduct ongoing impact assessments for incidents that have an ongoing rectification process;

c) reporting of outstanding breaches including age analysis greater than 90 days; and

d) a communication strategy with members.

245 On 24 March 2014 the Questor board met. Included in the papers was an extract from the IOOF Hold Co board report for the March 2014 meeting (CB4/36 p. 660):

As noted previously, we reported to ASIC on 5 October 2012 a significant breach of the Corporations Act due to a distribution being incorrectly classified as an asset in May 2009 resulting in an over-distribution to two internal unit holders. We await a response to our last letter to ASIC sent in January 2013 answering their questions and our offer to meet and discuss any issues.

Other internal activity, as previously reported, is continuing and includes reducing the “write off” time period (presently September 2014) to bring this issue to a close. Further, the ORFR is established for incidents like this (the effect on TPS RF receiving diluted distributions) and we will consider its application once development is completed (between March and June 2014). Legal advice has been sought to confirm its application. A meeting with the NAB to commence discussions on recouping some of the cost which can be paid into the ORFR occurred in February ’14 and we have been invited to submit a compensation claim; there is no admission of liability at this time.

246 The minutes of the meeting of Questor’s borad record:

1. Breach – CMT over-distribution: The Board noted an update is included in the Legal Compliance & Risk Report advising internal activity is continuing and includes the write-off time period (presently September 2014) to bring this issue to a close.

The Board noted the ORFR is established for incidents like this (i.e. the effect on TPS RR receiving diluted distributions) and management will consider its application once development is completed.

The Board noted management has met with NAB to commence discussions on recouping some of the costs which can be paid into the ORFR.

247 On 13 May 2014 Questor wrote to NAB seeking compensation, saying:

Our focus in any rectification action is to ensure that current and exited members of the TPS Funds are treated fairly and equitably and that any decisions made are in their best interests in accordance with the relevant regulatory requirements. In doing so, we determined that the most appropriate rectification action was for Questor to write back the over distribution over a three year period ending 30 September 2014. We have since modified this period by bringing it 3 months forward to end on 30 June 2014. Compensation will be required to be paid on a “see through basis” to any new investors who invested in the TPS Funds after June 2009 and received a diluted distribution resulting from the Scheme’s write off.

As at 31 March 2014, we have calculated the amount to be compensated to affected members at $1.192 million (note this amount is likely to increase as at 30 June 2014). Compensation has been calculated by reference to the following formula:

(A / B) x C = Compensation amount

Where:

A = Distribution received by Member

B = Distribution paid by the Scheme

C = Write off amount of distribution

The attached spreadsheet contains more information in relation to the breakdown for the compensation calculation.

The IOOF group has enjoyed a long standing relationship with NCS and we look forward to it continuing and growing further as our business expands. If there are any positives to take from the Incident, it is that both parties will have more robust investment and compliance frameworks going forward to prevent a recurrence. Ensuring those members affected by the Incident are not adversely affected remains the core outstanding issue that Questor needs to resolve with the NAB before we can notify ASIC that the breach has been closed in accordance with our Rectification Plan.

Although Questor does not absolve itself of its part in the Incident having occurred, we consider that NCS as custodian breached its duties under the Agreement by failing to exercise the requisite standard of care owed to Questor as a client and also by not having in place effective internal controls that should have detected the Incident. In this respect, we are seeking compensation from the NAB so that Questor can write back the over distribution and ensure the affected members of the TPS Funds are not adversely impacted by the Incident. The final amount of compensation will be confirmed by us as at 30 June 2014, which is the time of the next quarterly cash account distribution.

248 At a meeting of the Questor board on 26 May 2014 the report to the board records:

The Board was previously notified of this material breach which was reported to ASIC. Questor has since issued a letter to NAB, claiming compensation in relation to the over-distribution of scheme assets that occurred in May 2009. The basis of the compensation claim is that NAB as custodian breached its duties under the Custody Agreement by failing to exercise the requisite standard of owed to Questor as a client and also by not having in place effective internal controls that should have detected the error. If successful, the compensation will be used to write back the over-distribution and ensure the affected members are not adversely impacted. The final amount of compensation will be confirmed as at 30 June 2014, which is the time of the next quarterly cash account distribution. It is noted that the Responsible Entity of the Cash Management Fund has been IIML since 1 January 2014.

249 The minutes of the board meeting record:

The Board noted they had discussed the Cash Management Fund over-distribution breach. The Board noted Questor has issued a letter to NAB claiming compensation in relation to the over distribution of scheme assets that occurred in May 2009. It was noted if this is successful the compensation will be used to write back the over distribution and ensure the affected members are not adversely impacted.

250 At a further Questor board meeting on 18 August 2014 the minutes of the meeting record:

The Board noted that on 4 August 2014 NAB had requested further information to calculate its share of compensation. The compensation will be used to write back the over-distribution and ensure the affected members are not adversely impacted. Once the compensation is calculated management will communicate to the circa 9000 affected members.

251 On 22 August 2014 Questor engaged Ernst & Young to assess Questor’s compensation calculations. Ernst & Young provided its remediation report to Questor on 10 December 2014. Questor provided that report to NAB. On 23 March 2015 NAB responded to the effect that it would pay $1.565 million in compensation representing 50% of the amount identified as required to compensate beneficiaries in the Ernst & Young report.

252 APRA noted that the dilution of distributions to beneficiaries continued until 2014. It said that the board and IOOF’s risk and compliance committee (or **RCC**), which Mr Venardos chaired, were updated about progress about the CMT over distribution and the remediation plan. APRA provided a table summarising these updates which is reproduced below.

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | **Date** | **CB** | **Board meeting** | **CMT discussed** | **Summary of discussion** |
| 1 | 24/9/12 | 2/11 | Questor | Yes. | First disclosed to Board. |
| 2 | 29/10/12 | 2/14 | Questor | Yes. | Breach “noted”. |
| 3 | 25/3/13 | 3/21 | Questor | Yes. | ASIC letter “noted”. |
| 4 | 22/4/13 | 3/23A | RCC | Yes. | CMT described as “issue relating to an accounting entry (not actual loss)”. |
| 5 | 26/9/13 | 3/32E | RCC | Yes. | Discuss whistleblower report; note consideration to be given to new members; not issue of timing but “[o]nce escalated, the breach was assessed and reported to ASIC promptly”. |
| 6 | 28/10/13 | 3/32A | Questor | Yes. | Whistleblower investigation “noted”; further assessment of impact on members and compensation to be undertaken |
| 7 | 2/12/13 | 4/32F | Questor | No. | Convened to consider change of RE for CMT, from Questor to IIML. |
| 8 | 24/3/14 | 4/39 | Questor | Yes. | ORFR “is established for incidents like this”; management has met with NAB |
| 9 | 28/4/14 | 5/42A | RCC | Yes. | Group Legal working on a claim against NAB seeking 100% recovery. |
| 10 | 26/5/14 | 5/43A | Questor | Yes. | Note that Questor has issued letter to NAB; compensation will be used to “write back” over distribution. |
| 11 | 29/7/14 | 9/163 | RCC | No. |  |
| 12 | 18/8/14 | 5/52 | Questor | Yes. | Note that NAB has requested further information; circa 9000 affected members. |
| 13 | 25/9/14 | 5/67 | RCC | No. | Brief CMT update in report: Tab 66, p. 1446. |
| 14 | 27/10/14 | 5/70 | Questor | Yes. | Board asks for update from Riordan on meeting with NAB (no other update at this meeting) |
| 15 | 1/12/14 | 5/70I | RCC | No. |  |

253 A report to the meeting of the board of IOOF Hold Co on 15 May 2015 contained the following:

Cash Management Fund over-distribution – Questor

From previous updates, the Board would be aware that Questor has been negotiating a settlement with NAB Asset Servicing (NAS) in relation to their part for failing to identify an error that resulted in loss to members. NAS offered to pay 50% of the loss amount, which we accepted and that amount has been paid.

We propose to use the ORFR to fund the other 50% of the loss amount (approximately $1.6m), which will be made good from the Questor general reserve. Affected members will now be reimbursed for any loss suffered. As this incident was treated as a reportable breach, ASIC will be notified once our rectification plan has been completed.

254 Between March and September 2015 officers gave consideration to issues relating to the compensation of beneficiaries including taxation issues.

255 On 10 and 11 September 2015 Mr Rossitto and Mr Coulter communicated about the compensation by email. Mr Rossitto said:

You would have received notification that the Questor CMT Breach for TPS IDPS investors has now been executed.

The amount required to be transferred to TPS is $392,400. Can you please authorise the transfer of $392,400 from QFSL to TPS Personal Investment Plan.

There are two proposals below, we are only addressing IDPS at this stage. The options are (1) Use NAB monies to fund (2) use QFSL monies to fund (existing provision) (3) combination of both.

Alternatively, a decision on the allocation in QFSL’s books can be made once a ruling from the ATO is received in relation to superannuation and pension members.

Please note the following:

* We advised ASIC that QFSL would pay however this was before the introduction ofthe ORFR (superannuation & pension)
* There are ongoing discussions and queries with APRA on the use of the ORFR (superannuation & pension)

The latest note from Paul’s APRA meeting is as follows:

Use of the ORFR

IIML and Questor are intending to use the ORFR reserves held within the RSEs to compensate members for three active breaches. APRA reiterated its expectation that whilst the ORFR may be used to compensate members in the first instance, IIML and Questor still have an obligation to pursue sources for compensation. APRA has not observed adequate consideration of all sources for funding the compensation payable to members and notes that IIML and Questor are, in one instance, seeking to compensate members of the superannuation funds via the ORFR for an error that occurred within the managed investment scheme in which the RSEs invest.

In relation to the item highlighted, we saw this as 2 separate breaches / incidents and reported as such.

256 Mr Coulter responded “Approved and use NAB please”.

257 The IOOF Legal, Risk and Compliance Report for September 2015 records that “compensation payments amounting to $391k were made to 4,102 to IDPS and managed investment scheme investors…”.

258 On 16 October 2015, a paper prepared by Mr Rossitto and Ms Clark (a lawyer) to the Questor board said:

3. Compensation

Questor’s focus is to ensure that any current or exited members of the TPS Funds are treated fairly and equitably and that decisions are made in members’ best interests. Therefore, it was determined that the most appropriate course of action was to write-back the over-distribution over a three-year period (ending 30 June 2014).

In order to curtail the effect of the diluted distribution on members who invested in the TPS Funds post June 2009, Questor determined to compensate those members on a “see through” basis by increasing their distributions to what they would have received had the error and subsequent write-back never occurred…

4. Sources of compensation

4.1 Damages sought from third parties

As set out above, the error arose because of NCS’s failed monitoring and reconciliation processes. The compensation amount settled between Questor and NCS (and passed onto TRF) is considered acceptable on commercial and legal terms.

…

4.4 General reserves

Management recommends that a portion of TPS’s general reserve be used to top up the diluted distribution (and therefore compensate TRF members).

The Questor Reserves Policy (2014) provides that the general reserve may be used for any purpose that the Trustee deems appropriate….

…

APRA SPG 222 – Management of Reserves provides the following:

“The reserves of an RSE are typically regarded as monies forming part of the net assets of the RSE that have been set aside for a clearly stated purpose. Reserves are largely concerned with contingent events and, as such, APRA expects that an RSE licensee would exercise judgment in determining the need for them, their scope, size and operation. A prudent RSE licensee would also have robust and transparent policies and processes for the management of any reserves within an RSE.”

APRA also acknowledges that reserves can be maintained for “a number of different purposes” and does not exclude the use of reserves to compensate fund loss.

It is appropriate for Questor to utilise the general reserve in the circumstances described above as Questor has explored all other viable sources of compensation and the proposal accords with the TRF governing rules and Reserves Policy.

…

The Questor Board is requested to approve:

* the payment of compensation to TRF members impacted by the breach, to the value of $2.775 million plus an accrued interest component of $13,875 calculated to 30 September 2015;
* the compensation described above to be sourced from:
* he remaining proceeds of the settlement between National Custodian Services (NCS) and Questor, being $1.173million; and
* the shortfall to be returned from the TRF general reserve, being $1.616million.

259 The Legal, Risk & Compliance report for the Questor board meeting on 28 October 2015 said:

Compensation payments amounting to $391,000 were made to 4,102 to IDPS and managed investment scheme investors on 10 September 2015 and letters have now also been sent advising the investors of the payment. The Operations team has also written to investors with closed accounts asking for their bank details, so that their compensation can also be paid. No complaints have been received to date.

The payment of the compensation to the superannuation and pension members is on hold pending the outcome of our application to the Australian Taxation Office (ATO) for a private ruling allowing Questor to treat compensation payments as non-concessional contributions.

Proposals for completion of this matter are set out in a separate paper to the Board.

260 The minutes of the meeting of the Questor board on 28 October 2015 record:

**5.2 Questor CMT Over-Distribution Breach**

The Board noted the high level summary of the breach which was notified in 2012 and the proposed rectification strategy and source of compensation.

The Board considered the rectification strategy and questioned why the interest is being calculated to 30 September 2015 and not up until the date of actual payment. The Managing Director advised that this was for demonstration purposes and agreed that any interest paid wold be calculated up until the date of payment.

The Board queried how ex members would be remediated. The Managing Director advised there is a project being undertaken to identify the location of all ex members which have been impacted.

**Resolved** to approve the payment of compensation to TRF members impacted by the breach to the value of $2.775 million plus an accrued interest component to be calculated up until the date of payment.

**Resolved** that the compensation described above is to be sourced from the remaining proceeds of settlement between National Custodian Services and Questor being $1.173 million and the shortfall to be sourced from the TRF general reserve being $1.616 million.

261 By 30 April 2016 Questor had completed its compensation payments to the members of TPS Super who had been adversely affected by the remediation plan. The Legal, Risk and Compliance report for May 2016 records:

On 30 April 2016 compensation payments amounting to $2,528,825 were made to 21,197 members, with open accounts, in The Portfolio Service Retirement Fund (TPSRF). The compensation amount is to be treated as taxable income.

Where the compensation amount was less than 5% of the member's account balance at the time of the payment, it was funded by both the money received from NCS who contributed to the error, and the general reserves. Where the compensation amount was greater than 5% of the member’s account balance at the time of the payment, it was funded by NCS monies only to ensure a non-concessional contribution Impact did not occur.

The IDPS and managed investment scheme investors were compensated in September 2015. The remaining rectification action is to compensate 2081 TPSRF members with closed accounts. The compensation due to these members is approximately $295,557. These members will be compensated following the completion of the SFT.

262 In June 2016 there was a successor fund transfer of members of TPS Super to IPS Super.

263 On 18 August 2016 Questor provided APRA with a report on its decisions with respect to the over distribution, the remediation plan and the payment of compensation.

264 On 12 December 2016 APRA wrote to Questor stating:

APRA is of the view that the use of TPS Super Fund general reserve monies to compensate TPS Super Fund members for a loss caused by Questor as RE of the CMT is inappropriate.

In acting in the best interests of TPS Super fund members, APRA expects that Questor will:

1. Immediately replenish TPS Super Fund’s general reserve utilising funds from Questor as RE, to replace the full amount paid to TPS Super Fund members as compensation for the losses suffered as a result of the Remediation Plan; and

2. Provide a copy of its plan to replenish TPS Super Fund’s general reserve to APRA prior to any funds being transferred.

A failure by Questor to appropriately replenish TPS Super Fund’s general reserve will escalate APRA’s 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.

265 An internal APRA document of 13 April 2017 recorded that:

Questor recognised at an early stage that the Remediation Plan would disadvantage members of the TPS Super Fund who joined after the over-distribution was made (the New Members). The New Members were disadvantaged because, whilst they did not receive funds paid via the over-distribution, their CMT distributions were reduced to claw back the over-distributed funds.

…

At the commencement or at an early stage in the Remediation Plan, Questor devised a compensation methodology to apply at the Remediation Plan conclusion to calculate the amount due to each affected member.

266 The same document recorded that:

Questor RSEL advised that section 2.2.2 of the IOOF Reserves policy states:

The reserve may be utilised for any purpose that the Trustee deems appropriate and within the parameters disclosed by the Funds’ Trust Deeds. For example, but not limited to:

* Purchase of Frozen Funds from nominal member accounts;
* Transfers to other reserves;
* Payment of compensation to members; and
* Payment of operational and regulatory expenses (i.e. APRA Levy, Audit Fee etc.).

Questor RSEL further advised that the source of the reserves is not attributable to any individual member or even a particular group of members. It argued that as it had a means of compensating for the loss (from TPS Super Fund reserves) without inflicting further cost to the TPS Super Fund (e.g. cost of litigating against a third party), and held reserves for such purposes (as articulated in the Reserves Policy) in line with TPS Super Fund’s trust deed, it was an appropriate commercial and prudential decision to agree to use the reserves to restore members to their rightful financial positions.

It also contends that such a decision does not mean that it was not prioritising TPS Super Fund members’ interests in accordance with its obligations under the SIS Act - rather, it was making a commercial decision with all other parties to the dispute, which was in members’ interests, in order to avoid costly and prolonged litigation. APRA notes that Questor RSEL’s primary duty and priority is to the members of the TPS Super Fund.

39. Small quantum for members

The $1.616m utilised from TPS Super Fund’s general reserve may appear to not be a material amount as it represents 0.03% of the total assets of TPS Super Fund of $6.1bn as at 31/3/2016. APRA’s response to this argument would be that any monies taken from the TPS Super Fund, as a direct consequence of the actions of a related party in advancing its interests, is material and should be compensated.

…

43. Manage conflicts management and governance issues through ongoing supervision

Frontline advise that they will pursue the conflict and governance issues surrounding this matter through ongoing supervisory activities. They have made some progress in improving governance and conflicts through interactions with the board and directors, and have also secured a change in the APRA Regulated Entity boards to include two new non-executive directors who are not on the IOOF ASX listed company board. As part of Frontline’s ongoing supervision strategy they have planned and booked a review of the conflict framework, thematic governance and related parties for late May 2017. The good results being yielded through the above ongoing supervision of these issues outweigh the benefits of making further enquiries to determine whether any conduct issues have arisen in relation to this matter.

267 The document concluded that:

Recommendation

47. When weighing up the factors for pursuing this matter against the counter arguments, we consider that APRA should pursue the replenishment of the TPS Super Fund general reserve if it does not voluntarily occur.

A prudent RSE licensee would have discharged its trustee responsibilities under section 52 of the SIS Act and managed it conflicts by seeking compensation from a related party who caused and or contributed to the loss incurred by its fund. In this case Questor RE’s actions contributed to the remediation and compensation plans disadvantaging TPS Super Fund members. This matter is distinguishable from operational losses such as unit pricing errors which are typically due to errors. There was no operational error by Questor as RE.

While Questor RSEL may have a legal basis to support its decision to access the general reserve, a prudent trustee would have reasonably first sought compensation from Questor RE, which was the party that caused and or contributed to the loss to its members, and applied the general reserve funds as a measure of last resort.

48. While a fundamental misunderstanding of the role of a trustee and its directors appears to permeate this case, and may be an ongoing concern in the operations of IIML as some of the responsible officers of Questor are now occupying roles in IIML, we do not recommend making further enquiries to determine whether any conduct issues have arisen in relation to this matter. The good results being yielded through the ongoing supervision of the conflicts management and governance issues and the proposed review in May 2017 (as outlined in paragraph 43) outweigh the benefits of making further enquiries to determine whether any conduct issues have arisen in relation to this matter.

268 On 27 September 2018 the board of IIML resolved to replenish the general reserve, with the minutes recording as follows:

**1. NOTED**

* The Company is the trustee of the IOOF Portfolio Service Superannuation Fund (Fund).
* Questor Financial Services Pty Limited (Questor) was the trustee of The Portfolio Service Retirement Fund (TPS) and the responsible entity for the Cash Management Trust (CMT).
* As a result of an over-distribution of $6.16 million to unit holders of the CMT, various remediation exercises took place, with Questor resolving to compensate certain members of TPS by using the TPS general reserve in the amount of $1.616 million.
* Members and assets of TPS have since been transfened to the Fund by way of a successor fund transfer. o APFIA disagreed with the Questor approach and various correspondence and discussions have occurred, with the matter also the subject of witness evidence and submissions at the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry.
* The different legitimate views in relation to Questor's decision to use the general reserve to compensate members.
* This matter occurred a number of years ago, concerns a discrete issue and does not support broader conclusions about IOOF's conduct and culture generally.
* APRA's specific request to reconsider this decision and the replenishment of the general reserve.

**2. RESOLUTION**

Having regard to the above matters and as a sign of its good faith and constructive approach with APRA, the Directors of the Company hereby RESOLVE to replenish the general reserve in an amount equal to the amount of the general reserve that was used to compensate members in respect of the Questor matter, by 5 October 2018.

269 On 5 October 2018, IIML paid the funds into the general reserve to implement the replenishment.

9.2.2 APRA’s case – Questor’s alleged CMT remediation breaches

270 APRA said that the CMT overpayment having been made, Questor “needed to determine how it would compensate the trust fund and consequently superannuation beneficiaries for the losses suffered”. It described this need as arising from the “fundamental obligation of trustees to get the trust property in, protect it and vindicate the rights attaching to it: *CGU Insurance Ltd v One.Tel Ltd (in liq)* (2010) 242 CLR 174 at [36]; *Fischer v Nemeske Pty Ltd* (2016) 257 CLR 615 at [111]”. It said that nothing in the TPS trust deed or the SIS Act displaced this obligation but, rather, a range of provisions supported such a duty on the part of the trustee, namely:

(a) Cl 15.1 (CB 1/3, p. 162) provided Questor the power to do anything it considered appropriate to administer the Fund and comply with the SIS Act including, relevantly, to conduct legal proceedings and compromise any claim.

(b) Cl 22(g) (CB 1/3, p. 173) provided Questor with the power to do anything necessary or desirable to comply with the SIS Act.

(c) Cl 15.7 (CB 1/3, p. 163) provided that the powers and discretions of Questor could be exercised individually or jointly by a director or employee of Questor.

271 According to APRA, the exercise of any of Questor’s powers with respect to the prosecution or compromise or abandonment of any rights against third parties involved no mere exercise of a discretionary power and hence “discretionary decision” in the sense used in *Karger v Paul* (McGarvie J). APRA again referred to *Finch v Telstra* at [30] which said:

The Trustee was trustee of a trust. It had a duty to distribute to those who fell within the definition of "Total and Permanent Invalidity" and a duty not to distribute to those who did not. That affected its role in relation to the forming of its opinion under limb (b). Forming that opinion was not a matter of discretionary power to think one thing or the other; it was an ingredient in the performance of a trust duty. That duty was owed to the Members, including the applicant. The applicant was not the object of a discretionary power of appointment. He was the beneficiary of a trust, and although the precise form and quantum of his beneficial interest was contingent on particular events, he did have a beneficial interest.

272 On this basis APRA submitted that in considering the exercise of powers referable to its duty to get in the trust assets and vindicate rights attaching to it, Questor was required not to knowingly exclude relevant information from consideration in the performance of the trust duty, and where there was conflicting bodies of material or insufficient material, its duties of care, skill and diligence required that relevant information be sought. The problems with APRA’s approach relying on *Finch v Telstra* have been identified above.

273 APRA based its case against Questor with respect to the alleged CMT Remediation Plan Breach on the proposition that “in its capacity as licensee and trustee of TPS Super, Questor was obliged by s 52(c) and (d) of the SIS Act not to accede to any decision made by itself, in its capacity as RE, to ‘remediate’ the CMT Overpayment that was not in beneficiaries’ best interests and did not adversely affect beneficiaries”. It said that Questor failed to meet these requirements in “acceding to the CMT Remediation Plan, and passing on its effects to superannuation beneficiaries, from September 2011 to September 2014”.

274 APRA characterised the effect of Mr Rossitto’s plan as making the “investors in the CMT, and ultimately the superannuation beneficiaries of TPS Super and investors in the TPS MIS, responsible for the errors of NAB, IOOF Service Co and, ultimately, Questor itself”. According to APRA:

Acting in the best interests of superannuation beneficiaries, Questor as trustee should have taken steps to protect beneficiaries and ensure the RE adopted a course of action that remediated the error in a timely manner that mitigated the beneficiaries’ loss. One option would have been to promptly disclose the overpayment to beneficiaries (i.e. in February 2010), seek to recover the overpayment from the recipients (to the extent possible), and pay compensation to beneficiaries for any incidental losses suffered (e.g. additional taxes, fees and unit pricing errors). Such compensation could have been sourced by making a claim against one of the entities, including Questor itself, that had an exposure to liability by reason of the CMT Overpayment. Any shortfall that was not recoverable from beneficiaries (i.e. because they had a change of position defence) should then also have been recovered from NAB, Questor or IOOF Service Co and used to make good the CMT trust fund.

275 APRA said this approach would have been consistent with the guidance in the Joint ASIC and APRA Regulatory Guide 94: *Unit Pricing: Guide to good practice* (August 2008), pp. 97-98 (CB 1/6KA) which relevantly provided:

* in determining compensation, reasonable efforts should be made to return all unit holders (including the fund and the ongoing unit holders) to the financial position that would have existed if the error had not occurred;
* you must not benefit from an error in unit pricing – where it is not possible to restore all parties to the position that would have applied if the error had not occurred, you are responsible for meeting any deficit, while any surplus should remain in the fund for the benefit of ongoing unit holders; and
* in the case of superannuation funds, you are responsible to ensure that there is no breach of the SIS Act.

You have a responsibility to prevent unit pricing errors. You also have a duty to act in the best interests of unit holders as a whole. You must act honestly, diligently and impartially. As between unit holders, you must treat unit holders of the same class equally and unit holders in different classes fairly. You need to take particular care when determining compliance with your obligations.

When determining compensation in the circumstances of your fund …you must take all relevant legal obligations into account and be able to demonstrate how you have reconciled those obligations with your plans for rectifying the error and compensating affected members. In doing so, you should note that the allowance by the regulators of fixed dollar minima on compensation amounts to exited members does not affect third party rights against you in relation to non- compensation.

276 APRA said that, instead, Questor implemented “a drawn-out ‘claw back’ from investors and beneficiaries that had no responsibility to repay the overpayments. This plan had the effect of adversely impacting even more beneficiaries, and creating more loss, than the original CMT Overpayment”.

277 APRA submitted that Questor’s power to withhold income distributions was not unfettered. It had to be exercised by Questor in good faith, upon genuine consideration and “most relevantly in accordance with the purposes for which the discretion was conferred: *Finch v Telstra Super Pty Ltd* (2010) 242 CLR 254 at [269], citing *Karger v Paul* [1984] VR 161”. APRA said that there is nothing in the evidence that disclosed any genuine consideration or that the exercise of power was for a proper purpose under the CMT constitution. APRA characterised the remediation as having inflicted very real actual adverse impacts on superannuation beneficiaries. In APRA’s words:

A cost/benefit analysis, with an eye to beneficiaries’ best interests and their legal rights as against third-parties (other than NAB), is the very thing about which there is no evidence in Questor’s documents.

278 In its pleading, APRA contended that it was in the best interest of beneficiaries for the loss and damage caused by the overpayment to be recovered from NAB, IOOF Service Co, Questor out of its own funds, or IOOF Hold Co, or a combination of these sources of compensation. It said that in the face of the various overpayment “exposures” of NAB, IOOF Service Co and Questor the CMT Remediation Plan was not in the best interests of TPS Super beneficiaries.

9.2.3 Respondents’ case – Questor’s alleged CMT remediation breaches

279 The respondents submitted that this aspect of APRA’s case depended on an unproven assumption that Questor, as RSE of TPS Super, could have objected to the decision made at the RE of the CMT level to recoup the overpayment from future income distributions. The submission was:

…this aspect of APRA’s case is premised upon Questor as RSE having the ability to prevent Questor as RE from implementing the Remediation Plan. However, if Questor as RE had the power to reduce distributions to unitholders in order to recoup the CMT Overpayment (which is the key aspect of the Remediation Plan), then Questor as RSE would have no ability to prevent this, and the claim fails.

280 The respondents contended that it is clear that Questor as RE had a power of recoupment both as a principle of general law and under the CMT Constitution. The respondents said:

…at general law, it is a principle of longstanding authority that a trustee who overpays a beneficiary must recover the overpayment, and may recover it out of future payments of income to that beneficiary: *Downes v Bullock* (1858) 25 Beav 54; *Burns v Leda Holdings Pty Ltd* [1988] 1 Qd R 214; *Macphillamy v Fox* (1932) 32 SR (NSW) 427.

…

These principles apply unless the trust instrument says to the contrary: *Re Robertson (dec’d)* [1953] VLR 685.

281 The CMT trust instrument does not say to the contrary. To the contrary, as the submissions for the fourth to seventh respondent said, cl 12.7:

…gave Questor as RE a broad discretion to “at any time distribute any amount of capital or income to unit holders”. Further, clause 12.1 of the Fifth Schedule to the CMT Constitution confers a power on Questor as RE to decide the classification of any item as being on income or capital account and the extent to which reserves, or provisions need to be made. The words used are plainly apt to apply to the recovery of an overpayment via a reduction in future distributions.

282 The respondents said that it follows that Questor as RSE simply had no role or power whatsoever in “considering and accepting” the CMT Remediation Plan. Further, as to Questor as RSE “considering and deciding to pass on the consequences” of the CMT Remediation Plan to its members:

…it is unclear what else APRA suggests it might have done. It was simply distributing the income that was received from the CMT, as it was obliged to do.

283 The respondents said that Questor’s actions in compensating new member beneficiaries for the reduced distributions they would receive (without having received the initial overpayment) was entirely proper.

284 Further, they submitted that while APRA asserts that “a party ‘might’ have a potential ‘exposure’ which ‘might’ have led to the payment of some unspecified amount of compensation, it does not address any of the factors necessary to establish liability in any detail, and its pleading assumes - contrary to the fact - that this would be straightforward exercise”. Otherwise:

…nowhere does APRA lead evidence, or even make submissions, concerning the practical realities of pursuing the alleged ‘exposures’. That is to say, even assuming such ‘exposures’ existed and Questor as RSE ‘gave consideration’ to the possible exposure of the various parties suggested, APRA’s case is silent about the cost, time and downside risks involved in taking ‘steps’ or ‘action’ to pursue the ‘exposures’. The cost of the investigation and pursuit of claims against other parties would be borne by members, and that is a factor to be weighed in the assessment of whether not pursuing them was in the best interests of members. But APRA provides no evidence upon which the Court could assess those matters. And, tellingly, APRA’s case is also silent as to the likely outcome or range of outcomes, and what impact that would have on the best interests assessment.

285 The fourth to seventh respondents said that:

…Questor observed in the fourth to seventh respondents’ opening submissions at [3] that APRA has only looked to the upside when framing its alternative actions as being in the best interests of members and has left out of the account what a reasonable trustee would have recognised at the time was the potential, sometimes inevitable, adverse impact on members. APRA does not appear to disagree with this proposition; but nor does it provide any answer to it.

Taking only the most obvious adverse impact of pursuing claims, namely legal costs: given that APRA is suggesting that the beneficiaries of TPS Super should have been made to pay for the pursuit of these exposures, it might have been expected that APRA would adduce evidence explaining why the game would be worth the candle. The fact that it has chosen not to do that, allows a compelling inference to be drawn, that APRA’s preferred course of conduct would not, in fact, have been in the best interests of members.

286 In respect of the asserted exposures to liability, the fourth to seventh respondents responded as follows.

287 As to NAB, APRA has not proven any loss to the beneficiaries by reason of the over payment.

As to ‘loss of capital’, the parties agree on the pleadings that the capital was distributed to the unitholders and then further distributed to the beneficiaries. Questor as RE obviously held the capital as trustee, and it has been returned. There has been no loss of capital.

As to ‘loss of interest earned by reason of the investment of such capital,’ there is no evidence of any such loss having been suffered. As the second respondent submits at VCS at [225], what APRA is required to establish is that one or more beneficiaries earned a lower return on the portion of the overpayment distributed to it that it would have received if the overpayment had not been made. Even if this had been done, APRA would then need to have led evidence quantifying this loss so that the materiality of any “exposure” could have been assessed and taken into account by a prudent trustee when considering what was in members’ best interests (for example, a prudent trustee, acting in accordance with its Best Interests Covenant would be unlikely to pursue a small claim of this type, particularly given the difficulties, costs, and risks of doing so).

288 Further, NAB’s immediate answer to any such claim would have been that Questor as RE could recoup the overpayment to beneficiaries, including by withholding future income distributions.

289 Accordingly:

…the NCS CMT Overpayment Exposure did not exist, and no reasonable superannuation trustee would have pursued it. Of course, ultimately NAB did accept that its breach of duty had caused a different loss (i.e., that which was determined by the Ernst and Young report). But that is not APRA’s pleaded case, and NAB was pursued (and settled) that exposure.

290 As to IOOF Service Co’s Overpayment Exposure 1, that is the asserted liability of IOOF Service Co to Questor as RE for the loss and damage caused by the overpayment, “any such claim would suffer the same difficulty as that confronting the NCS CMT Overpayment Exposure: namely, no loss was suffered by reason of the overpayment itself”.

291 Further, while APRA contended that IOOF Service Co was contractually obliged to undertake to audit, monitor, assess, detect and reconcile income distributions by the CMT, the evidence does not establish this given the role of NAB as Custodian for the calculation and distribution of income by CMT. As the fourth to seventh respondents put it:

The only evidence relied upon by APRA in relation to these matters are Mr Rossitto’s documents referred to above…. Those documents do not even refer to IOOF Service Co, let alone its obligations or any failings on its part to meet its obligations. Further, for these reasons given above, APRA’s reliance on these documents is misplaced, and in any event, they have very little probative value for the reasons given.

292 In relation to the asserted liability of Questor as RE to Questor as RSE, the same question of absence of proven loss arises. Further, as the fourth to seventh respondents put it, Questor was obliged to recover the wrongly paid capital which accordingly meant that Questor as RSE (as a unitholder in the CMT) would have had no right to object to the recoupment. In addition, “there remains the difficulty that APRA has not adduced any probative evidence to demonstrate that Questor as RE breached any obligation giving rise to a right of action against it.”

293 The fourth to seventh respondents said:

Finally, as pleaded by Questor in its Defence, Questor as RE had good defences under the CMT Constitution. In particular, it:

(a) had no liability for any such loss or damage that may have been suffered, as it acted and relied upon information received from NAB and did not have reasonable grounds to believe that that information was not genuine;

(b) acted in good faith and without default or negligence; and/or

(c) in any event was entitled to an indemnity out of the assets of the CMT for any liability it incurred in performing or exercising any of its powers or duties in relation to the CMT.

294 They continued, saying that APRA’s belated and unpleaded attempt to raise new claims based on the provisions of the Corporations Act to avoid these provisions ought not be permitted.

295 As to IOOF Service Co’s Overpayment Exposure 2, that is the asserted liability of IOOF Service Co to Questor as RSE, for further distributing the overpayment, the fourth to seventh respondents said the “claim flounders for the same reasons identified above in relation to the Questor’s CMT Exposure as RE”.

296 As they put it:

(a) there was no loss;

(b) Questor as RE was entitled (if not obliged) to recover the overpaid capital by way of withholding future income distributions;

(c) as the recipient of distributions paid to it Questor as RE, IOOF Service Co (on behalf of Questor as RSE) was not required to investigate or audit the source of distributions paid to it;

(d) in any event, under the TPS Trust Deed, unless the loss resulted from the trustee’s dishonest or reckless failure to exercise the degree of care and diligence required of it (which is not alleged), Questor:

(i) had no liability; and

(ii) alternatively, had the benefit of an indemnity from the Fund in relation to any such loss it was liable for.

297 The first respondent noted that APRA pleaded that the plan Mr Rossitto developed in September 2011 (what it calls the “CMT Remediation Plan”) was a plan simply to reduce distributions from the CMT without paying compensation to TPS MIS investors and TPS Super beneficiaries (ASOC [235]; ACS [204]-[208]). The first respondent said this contention should be rejected. In his 19 September 2012 email to Mr Coulter, Mr Rossitto said that new investors in TPS Super would receive a diluted distribution and would most likely need to be compensated: CB2/9A p.266\_0001. If the plan had no compensation element then it could be said that new investors, who had not had part of the capital wrongly distributed to them, would be adversely affected by the dilution of their distributions. But, the first respondent said, it should be inferred that Mr Rossitto always intended that these beneficiaries would be compensated for their loss but that the amount of the compensation could not be calculated until the write back had been completed.

298 According to the first respondent the remediation plan as conceived by Mr Rossitto had at least these aspects:

a) TPS MIS investors and TPS Super beneficiaries who took the benefit to the overdistribution, and who had settled their tax and superannuation affairs on that basis, were not required to disgorge that benefit. APRA implicitly concedes that it may not have been possible to clawback that benefit (ACS [211]). There were obvious difficulties in doing so, particularly in circumstances where the money was in superannuation accounts that were still in the accumulation phase. Such amounts could not necessarily be withdrawn easily or without other consequences.

b) The CMT would be restored to its correct capital position, with minimal impact to its returns.

c) TPS MIS investors and TPS Super beneficiaries who were negatively impacted would be fully compensated and would suffer no loss.

299 The first respondent submitted that there was “nothing in that plan that was necessarily inconsistent with the best interests of TPS beneficiaries”. Further, Mr Rossitto’s thinking, as disclosed in his 18 October 2013 report, is entirely consistent with the best interests of beneficiaries: “Mr Rossitto was concerned to prevent financial shocks that would have affected all TPS Super beneficiaries and recognised that compensation would need to be paid to new beneficiaries who were disadvantaged by the reduced distributions”.

300 The first respondent pointed out that there is no evidence that any other strategy in September 2011 would have better served the interests of the TPS Super beneficiaries than that which Mr Rossitto implemented. In response to APRA’s submission that the best course would have been to “promptly disclose the overpayment to beneficiaries (i.e. in February 2010), seek to recover the overpayment from the recipients (to the extent possible), and pay compensation to beneficiaries for any incidental losses suffered (e.g. additional taxes, fees and unit pricing errors)” and that this could be funded “by making a claim against one of the entities, including Questor itself, that had an exposure to liability by reason of the CMT Overpayment”, the first respondent submitted that:

(1) there is no evidence to support APRA’s contention;

(2) insofar as APRA says that Questor should have “sought to recover the overpayment from recipients”, there were obvious barriers to doing so and APRA does to identify how those difficulties could be overcome;

(3) insofar as APRA says that compensation should have been paid for “any incidental losses suffered (e.g. additional taxes, fees and unit pricing errors)”, it minimises the self-evident difficulties in identifying those losses, particularly given Questor would have no visibility into the tax impacts on investors and beneficiaries; and

(4) insofar as APRA contends that compensation could have been sourced from Questor or third parties, that submission ought be rejected for the reasons dealt with in relation to Step 1.

301 According to the first respondent, the course of action which APRA proposes as in the best interest of the beneficiaries is “so undetailed and unsupported by evidence as to be meaningless” and that if APRA wanted to mount a case that Mr Rossitto’s plan was not in the best interests of beneficiaries it had to adduce reliable evidence that dealt with the full complexity of the problem that Mr Rossitto faced in September 2011. As such:

Simply asserting that Mr Rossitto ought to have “taken steps to protect beneficiaries and ensure the RE adopted a course of action that remediated the error in a timely manner that mitigated beneficiaries’ loss” (ACS [211]) is meaningless unless APRA can prove what better course was actually available. It has not even attempted to do so.

9.2.4 Discussion – The alleged CMT Remediation Plan breaches

302 I accept the respondents’ submissions.

303 APRA’s case on Questor’s alleged CMT Remediation Breach is affected by the same problems as its case on the CMT Overpayment Breach, a lack of reliable evidence. Again, APRA appears to have assumed that the mere assertion of reasonably arguable cases for liability on the part of NAB, IOOF Service Co and Questor as RE and as RSE, would be sufficient to prove that part of its case and that the mere assertion of another approach to dealing with the problem with which Mr Rossitto was confronted in September 2011 would be sufficient to prove that Mr Rossitto’s plan was in breach of the due care and conflict covenants.

304 Mr Rossitto’s explanation of his consideration of how to deal with the problem in the 18 October 2013 document, albeit after the event, does disclose the close consideration he gave as to how to deal with the problem in the best interests of the beneficiaries. He expressly refers to these best interests saying that the plan he formulated was seen by him to be in the best interests of beneficiaries. He provides details of the various alternatives that were considered which show the close consideration he gave to the problem within a framework which was set by the best interests of the beneficiaries. The document also expressly stated that the focus in any rectification is to “ensure that current and existed members are treated fairly and equitably and any decisions made are in their best interests”.

305 It is easy now, after the event, to contend that another plan would have been better because it would have enabled more timely resolution of the issue. It is easy also to say that compensation from the entities, Questor, IOOF Service Co and NAB, should have been pursued from the outset. But APRA’s case, at every level, lacks reliable proof. APRA does not have evidence from which it would be inferred that there was any reasonably arguable cause of action to recover loss (indeed, it has not even proved loss from the over payment) from these entities. Its case rises no higher than assertion and speculation. The best evidence for APRA ended up being the way in which NAB responded to Questor’s claim for compensation for losses caused by the dilution of the distributions, not losses caused by the over payment. It may be accepted that NAB responded readily to the claim and made a 50% contribution to those losses. But if anyone was at fault in this matter it was plainly NAB. As soon as Questor and IOOF Service Co are considered, any proposed claim is immediately confronted by real, potentially insurmountable, hurdles, none of which APRA has acknowledged.

306 APRA also sought to characterise the decision whether or not to spend money on considering and pursuing entities for compensation as no mere discretionary decision. As already noted, I disagree with APRA’s approach to this issue. Questor was not confronted by the kind of decision with which the High Court was dealing in *Finch v Telstra*. The decision to consider seeking redress from other entities would have been complex and potentially costly. Mr Rossitto, it must be inferred, was aware of these basic circumstances and took the view that his approach was in the best interests of members. Given that the plan allowed recoupment of the capital and the compensation of adversely affected beneficiaries, it is difficult now to second-guess Mr Rossitto by concluding that he was wrong. This is made still more difficult by the fact that APRA has no evidence of the kind that would be required which supports the inference that its approach, in fact, would have been better for members than the approach which Mr Rossitto conceived and implemented.

307 APRA’s case also ignores the fact that Mr Rossitto’s plan involved Questor in doing precisely that which APRA said it needed to do, namely, getting the trust property in. Mr Rossitto’s plan had as its object the recoupment from beneficiaries of the overpaid capital. To the extent APRA suggested that the plan never included any element of compensation for new members who had not had the benefit of the over payment, I disagree. Mr Rossitto was plainly aware of this issue and should be inferred to have been so aware from the outset. What must also be inferred is that Mr Rossitto knew that compensation could not be calculated until the write back process was complete.

308 APRA’s case appears to assume that merely because beneficiaries’ distributions were being diluted it virtually goes without saying that Mr Rossitto’s plan could not have been in the best interests of members. But this overlooks the fact that some members had the benefit of the wrongly distributed capital (to their advantage) and others who did have that benefit were intended to be compensated for any loss. Mr Rossitto’s plan, all in all, was a practical and sensible way to cause the least inconvenience to the members whilst nevertheless ensuring all were treated fairly and equitably, even if over the longer-term. As I have said, it is easy to criticise with the benefit of hindsight but there is simply nothing in the evidence which would cause me to conclude that, in the circumstances as they existed in September 2011, Mr Rossitto was doing anything other than exercising due care, skill and diligence with the sole object of giving priority to the best interests of the members by recouping the wrongly distributed capital, in a manner calculated to cause the least difficulty for members and on the basis that those who suffered loss as a result would be compensated once the loss was known. Mr Rossitto’s plan did not have to be perfect. Further, the mere fact that APRA thinks another plan would have been in the best interests of members does not mean Mr Rossitto’s plan was not in the best interests of members.

309 I do not accept APRA’s pleaded case that there was no practical difficulty in Questor making a claim against IOOF Service Co. There were numerous practical and legal difficulties. APRA’s case in this and other regards seems divorced from the reality that, leaving aside the position of NAB, the legal complexity of any claim against Questor and IOOF Service Co was obvious and at the high end of the scale. I do not think APRA’s case is improved by saying the plan did not include obtaining legal advice on the potential to make claims against Questor as RE and RSE and IOOF Service Co. Again, it is easy to criticise what was done with hindsight but there is no evidence that if legal advice had been obtained it would have been apparent that Mr Rossitto’s plan was not in the best interests of beneficiaries. I do not consider that there was any duty on Questor to obtain legal advice, let alone independent legal advice, on the various alleged exposures APRA has identified. Mr Rossitto acted on the basis of the information he had and nothing in the evidence suggests that he did other than give priority to the best interests of members in so doing. The fact that something different could have been done, with or without legal advice, is immaterial. Further, I infer that if legal advice had been obtained then, contrary to APRA’s apparent assumption, all of the hurdles to the making of any such claims against Questor in its different capacities and IOOF Service Co would have emerged at that time.

310 I also do not accept APRA’s submission that because none of the legal complexities were part of the reasoning at the time, those complexities are immaterial. For one thing, APRA has not proved that the legal complexities were unknown and not taken into consideration at the time. At least some of them would have been obvious to anyone familiar with the services arrangements. For another, as I have said, I consider it likely that had independent legal advice been sought the issues which the respondents identified would have emerged through that process.

311 It is APRA’s case that Questor should have made claims against NAB (which, as I have said, it did but not for any loss from the over payment), Questor in its two capacities and IOOF Service Co. APRA bore the evidentiary burden of establishing these claims were reasonably arguable, yet has failed to bring forward the evidence to establish the claims were reasonably arguable or grapple with the submissions of the respondents which expose the very real problems that any such claims would have encountered. There is simply no evidence from which any conclusion could be drawn that what APRA has suggested should have been done would have yielded a better result in any way for beneficiaries than what in fact was done. As the respondents put it, APRA is simply silent about all these matters making it impossible to reach any rational conclusion that its approach would have been in the best interests of members but Mr Rossitto’s approach was not in the best interests of members.

312 Consistently with my reasoning about the CMT Overpayment Breach, I accept the respondents’ submissions as set out above to the alleged exposures of NAB, IOOF Service Co and Questor.

313 APRA also has not come close to proving that by the remediation plan Questor preferred its own interests to those of the beneficiaries. There is no reason to doubt that Mr Rossitto formulated the plan that he believed gave priority to the best interests of beneficiaries. Nothing in the evidence suggests that Mr Rossitto was preferring the interests of the IOOF Group to those of the beneficiaries when formulating his remediation and compensation plan.

314 I also accept the respondents’ submissions that APRA assumed but has not proved that Questor as RSE could have done anything to prevent Questor as RE from implementing the remediation plan. Questor as RE had the power to do what it did and, in my view, was doing what it did for the proper purpose of getting in the trust property, as APRA would have it. Questor as RSE also had to distribute the income it received from the CMT to members, being the diluted income for the period of the remediation plan. As the respondents put it, what else could it have done?

315 Nor can I see any actual conflict of interest which might have had a significant impact on the capacity of any respondent to act in the best interests of the beneficiaries. APRA has assumed the existence of such conflicts but has not explained how they arise in the particular factual circumstances.

316 For these reasons I do not accept APRA’s case relating to Questor’s alleged CMT Remediation Breach. Questor did not breach its obligations pursuant to Questor’s Pre-2013 Best Interests Covenant, Questor’s Best Interests Covenant or Questor’s Conflicts Covenant.

9.2.5 Mr Kelaher’s alleged CMT Remediation Plan breaches

9.2.5.1 Some additional facts

317 These additional facts, focused on Mr Kelaher, are adopted from the written submissions filed on his behalf.

318 On 19 September 2012, Mr Rossitto emailed Mr Coulter in relation to the CMT issue. He noted in that email that he was not sure if Mr Kelaher (“Chris K”) was aware of the issue. Mr Coulter replied the same day saying, “Chis [sic] has had no explicit briefing on it other than to say ‘we’re handling it’”.

319 At the Questor board meeting on 25 September 2012:

Mr Vernados asked who wears the costs associated with this potential breach. Mr Coulter advised the member would not be impacted and it was a decision between the Custodian and the company who wears the costs… Mr Rossitto advised that the issue is essentially one where an incoming member of TPS post the breach will have received a diluted distribution.

320 On 1 November 2012, Mr Thomas Robertson (Head of Compliance, IOOF Hold Co) wrote to APRA. Mr Robertson’s email is evidence that the resolution being pursued by Mr Rossitto (without board approval) envisaged that new members of the TPS MIS and TPS Super would receive compensation. This document also disclosed a timing issue in that it was not possible to ascertain compensation until the end of the write-back period.

321 There was a board meeting of Questor on 25 March 2013, but again there is nothing in the minutes of that meeting to indicate that the board was told anything regarding the impact of the CMT remediation on TPS MIS investors or TPS Super beneficiaries. At this point, the write-back had been in effect for approximately 1.5 years.

322 On 11 September 2013, approximately two years after the write-back process began, a whistleblower within the IOOF Group anonymously reported that management was “reducing the rate of return in respect of the cash fund of the Questor product in order to recover an earlier over distribution, to the detriment of retail investor[s] who were not members of the fund at the time of the over-distribution”.

323 Mr Venardos proposed engaging PwC to investigate the issue and said the board and Audit Committee should be notified. One of the steps taken was the appointment of Mr Urwin (Head of Risk, IOOF Hold Co) to undertake an internal investigation.

324 Mr Urwin reported his findings in October 2013. His report said:

Incomplete reporting to Board: Our examination of the Board papers of 24 September 2012 noted that the Board may not have been informed that the 3-year ‘asset write back’ (claw-back) of the over distributed funds from member accounts was already in place. This started in September 2011

There is a risk that decisions are made by the Board based on incomplete or inaccurate information

In addition to the notification to the Board, the minutes state that the members would not be impacted and it was a decision between the Custodian and the company who wears the costs.

325 At a Questor board meeting on 28 October 2013, the board noted that “at the very least” a further assessment of the impact on members and proposed compensation was required. The minutes continue, “[t]his review will be brought forward instead of waiting for the 3 year period to lapse to ensure the right level of exposure is identified which takes into account the entry and exit of members and the amount of compensation”.

326 On 14 March 2014, the IOOF Hold Co Legal, Compliance and Risk report contained the following update:

Other internal activity, as previously reported, is continuing and includes reducing the “write off” time period (presently September 2014) to bring this issue to a close. Further, the ORFR is established for incidents like this (the effect on TPS RF receiving diluted distributions) and we will consider its application once development is completed (between March and June 2014). Legal advice has been sought to confirm its application. A meeting with the NAB to commence discussions on recouping some of the cost which can be paid into the ORFR occurred in February '14 and we have been invited to submit a compensation claim; there is no admission of liability at this time.

9.2.5.2 APRA’s case

327 According to APRA, Mr Kelaher as managing director of IOOF Hold Co, Questor and IOOF Service Co, “had a conflict between his duties to superannuation beneficiaries under s 52A and the interests of the IOOF Group in relation to the decision as to how to remediate the CMT Overpayment”. As APRA put it:

Any money paid by IOOF Group entities to compensate beneficiaries would have an impact on the earnings of those entities and was therefore in conflict with Kelaher’s duty to shareholders and his own personal interest as shareholder. There was also a conflict between Kelaher's duties under s52A and his duties to non-superannuation investors. None of those conflicts were identified at the time.

328 APRA said that it did not suggest that Mr Kelaher had developed the CMT Remediation Plan. However, he was aware of sufficient facts from at least 25 September 2012 to know the plan was in place and adversely affecting beneficiaries of TPS Super. By reason of the matters disclosed at the board meeting on 25 September 2012, Mr Kelaher knew, said APRA:

(a) that there had been an unauthorised overdistribution of over $6 m capital from the CMT to unitholders that Questor had approved (as recorded in the Board Paper);

(b) that management had determined to address the overdistribution by amortising the asset and diluting distributions from the CMT to unitholders over a period of three years;

(c) that the dilution of distributions from the CMT meant that beneficiaries of TPS Super (including beneficiaries joining the fund after the distribution) who had money invested in the CMT were, in turn, receiving diluted income distributions;

(d) that no steps had yet been taken by management to recover any of the losses by unitholders or beneficiaries from any other source.

329 APRA said that in addition Mr Kelaher knew “by reason of his position as Managing Director of the IOOF Group and director of IOOF Service Co the role that IOOF Service Co played in the group, namely providing all personnel and administration services required by each subsidiary (including Questor) to run their business”.

330 According to para 244 of the ASOC, Mr Kelaher (and Mr Venardos) knew or ought to have known that:

(a) the CMT Remediation Plan was not in the best interests of the beneficiaries of TPS Super, as pleaded at paragraphs [238] and [239];

(b) the NCS CMT Overpayment Exposure existed;

(c) there was no practical difficulty in making a claim against NCS;

(d) the IOOF Service Co's CMT Overpayment Exposure 1 existed;

(e) the IOOF Service Co's CMT Overpayment Exposure 2 existed;

(f) there was no practical difficulty in Questor making a claim against IOOF Service Co in its capacity as service provider to Questor as RE of the CMT or as service provider to Questor as trustee for TPS Super.

331 APRA submitted that armed with this knowledge “a prudent superannuation trustee director exercising care, skill and diligence and performing their duties in the best interests of beneficiaries would not simply have continued to accept the implementation of the CMT Remediation Plan”. Rather, as pleaded, a prudent superannuation trustee director would have:

(a) questioned management as to whether the continuation of the CMT Remediation Plan was in the best interests of beneficiaries;

(b) instructed management to cease the CMT Remediation Plan and restore to beneficiaries their distribution entitlement until satisfied that there was no other option that was in the best interests of beneficiaries;

(c) instructed management to seek legal advice on the potential exposure of NAB, Questor or IOOF Service Co to compensate for losses and contribute to the remediation, rather than taking money from beneficiaries;

(d) instructed management to seek legal advice as to whether Questor as trustee and investor in the CMT had any available defences to Questor as RE’s attempt to “claw back” the CMT Overpayment (in which case, those defences should have been asserted);

(e) taken steps to manage conflicts of interest when considering the CMT Remediation Plan including, identifying all relevant conflicts and ensuring the Board’s decision-making recorded how those conflicts had been addressed;

(f) would not have accepted the CMT Remediation Plan until satisfied that conflicts had been appropriately managed or avoided, to ensure decisions were being made in the best interests of beneficiaries.

332 Mr Kelaher did not take any of these steps. “APRA accordingly submits that between 25 September 2012 and 30 June 2013 he contravened s 52(8) (as then in force). From 1 July 2013 until October 2015, he contravened ss 52A(2)(b), (c) and (d) (**Kelaher's CMT Remediation Plan Breach**).”

333 APRA submitted further that:

(1) “As a superannuation entity director, Kelaher was required to act at all times in accordance with s 52A in discharging his duties as a director of a superannuation trustee. It was not open to Kelaher to ignore the CMT Remediation Plan simply because it was already in place before he became aware of it, in light of Questor’s fundamental obligation to protect the trust property and vindicate rights attached to it.”

(2) “APRA is not aware of any reason why the CMT Remediation Plan could not have been interrupted or reversed. Doing so would have stemmed the bleeding of beneficiaries’ funds at an earlier point in time, and potentially have minimised the overall loss suffered.”

9.2.5.3 Mr Kelaher’s case

334 Mr Kelaher’s submissions noted that by “considering and accepting” the “CMT Remediation Plan” in September 2011, Mr Kelaher was said by APRA to have breached the Due Care Covenant and Best Interests Covenant (ASOC, [245]).

335 It was submitted for Mr Kelaher that this claim must fail:

(1) APRA has mischaracterised the remediation plan adopted by Mr Rossitto in September 2011 by ignoring that it included a compensation component.

(2) Insofar as APRA alleges Mr Kelaher had knowledge of Mr Rossitto’s plan prior to October 2013, the claim must fail as the evidence is that Mr Kelaher was not informed that members were bearing any cost in relation to the CMT issue until October 2013. That was the finding of the internal investigation conducted by Mr Urwin following the whistleblower report. Accordingly, there is absolutely no basis to allege that Mr Kelaher “considered or accepted” Mr Rossitto’s plan because he had not been made aware of its key features, including the impact on members. All Mr Kelaher had been told was that management was “handling it”. The minutes of the meeting of 25 September 2012 record Mr Coulter’s advice that members would not be impacted and Mr Kelaher had no reason to doubt that advice and, in light of it, had no reason to consider any claim against IOOF Service Co.

(3) It is clear from the chronology that once Mr Kelaher and the board of Questor became aware of the effect of the write-back on members in October 2013, it took immediate steps towards progressing a compensation plan. As early as 28 October 2013, the board had determined that, “at the very least”, a further assessment of the impact on members and proposed compensation was required. The allegation that Mr Kelaher considered and approved a plan to reduce CMT distributions without paying any compensation to members is inconsistent with the evidence that shows that Mr Kelaher and the rest of the Questor board were immediately concerned to begin the process of compensating members when they learned of members’ detriment in October 2013.

(4) APRA fails to identify with precision exactly how, and by what act or acts, Mr Kelaher “considered” and “accepted” the “CMT Remediation Plan”.

(5) “APRA does not identify what Mr Kelaher ought to have done in the period September 2013 to October 2015. APRA appears to contend that the ‘CMT Remediation Plan’ should have been ‘interrupted or reversed’ in this period to ‘stop the bleeding’ and that this would have ‘minimised the overall loss suffered’ (ACS [230(c)]). That submission is nonsensical in circumstances where no beneficiary in fact suffered any loss, but it suffers from a more significant defect; had Mr Rossitto’s plan been discontinued in the period September 2013 to October 2015, the effect would have been to leave the CMT overdistribution unremediated but with the additional problem that the reduced distributions in the period after September 2011 had created a need for TPS MIS investors and TPS Superannuation beneficiaries to be compensated. Stopping Mr Rossitto’s plan would not have ‘stopp[ed] the bleeding’, it would have left two open wounds. Similarly, it was by no means clear that Mr Rossitto’s plan could be easily “reversed”. There may not have been power to do that under the CMT Constitution. Even if there was, attempting retrospectively to increase CMT distributions for a period of two years would have significant and possibly deleterious implications for the tax and superannuation affairs of TPS MIS investors and TPS superannuation beneficiaries. Again, the issue is once of significant complexity. That is why it was incumbent upon APRA to adduce expert evidence on these matters if it wished to contend that the course taken was deficient.”

(6) “…it is a mischaracterisation to suggest that the Board or Mr Kelaher ‘accepted’ the ‘CMT Remediation Plan’ or something like it. The true position was that, in the period from September 2013 to October 2015, Mr Kelaher and the Board of Questor were dealing with an inherited problem stemming from the CMT overdistribution and the consequences of Mr Rossitto’s [sic] subsequent actions (which had been undertaken without authorisation and had been in place for a period of two years). Mr Kelaher’s conduct in addressing that issue and working to progress the payment of compensation was not the ‘acceptance’ of any plan, so much as an earnest and diligent response to a problem that was not of his making.”

(7) “…something should be said about the submission made by APRA at ACS [225] that there was a conflict between Mr Kelaher’s interests as shareholder of IOOF Hold Co Limited and the best interests of beneficiaries because any money paid to the latter would impact the earnings of the former. That is a submission of especial silliness. For the submission to have any force, the amounts at stake would have had to have been sufficiently large to be material such that they might affect the share price of IOOF Hold Co. There is no allegation that they were and they self-evidently were not.”

9.2.5.4 Discussion

336 My conclusions above mean that APRA has not proved the existence of reasonably arguable cases for liability on the part of NAB, Questor or IOOF Service Co in respect of the CMT Overpayment. I have also concluded that APRA has not proved that the CMT Remediation Plan involved any breach of the covenants by Questor. This inevitably impacts on Mr Kelaher’s potential to have breached the due care, best interests, no conflicts and compliance covenants (the latter being the covenant in s 52A(2)(f) of the SIS Act requiring directors to exercise a reasonable degree of care and diligence for the purpose of ensuring that the corporate trustee carries out the covenants referred to in s 52).

337 Apart from these problems confronting APRA, I find the submissions for Mr Kelaher compelling. It is inaccurate to characterise Mr Kelaher as having “considered and accepted” the CMT Remediation Plan. He, along with the rest of the board, was presented with a plan that had already been implemented for a period of 12 months. This is an important fact which cannot simply be ignored or dismissed as immaterial.

338 The minutes of the meeting of 25 September 2012 record both Mr Coulter’s advice that members would not be impacted “and it was a decision between the Custodian and the company who wears the costs” and Mr Rossitto’s comment that the issue was the dilution of the incoming beneficiaries’ distributions. In contrast to the first respondent’s submission, I do not believe the recorded fact of Mr Rossitto’s comment can be disregarded. Given that both comments appear in the minutes, I consider the inference that should be drawn is that it was common ground between the management and the board that any member who might suffer loss would be compensated. Otherwise, it is not possible to understand Mr Coulter’s comment that members would not be impacted. Mr Coulter could only have meant that members would not ultimately be impacted given the nature of the remediation plan.

339 Accordingly, I consider that Mr Kelaher, as a result of the 25 September 2012 meeting, had been advised by Mr Coulter that members would not be impacted as either NAB or Questor would pay compensation and thus he had no reason to consider any claim against Questor, IOOF Service Co and NAB at this time. Further, had he considered these claims then, consistently with my conclusions above, APRA has failed to prove that the advice Mr Kelaher would have received was that there existed a reasonably arguable case for compensation. Rather, the advice would have been as the respondents proposed.

340 The further misconception in APRA’s case is apparent from its contention that Mr Kelaher should have “instructed management to cease the CMT Remediation Plan and restore to beneficiaries their distribution entitlement until satisfied that there was no other option that was in the best interests of beneficiaries”. The contention assumes that what was being done was not in the best interests of the beneficiaries, but this has not been proved. A range of options had been considered by Mr Rossitto and, on the evidence, with a view solely to the best interests of beneficiaries he had implemented the CMT Remediation Plan. APRA has not proved that Mr Rossitto’s view was motivated by anything other than the best interests of the beneficiaries or was objectively incorrect or unreasonable. Further, APRA has not proved that stopping and reversing the remediation plan would itself have been in the best interests of members.

341 I accept also the first respondent’s submission that the alleged breach of the no conflicts covenant cannot succeed. APRA has not (and presumably could not) prove the existence of any actual conflict of interest between Mr Kelaher’s duty to beneficiaries and his interest as a shareholder or his duties to shareholders. Nothing in the evidence founds any inference of any potential impact on the share prices of the entities. APRA left unexplained the alleged conflict between the interests of superannuation and non-superannuation investors. Again, however, the proposed conflict is left at the level of mere theory and does not arise as an actual conflict capable of having a material, let alone significant, impact on the prioritising of the interests of the beneficiaries.

342 APRA has also not explained why Mr Kelaher (or Mr Venardos) knew or ought to have known of the matters in para 244 of the ASOC. As the submissions for Mr Venardos identified, these matters involve complex questions of mixed fact and law. On my findings, none of the directors could have known or ought to have known the pleaded matters because they have not been proved by APRA to be true. That is, APRA has not proved that:

(1) the CMT Remediation Plan was not in the best interests of the beneficiaries of TPS Super;

(2) the exposure of NAB existed (because no loss has been proved and NAB’s defence would have been the capacity for Questor to recoup the capital from the overpaid beneficiaries);

(3) there was no practical difficulty in making a claim against NAB (when there was given the difficulty of proving loss from the overpayment);

(4) the exposure of IOOF Service Co existed; and

(5) there was no practical difficulty in Questor making a claim against IOOF Service Co in its capacity as service provider to Questor as RE of the CMT or as service provider to Questor as trustee for TPS Super (when there was for the reasons already identified).

343 I also consider that APRA’s case that Mr Kelaher, in order to comply with his covenants, had to question management as to whether the remediation plan was in the best interests of members, instruct management that the remediation plan must cease, seek or instruct management to seek independent legal advice about the liabilities of NAB, IOOF Service Co and Questor is misconceived and based on flimsy evidentiary foundations. On the incomplete information that had been provided to the board, Mr Kelaher had no reason to question the actions of management nor any reason to consider legal advice necessary. The idea that he should have stopped the remediation plan is unrealistic. APRA posits that it knows of no reason why the plan could not have been stopped but it is obvious that doing so when the plan had been on foot for 12 months would involve substantial complexities none of which APRA has considered. In any event, it was for APRA to prove that what it said should have been done was in the best interests of the beneficiaries and that what was done was not in the best interests of beneficiaries. APRA has not proved either aspect of its case.

344 The first respondent’s submission that the board was dealing with an inherited problem, which had only belatedly been drawn to its attention, is persuasive. Further, when it was seized of all of the relevant information the board acted to ensure the matter was brought to a full resolution as quickly as possible, including the issue of compensation for the new members whose distributions had been diluted. As the first respondent put it, the evidence discloses that the board made an earnest and diligent response to a problem that was not of its making and about which it had been uninformed for a year and was the recipient of incomplete information for another year.

345 For these reasons I do not accept that Mr Kelaher’s conduct involved any of the CMT Remediation Breaches as APRA proposed.

9.2.6 Mr Venardos’ alleged CMT Remediation Plan breaches

9.2.6.1 APRA’s case

346 APRA made the same claims against Mr Venardos as it did against Mr Kelaher.

347 APRA noted that Mr Venardos was not a director of IOOF Service Co and that his conflict arose from his dual position as a director of IOOF Hold Co and Questor. APRA said that in these capacities Mr Venardos:

…ought to have known about the role that IOOF Service Co played in the group, namely providing all personnel and administration services required by each subsidiary (including Questor) to run their business. He would accordingly have known that the personnel who had authorised the CMT Overpayment (as disclosed in the Board paper) were IOOF Service Co staff.

348 APRA said that it accepted that at the 25 September 2012 meeting Mr Venardos asked the pertinent question: “who wears the costs associated with this potential breach”. APRA’s submission was that it was not enough for Mr Venardos to ask this question. Having been told by Mr Rossitto that the distributions to incoming members were being diluted, APRA contended that Mr Venardos was required to implement the same steps as Mr Kelaher, namely:

(a) questioned management as to whether the continuation of the CMT Remediation Plan was in the best interests of beneficiaries;

(b) instructed management to cease the CMT Remediation Plan and restore to beneficiaries their distribution entitlement until satisfied that there was no other option that was in the best interests of beneficiaries;

(c) instructed management to seek legal advice on the potential exposure of NAB, Questor or IOOF Service Co to compensate for losses and contribute to the remediation, rather than taking money from beneficiaries;

(d) instructed management to seek legal advice as to whether Questor as trustee and investor in the CMT had any available defences to Questor as RE’s attempt to “claw back” the CMT Overpayment (in which case, those defences should have been asserted);

(e) taken steps to manage conflicts of interest when considering the CMT Remediation Plan including, identifying all relevant conflicts and ensuring the Board’s decision-making recorded how those conflicts had been addressed;

(f) would not have accepted the CMT Remediation Plan until satisfied that conflicts had been appropriately managed or avoided, to ensure decisions were being made in the best interests of beneficiaries.

349 According to APRA:

[t]he failure to exercise reasonable care and diligence in reviewing the plan from the perspective of beneficiaries, caused Questor to continue to implement the CMT Remediation Plan and breach its own covenants under s 52(2). This was a breach of s 52(8) at the time, and the continued failure to take these steps after 1 July 2013 was a breach of s 52A(2)(b), (c) and (d).

350 APRA said its case was not that Mr Venardos should have caused Questor to take legal proceedings but that he was required to “oversee the management of the company by causing Questor to properly consider such claims (with conflicts of interests being appropriately managed), before accepting the dilution of beneficiaries’ distributions”.

351 APRA said that it did not need to make any allegations against the other directors of the board against whom proceedings had not been taken. Further, that the covenants in s 52A of the SIS Act apply to the performance of the director’s duties and not merely to the exercise of powers.

352 APRA said that it did not matter that the purpose of the meeting of the board on 25 September 2012 was the approval of the annual accounts. The covenants apply at all times and not only when a director is asked to specifically turn their mind to the interests of beneficiaries.

9.2.6.2 Mr Venardos’ case

353 For Mr Venardos it was submitted that the decision by Questor to adopt the CMT Remediation Plan was made by management and not the board. Further, there is no allegation that the decision was made by management without authority.

354 It was also submitted that the decision was made by Questor in its capacity as RE to reduce distributions to the two CMT unitholders, being Questor as the trustee of TPS Super and Questor as RE of the TPS MIS. Accordingly:

Questor in its capacity as RE of the CMT is not subject to the SIS Act. In that capacity, it is not subject to the s 52 SIS covenants and its directors, if and to the extent they exercise powers as directors of Questor in that capacity, are not subject to the s 52A SIS covenants.

The conduct of Questor in its capacity as RE of the CMT is not within the supervisory jurisdiction of APRA. There is no allegation that Questor’s decision to adopt the CMT Remediation Plan was: (a) beyond its power as RE of the CMT; or (b) in breach of its duties as trustee of the CMT. The allegation in ASOC [239] that the remediation plan was not in the best interests of beneficiaries of TPS Super is not an allegation that Questor was in breach of trust as RE of the CMT in adopting the plan to reduce distributions or in breach of its duty to its three unitholders or against the interests of its unitholders…

355 According to the submissions for Mr Venardos, there is no pleading of any claim that could have been made by Questor as TPS Trustee against Questor as RE of the CMT for the reduced distribution decision. APRA cannot avoid the circularity which would have resulted if any such claim had been pleaded given the following clauses of the CMT Constitution:

9.3 The Manager is entitled to be indemnified out of the Assets of a Trust for any liability incurred by it in performing or exercising any of its powers or duties in relation to that Trust. This indemnity is in addition to any indemnity allowed by law. Nothing in this constitution will prevent the Manager exercising its powers to satisfy any right of indemnity out of the Assets or to exclude or limit its personal liability.

16.3 Subject to the Corporations Act, if the Manager acts in good faith and without default or negligence, it is not responsible to Members for any loss suffered in respect of a Trust. The liability of the Manager in relation to a Trust is in any case limited to the Assets of the Trust.

16.5 The Manager has absolute discretion on how and when to exercise its powers.

356 APRA’s submission that “it was highly unlikely that Questor as RE could be indemnified from the assets of the fund where the conduct of NAB and IOOF Service Co, directly imputed to Questor by s 601FB(2) of the Corporations Act, did not amount to the ‘proper performance’ of Questor’s duties as RE in s 601GA(2) of the Corporations Act” should be rejected. Mere inadvertence will not render performance improper: *Saker Re; Great Southern Managers Australia Ltd (recs and mgrs. apptd) (in liq) (No 2)* [2011] FCA 958; (2011) 85 ACSR 211 at [50]-[52].

357 APRA’s case that Mr Venardos considered and accepted the CMT Remediation Plan confronts the difficulty that neither he nor the board as a whole made any decision in respect of the CMT Remediation Plan. The only decision made on 25 September 2012 related to the adoption of the annual accounts. The relevant decision to implement the CMT Remediation Plan had been made a year earlier and the plan had been implemented for that period before it came to the attention of the board. As submitted for Mr Venardos:

Plainly it was not being suggested that the plan required or depended on its consideration or acceptance by the board of Questor in its capacity as trustee of TPS Super. In relation to passing on the consequences of the plan, not only was that not an issue for consideration, the passing on of the consequences was simply distributing among TPS Super beneficiaries the distributions received from the CMT by Questor in its capacity as trustee of TPS Super. There was no occasion for Questor as trustee of TPS Super to hold back or consider holding back those reduced distributions. In fact, any attempt by Questor as trustee of TPS Super to do so would likely be a breach of trust.

358 It was submitted that APRA’s response that Mr Venardos had a duty in the performance of his functions does not accord with its pleading that he considered and accepted the CMT Remediation Plan, which are both exercises of power.

359 Further, it was submitted that APRA had led no evidence as to what a prudent superannuation director would have done if confronted by the same circumstances on 25 September 2012. There is evidence, however, of the qualifications and experience of the other members of the board, none of whom acted any differently from Mr Venardos. The submission was in these terms:

…there is evidence before the court of the qualifications and experience of the other members of the board. There is no reason to suppose that such directors were and are not prudent superannuation trustee directors. They provide an evidentiary litmus test as to what such a director would have done. They did no more or less than Mr Venardos. That is powerful evidence in support of Mr Venardos’ position. APRA submits that other persons who are not parties to the proceedings “may also have contravened the SIS Act is not an excuse for Venardos” (ACS [233(b)]). The conduct of the other directors is not relied on as an excuse, but rather as evidence of the conduct of prudent superannuation trustee directors. APRA has not alleged that those directors breached any duty. If it had alleged that those directors had breached their duty, whether or not they were made parties to the proceedings and whether or not relief was sought against them, they would be entitled to be notified of the allegations against the possibility that they wished to be heard to defend their reputations. The fact that APRA has not made the allegation has the consequence that it is not open to the Court to find that they did breach any obligation. As such, their conduct represents evidence of what a prudent superannuation trustee director would have done in the same circumstances.

360 Otherwise, in dealing with APRA’s allegations as to what he was required to do, the following submissions were made:

(1) It is alleged that Mr Venardos breached the covenants because he did not question management as to whether the CMT Remediation Plan was in the best interests of beneficiaries of TPS Super: however, there was discussion about the impact on incoming members and advice that members would not be impacted as the cost would be borne either by NAB or Questor as RE of the CMT. In these circumstances, it could not be said that the remediation plan was not in the best interests of members.

(2) It is alleged that he breached the covenants because he did not instruct management to cease the CMT Remediation Plan: however, it is not apparent how Questor as trustee of TPS Super could have directed Questor as RE of the CMT to cease the remediation plan. It was submitted that:

There is no exposition in the pleading or in ACS as to the power in Questor as TPS Super trustee to instruct Questor as CMT RE to cease the reduced distributions. Far less is there any exposition as to how Mr Venardos ought to have known about such a power. Even now APRA itself is incapable of either pleading or elucidating such a power yet invites the Court to find that Mr Venardos breached the Act by not requiring such a power be exercised.

(3) It is alleged that he breached the covenants because he did not seek independent legal advice or instruct management to seek independent legal advice as to whether NAB or IOOF Service Co was liable for TPS Super beneficiaries’ losses or the management of the conflict of interest: however, the losses are not identified. Further:

…if it means losses due to the overpayment, there is no allegation or elucidation as to how or why Mr Venardos would know or assume there were losses or what they were. If it is a reference to losses due to the reduced dilutions, he was told that the custodian (i.e. NAB) or the company (i.e. Questor) would pay any costs of the beneficiaries. The need for further legal advice is not demonstrated. Even if there was a basis for the alleged assumed duty, that answer was sufficient and Mr Venardos was entitled to rely on it.

(4) It is alleged that he breached the covenants because he did not seek independent legal advice or instruct management to seek independent legal advice as to whether “Questor in its capacity as trustee of TPS Super had any available defence to a claim by Questor in its capacity as RE of the CMT for restitution of the CMT Overpayment” (ASOC [245(g)(ii)], ACS [228(d)]): however, the proposition:

…demands from Mr Venardos a level of legal sophistication that is beyond the articulation of APRA even now. Further, in any event, there was no answer to a recoupment by a trustee of an overpayment from an overpaid beneficiary.

(5) It is alleged that he breached the covenants because he should have “taken steps to manage conflicts of interest when considering the CMT Remediation Plan including, identifying all relevant conflicts and ensuring the Board’s decision making recorded how those conflicts had been addressed”: however, the submission assumes that Mr Venardos was considering the plan in his capacity as a director of Questor as TPS Super trustee, a proposition contradicted by the evidence as referred to above, hence the submission does not arise on the facts.

(6) It is alleged that he breached the covenants because he should “not have accepted the CMT Remediation Plan until satisfied that conflicts had been appropriately managed or avoided, to ensure decisions were being made in the best interests of beneficiaries”: however, this :

…relies on Mr Venardos having accepted the plan in his capacity as a director of Questor as TPS Super trustee, which is not borne out by the evidence. Further, it is unclear what conflicts had to be managed and avoided and in the exercise of what power or fulfilment of what duty. The reference to “decisions” is unclear. It is not possible to know whether they are decision of Questor in one capacity or another. The very opacity of the submission renders it inutile. Further, fundamentally, there was nothing for an overpaid beneficiary to do but accept the recovery by the trustee of an overpayment.

9.2.6.3 Discussion

361 Mr Venardos must succeed in his defence of APRA’s case against him for the alleged CMT remediation breach for the same reasons as Mr Kelaher has succeeded.

362 Otherwise, to the extent Mr Venardos made submissions which do not overlap with the submissions for Mr Kelaher, I accept that the following matters are of significance and present insuperable difficulties for APRA’s case against Mr Venardos and Mr Kelaher.

363 APRA led no evidence as to what a prudent superannuation trustee would have done on and from 25 September 2012. However, there is evidence of the qualifications and experience of the other members of the boards of the IOOF Group, the details of which were contained in the submissions for Mr Venardos. I accept that the conduct of these directors, given their qualifications and experience, is a proxy for the standard of the prudent superannuation trustee. APRA submitted that no assumption about the conduct of these other directors could be made one way or another. The relevant process, however, is one of inference, not assumption. The steps in the process of the drawing of the inference are rationally available. First, APRA makes no allegations about the conduct of any of those directors. Second, there is evidence which proves that those directors are all highly qualified and well experienced in the relevant field. Third, those directors were in fact confronted by the same circumstances as Mr Kelaher and Mr Venardos. Fourth, nothing in the circumstances provides any reason to infer that those directors acted other than in conformity with their duties. In these circumstances, the fact that the minutes disclose that all conduct of the board was unanimous at all times is the best evidence that neither Mr Kelaher nor Mr Venardos were involved in any breach of their director’s duties in relation to the CMT Remediation Plan.

364 APRA’s contrary submissions are unpersuasive. As I have said, the relevant process is one of inference from the evidence, not assumption. APRA does not challenge the experience or qualifications of the other members of the boards. It is not to the point that in another case, *Morley v ASIC* [2010] NSWCA 331; (2010) 81 ACSR 285, Gzell J did not use the conduct of another director as evidence of the conduct which would meet the relevant standard of care. It may be accepted that the relevant conduct is that of Mr Venardos (and Mr Kelaher). But that does not mean that available evidence as to what highly experienced directors did in the same circumstances is not relevant evidence of what the prudent superannuation trustee director would do.

9.2.7 Mr Coulter

9.2.7.1 Findings sought by APRA

365 APRA did not allege any breach by Mr Coulter of the SIS Act because the covenants in s 52 and s 52A do not apply to him. However, APRA sought that certain findings be made with respect to Mr Coulter. I deal with the findings below:

366 *By no later than 12 September 2012, Mr Coulter had actual knowledge that: (1) the CMT Remediation Plan was already being implemented by his direct report Mr Rossitto; (2) it was causing new TPS Super beneficiaries to receive diluted distributions; and (3) no steps had been taken to compensate those beneficiaries*: I accept that Mr Coulter was aware of these matters by 17 September 2012 but also infer that by then it was also common ground between Mr Rossitto and Mr Coulter that any adversely impacted new member would be compensated either by NAB or Questor as RE. Further, in common with the directors, Mr Coulter first became aware of these matters a year after the CMT Remediation Plan was implemented.

367 *By that time, Mr Coulter was aware or ought to have been aware that the CMT Remediation Plan, in so far as it sought to remedy the CMT Overpayment by diluting superannuation beneficiaries distributions, was not in beneficiaries’ best interests*: no such finding could be made. For the reasons given above, APRA has not proved any facts from which it would be inferred that the CMT Remediation Plan was other than in the best interests of the beneficiaries. It is clear that Mr Rossitto, the author of the plan, considered a range of options and selected the CMT Remediation Plan because he believed it was in the best interests of beneficiaries. APRA has not proved otherwise. Mr Coulter had no reason to believe otherwise.

368 *Mr Coulter was aware or ought to have been aware that he, Mr Rossitto and Questor had a conflict of interest or duty in considering whether the CMT Remediation Plan could continue*: APRA has not explained this conflict of interest. If it is a conflict because of their role as employees of IOOF Service Co, it is difficult to see how the conflict could arise given IOOF Service Co’s responsibilities to Questor, in effect, to assist Questor in fulfilling its SIS Act obligations. In any event, APRA has not proved the existence of an actual conflict of interest between Mr Coulter’s role as an employee of IOOF Service Co and the interests of beneficiaries. APRA assumes the existence of a reasonably arguable claim by Questor as the trustee against IOOF Service Co and itself but has not proved the facts necessary to found the existence of such claims.

369 *Mr Coulter allowed Mr Rossitto and his finance department to continue to implement the CMT Remediation Plan without managing that conflict and seeking advice as to whether compensation from any of the entities that may have been responsible for the original error*: as the submissions for Mr Coulter point out, by this time, the board was becoming involved and the matter had been referred to the Compliance and Legal departments of IOOF. Under IOOF’s Breach and Incident Policy, it was Compliance’s role to request any further information and/or legal advice required to ensure a complete analysis could be made of the issue and an appropriate corrective plan adopted, and to then monitor the implementation of the rectification plan and periodically report to the relevant Boards and the RCC.

370 Contrary to APRA’s case, I accept the submissions for Mr Coulter that:

First, it is clear from the evidence that Mr Coulter did not consider, approve, pass on or implement the CMT Remediation Plan.

Secondly, when it was brought to his attention, it was promptly then communicated to the Questor Board and notified to Compliance in accordance with IOOF’s Breach and Incident Policy.

It was then in the hands of the Questor Board and Legal, Compliance and Risk. The Compliance rectification plan did not include him as the relevant ‘owner’ of the steps to be taken to address the issue, and there is no evidence that they raised any issue with Mr Coulter as the appropriateness of CMT Remediation Plan.

Thirdly, taking into account the relative responsibilities and expertise, it cannot be properly suggested that Mr Coulter was in a better position than Legal, Compliance and Risk, or the Questor Board, to appreciate or consider if independent legal advice should be taken or other steps taken in beneficiaries’ best interests to address the issues, or to assess potential legal claims as between Questor and itself, IOOF Service Co or NAB. The relevant facts were known to members of the Board and the Legal, Compliance and Risk teams.

Fourthly, it is not the case there were no practical difficulties in making claims against NAB or others. As Mr Coulter noted in his email to Mr Rossitto on 19 September 2012, it would be necessary to “have a mathematically sound calculation of how much is their share” and the loss before any meeting with NAB about amounts to be paid in compensation. Even leaving aside legal issues on liability and indemnities, there was also the difficulty referred to in Mr Riordan’s email of 30 October 2014 that members had the benefit of overpayments of circa $2 million, which it was expected would need to be taken into account.

Fifthly, the allegation that Mr Coulter himself did not prioritise Questor’s duties to and the interests of beneficiaries ought not to be accepted. It is apparent from the statements made by Mr Coulter at the Questor Board meeting on 25 September 2012 (including “the member will not be impacted and it is a decision between the Custodian and the company who wears the costs”) that Mr Coulter was seeking to prioritise members’ interests. It is also apparent that the exercise of assessing how many members were adversely affected was not a straightforward one due to the extensive data mining exercise required

###### 9.3 Step 3: The CMT Compensation Plan

9.3.1 APRA’s case – background facts

371 APRA said that Questor was again required to make a decision about how beneficiaries would be compensated and in using the general reserve was exercising a power in cl 10.11 of the Trust Deed which provided that Questor may “apply amounts held in a Reserve Account for…other purposes which the Trustee determines”.

372 As APRA put, it this provision required Questor to form an opinion which was not purely discretionary. Its case is that in doing so “Questor, Kelaher, Venardos, Coulter and Vine failed to act with the required degree of care, skill and diligence; discharge their duties in the best interests of members; and give priority to those interests in circumstances of conflict”.

373 APRA submitted that the respondents’ case does not square with the documents to the extent they said there was always a proposal for compensation. According to APRA, the compensation contemplated in 2011 and 2012 was compensation by NAB or Questor itself whereas the CMT Compensation Plan as developed was of a different nature because it used the members’ funds in the general reserve. This is the decision which founds APRA’s claims of contraventions of s 52 and s 52A of the SIS Act.

374 APRA said that after the compensation from NAB had been negotiated, the issue of the balance of the required compensation had to be considered. The initial proposal was to use funds from the ORFR because it was believed that it had been established for such incidents. APRA said that despite this “proposal being raised at multiple meetings of the Board of Questor and the IOOF Risk & Compliance Committee, the minutes record no challenge by the Board members (including Mr Kelaher or Mr Venardos) as to whether this is the best course of action. The first time the minutes record any real discussion of the source of compensation is at a meeting of the Questor Board on 26 August 2015: CB 9/177. At that meeting, Mr Ian Griffiths, a Questor director, is recorded in the minutes as stating”:

…if this is a custodian error why should any contribution come from the members, it should be the responsibility of the Trustee. It is important to consider members’ best interests, therefore what is fair and equitable to members (i.e. those that were actually impacted).

375 APRA said that this response was appropriate and there is no evidence of any response from other directors. However, on 5 October 2015 Mr Vine and Mr Riordan attended a meeting with APRA where APRA advised that “it had reviewed the breach rectification strategies adopted by IOOF and was concerned that the minutes and papers to the Board did not recognise conflicts”.

376 APRA’s submissions disclosed the sequence of the events on which it relied and its characterisation of those events:

On 16 September 2015, APRA sent an email to Vine (copying Riordan) noting that its review of Questor’s board papers had identified that Questor proposed to use the ORFR to fund compensation for the CMT incident.

APRA asked Vine whether “formal approval” had been sought in respect of the use of the ORFR for the CMT issue and queried whether non-superannuation investors had already been compensation [sic], and from what source of funds: CB 10/211, p. 3299. This email correspondence was followed up by a formal letter from APRA making the point that the use of superannuation fund’s ORFR was not appropriate where the loss arose at the RE level: CB 10/188, p. 3126.

…

…APRA’s query sparked a search by Vine, Mr Rossitto and Ms Erica Clarke (and IOOF Legal Counsel) to find another source of beneficiaries’ reserves that could be used to pay the compensation amounts. Coulter was copied on all of these emails. The sequence of events is as follows:

(a) On 22 September 2015 (CB 10/192A), Vine and Mr Rossitto exchanged emails about “[w]hy we say the ORFR can be used to compensate clients in relation to the CMT breach”. As part of this exchange, Mr Rossitto explained:

“Isn’t the use of the ORFR designed to compensate for such errors at TPS fund level? … Unit pricing incidents, system incidents, human error etc are what the ORFR was established for. It’s established for errors, historical errors, **some caused by third parties where compensation can be recouped, the rest to be used by the ORFR**. Perhaps Legal can look at the standard and our policy and provide confirmation. Will discuss with Erica.” (emphasis added)

Mr Rossitto also explained to Vine in the same email that non-superannuation investors had already been compensated from the NAB settlement money (as identified above).

(b) On 30 September 2015 (CB 10/192A), Ms Clarke responded with some advice on whether the ORFR could be used. Vine and Coulter were both recipients of this email. Ms Clarke concluded that the ORFR would not be available as:

“…the original error involved human error / failed internal processes that occurred at the custodian and/or CMT level not the fund level so the trustee would not be permitted to use the ORFR for operational risks arising at the CMT level.”

Relevantly, Ms Clarke also advised:

**“In considering what is fair and equitable, the trustee should consider what rights to damages it has from the CMT where the original error occurred and whether it is appropriate to recover any amounts from the CMT (in addition to the settlement amount already received from NAB).**

…

It is open to the trustee to utilise funds from the general reserve to fund compensation and this might be a more risk averse solution than seeking to access the ORFR for this particular error.” (emphasis added)

The highlighted section is noteworthy. It represented legal advice by Ms Clarke that Questor’s duties to act fairly and equitably (implicitly pursuant to s 52) required it to consider whether it was in the best interests of beneficiaries to pursue other sources of compensation, in addition to the settlement with NAB, and in particular from itself as RE of the CMT.

(c) On 13 October 2015 (CB 10/211A) Vine replied to Ms Clarke’s email (again, copying Coulter) and said “Perhaps we can all agree the preferred solution from a reserve perspective then work back from there?”

This comment, which suggested “work[ing] back” from a solution involving the use of a reserve, appears to have ignored the aspect of Ms Clarke’s advice concerning consideration of “rights of compensation”. It demonstrated that Vine had effectively closed his mind to the possibility of sources of compensation other than the reserve.

(d) On 15 October 2015 (CB 10/211A), Mr Rossitto also replied to Ms Clarke’s email (again, copying Vine and Coulter). In his response, he re-confirmed (consistent with his earlier report) that the CMT Overpayment was in fact a failure of processes at both the RE and RSEL level. Mr Rossitto said:

“In relation to this particular breach, over the last few years I have documented control weaknesses of Questor in its capacity as Responsible Entity of the CMT and in its capacity as RSE of the TPS Retirement Fund…

…

Operationally, at the time of the incident, this was seen as all TPS related as there was no understanding nor comprehension of the legal structure where a separate CMT sat outside of TPS.

Given APRA’s feedback and the general reluctance to use the ORFR directly to fund compensation I agree with Erica’s sentiments to use the general reserve directly…”

This was a further acknowledgement by Rossitto, seen by Vine and Coulter, that Questor as RE or trustee was the responsible party for the CMT Overpayment, in addition to any responsibility that NAB had.

377 During this period APRA noted that Mr Kelaher was being kept informed:

(a) On 5 October 2015 (CB 10/193A) Mr Rossitto (copying Coulter) passed on aspects of Ms Clarke’s advice to Kelaher noting:

“Legal have advised on the use of the ORFR and prefer that general reserves be used … General reserves may be used but I believe APRA has some outstanding queries”.

(b) On 15 October 2015 CB (10/193B), Mr Rossitto provided a further update to Kelaher (copying Coulter) that said:

“In conjunction with legal, propose to fund compensation from general reserve as it is a less riskier path to take with APRA. Legal/Compliance to advise Board of this approach.”

There is no evidence that Kelaher pushed back on this approach, or queried why APRA would be more content with the use by the trustee of the beneficiaries’ general reserve as opposed to the ORFR.

378 APRA noted that on 16 October 2015, Ms Clarke shared her first draft of the CMT compensation board paper with Mr Vine: CB 10/212B. The draft (consistent with the final version) included a recommendation that the TPS Super general reserves be used to pay compensation. APRA said that Ms Clarke sought to justify the use of the reserves as follows:

Other sources of funding were considered but the alternatives were neither legally nor commercially viable in these particular circumstances, on the following bases:

* Funding TPS Super via the ORFR - the breach occurred as a result of an operational risk event occurring within the CMT therefore the trustee does not consider that it is compensable from the ORFR;
* Making a PI claim for TPS Super's loss - the compensation amount is below the insurer's excess of $xx; or
* Trustee taking legal action against NCS for the entire amount - given the circumstances, favourable settlement terms were met without the need to resort to litigation.

379 Mr Vine reviewed this early draft and provided comments (CB 10/212BA:

Thanks that is coming along well. Initial thoughts:

…

* Can you please insert in section 4 why we could perhaps use the ORFR (from your email advice) and why it’s better to use the GR [general reserve] (this will be useful for APRA).
* **PI claim – not sure this was ever considered although the loss amount would be well above the excess. Maybe we say that other sources of funding were considered and pursued, with a favourable commercial settlement with NAS**?” (emphasis added)

380 APRA said that the outstanding amount of compensation was well over the excess ($250,000 compared to the 50% balance of compensation of $1.616 million) but Questor’s capacity to make a claim had lapsed in 2010. Otherwise, APRA said that the second comment of Mr Vine was difficult to reconcile with the facts as the only claim that had been made was against NAB.

381 Mr Vine settled the final version of the paper on 19 October 2015 (CB 10/212G). The final version contained a section prepared by Mr Rossitto which said:

Questor’s investigation into the breach found that there was a control gap relating to the monitoring and review of investment performance and daily yields. Questor’s investigation also highlighted the following:

* investment governance, investment compliance and monitoring of third party outsourcing required improvement;
* a lack of clarity around roles, responsibilities, procedures and process flows;
* a lack of understanding of the legal structures of the CMT and TPS;
* poor understanding of source documents and reports supplied by external parties and investigation of reconciling, outstanding and excluded items

382 According to APRA, these statements would have alerted Mr Vine to the fact that Questor, both as RE and trustee, had a potential exposure to compensate for the losses suffered by beneficiaries. APRA said:

Rossitto was informing Vine that, by not having in place basic investment governance procedures (such as reviewing yields and distributions), Questor had failed to act with the degree of care, skill and diligence required of it both as RE and trustee. Further, to any reader familiar with the IOOF Group structure (which must have included Vine), the exposure of IOOF Service Co would also be clear. It was the entity that supplied the personnel and services to Questor in its various roles and therefore should have been carrying out those procedures.

383 APRA recorded that the final version of the paper that went to the meeting of the Questor board on 28 October 2015 is at CB 10/212. It is dated 16 October 2015, although it must in fact have been signed after 19 October 2015 (see above). It is authored by Mr Rossitto and Ms Clarke, and endorsed by Mr Coulter and Mr Vine (p. 3309).

384 The recommendation to the board made in the report was that the payment of compensation to TPS Super beneficiaries impacted by the breach, to the value of $2.775 million (plus interest of $13,875), be sourced from:

(a) the remaining proceeds of settlement between NAB and Questor ($1.173 million);

(b) the “shortfall” be paid from the TPS Super general reserve ($1.616 million),

(the **CMT Compensation Plan**: CB 10/212, p. 3310)

385 APRA said:

The paper further noted that Questor, as RE of the TPS MIS, has already fully compensated non-superannuation beneficiaries to the value of $392,000 using the NAB settlement (p. 3310). The paper accordingly squarely put Kelaher and Venardos on notice that the NAB settlement had been preferentially paid to non-superannuation members rather than being distributed pro-rata. Coulter and Vine, of course, already knew this fact.

The paper then set out the “Background to the breach” prepared by Mr Rossitto. As indicated above, that section – in no uncertain terms – identified that the CMT Overpayment was not solely caused by NAB’s breach. It was a significant breach by Questor as RE (as had been reported to ASIC), and had highlighted a control gap relating to Questor and IOOF Service Co’s monitoring and review of investment performance and daily yields.

Under the heading “Sources of compensation”, Coulter and Vine explained the rationale for recommending the use of the beneficiaries’ own reserves to pay compensation (pp. 3312-3313). In essence, the explanation given was as follows:

(a) The error had arisen because of NAB’s failed monitoring and reconciliation process. Questor had pursued compensation from NAB and had reached a commercial settlement.

(b) Based on internal legal advice (presumably Ms Clarke’s earlier advice), the ORFR was not available because the requisite “operational risk” did not arise at the super fund level.

(c) An insurance claim under Questor’s professional indemnity policy may have been “potentially open” but was “commercially unviable” due to the “complexities of the claim” and the “potential effect on future premiums (which may need to be passed onto members via an increase in administration fees)”.

(d) The general reserve was therefore recommended because Questor’s internal policies allowed it to be used for “any purpose the Trustee deems appropriate” and APRA “did not exclude the use of reserves to compensate fund loss”. It was further asserted that Questor “has explored all other viable sources of compensation”.

386 On 28 October 2015, the Questor board met and considered the CMT Compensation Plan endorsed by Mr Coulter and Mr Vine. Mr Kelaher and Mr Vine attended this meeting. According to the minutes the discussion involved three points:

(a) Noting the summary of the breach had been notified in 2012 and the proposed rectification strategy and source of compensation;

(b) Questioning how the interest component was being calculated;

(c) Querying how ex members would be remediated.

387 The board resolved unanimously to approve the compensation payment, including the use of the general reserve to the value of $1.616 million. The meeting took 32 minutes.

388 In APRA’s words:

The minutes do not record any discussion by the Board of whether the source of compensation was appropriate, whether it should pursue other sources of compensation (including itself or IOOF Service Co), or whether it was in beneficiaries’ best interests to use their own general reserve to pay this compensation. The minutes are signed and are evidence of the proceedings of the Board unless the contrary is proved: Corporations Act 2001 (Cth), s 251A. Neither Kelaher nor Venardos have led any evidence that would prove that any further discussion occurred at the meeting other than recorded in the minutes. APRA submits that based on the minutes and the length of the meeting, the Court would infer that the proposal was adopted with minimal critical engagement by either Kelaher or Venardos.

No conflicts of interest were declared in relation to compensation plan, despite Kelaher and Venardos each being directors of IOOF Hold Co and Kelaher being a director of IOOF Service Co (p. 3321). There is also no record that the Board declared they had acted as trustee in the best interests of beneficiaries, as required by IOOF’s COI Policy.

389 Questor implemented the CMT Compensation Plan. Questor paid compensation to TPS Super beneficiaries in April 2016. In accordance with the CMT Compensation Plan, the compensation was funded partially from the remainder of the NAB settlement and partially from the general reserves.

390 According to APRA, Mr Kelaher and Mr Venardos each had ample opportunity to reconsider the CMT Compensation Plan and revoke the decision or, after the reserve had been used, to replenish the reserve. APRA provided the following table summarising each of the meetings of the board of Questor or (after the SFT in June 2016) IIML following the approval of the plan. At none of these meetings, APRA said, was there any serious reconsideration of the approach to compensation.

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | **Date** | **CB** | **Board meeting** | **CMT discussed** | **Summary of discussion** |
| 1 | 27/1/16 | 11/224 | Questor | No. | Meeting convened to consider SFT of TPS Super to IPS Super. |
| 2 | 6/2/16 | 11/262 | RCC | Yes. | Compensation on hold pending ATO ruling. |
| 3 | 24/3/16 | 11/244A | Questor | Yes | Compensation on hold pending ATO ruling. |
| 4 | 25/5/16 | 11/258C | Questor | Yes. | Note that payment made on 30 April 2016 from general reserve. |
| *TPS Super transferred to IPS Super; IIML responsible for CMT compensation* | | | | | |
| 5 | 17/11/16 | 12/297C | RCC | No. |  |
| 6 | 13/2/17 | 13/312 | IIML | No. |  |
| 7 | 13/2/17 | 13/314  p. 4221 | Questor | Yes. | Notes meeting with APRA and “difference of opinion”. |
| 8 | 28/3/17 | 13/322 | IIML | No. |  |
| 9 | 25/5/17 | 13/352B | RCC | No. |  |
| 10 | 28/8/17 | 15/368A | IIML | No. |  |
| 11 | 25/10/17 | 15/ 376A | IIML | No. |  |
| 12 | 12/2/18 | 15/387C | IIML | No. |  |

391 On 12 December 2016, after learning of the details of the CMT Compensation Plan, APRA had advised Questor that it did not consider the use of beneficiaries’ reserves to compensate members for breaches by Questor or related entities to be in members’ best interests. APRA requested that Questor look to replenish the reserve from its own funds: CB 13/302, p. 4093.

392 On 19 April 2017, Mr Kelaher (on behalf of Questor) replied to this letter: CB 14/331, p. 4973. As APRA put it:

That letter sought to justify the decisions that Questor had made, asserting that it had (unclear when) received “senior legal advice” that it was not liable as RE. That legal advice has never been disclosed to APRA and is not relied upon by any of the respondents in this proceeding to defend their position. Kelaher’s letter signed off by asserting that Questor had passed the “pub test”, which he described as a “proxy for members’ interests” (p. 4978). It appears from the Board minutes that IIML effectively considered the issue closed after this; despite their ongoing obligation to act in members’ best interests.

393 There were other interactions between APRA and IOOF about the use of the reserves and conflicts of interest. In APRA’s words:

It was only following IOOF’s appearance at the Royal Commission into Banking Misconduct and Kelaher’s resignation from the IIML Board that the reserve was finally replenished in September 2018. Even then, Questor and Venardos refused to acknowledge the earlier breach, labelling the replenishment as a sign of “good faith” to APRA: CB 17/428, p. 6138.

9.3.2 APRA’s case – Questor and IIML’s alleged CMT Compensation Plan breaches

394 APRA contended that Questor was in a position of conflict in considering, adopting and implementing the CMT Compensation Plan as it was a potential source of compensation, as was its related party, IOOF Service Co. It also had competing duties to investors in the TPS MIS with regard to the distribution of the finite NAB settlement monies.

395 According to APRA:

In circumstances where those other potential sources of compensation outside of the trust fund existed, APRA submits that it was not in the best interests of beneficiaries to approve and implement a compensation plan that preferentially paid third-party sourced compensation to MIS investors and used beneficiaries’ trust money to compensate them for losses without first at least exploring the possibility of making a claim against the IOOF Group companies involved, or making good the loss from the trustees funds. To the extent there was any indemnity available to the trustee (as to which, see above) that – as with the reserves – should have been a last resort after all other avenues of compensation had been exhausted. It is not in beneficiaries' best interest for a trustee to indemnify itself from trust funds where it has other sources of indemnity (i.e. from IOOF Service Co) available to it.

APRA submits that by considering, adopting and implementing the CMT Compensation Plan (including the use of beneficiaries’ reserves) until September 2018, without taking steps to seek to recover compensation from itself or IOOF Service Co, Questor contravened the statutory covenants in s 52(2)(c) and (d) because it failed to act in beneficiaries best interests and prioritise those interests despite the conflict. Not only was this a breach of the statutory norm of conduct, but it was a breach of Questor’s own conflicts of interest management policy that, by means of SPS 521 and s 52(2)(d)(iv), informed the standard of conduct required.

APRA submits that following the successor fund transfer of the assets and members of TPS Super to IPS Super in June 2016, IIML became responsible for the ongoing consideration of the CMT Compensation Plan. It accordingly breached its obligations under s 52 for the same reasons as Questor from that date until September 2018.

9.3.3 Questor’s and IIML’s case – alleged CMT compensation plan breaches

396 Questor noted that the compensation payment to TPS Super beneficiaries was approximately $2.8 million with approximately 50% sourced from the NAB settlement sum and 50% from the TPS general reserve. APRA’s claim was that Questor as RSE breached Questor’s Best Interests Covenant and Questor’s No Conflicts Covenant, those alleged contraventions being defined in the ASOC as Questor’s CMT Compensation Breach.

397 Questor submitted that for the reasons already given, none of the alleged exposures to liability of IOOF Service Co or Questor existed, so APRA’s case must fail.

398 Questor noted that the core of APRA’s complaint is that Questor failed to pursue the other possible claims or exposures, and instead used the TPS general reserve to compensate members for loss, which was not in the best interests of beneficiaries. However:

Questor had the power and entitlement to utilise the General Reserve. In particular, the payment of compensation to members from the general reserve was permitted by the TPS Trust Deed and Questor’s Reserves policy. Further, Questor’s use of the general reserve was only undertaken after Questor had successfully pursued the party responsible for the error and recovered compensation from that party. Additionally, a prudent trustee in Questor’s position would not have pursued these other “exposures” given they either did not exist or were weak at best, they were complex and difficult to quantify, and would have exposed the Fund to the difficulties, costs and risks associated with the pursuit of such claims (as explained in greater detail above). In any event, the general reserve was subsequently replenished by IIML with a payment from IIML’s own funds.

399 According to Questor, APRA’s submission that the NAB settlement was not pursued with any vigour should be rejected. To achieve a 50% settlement sum without expending significant legal costs was a good result.

400 Further, the implementation of the CMT Compensation Plan had the desired result that all members were fully compensated as confirmed by Ernst & Young in its independent analysis. As such, Questor clearly acted in the best interests of members.

401 It was also submitted that the part of APRA’s case that asserted breach “by using the NAB Settlement Amount to wholly and preferentially pay those investors in the TPS MIS but not wholly or instead compensate the beneficiaries of TPS Super” was misconceived. This was because:

(a) NAB paid the settlement amount to Questor as RE; and

(b) Questor as RE then decided how those monies would be dealt with as between the two unit holders in the CMT (being Questor as RE of the TPS MIS and Questor as RSE of TPS Super).

How Questor in its capacity as RE chose to deal with the NAB settlement amount was a matter for it. On no view can it be said that the RE’s decision could somehow give rise to a breach of the Best Interests and No Conflicts Covenants by Questor in its capacity as RSE. This is a further reason why APRA’s allegations relating to Questor’s CMT Compensation Breach should be rejected.

402 The case against IIML depends on the case against Questor and thus must also fail. In addition, however, APRA’s submission is that merely by reason of the successor fund transfer IIML became responsible for the ongoing consideration of the CMT Compensation Plan and therefore breached its obligations under s 52 of the SIS Act. But Questor had fully compensated all members of TPS Super prior to the successor fund transfer to IIML. Further, it was submitted:

…if APRA’s case in relation to this alleged breach, is that IIML somehow continued to implement the CMT Compensation Plan by not replenishing the General Reserve despite the fact investors had been fully compensated by the time it became RSE (which we say cannot sensibly constitute “implementation” of a plan), then this is entirely dependent on the true characterisation of the General Reserve and how and when it can be used by the RSE. For the reasons detailed above at paragraphs [106] to [108] use of, and therefore failure to replenish, the General Reserve could not constitute a breach of s 52 of the SIS Act.

403 At [106] - [108], the submissions for the fourth to seventh respondents noted that IOOF’s Reserves Policy provides that:

(a) the purpose of the General Reserve 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;

(b) there are a number of specific types of general reserves that can be created and maintained by the Funds, including ‘Operational Risk’;

(c) the General Reserve is otherwise made up of funds including, for example:

(i) contributions to the fund which, at year-end, are yet to be allocated to members (and therefore do not yet form part of members’ benefits);

(ii) unallocated bank or ATO interest;

(iii) frozen investments from redemption of members through financial hardship claims;

(iv) interest earned on the General Reserve’s assets each month.

(d) the General Reserve may be utilised for any purpose that the Trustee deems appropriate and within the parameters disclosed by the Funds’ Trust Deeds.

404 Further:

The General Reserves Policy has been amended a number of times since 2013, and in May 2016 for example it was amended to make express reference to “the payment of compensation” as one of the permitted applications of the reserve. However, given the breadth of the Trusts Deeds and the working of the previous policy, this was always a permitted use of the reserve but was made express by the amendment.

9.3.4 Discussion

405 The submissions for the respondents should be accepted.

406 APRA’s essential complaint, as its oral submissions disclosed, is that no payment out of the reserves can constitute “compensation” because the reserves constitute members’ money. Further, because the reserves constitute members’ money, APRA would have it that all possible sources of compensation other than the reserves have to be considered (and, it seems, eliminated as not reasonably arguable sources of compensation) before any reserve may be accessed to pay beneficiaries.

407 Even if APRA had proved the underlying facts necessary to make good its case, this case theory is too rigid. Contrary to APRA’s refrain, a decision whether or not to pursue a potential source of compensation is discretionary and will be affected by a wide range of factors. It cannot be that in every case the kind of rigid exercise which APRA would impose on the decision-making process is mandatory and but for which the corporation and its directors would be in breach of their covenants.

408 In the present case, the underlying facts have not been proved. It has not been proved by APRA that there was any viable claim that could have been made. It has not been proved that in the circumstances as they existed it was not in the best interest of members for the compensation plan to proceed as it did. It has not been proved that there was any actual, as opposed to theoretical, conflict of interest capable of having any significant impact on the capacity of the respondents, as relevant, to give priority to the interests of the beneficiaries of the trust. It has not been proved that such priority was not given. Further, in terms of use of the general reserve, its use to compensate the adversely affected beneficiaries was within power and was for a proper purpose. Indeed, in the circumstances as they existed using the general reserve ensured that members were treated equitably and fairly, having regard to the fact that it was incoming members who had suffered loss as a result of the remediation plan and one purpose of the reserves was to amortise losses across past, existing and future members. Accordingly, I accept the submission made for the first respondent that:

While the general reserve was “trust money”, use of the general reserve to compensate members in the circumstances was within the terms of trust, caused no financial or other detriment to any member and compensated members of TPS Super who had suffered losses as a result of the CMT issue. On any view, that use of the general reserve was in members’ best interests.

409 On the facts as I have found APRA’s case based on, the no conflicts covenant must also fail. The absence of any reasonably arguable claim against Questor and IOOF Service Co means that there was no competing interest to the best interests of the beneficiaries. APRA has not proved that any action was taken other than with the best interests of beneficiaries as the priority over any competing interest to the extent any such interest might have existed.

9.3.5 APRA’s case – Mr Kelaher’s alleged CMT Compensation Plan breaches

410 According to APRA, Mr Kelaher had the same conflicts as he did for the alleged CMT Remediation Plan breaches and, as a superannuation trustee director, had to bring a critical mind to the CMT Compensation Plan, which was presented to the board on 28 October 2015 to determine whether that plan was in the best interests of beneficiaries, despite the conflict, before exercising his power as a director to vote in favour of the plan. APRA said that it was relevant that Mr Kelaher knew or ought to have known that:

(a) The losses to beneficiaries flowing from the CMT Remediation Plan and CMT Overpayment flowed directly from the actions and omissions of Questor and IOOF Service Co;

(b) Accordingly, the proponents of the plan, Coulter and Vine, who were both senior executives of IOOF Hold Co and IOOF Service Co as well as acting as responsible officers of Questor, had a conflict of interest;

(c) That he himself, as Managing Director, had the conflict of interest mentioned above, and needed to make sure that his decision was not consciously or unconsciously swayed by interests other than those of the beneficiaries (which he was required to prioritise by reason of s 52A(2)(d)).

411 As he was on notice of these conflicts, “special vigilance” and “scrupulous concern” was required: *HIH Insurance* at [372(14)]. APRA’s case is that Mr Kelaher did not exercise the required standard of care, skill and diligence in approving this plan and did not act in the beneficiaries’ best interest. In particular:

The brief discussion at the 28 October 2015 Board meeting did not touch upon the relevant question, namely the one asked by Ian Griffiths at the previous meeting: why are beneficiaries paying for the IOOF Group’s errors? It was incumbent upon Kelaher to seek an answer to this question before voting to approve the compensation plan. Considering the conflicted position of management, the most prudent course would have been to answer that question by way of independent legal advice. This was not considered.

412 According to APRA, the submission for Mr Kelaher that the compensation plan was the subject of a “detailed memorandum prepared by experienced senior managers and lawyers within the IOOF Group” which “was, on its face, well-reasoned and logical, and exhibited a large degree of commercial common sense” should not be accepted. In short, as to this report, APRA submitted:

(a) It is not detailed with respect to management’s consideration of other sources of compensation other than the reserves. There is no consideration of the paper Questor’s own potential liability as RE of the MIS (which Kelaher was aware of by virtue of having seen the ASIC letter and NAB letter’s that each appeared to acknowledge that Questor was liable) or IOOF Service Co’s potential exposure (as the administrator of the relevant funds).

(b) It is not “well-reasoned and logical”. Despite noting that the cause of the original CMT Overpayment was various failures by Questor’s investment governance framework, it does not propose holding those responsible for those failures (namely, Questor or IOOF Service Co) accountable for the losses suffered.

(c) It may have exhibited a “large degree of commercial common sense”, but only when considered from the perspective of the IOOF Group as a whole; not from the perspective of beneficiaries’ best interests. The same blind spot is apparent in Kelaher’s letter to APRA dated 19 April 2017 (CB 14/331, p. 4976 – penultimate paragraph). While it may have been an inconvenience to the IOOF Group to have had to pay money to beneficiaries for its own errors, that it is no reason for a trustee to decline to make a claim for such compensation.

413 APRA said further that Mr Kelaher was on notice by 28 October 2015 that what was recorded in the paper may not be the complete picture as to why the reserve was being used. By email dated 15 October 2015, he was told by Mr Rossitto that it was proposed to “fund compensation from [the] general reserve as it is a less riskier path to take with APRA”:

414 At ASOC [271] and [273] APRA identified the steps which Mr Kelaher should have taken, which are largely the same as those identified for the CMT Remediation Plan. APRA said:

In short, a prudent director would have identified and declared the conflicts and not approved the plan without undertaking further inquiries to ensure the plan was in beneficiaries’ best interests including, most importantly, determining whether all other avenues of compensation had been exhausted. The most prudent way to have done this would have been to seek advice from an independent (i.e. non-conflicted) lawyer.

415 Further, Mr Kelaher did not comply with IOOF’s own conflicts management policy in making the decision. He did not identify the conflict and he did not ensure that the minutes of the meeting addressed the conflict. This was not only a breach of an internal policy (which sounds in a failure to exercise care, skill and diligence) but a breach of his responsibilities under SPS 521, and therefore s 52(2)(d)(iv).

416 Accordingly, APRA submitted that Mr Kelaher:

…breached his statutory covenants under s 52A(2)(b), (c), (d) and (f) by approving the plan without taking adequate steps to protect beneficiaries’ interests. Further, APRA submits that the Court would find that Kelaher continued to contravene s 55(1) for so long as he refused to revoke the CMT Compensation Plan. As set out above, he had ample opportunity to revisit and re-make the decision, including after the general reserve had been used by directing management to replenish it. APRA requested that he do this; he refused to do so. It was only ultimately once he had left the Board of IIML (the successor to Questor) that the decision was reversed.

417 APRA said, in response to submissions for Mr Kelaher, that:

(1) “A prudent superannuation trustee director could not be satisfied, having read that paper, that the best interests of beneficiaries had been taken into account, let alone prioritised, or that Coulter and Vine’s conflicts of duty had been managed in accordance with s 52(2)(d) and SPS 521. In those circumstance, it would hardly have been ‘silly’ to have called Vine and Coulter in to answer questions about the formulation of this plan and, in particular, the extent to which other sources of compensation had been considered. An obvious question would have been ‘have you received any independent legal advice on those liabilities or this plan?’. Contrary to Kelaher’s submissions; this is the course that a prudent director, acting with the requisite degree of care, skill and diligence, would have taken.”

(2) Mr Kelaher’s submission “appears to assert that accepting management’s conclusions in [a] paper presented to the Board would only be a breach of the SIS Act if the conclusions in that paper were ‘so deficient that no director or officer of a registrable superannuation entity could reasonable accept the recommendations therein’. This is not the relevant test. For the reasons set out above, APRA does submit, however, that the conclusions in the paper were deficient and that a prudent superannuation trustee director would not have accepted them without making further enquiries.”

(3) Mr Kelaher’s submission that the “substance of the advice” was that there was “no clear factual basis for the claims that APRA contends should have been made, and there were practical difficulties in bringing such claims in any event” cannot be sustained.

(4) Mr Kelaher’s submission of the need for expert evidence should not be accepted as the Court is well placed to assess whether his conduct measured up to the relevant standards of care.

(5) The description of APRA’s case as superficial and insubstantial should be rejected. The primary allegation is that Mr Kelaher and Questor had a conflict of interest “and should not have approved the compensation plan without ensuring that it was in beneficiaries’ best interest. The particular steps that it is said he should have undertaken are the steps that a prudent superannuation trustee director would have taken to ensure this occurred.”

9.3.6 Mr Kelaher’s case – Mr Kelaher’s alleged CMT Compensation Plan breaches

418 It was submitted for Mr Kelaher that unless Questor’s CMT Compensation Plan breach is accepted then the claim against Mr Kelaher must fail.

419 By reference to the pleadings, the submissions for Mr Kelaher identified three distinct allegations of breach.

420 The first is that Mr Kelaher breached the Due Diligence Covenant, Best Interests Covenant and Director Compliance Covenant because he:

a) relied on the CMT compensation paper and “did not ask management to attend the meeting of the Board and explain and answer questions” (ASOC [271(d)]);

b) accepted management’s conclusion in the CMT compensation paper that making a claim against Questor’s insurance policy was not commercially viable (ASOC [271(e)]);

c) did not seek independent legal advice or cause management to do so as to whether Questor was liable or IOOF Service Co was liable to compensate superannuation beneficiaries (ASOC [271(f)]); and

d) did not reject the plan or adjourn the meeting so that management could answer questions and legal advice could be obtained (ASOC [271(g)]).

421 As to (a), it was submitted that a director is not “not required by ss 52 or 52A of the SIS Act to receive recommendations in person, nor required to ensure that management are available in person at Board meetings to answer questions. If the Board of IIML had questions regarding any matter proposed by management, they doubtless felt able to request further information. The absence of management from board meetings could not, of itself or in combination with any other matter, result in Mr Kelaher breaching his obligations under the SIS Act. In any event, APRA does not suggest that, had management attended, the decisions of the Boards would have been different. Indeed, it does not even suggest what information ought to have been sought from management that was not clearly addressed in the memoranda or known to Mr Kelaher”. Further, it is “apparent on the face of the paper that no independent legal advice had been obtained — indeed, that is one of APRA’s criticisms of it. There was no reason to require Mr Vine and Mr Coulter to attend the Board meeting merely so that they could provide obvious answers to unnecessary questions”.

422 As to (b), it was submitted that there is “no evidence whatsoever to suggest that the second point was anything other than a correct analysis of the position and, in any event, there is no evidence to suggest that Mr Kelaher would have known that it was incorrect even if that was, in fact, the case”.

423 As to (c), it was submitted that “Ms Clark was the author of the paper and a lawyer. Mr Kelaher had no reason to doubt the correctness of the advice she was providing and no reason to believe that she would provide anything that a complete account of the legal rights and liabilities at issue. Notably, Mr Kelaher did not receive the correspondence on which APRA places so much reliance at ACS [258]-[261] and [263]-[271], other than the undetailed updates referred to at ACS [262]. In those circumstances, Mr Kelaher had no reason to believe that independent legal advice was needed. APRA tries to make something of the fact that Mr Kelaher was informed that using the general reserve, as opposed to the ORFR, was less ‘risky’ in terms of dealing with APRA,…[but] The more natural reading of that statement, however, is that Mr Vine and Mr Riordan were proposing using the general reserve because they thought the company should not pursue a course that APRA would disapprove of. That is no doubt how Mr Kelaher read it”.

424 As to (d), it was submitted that the point is merely repetitive and thus also must be rejected.

425 The second alleged breach against Mr Kelaher in relation to the CMT issue is the same conflicts of interest breach alleged in relation to the Pursuit and Sweep issues (ASOC [274]) and suffers from the same deficiencies. That is, Mr Kelaher had no reason to suppose that the conflicts of interest in fact existed. Accordingly, it was said “[o]nce it is appreciated that the conflicts of interest did not exist in substance, the allegation fails”.

426 The third alleged breach against Mr Kelaher in relation to the CMT issue is that, from 28 October 2015 to 5 October 2018, he did not take any, or any adequate, steps to cause Questor or IIML to revoke or amend the CMT Compensation Plan so that the compensation was wholly paid, or wholly reimbursed, from sources other than the general reserve (ASOC [274A]-[274B]). In answer it was said:

There is an obvious difficulty with that allegation in circumstances where Mr Kelaher was only one member of the Board and was not able himself to force IIML or Questor to conduct themselves in a manner other than that approved by the Board. For that reason, the allegation must be rejected. In any event, compensation had already been pursued and obtained from NAB and, for the reasons explained above, there was no reason for Mr Kelaher to consider that compensation should be pursued, and would be obtained, from other sources.

9.3.7 Discussion

427 Again, I find the submissions for the first respondent compelling. APRA’s case against Mr Kelaher for the CMT Compensation Plan breaches cannot succeed in the face of my other conclusions. The inescapable fact is that APRA’s case fails at each step on the question of proof. It has not proved the underlying facts from which it would be inferred that the CMT Compensation Plan was other than in the best interests of beneficiaries. It is not possible to conclude that in acting as he did Mr Kelaher contravened any of his director’s covenants. The conflicts said to exist are merely theoretical in the actual circumstances as they existed at the time. The material with which the board was presented was, on its face, clear, comprehensive and logical. There was no reason for the board to require management to attend to answer questions. Further, on my findings there was no reasonably arguable case against anyone for the loss caused by the CMT Overpayment, recalling that NAB’s settlement related to loss caused by the CMT Remediation Plan. As such, there was never a call, let alone a requirement, for independent legal advice to be obtained. The general reserve was appropriate to be used in the circumstances as they existed. None of the allegations against Mr Kelaher are sustainable for the reasons given by the first respondent.

9.3.8 APRA’s case – Mr Venardos’ alleged CMT Compensation Plan breaches

428 APRA submitted that Mr Venardos contravened his obligations under ss 52A(2)(b), (c), (d) and (f) of the SIS Act largely for the same reasons as Mr Kelaher had done so.

429 APRA noted that Mr Venardos in particular emphasised that he did not breach his duty because he relied upon management and his fellow directors. According to APRA, this reliance was misplaced as Mr Venardos knew or ought to have known that “Coulter, Vine and his fellow directors all had a conflict and that accordingly the proposal being presented to him required ‘*special vigilance*’. He ought to have known this because of his knowledge that Coulter and Vine were officers of IOOF Service Co (as he admits in his Defence, [12]-[13]) and because APRA had raised the issues of conflicts directly with him at the meeting on 13 October 2015. Despite this knowledge, there is no evidence in the board minutes of the 28 October 2015 meeting or any later meeting that he exercised the required vigilance”.

430 APRA submitted that “the Court would find that Venardos continued to contravene s 55(1) for so long as he refused to take steps to revoke the CMT Compensation Plan. He knew that APRA had requested that Questor do this and that Questor had refused to do so. It was only in September 2018, after IOOF had appeared in the Royal Commission and APRA had made a further request for reconsideration that Venardos ultimately ‘*as a sign of good faith*’ agreed to the replenishment”.

431 APRA said that the submission against it that the complaint is merely that it was reasonably arguable that Questor and IOOF Service Co was liable and Mr Venardos could not have known that should be rejected as:

First, as a member of the Board of Questor and of the RCC, Venardos had received continual updates from September 2012 on the CMT issue. A number of those updates (including the updates attaching the ASIC letter) indicated that Questor was proposing to pay the compensation.

Second, at the meeting immediately prior to the October 2015 Board meeting, Mr Ian Griffith’s had asked why Questor as RE was not paying the compensation. Contrary to Venardos’ submission, the potential liability of Questor was known by the other directors on the Board.

Third, the paper presented to the Board did include facts that should have put Venardos on notice of Questor (or IOOF Service Co’s) potential liability. Relevantly, the paper said that *“Questor’s investigation into the breach found that there was a control gap relating to the monitoring and review of investment performance and daily yields”* and identified that Questor had reported this as a breach to ASIC (which, of course, was a matter than Venardos already knew from previous meetings). Venardos ought to have known that IOOF Service Co was potentially liable for this conduct too as he was required as a director to be familiar with the business of Questor, including that it outsourced all of its administrative services to IOOF Service Co

9.3.9 Mr Venardos’ case – Mr Venardos’ alleged CMT Compensation Plan breaches

432 Mr Venardos’ submissions noted that on 28 October 2015, the board of Questor resolved to approve the payment of compensation to beneficiaries of TPS Super in a total amount of   
$2.775 million plus interest accrued to payment and to source that compensation from the balance of the proceeds of settlement with NAB being $1.173 million and as to $1.616 million from the General Reserve of TPS Super. The resolutions were passed by reference to a board paper dated 16 October 2015 on the issue. The board paper was for Questor “in its capacity as Trustee of The Portfolio Service Retirement Fund (TRF)”. The submissions noted that in section 3 under the heading “Compensation” this paper said:

Questor’s focus is to ensure that any current or exited members of the TPS Funds are treated fairly and equitably and that decisions are made in members’ best interests. Therefore, it was determined that the most appropriate course of action was to write-back the over-distribution over a three-year period (ending 30 June 2014).

In order to curtail the effect of the diluted distribution on members who invested in the TPS Funds post June 2009, Questor determined to compensate those members on a “see through” basis by increasing their distributions to what they would have received had the error and subsequent write-back never occurred.”

433 That is, the board was told that the compensation was for the diluted distributions to members who invested post June 2009.

434 Under the heading “Sources of Compensation”, the board was informed that internal legal advice was to the following effect:

* Because the requisite “operational risk” did not arise at the super fund level, the Trustee cannot access the ORFR to fund the compensation.
* An alternative view is that loss caused to new members was not a direct result of the original error; it was the result of a secondary event being the method of rectifying the error (eg smoothing distribution returns over three years). However, this position is not recommended because loss that could be attributable to “investment underperformance” is specifically precluded by APRA (see SPS 114.43). Although the Trustee chose to dilute the distribution to remedy the error, it is likely to be classified by APRA as underperformance loss.
* The recommendation is that the preferred approach would be to compensate any shortfall from the general reserve (see 4.4 below).

435 That is, the board was told that the compensation to be paid was a consequence of the CMT decision to recover the overpayment by diluted distributions and the use of the general reserve was available for that purpose, which was a logical and equitable thing to do.

436 Further, the board was told that Questor’s reserves policy allowed the general reserve to be used “for any purpose that the Trustee deems appropriate”:

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.

437 The submissions noted that APRA did not allege that the use of the general reserve was not authorised by Questor’s reserves policy or the trust deed for TPS Super.

438 As to the matters APRA alleged Mr Venardos knew or ought to have known (in italics below), the following responses were given.

439 *Questor was liable to make good the trust fund for losses suffered by beneficiaries of TPS Super by reason of the CMT Remediation Plan as pleaded in ASOC [242]*: “The liability is alleged in ASOC [242] to arise by Questor as TPS trustee ‘considering and accepting the CMT Remediation Plan for itself as unitholder’ and ‘in considering and deciding to pass on the consequences of that plan to beneficiaries of TPS Super’. The allegation is fundamentally flawed insofar as it assumes a relevant act on the part of a unitholder in the decision of the RE causative of that decision taking effect. The allegation blurs the distinct roles of Questor as RE of the CMT and as TPS Super trustee. Further, it incorrectly assumes that there was any capacity in Questor as TPS Super trustee to resist a trustee’s entitlement to recoup an overpayment.”

440 Further, these submissions were made for Mr Venardos:

(1) ASOC [241(a)] pleads issues of conflict. However, the premise of the conflict is that there was something that Questor as TPS Super trustee could do about the remediation decision by Questor as RE of the CMT, a premise which is not pleaded and not established.

(2) ASOC [241(b)(i)] alleges that Questor as TPS Super trustee breached various obligations by not taking steps to prevent Questor as CMT RE from implementing the CMT Remediation Plan. If this is an allegation that Questor should have blurred its distinct roles to cause the cessation of the plan, it is plainly unsustainable and is inconsistent with APRA’s contentions elsewhere that the roles must be kept distinct. If it is an allegation that assumes some other basis on which steps could be taken, it is fundamentally flawed because there is no allegation that there was a legal basis on which such steps could be taken. As previously submitted, there is no basis established and none pleaded on which any such steps could be taken.

(3) ASOC [241(b)(ii) to (iii)] allege matters previously addressed.

(4) ASOC [241(b)(iv) to (vi)] allege that the profit interests of IOOF were preferred in pursuing the plan. The allegation is not substantiated. Furthermore, the allegations proceed on an undemonstrated assumption that there was a loss that could be recovered by reason of the overpayment. As previously submitted, none of that has been substantiated.

441 In response to APRA’s other contentions the following propositions were put for Mr Venardos.

442 *Questor was liable to make good the trust fund for losses suffered by beneficiaries of TPS Super, by reason of Questor’s CMT Overpayment Breach as pleaded at paragraph [233(b)(ii)]*: “APRA has not demonstrated that any TPS Super beneficiaries suffered any such loss. Nor is it demonstrated that Questor as TPS Super trustee breached any obligation simply by passing on distributions from the CMT. In any event, the proposition that Mr Venardos knew or ought to have known of that matter is simply not established. He was specifically told in the board paper that ‘because the ‘operational risk’ did not occur at the super fund level, the Trustee cannot access the ORFR to fund the compensation”. There is no reason for Mr Venardos or any other director to question that conclusion. Further, the compensation issue being addressed in the meeting was that relating to the reduced distributions not the overpayment”.

443 *Questor’s CMT Overpayment Exposure as RE existed*: this allegation has been addressed already but “the proposition that Mr Venardos knew or ought to have known of that matter is simply not established. Further, the compensation issue being addressed in the meeting was that relating to the diluted distributions not the overpayment”.

444 *IOOF Service Co’s CMT Overpayment Exposure 1 existed:* this has been addressed already but “the proposition that Mr Vernados knew or ought to have known of that matter is simply not established. Further, the compensation issue being addressed in the meeting was that relating to the reduced distributions not the overpayment”.

445 *IOOF Service Co’s CMT Overpayment Exposure 2 existed*: this has been addressed already but “the proposition that Mr Venardos knew or ought to have known of that matter is simply not established. This is another way of alleging that Mr Venardos knew or ought to have known that the error occurred at the TPS Super level. That is the opposite of what he was told in the board paper”.

446 *There was no practical difficulty in Questor making a claim against IOOF Service Co in its capacity as service provider to Questor as RE of the CMT or as service provider to Questor as trustee for TPS Super*: this has been addressed already but “the proposition that Mr Venardos knew or ought to have known of that matter is simply not established”.

447 *The TPS General Reserve was trust property and that the superannuation beneficiaries of TPS Super had a beneficial interest in the money held in the TPS General Reserve*: this does not advance the matter.

448 *APRA had advised IIML that it should consider other sources of compensation other than the beneficiaries’ reserves, and that advice had been provided in relevantly similar* *circumstances*: this does not advance the matter.

449 It is alleged in ASOC [271] that Mr Venardos breached various covenants in considering and approving the compensation plan by reason of four matters. The submissions for Mr Venardos responded to APRA’s contentions as follows:

(1) *He breached his covenants because he relied on the CMT Compensation Paper and did not ask management to attend the meeting of the Board and explain and answer questions whether the plan was in the best interests of the beneficiaries of TPS Super*: it was submitted that if those questions were not asked (the minutes being insufficient evidence to prove this fact) they were not asked by any of the members of the board including Mr Venardos, and Mr Venardos relies on the conduct of the other board members as evidence of what the prudent superannuation trustee director would do faced with the same situation. The allegation also assumes that Mr Venardos knew of each of the alleged exposures or breaches but this has not been established.

(2) *He breached his covenants because he accepted management’s conclusion in the CMT Compensation Paper that making a claim against Questor’s insurance policy was not commercially viable*: it was submitted that it remained unclear why Mr Venardos would not be entitled to rely on management’s advice to this effect. Further, the other directors are in the same position which provides evidence of the conduct of a prudent superannuation trustee director.

(3) *He breached his covenants because he did not seek or cause management to seek independent legal advice as to whether Questor was itself liable, whether in its capacity as RE of the CMT or in its capacity as trustee for TPS Super, for the loss suffered by beneficiaries of TPS Super*: no other director thought this step was necessary proving the conduct of a prudent superannuation trustee director. Further, the board paper contained internal legal advice as Ms Clarke was one of the authors and the paper was endorsed by Mr Coulter as CFO, and Mr Vine, GM, Legal, Risk & Compliance. The effect of the legal advice was that there were no other sources of compensation available. It was also submitted that Mr Venardos ought not to have relied on Mr Coulter and Mr Vine’s paper because he knew they were directors of IOOF Service Co (ACS [306]). Inherent in this is an allegation that “Mr Venardos ought to have assumed that legal advice from Mr Vine inherent in the paper was not in fact legal advice but commercial advice influenced not by matters of law but Mr Vine’s interest in IOOF Service Co. That is a very serious allegation which ought to have been pleaded. There is no reason for Mr Venardos to have questioned the integrity of Mr Vine in that way. Furthermore, the first named author was Erica Clark, Legal Counsel, who is not alleged to have been a director of Service Co and again there is no plausible basis on which Mr Venardos could have assumed her legal view was not based on law but on IOOF’s alleged commercial considerations”.

(4) *He breached his covenants because he did not reject the plan or adjourn the meeting so that management could answer the questions referred to in paragraph [271(d)] or seek the legal advice referred to in [271(f)]*: this allegation depends on the earlier allegations.

9.3.10 Discussion

450 APRA’s case against Mr Venardos for the alleged CMT Compensation Plan breaches cannot succeed for the same reasons as its case against Mr Kelaher.

451 Again, I find the submissions for Mr Venardos compelling. The board was presented with a paper that was clear, apparently comprehensive, rational and reasonable. The board relied on the paper to reach its decision, as the members of the board were entitled to do. The conduct of the other members of the board excluding Mr Kelaher provides good evidence of what a prudent superannuation trustee director would have done in the same circumstances, which was precisely what Mr Venardos (and Mr Kelaher) did.

452 The paper represented that the compensation plan had been formulated in the best interests of members. There was no reason for Mr Venardos (or Mr Kelaher) to doubt that advice. APRA has not proved otherwise. It has also not proved any of the other foundational facts on which it relies to implicate Mr Venardos in breach of his covenants.

9.3.11 APRA’s case against Mr Coulter and Mr Vine

453 APRA sought findings against Mr Coulter which are addressed below, having regard to the competing submissions.

454 *Mr Coulter approved the use of the NAB settlement to wholly compensate non-superannuation investors without adequately considering the flow-on effect of this decision on superannuation beneficiaries*:APRA has not proved that Mr Coulter did not consider the effect on superannuation beneficiaries. It is apparent that compensation to those beneficiaries was being delayed for a number of reasons including taxation considerations. The payment of compensation to MIS members from the NAB settlement was a discretionary decision. It is not the case that Mr Coulter was bound to ensure Questor held all of the NAB settlement money to compensate the superannuation beneficiaries.

455 *Mr Coulter endorsed the Board paper setting out the CMT Compensation Plan and thereby adopted the conclusions and reasoning within it, including the endorsement of the use of the general reserve and his earlier decision as to the application of the NAB settlement*: this may be accepted.

456 *At the time he endorsed that plan, Mr Coulter knew or ought to have known*:

(1) *the facts giving rise to the CMT Overpayment including Questor’s role in authorising the payment and that the error was due, at least in part, to failures in Questor’s investment governance processes*: Mr Coulter was not employed by IOOF Service Co when the overpayment was made and could not be expected to know of the required procedures as they existed at the time of the overpayment. Leaving aside the fact that NAB made the initial error, none of the evidence in fact discloses why Questor did not notice NAB’s error or what its systems were to do so or needed to be to do so. The generalisations contained in Mr Rossitto’s commentaries are at far too high a level of abstraction to be useful in this regard. For example, I do not know what in fact Questor’s investment governance processes were, whether they were applied or not and, if so, whether they would have detected the error. Accordingly, the allegation that Mr Coulter knew or ought to have known of these matters cannot be accepted. All that Mr Coulter could know is that Mr Rossitto had said this (amongst other things) but that does not prove them to be correct.

(2) *IOOF Service Co’s exposure by reason of it providing the services that Questor relied upon in administering the CMT*: Mr Coulter was not a lawyer and could not be expected to have known of this matter. Mr Coulter was entitled to rely on the legal advice in the paper to the effect that there were no other viable sources of compensation.

(3) *Their own conflicts of interest or duty by reason of the exposure of Questor as RE and IOOF Service Co to liability*: the proposed conflicts are theoretical at best. They assume an exposure which has not been proved.

457 *Further, by the time he endorsed that plan, Mr Coulter knew (by virtue of the email exchanges on 15 October 2015 of which he was a recipient) that*:

(1) *internal legal advice from Ms Clarke was that the trustee (Questor) “should consider what rights of damages it has from the CMT”:* there was no reason for Mr Coulter, who was not a lawyer, to try to second-guess the legal advice.

(2) *Mr Rossitto’s view was that the CMT Overpayment was caused, at least in part, by “control weakness of Questor in its capacity as Responsible Entity of the CMT and in its capacity as RSE of the TPS Retirement Fund (TPS Super)”*: there was no reason for Mr Coulter to know what precisely Mr Rossitto had in mind by these comments. The details of what happened within Questor remain unknown today.

458 *Despite this knowledge*:

(1) *Mr Coulter did not identify and seek to manage his conflict of interest in accordance with IOOF’s Conflicts of Interest Management Policy*: there was no actual conflict of interest in the circumstances as they existed because there was no reasonably arguable claim against IOOF Service Co.

(2) *Mr Coulter knew that Vine had given the instruction to Ms Clarke referred to above (as he was copied on the email to Ms Clarke) and did not dissent from this course*: this allegation goes nowhere.

(3) *Mr Coulter endorsed the paper prepared by Ms Clarke and Mr Rossitto, including the recommendation that the trustee exercise its power to apply the general reserve to pay compensation without further consideration of the liability of Questor as RE or IOOF Service Co*: this may be accepted.

459 APRA sought findings against Mr Vine which are addressed below, having regard to the competing submissions.

460 *Mr Vine endorsed the Board paper setting out the CMT Compensation Plan and thereby adopted the conclusions and reasoning within it, including the endorsement of the use of the general reserve*: this may be accepted.

461 *At the time he endorsed that plan, Mr Vine knew or ought to have known the same matters as alleged against Mr Coulter*: there was no reason for Mr Vine to know these things. As the submissions for Mr Vine noted, he commenced employment with IOOF in August 2014 which was about “five years after the CMT Overpayment occurred, three years after the CMT Remediation Plan commenced and two months after the CMT Remediation Plan had concluded”. As was submitted:

(1) APRA has not identified the evidence to support the findings it seeks.

(2) The “only facts regarding the CMT Overpayment which Mr Vine knew or ought to have known from this evidence are those set out in the 16 October 2015 board paper (including that the CMT Overpayment was caused by an error on NAB’s part)”.

(3) “…there is insufficient evidence before the Court to make a finding that Mr Vine knew, or a reasonable person in his position would have known, that IOOF Service Co had a legal liability (or even that there was a material risk of such liability) because of its unspecified role in administering the CMT.”

(4) “…there is insufficient evidence to make a finding that Mr Vine knew, or a reasonable person in his position, would have known that Questor as RE and Service Co had a legal liability (or even that there was a material risk of such liability) which underpins the finding [of conflicts of interest] now sought by APRA. Even if there was, there is insufficient evidence to support the finding that Mr Vine had a conflict that would have had a significant impact upon his capacity to act in the best interests of beneficiaries.”

(5) While the finding about Mr Vine having received Ms Clarke’s advice relating to Questor’s rights of damages is accepted, at the same time, Ms Clarke also advised that it was open to the trustee to use funds from the general reserve to compensate beneficiaries. Otherwise:

In relation to the finding sought by APRA at [311(c)(ii)], it is submitted that the email chain relied on by APRA does not contain sufficient evidence to support a finding that Mr Vine knew that Mr Rossitto’s view was that the CMT Overpayment was caused, at least, in part by control weaknesses of Questor as RE and RSE. The email Mr Vine received from Mr Rossitto refers to Mr Rossitto documenting control weaknesses “*over the last few years*”. Accordingly, this email does not alert Mr Vine to control weaknesses which Mr Rossitto claims to have identified at the time of the CMT Overpayment (noting that this issue occurred over 6 years prior to Mr Rossitto’s email). Rather, all Mr Vine could have gleaned from Mr Rossitto’s email was that in more recent times, Mr Rossitto had identified what he believed were control weaknesses. Further, even if it is accepted that Mr Rossitto’s email was understood by Mr Vine as referring to control weaknesses existing in 2009 at the time of the CMT Overpayment, it is submitted that it is not open for the Court to conclude that Mr Vine would therefore have concluded that these weaknesses caused the CMT Overpayment.

462 The relevant comment made by Mr Vine was as follows:

PI Claim - not sure if this was ever considered although the loss amount would be well above the excess. Maybe we say that the other sources of funding were considered and pursued with a favourable commercial settlement with NAS?

463 As was submitted, on a “fair reading of Mr Vine’s email, it is apparent that he is uncertain as to what occurred in relation to any potential insurance claim. This is not surprising given that the insurance claim would have had to have been considered and made many years before Mr Vine even commenced his employment at IOOF”.

464 Otherwise I also accept the following propositions put for Mr Vine:

(a) APRA has not identified the alleged conflict of interest which it says Mr Vine possessed and, in any event, Mr Vine had no conflict that would have a significant impact upon his capacity to act in the best interests of beneficiaries in commenting on and endorsing the 16 October Board Paper;

(b) Mr Vine did not instruct Ms Clark to “*develop a proposal for the Questor Board that focussed on the use of the reserves, and ‘work back from here*’” as alleged by APRA. Rather, after receiving legal advice from Ms Clark which indicated that Questor could use the General Reserve to fund the compensation and arguably the ORFR also, Mr Vine asked Ms Clark “*[p]erhaps we can all agree the preferred solution from a reserves perspective and then work back from there?*”. Once again, APRA has sought to take a question of Mr Vine out of context and then infer something sinister was going on with the use of the Reserves. When read fairly and in context, all that the Court can conclude from Mr Vine’s query to Ms Clark is that what he was suggesting to Ms Clark and the individuals copied into the email was that they seek to agree whether, based on Ms Clark’s legal advice, the use of the General Reserve or the ORFR was more appropriate.

(c) as noted above, the Court can make a finding that Mr Vine endorsed the paper prepared by Ms Clark and Mr Rossitto. However, that paper does not contain a recommendation in the form or to the effect that APRA now contends should form the basis of a finding by the Court against Mr Vine in paragraph [311(e)(iii)] of its written closing

(d) in ACS at [311(e)(iv)], APRA seeks to summarise the content of the 16 October board paper. That summary is incomplete. However, Mr Vine does not dispute that he endorsed the statement made by Ms Clark and Mr Rossitto in that board paper concerning what they considered to be the reasons why an insurance claim had not been pursued (noting that this allegation is not made in the ASOC and appears to be irrelevant to the issues for determination by the court relating to the alleged CMT contravention).

465 In response to the proposed finding that at all times from 28 October 2015 to September 2018, Mr Vine did not take any steps to revisit or have the board revisit this decision (that is, the decision to use the general reserve for compensation):

There is no allegation in the ASOC that Mr Vine was obliged to or otherwise ought to have taken any steps to revisit, or have the board revisit, the decision in relation to the payment of the CMT compensation. Indeed as outlined earlier in these submissions (CS at [157]), Mr Vine was not a decision maker and his role was limited to providing those charged with making a decision with sufficient information to enable those person to perform their duty.

###### 9.4 Conclusions – CMT

466 APRA has not proved its claims against the respondents in relation to the CMT Overpayment, the CMT Remediation Plan or the CMT Compensation Plan.

##### 10. THE ALLEGED PURSUIT FAILURE AND BREACHES

###### 10.1 Background facts

467 The following summary is taken from APRA’s submissions, with some amendments to reflect my inferences based on the evidence.

468 At all times from 2007 to 2014, IIML was the trustee of IPS Super and the administrator and operator of the “Pursuit” investment platform. The “Pursuit” platform was used by IIML to make investments on behalf of superannuation beneficiaries of IPS Super, and in addition, to make investments on behalf of investors in an MIS known as the IDPS: ASOC [98]; admitted by all respondents.

469 The Pursuit failure involved a failure by IIML (from 1 June 2007), and both IIML and IOOF Service Co (from 1 July 2009), to follow beneficiaries’ investment instructions or to detect the fact that those instructions were not being actioned, resulting in beneficiaries’ funds sitting in low-return cash accounts rather than being invested in their nominated investment: ASOC [100], admitted IIML and Questor Defence, [100]-[100A].

470 The “Pursuit” platform was launched in October 2006 as part of what was then (before the merger with AWM Ltd), the IOOF Group’s “IOOF Portfolio Solutions” Business: CB 1/6B,   
p. 219\_0110. IIML’s IT team updated one of its existing computer applications called “ORION” for use with the Pursuit product suite, including for the processing of investor instructions: IIML Defence [100A(c)].

471 The reinvestment options offered by the Pursuit platform were part of its signature offering; the “product spec” given to the IT specialists when designing the processes and systems expressly “specified a need for reinvestments”, and nominated it as its key advantage over existing products: CB 6/102B, p. 1768\_0004; 6/100B, p. 1755\_0035. Reinvestment was in fact the “default option”: CB 1/6E, p. 219\_0283.

472 The Pursuit failure began on 1 June 2007: CB 5/57, p.1340.

473 However, from late 2007, being not long after the Pursuit failure began, separate service providers were introduced into IIML’s business arrangements.

474 IOOF Services Pty Ltd (**IOOF Services**) was the IOOF Group’s service company prior to its merger with the AWM Group: MFI-1. It was registered on 18 October 2007: CB 20/499. On 30 November 2007, it entered a services agreement with IIML: CB 1/6H, p.219\_0412. The services required to be supplied pursuant to that agreement were extensive and detailed:   
CB 1/6H, p. 219\_0430 to 219\_0447. In Schedule C (“Service Levels and Performance Standards”), multiple rows over four pages are devoted to the services required of IOOF Services in respect of “Management, investment operations and investment reporting services” for IIML (pp. 219\_0433 to 219\_0437) and later in the spreadsheet, additional services are nominated in respect of administration of the Pursuit platform specifically (p.219 \_0445).

475 That kind of outsourcing arrangement of IIML’s business activities continued after the merger of AWM Ltd and IOOF Hold Co.

476 From 1 July 2009, IOOF Services ceased being the service provider to IIML. The former service company for the AWM Group was renamed “IOOF Service Co”: CB 20/496, p.881 (ASIC extract for IOOF Service Co). That service company became IIML’s new service provider pursuant to a “Supplemental Deed” executed in 2009 (CB 1/7, p. 220, 223), supplementing the provisions of the original “Services and Resources Support Deed” dated   
19 July 2005 previously used by the AWM Group (CB 1/2, p. 68). Mr Kelaher executed the new service agreement: CB 1/7, p. 224.

477 All respondents have admitted that “as part of the Pursuit offering, [beneficiaries of IPS Super] and investors [of the IDPS MIS] had an option to have 100% of any income distribution automatically invested back into the same investment that made the income distribution”: ASOC [98], Defences [98].

478 The IPS Super Trust deed expressly recognised the right of superannuation beneficiaries to choose to invest in particular Fund Investment Pools, and in particular to “use contributions or earnings received in respect of the member, to apply for the issue of units or acquire shares as investments offered through the Fund Investment Pools or be allocated Units in those Fund Investment Pools”: CB 4/37, p. 670 (cl 3.7). IIML as trustee was required by cl 3.8 of that deed to “accept or reject” an Investment Direction, but the ability to reject it was circumscribed: p. 670 (cl 3.8). There was no power or discretion to ignore an Investment Direction.

479 The form given to IPS Super beneficiaries for investments using the Pursuit service is in evidence: CB 1/6E, p. 219\_0282. The front page discloses that it was attached to the Application Form “located in the back of the Product Disclosure Statement (PDS)/Offer Document for the relevant product or service”. The text at the top of that page also identifies that IIML was acting in two capacities in providing that form: (i) as trustee of IPS Super and (ii) as “Service Operator of the Pursuit Select Investment Service”.

480 Step 4 of the form set out the options beneficiaries had when giving directions for the management of income distributions. “Reinvest” was the first option that could be checked, and also the “default option”: CB 1/6E, p. 219\_0283.

481 The problem was that in administering and operating that platform from 1 June 2007 to August 2014, IIML, and for five of those years from 1 July 2009 to August 2014 also its service provider IOOF Service Co, failed to give effect to beneficiaries’ reinvestment instructions. They also failed to detect the problem during that period. These facts are admitted by IIML: ASOC [99], [100(a), (b)]; IIML Defence [99(a), (b)], [100(a), (b)].

482 The failure was only detected after a superannuation beneficiary detected it and notified IIML in July 2014: IIML Defence [100A(h)]; CB 5/47A, p. 1252\_0001.

483 On 11 September 2014, Mr Riordan (on behalf of IIML) submitted a breach notice about the Pursuit failure to APRA: CB 5/57, p.1340, 1344 (Pursuit Breach Notice).

484 That Pursuit Breach Notice admitted, as does IIML’s Defence at [100(c)] and [100A(h)] that:

(a) 7729 accounts were affected, of which 6531 were superannuation accounts;

(b) the failure “occurred an aggregate 18,588 times” from 2007 to 2014;

(c) the total amount not reinvested was $12.3 million;

(d) consequently, beneficiaries and investors did not obtain the returns they would have obtained had the amounts been invested in accordance with their instructions; and

(e) the failure was only detected after a superannuation beneficiary detected it and notified IIML in July 2014.

485 In its Defence at [100(c)], IIML also admitted that as at May 2015, the loss to the trust property of IPS Super by reason of these failures was approximately $816,754.

###### 10.2 APRA’s case – the alleged Pursuit failure and breaches

486 The Pursuit Breach Notice notified APRA that IIML considered the Pursuit failure to be a significant breach by it of s 52(2)(b) of the SIS Act: CB 5/57, p.1342. The reasons for that admission were set out in two attachments recorded at CB 5/57, p.1344, being an “Issue Notification Form” and an “Issue Assessment Form” (reproduced at CB 5/60 and 5/61 respectively). These were documents that IIML’s internal processes at the time required staff to complete upon becoming aware of an actual or potential “breach”. “Breach” was defined in those policy documents to mean “a contravention or likely contravention of a regulatory obligation”: CB 2/8I, p. 252\_0282.

487 The Issue Assessment Form submitted to APRA by Mr Riordan assessed the Pursuit failure as a significant breach of s 52(2)(b) by IIML (CB 5/61, p.1360) because:

(a) IIML “failed to act with the standard of efficiency, due care or reasonable care and diligence, as is expected by the law and that would have been reasonably expected by clients”;

(b) IIML did not have IT systems “correctly configured to process reinvestments”;

(c) IIML “did not…have a framework in place to prevent mitigate, manage or detect such bugs in the IT system that led to the failure to reinvest, and to pick up on the fact that clients’ distributions were held in cash”;

(d) the breach demonstrated the inadequacies of

(i) IIML’s “initial incorrect configuration of ORION”,

(ii) IIML’s monitoring and detection systems given it “took 8 years for the issue to come to IIML’s attention” and “even when” it did, “it was due to a client’s notification as opposed to being due to IIML’s proactive identification”;

(iii) IIML’s systems and its systems, structures, people and processes which “did not help identify the breach”.

488 APRA said that despite this, each of the respondents now denied that IIML breached s 52(2)(b) of the SIS Act with respect to the Pursuit Failure: ASOC, [106]; Defences [106].

489 According to APRA the original notification was correct as:

A failure by a superannuation trustee:

(a) to have systems in place to action beneficiaries’ basic – indeed the “default” – investment instructions to reinvest their earnings pursuant to an option offered by the trustee as part of the investment package, and/or

(b) to detect that it had failed to act on beneficiaries’ instructions over a period of seven years,

is a failure to exercise the degree of care, skill and diligence required of a prudent trustee by its s 52 SIS Act covenants. That is the case pleaded at ASOC [100], [105], and [106] to comprise IIML’s Pursuit Breach.

490 APRA said:

APRA relies upon the Pursuit Breach Notice and attached “Issue Notification Form” and an “Issue Assessment Form”, including the opinions expressed within them, as admissions: *Evidence Act 1995* (Cth), s 81, 82(b). Riordan submitted the forms to APRA and can be taken to have approved of adopted what was contained within them. As General Counsel of IIML, the representations made by Riordan in those documents were made within the scope of his authority for the purposes of s 87 of the *Evidence Act 1995* (Cth) and are accordingly attributed to IIML. Any objection by Riordan or IIML to the reliance on those documents should be rejected.

As against each of the other respondents, APRA relies upon the Pursuit Breach Notice, Issue Notification Form and Issue Assessment Form as business records pursuant to s 69 of the *Evidence Act 1995* (Cth). They are admissible as evidence of the facts represented within them which, APRA says, prove IIML and IOOF Service Co’s negligence.

491 APRA submitted that, contrary to the respondents’ submissions, it was not required to identify (i) “what the relevant ‘system’ would have been”, (ii) “whether [such a system] was technologically feasible”; (iii) “whether a reasonable trustee would have perceived the need for that (unspecified) system in the circumstances”; and (iv) “any other matter going to establishing that a reasonable trustee would have acquired or developed software of the unspecified kind for which APRA contends”. It said that in “circumstances where IIML’s offering (as admitted) was that beneficiaries could choose to have their earnings re-invested automatically, and that was the default instruction to be acted upon even where a beneficiary had failed to give a direction, there were any number of systems and processes that IIML might have adopted to action correctly beneficiaries’ re-investment instructions, and to detect any failures to action the instructions in fact given.” Further, according to APRA it cannot “reasonably be suggested that a reasonable trustee offering beneficiaries the choice of automatic reinvestment and representing that it would default to this arrangement even in the absence of express election would not have perceived the need for a system or process which was capable of giving effect to beneficiaries’ reinvestment choices and monitoring and detecting errors in actioning such choices”. This conclusion, said APRA, goes without saying.

492 APRA also noted:

(1) “IIML’s own admissions in its Pursuit Breach Notice in September 2014 accept that the law and reasonable expectations of beneficiaries required that their reinvestment instructions be actioned and be capable of being actioned, and if there were mistakes in doing so, that there be adequate processes in place to detect and remedy them promptly: ref.CB 5/57, p.1340 – 1344”;

(2) “…the evidence tendered by IIML itself in this proceeding accepts that proposition. That evidence identifies that the need for an IT system which was capable of handling requests for reinvestments was fundamental to the design brief for the Pursuit platform; the product spec “specified a need for reinvestments”: CB 6/102B, p. 1768\_0004. The Pursuit optionality to reinvest 100% of distributions received was part of its marketed appeal when launched, a fact which suggests the importance in this context that reinvestment instructions be capable of being actioned by the trustee’s processes and that of its service providers: CB 6/100A, p. 1755\_0001 and 6/100B, p. 1755\_00028”;

(3) “IIML’s evidence also contains the admission that the IT capability to give effect to reinvestment instructions was not at all difficult, and it could have even been done with only a ‘slight modification’ of the standard ORION logic: CB 6/100B, p. 1755\_00028. As that same document admits, the issue was not technological limitations but failure to think about the way the processing was done or might be done when doing the build, and failure thereafter to reassess the design as the business grew and other systems and processes were changed. As Vine admitted in the speaking notes for Riordan, the ‘reinvestment logic built in Orion did not *properly* contemplate’ the scenario where distribution receipt and reinvestment processing could span more than one reporting month (CB 6/100B, p. 1755\_00028) an error that could be attributed to a failure to appreciate the challenges and implications of a growing business and a design process that was compromised in its engagement with business stakeholders and testing:   
CB 6/100B, p. 1755\_0003”;

(4) “the insurance documents admit IIML’s liability for failures of due care, skill and diligence. IIML notified its insurer of the claim by at least October 2014: CB 5/70H, p. 1565\_0063”, saying:

8. Clearly, in this case, the definition of Claim has been satisfied:

…

c. The failure to reinvest distribution constitutes non-performance of financial, trustee and superannuation services; as is evidence by the breach notice lodged with ASIC and APRA as industry regulators.

…

9. IIML’s legal and fiduciary duties are to act fairly and equitably across all accountholders, compelling it to compensate all accountholders for loss, not just Ms Stephen. This is the nexus of its civil liability to accountholders and the very purpose of having civil liability insurance in place.

493 APRA noted that at “ASOC [107], APRA pleads that IIML’s Pursuit Breach caused loss and damage to the property of IPS Super and/or the interests of beneficiaries of IPS Super in that: the Pursuit failure and IOOF Service Co’s Pursuit Exposure…were not detected from 1 July 2009 to August 2014; the investments held by IIML on trust for beneficiaries of IPS Super did not generate the returns that would have otherwise been generated; and there was loss or damage to property held on trust by IIML of approximately $816,754”. APRA pleaded that “IIML was liable pursuant to SIS Act s 55(3) to compensate beneficiaries of IPS Super for the losses referred to in paragraph [107]. The reference to liability under s 55(3) picks up APRA’s pleading at ASOC [106] that IIML contravened s 55(1) by contravening its s 52(2)(b) covenant of due care, skill and diligence (ie IIML's Pursuit Breach)”.

494 In response to the respondents’ submissions that there was no basis for IIML being liable to beneficiaries, APRA submitted that:

(a) Part 6 of the SIS Act, properly construed, does not permit the statutory obligation imposed by s 55(1) to comply with the statutory covenants specified in s 52, to be excluded by way of an exemption clause in the governing rules of a superannuation trust fund;

(b) further or alternatively, because the effect of s 55(1) is to impose by law obligations on superannuation trustees, the general law applicable to the validity and effect of exemption clauses in trust deeds would have the effect of invalidating so much of an exemption clause which purported to exclude liability for the statutory obligation, even if it was effective to exclude liability for other non-statutory obligations contained in the trust deed and being other than exemptions for dishonesty or intentional or reckless breaches of trust;

(c) IIML’s trustee right of indemnity did not “cancel out” its personal liability for want of due care, skill and diligence, or entitle it to rely on that indemnity to use the assets of the fund (including its reserves) as a first port of call instead of third parties (including its professional indemnity insurer) liable to, or reasonably exposed to the possibility of liability to, restore the trust fund for losses.

495 APRA contended at ASOC [101] that IOOF Service Co had an exposure to liability in respect of the loss and damage to the trust property of IPS Super caused by the Pursuit Failure, limited to the period from 1 July 2009 (when IOOF Service Co became IIML’s service provider) to July or August 2014 (when the error was detected and the systems and processes reconfigured to prevent its recurrence). According to APRA, IOOF Service Co’s liability arose by reason of:

(a) IOOF Service Co’s contractual obligations to IIML under the service agreements (pleaded at ASOC [69] – [72]), and the specific services and resources it provided and the obligations it had in respect of IIML’s business as trustee of IPS Super and as administrator and operator of the Pursuit platform (pleaded at ASOC [99], [100])…; and

(b) the nature of the failings which comprise the Pursuit Failure, and which directly correspond to services and resources which IOOF Service Co was required to provide in respect of IPS Super and the operation and administration of the Pursuit platform.

496 At ASOC [101] APRA identified its case as involving the exposure to liability of IOOF Service Co from “its failure to configure its IT systems to process correctly beneficiaries’ re-investment instructions, and its failure to have an adequate framework or appropriate controls for detecting and mitigating ‘bugs in the IT system that could and did lead to the failure to re-invest distributions’ or the possibility that beneficiaries’ express instructions for re-investment were not being actioned”. APRA pleaded that this conduct on the part of IOOF Service Co either constituted a breach or alternatively it was reasonably arguable that it constituted a breach by IOOF Service Co of one or more of its contractual obligations. APRA pleaded further that “IOOF Service Co was liable, or arguably liable, to compensate or indemnify IIML for the loss or damage suffered by IIML as trustee of IPS Super (ie the loss caused by the Pursuit Breach to the trust property) because it was a breach or arguable breach of IIML’s obligations in the service agreement, or alternatively, because of the Service Co indemnity: CB 1/2, p. 77 (cl 11.1)”.

497 APRA denied that the losses were indirect or consequential. It submitted that:

To paraphrase the test in *Macmahon Mining Services v Cobar Management* [2014] NSWSC 731 at [13] (McDougall J), the “direct” damage “which flows naturally from” the failure to process reinvestment instructions” is the lost yield from the failure to reinvest. That loss does not involve any “other intervening cause” taking effect “independently” of the conduct that comprises the contravention. The direct loss is the difference in the actual value of the investment portfolio and the value that it would have had if the contract had been performed in accordance with its terms. There is no intermediate step between the breach and the loss, and the loss does not depend on any investment decision by the client: *Patersons Securities Ltd v Financial Ombudsman Service Ltd* [2015] WASC 321; 108 ACSR 483 at [145]-[150].

###### 10.3 The respondents’ case

498 The respondents submitted that to:

…make out a breach of the due care and skill covenant, APRA must establish, by evidence, that IIML did not exercise the degree of care, skill and diligence that an ordinary prudent person would have exercised in dealing with property of another for whom they felt morally bound to provide (in the case of the pre-2013 form of the covenant) or that a prudent superannuation trustee would have exercised (in the case of the post-2013 form of the covenant). This involves an evaluative judgment by the application of a legal standard. In this respect APRA could have, but has not, led expert evidence as to how a prudent superannuation trustee would have approached the kind of problems thrown up by the Pursuit Failure.

Rather than seeking to meet its burden, APRA’s case proceeds from the banal assumption that all errors that occur within a business are necessarily preventable and give rise to a breach of the exercise of care, skill and diligence. That assumption not only fails to discharge APRA’s evidentiary burden, it is also inconsistent with the evidence which shows that no controls could have been put in place or strengthened which would have detected the Pursuit Failure.

499 The latter statement is a reference to a document circulated on 27 February 2015 which provided an overview of the matter, after the event and rectification of the system, which considered the possibility of further controls to detect such errors in the future. As the respondents pointed out in a meeting with APRA, documented on 3 March 2015 by APRA, Mr Vine and Mr Riordan advised APRA that:

(i) it was unclear how the Orion configuration issue had come about;

(ii) IIML had not been able to locate the configuration specification request from 2007 that would clarify who was at fault;

(iii) it was unclear whether IOOF Service Co was at fault or negligent;

(iv) the amounts involved were small and not detected by IIML’s existing controls;

(v) **upon further investigation, IIML did not believe that there was a control that could be introduced to detect issues such as the Pursuit Failure**;

(vi) IIML did not want to get into a legal argument with IOOF Service Co which would result in an outcome that may not be in the best interests of members; and

(vii) IIML intended to pay compensation to superannuation members “out of the ORFR in the first instance and that it would then consider options available to it in terms of seeking reimbursement”

500 The respondents noted that it does not follow merely from fact that IIML has failed to do something it was obliged to do under the trust deed that it has breached its due care and skill covenant. Further, APRA’s case “makes the error of assessing the legal standard of due care and skill imposed on superannuation trustees through the prism of hindsight”. As the fourth to seventh respondents put it, APRA’s case theory is that:

There was an error, harm resulted and therefore the risk which gave rise to the error was foreseeable and preventable. That is an erroneous mode of analysis and proof. In the words of Barwick CJ in *Maloney v Commissioner for Railways (NSW)* (1978) 52 ALJR 292 at 292:

“[T]he respondent's duty was to take reasonable care ... It is easy to overlook the all important emphasis upon the word 'reasonable' in the statement of the duty. Perfection or the use of increased knowledge or experience embraced in hindsight after the event should form no part of the components of what is reasonable in all the circumstances.”

501 According to the respondents, APRA’s attempts to discharge its evidentiary burden were insufficient and misconceived.

502 The assessment form prepared by a member of IOOF’s compliance team at the time the matter was reported to APRA contained the following statements:

It appears IIML failed to act with the standard of efficiency, due care or reasonable care and diligence, as is expected by the law and that would have been reasonably expected by clients. Specifically, IIML did not:

* enable clients to reinvest their distributions in accordance with their instructions
* give clients the opportunity to be exposed to the markets and enjoy potential, favourable returns
* have IT systems correctly configured to process reinvestments
* have a framework in place to prevent, mitigate, manage or detect such bugs in the IT system that led to the failure to reinvest, and to pick up on the fact that clients’ distributions were held in cash.

Accordingly in my view IIML breached…s 52(2)(b) in its capacity as Trustee.

503 However, the respondents submitted that these statements are inadmissible to prove the legal conclusions as to breach of s 52(2)(b) of the SIS Act. It was also submitted:

The opinions expressed by compliance officers, in the conservative context of discharging reporting obligations, were, in any event, tentative and qualified and understandably were not the product of detailed legal analysis directed to the precise legal standard contained in s 52(2)(b) of the SIS Act.

504 According to the respondents, APRA’s approach to the 27 February 2015 document is incorrect. In the respondents’ words, the document in fact counters the “proposition that the inability by IIML to detect the Pursuit failure from July 2009 onwards was as a result of a failure on its part to have had adequate systems or processes to audit, monitor or assess IOOF Service Co”. Further, APRA’s reliance on the fact that distribution reinvestment functionality was recognised by IIML as being an important feature of the Pursuit product was misconceived. As the fourth to seventh respondents put it the:

…submission appears to proceed upon an erroneous assumption that the Pursuit Failure consisted of IIML failing to have had in place any system or capacity to reinvest distributions. To the contrary, the Orion configuration error which led to the Pursuit Failure occurred only in a highly specific and limited set of circumstances (that is, where there was a crossover in reporting periods between when a distribution was received and processed by the finance team) which were “*not reasonably anticipated*”.

505 The lack of reasonable anticipation is referred to in the 27 February 2015 document which states that:

Historically, most distributions were being received at the start of a month and processed promptly therefore crossing over a reporting period was not reasonably anticipated at the time the functionality was built in Orion [that is, in October 2006].

…

…there is now a higher likelihood of crossover between reporting periods when processing the distribution reinvestments than would have been initially anticipated.

506 Further, on 3 March 2015 in an internal email Ms Tanner of the compliance team responded to a question about the potential liability of IOOF Service Co by stating that “negligence or breach of contract” could not be argued for something not reasonably anticipated at the time”.

507 Thus it was submitted that the:

…fact that IIML regarded the distribution reinvestment functionality in a general sense to be an important aspect of the Pursuit product (which is, of itself, unremarkable) does not assist APRA to discharge its burden in establishing that IIML failed to exercise the requisite degree of care, skill and diligence by not detecting the Pursuit Failure (or, on APRA’s expanded case, in not preventing the Orion configuration error from occurring).

508 As to the alleged admissions made by IIML to its insurance broker, the “legal conclusions relied on by APRA as to breach of s 52(2)(b) of the SIS Act are in the same inadmissible category as the legal conclusions in the compliance notices…”. Further, as the fourth to seventh respondents put it:

…as is readily apparent from even a cursory review of them, the particular statements upon which APRA relies at ACS at [345] suffer from many of the limitations identified earlier in respect of the assessment form prepared by IOOF’s compliance team. In particular, the statements do not reflect the statutory language of the due care, skill and diligence covenant and are not supported by any detailed legal analysis. As explained further below, to the extent that the statements relied upon by APRA support the proposition that, as at the time those statements were made, IIML honestly but mistakenly considered itself to be “liable” to compensate beneficiaries for losses sustained as a result of the Pursuit Failure, that matter does not relieve APRA of its burden to prove the breaches alleged.

509 The first and second respondents submitted that IIML’s liability could be readily dismissed because of the exclusion in cl 11.5 of the TPS Super trust deed. I have rejected that approach to the covenants and liability under s 55(3) of the SIS Act above. The first respondent also said that APRA’s principal basis for alleging that IIML had a liability for the Pursuit distribution reinvestment failure appears to be self-reporting forms submitted by employees to management, and that APRA appears to contend that the opinions in those documents that the conduct constituted breaches by IIML are admissible against Mr Kelaher as evidence of that fact. As the first respondent put it, the opinions in the self-reporting documents are not admissible against Mr Kelaher as evidence of the matters expressed in the opinions. The submissions continued:

More fundamentally, the Court would be slow to rely on any statement of opinion in a self-reporting document as being conclusive that a breach of the law has occurred. As a matter of public policy, it is desirable that the Courts not take an approach to such documents that will create disincentives to be candid on the part of companies self-reporting breaches or potential breaches. The public interest is in such matters being reported quickly and comprehensively, without obfuscation, reservation or delay. That interest will not be served if opinions in those documents are treated by the courts as effectively conclusive that a legal wrong has occurred.

APRA places considerable reliance on statements made by IIML’s insurance broker in April 2017 in relation to a claim by IIML in relation to the Pursuit distribution reinvestment failure (ACS [347], [399]). When scrutinised, however, that document simply repeats what was said in the self-reporting forms and is entitled to no more weight. Certainly a statement by IIML’s insurance broker is not an admission by Mr Kelaher.

510 The alleged liability of IOOF Service Co was also misconceived. In the first respondent’s submission:

a) First, it is not clear that the Pursuit distribution reinvestment failure arose as the result of any failure of care, skill or expertise by anyone. To the extent that there is evidence of the cause of the issue, it appears that it was caused by the fact that ORION could not backdate reinvestments, but this rule against backdating in ORION’s configuration was “by design”.

b) Secondly, as noted above, to the extent the issue was originally caused by some lack of care or skill on the part of the service provider, the relevant service provider was Old Service Co, not IOOF Service Co… Again, APRA does not allege that IIML had any claim against Old Service Co.

c) Thirdly, insofar as the allegation is that IOOF Service Co ought to have detected the error, APRA has ignored IIML’s obligations to IOOF Service Co under the AWM Services Deed and IOOF Services Deed, which obliged IIML to provide IOOF Services Co with adequate systems, procedures and processes and which arguably imposed on IIML the obligation to ensure ORION functioned appropriately (see paragraph 145 above).

d) Fourthly, while APRA alleges that IOOF Service Co ought to have “detected” the Pursuit distribution reinvestment failure after 1 July 2013, it has not adduced any evidence as to how IOOF Service Co should have done so. In particular, there is no evidence of what systems or measures could have been adopted by IOOF Service Co to detect the issue. In the circumstances, the Court would reject the proposition that IOOF Service Co could have, or should have, implemented IT or control systems that would have detected the Pursuit distribution reinvestment failure (cf. ASOC [101(a)(i), (ii), (iii)]). APRA tries to avoid this difficulty by re-characterising its claim as, in effect, a quasi-misrepresentation case whereby IIML was liable because the Pursuit product did not do what IIML had represented to clients it would do (see ACS [336], [340]). That case is not pleaded and APRA should not be permitted to pursue it. Further, the argument is misconceived. Even if, as APRA contends, actioning beneficiaries’ re-investment instructions was a “basic” (ASC [336]) or “fundamental” (ASC [462]) part of IIML’s responsibilities as trustee, or even a “signature offering” of the Pursuit platform (ASC [316]), this is not a case of IIML having no system at all to deal with such instructions (contrary to some representation to clients) and it simply cannot be assumed away, in the absence of any evidence, that IOOF Service Co could and should have implemented systems or measures that would have actioned beneficiaries’ re-investment instructions in every possible situation without any error whatsoever, or detected “any” failures to do so (ACS [340]).

Thus, there was no “plain as a pikestaff” (T21.39) or “reasonably arguable” claim against IOOF Services Co in respect of the Pursuit distribution reinvestment failure. Indeed, any such theorised claim faced a number of obvious difficulties which were likely to prove insuperable.

511 The submission at [145] of the first respondent’s submissions, referred to in the preceding paragraph at (c), is as follows:

…the Pursuit distribution reinvestment failure began in 2007 at a time before IOOF Service Co commenced providing services to IIML. The issue arose out of the manner in which the software platform that IIML used to process the distribution reinvestments (known as “ORION”) was configured. Thus, while APRA alleges that it was “reasonably arguable” that IOOF Service Co was liable to IIML for failing to detect the Pursuit reinvestment failure in the period 2009 to 2014 (ASOC [101(b)]), IOOF Service Co would have a basis to allege in response to such a claim that any failure arising from a deficiency in the configuration of ORION was a breach by IIML of its obligations under clause 9.1(g) of each of the AWM Services Deed and IOOF Services Deed.

512 The second respondent made similar, but nevertheless useful, submissions. It was said, as is the fact:

There is no evidence of the “IT systems” employed by IOOF Service Co, let alone evidence of the way in which those systems were configured or their adequacy. There is no evidence of the appropriateness of Service Co’s frameworks, controls and checks to detect and manage system bugs, nor is there any evidence that the alleged deficiencies of Service Co’s systems caused the initial failure. There is no evidence to prove that the alleged deficiencies in Service Co’s systems and processes did not meet the relevant contractual standard nor is there any evidence that these alleged deficiencies were causative of the loss suffered by IIML.

513 As the second respondent put it, APRA’s case seemed to be to confined to the facts that IOOF Service Co failed to give effect to beneficiaries’ reinvestment instructions and failed to detect the problem, as if those facts were sufficient proof of IOOF Service Co’s alleged exposure – a proposition that “only needs to be stated to be rejected” as those facts, without more, do not found a liability in law for any loss suffered by the beneficiaries.

514 The second respondent submitted:

The short point is that APRA’s allegations of IOOF Service Co’s “exposure” are entirely unsubstantiated and based on pure supposition. Furthermore, the Board paper tendered by APRA includes the statement that management did not recommend action against IOOF Service Co for a number of reasons, the first of which was that “[t]he complex historical background involving Orion product changes makes it difficult to attribute a breach of contract or negligence to the administrator” (ie IOOF Service Co). That is a view expressed by lawyers familiar with the facts. That is evidence for all purposes that contradicts APRA’s presumptive assertion of liability in the administrator.

515 As to IIML, the second respondent said it was plain that the parts of the documents on which APRA sought to rely involved conclusions of law and the Court cannot rely on such statements as an admission that IIML breached the s 52(2)(b) covenant. Mr Venardos submitted that, in any event, none of the documents could amount to admissions admissible against him (a submission also made for Mr Kelaher). As to the insurance documents it was said:

…the statements identified by APRA are not, on their proper construction, an admission of liability under s 52(2)(c) of the SIS Act. The express purpose of the letter was to respond to the insurer’s position that “Insuring Clause 1.1” of the policy had not been triggered; under that clause, the insurer had agreed to indemnify the insured against any “Claims”, which in turn was defined as a demand for compensation made by a third party against the insured. The letter then set out the reasons why “the definition of Claim has been satisfied”. The document is nothing more than evidence of a belief that the insurance policy had been triggered and cannot, on any view, be used by the Court to make a finding of liability under a specific statutory scheme, in this case, the SIS Act.

516 The second respondent continued:

Apart from these documents, APRA has adduced no evidence to prove that IIML breached the s 52(2)(b) covenant. There is no evidence of the adequacy of IIML’s audit and monitoring systems and processes pleaded in ASOC [105(a1)], let alone evidence of the appropriateness of IIML’s control testing pleaded in ASOC [105(b)]. There is no evidence that had IIML conducted “regular and appropriate control testing” as pleaded in ASOC [105(b)], such testing would have detected the error. There is no evidence of the standard of care a prudent superannuation trustee would have exercised in such a case. For the reasons already submitted, APRA’s reliance on the “cardinal facts” also provides no answer. There is no evidentiary basis for the allegation in ASOC [125(b)] that IIML was liable by reason of a breach of the s 52(2)(b) covenant.

###### 10.4 Discussion

517 I consider the respondents’ submissions persuasive.

518 APRA’s case fails to confront a number of difficulties.

519 First, APRA’s case does appear to assume that the Pursuit failure comprised an overall inability of the Orion system to reinvest distributions when, in fact, the flaw in the system was that it did not reinvest distributions which were received in one reporting period but not processed until the following period, described in the IOOF briefing paper of 27 February 2015 as an activity which was not “reasonably anticipated” at the time the Orion system was configured in 2006. Accordingly, APRA’s case to the effect that the facts speak for themselves to establish a breach by IIML of the due care, skill and diligence covenant is misconceived. Had the Orion system not been capable of reinvesting any distributions then APRA may have been on firm ground to assert the equivalent of the *res ipsa loquitor* doctrine. But as it is, in the circumstances of this case, it is by no means apparent that this particular flaw in the software system, or the inability to detect it until a client brought the issue to IIML’s attention, constituted a failure to measure up to the required standard of care both before and after 1 July 2013. While I know that the Orion system was not configured to enable such distributions to be reinvested and that the system was subsequently able to be modified to perform this function, there is an insufficient evidentiary foundation from which it would be inferred either that the original configuration or the failure to detect it involved any breach of the due care, skill and diligence covenant.

520 Second, APRA has substituted for reliable evidence which might be capable of establishing a breach of the due care, skill and diligence covenants so-called “admissions” in documents created by people for different purposes, containing mixed statements of facts, law and opinion brought into existence after the event and with the benefit of hindsight. Even assuming the admissibility of the opinions as admissions (which I do not accept) documents of this character are not a reliable foundation for rational conclusions. For example, the documents provide no explanation as to why distributions crossing reporting periods was not reasonably anticipated. They provide no foundation for inferring that such distributions should have been reasonably anticipated. They do not provide any clue as to why the issue remained undetected for so long (apart from the fact that the amounts involved apparently were individually too small to be noticed by the systems that were in place, whatever those systems might have been, another fact which is unknown). However, nothing in the evidence enables any inference to be drawn as to whether the system for detecting errors that was in place was reasonable or not in the circumstances. In short, APRA’s apparent assumption that the facts and the documents speak for themselves is undermined when the nature of the systemic flaw (that is, a flaw confined to distributions crossing reporting periods which was not reasonably anticipated when the system was configured) and the terms of the documents are considered.

521 Third, the opinion of a compliance officer that IIML had failed to act with due care or reasonable care and diligence is no substitute for evidence from which it can rationally be inferred that there was a failure by IIML to measure up to the requisite standards of care, skill and diligence before and after 1 July 2013. It is not that APRA has to prove what a complying system would have been. It is that it has not proved that the flaw in the system which did exist was one that meant IIML had failed to measure up to the requisite standards of care. It has not done so because it has wrongly assumed that the facts and the documents speak for themselves when the facts are by no means as straightforward as APRA’s case suggests and the documents do not provide a reliable evidentiary foundation for the required evaluation. As with the alleged CMT breaches APRA has not proved what the system was or how it operated and why it operated in that way. It has not proved that it was reasonably foreseeable that distributions would be made but not processed across accounting periods at the time the system was used for the Pursuit platform. These are critical gaps in the factual foundation of APRA’s case.

522 Fourth, it is apparent that all of the documents on which APRA relied were prepared well after the event and with the benefit of hindsight. The question of IIML’s conduct, however, is to be judged by reference to the objective circumstances as they existed at the time. Evidence of this kind is sparse to non-existent. The evidence, such as it is, appears to support the information that was provided to APRA that it was unclear how the Orion configuration issue had come about, it was unclear whether IOOF Service Co was at fault or negligent and, upon further investigation, IIML did not believe that there was a control that could be introduced to detect such issues as the Pursuit failure in the future. As the respondents submitted, the facts (in contrast to the opinions) in the documents do not support APRA’s case of a breach of the standard of due care, skill and diligence. APRA proceeds as if the mere failure of the system in one specific respect is sufficient to discharge the burden of proof, which it is not.

523 Fifth, I agree also with the first and second respondents that to the extent that any IOOF document contains admissions, those admissions are not admissible against those respondents. The fact that the documents are business records does not mean that the statements of fact (still, less opinion) are attributable to Mr Kelaher and Mr Venardos. This said, however, for the reasons given above I do not consider the evidence is sufficient to prove APRA’s case of liability or reasonably arguable liability against IIML or IOOF Service Co. After the internal investigation the management of IIML was unable to identify the cause of the failure but did identify that at the time it was not reasonably anticipated that distributions would cross over reporting periods. Absent evidence capable of undermining this proposition, I do not see how APRA can succeed in its contentions that IIML or IOOF Service Co (from 2009) failed to measure up to the requisite standard of care. I also accept the submissions for the respondents that the insurance documents do not take the matter further. An honest but mistaken belief as to liability on the part of IIML does not make good APRA’s case which must be proved by admissible and reliable evidence, which is lacking.

524 Sixth, I accept the respondents’ submission that the fact that it was an important part of the Pursuit platform that distributions could be re-invested does not prove that IIML or IOOF Service Co (from 2009) failed to measure up to the requisite standard of care. APRA’s submissions to this effect appear to involve an assumption that because the product description involved the capacity to reinvest, any flaw in the system for reinvestment necessarily breaches the relevant standard of care. To adopt this approach would be to make the trustee an insurer against all loss which is impermissible.

525 Seventh, I accept the first respondent’s submissions that the relevant default cannot be the original configuration of the Orion system because that was carried out under the auspices of the old service provider against which there are no claims. Whatever APRA says, the default must be confined to the failure to detect the flaw in the system. APRA, however, has not explained the system or how the flaw could or reasonably should have been detected. In the face of the evidence that even in 2015 IIML did not believe that there was a control that could be introduced to detect issues such as the Pursuit failure, it is impossible to see how APRA’s case of a failure on the part of IIML or IOOF Service Co to have detected the error constituting a breach of the due care, skill and diligence covenant can be maintained. As the first respondent put it, it is not the case as APRA assumes that there was no system to deal with the reinvestment of distributions. It is that in one limited category the system did not operate to achieve the reinvestment. APRA’s case is no different from saying that IIML or IOOF Service Co was bound to achieve perfection in complying with beneficiaries’ instructions but this is not the relevant standard of care either before or after 1 July 2013.

526 Eighth, APRA has failed to grapple with the fact that insofar as IOOF Service Co is concerned it could readily have maintained in the face of any claim by IIML that the failure in fact was IIML’s responsibility.

527 For these reasons APRA’s case against IIML and IOOF Service Co for the Pursuit failure is not sustained by the evidence. The evidence does not establish that there were reasonably arguable claims against IIML and IOOF Service Co for the Pursuit failure, still less that those companies would have been liable for the failure.

##### 11. THE PURSUIT COMPENSATION PLAN

###### 11.1 APRA’s case – background facts

528 APRA said that having identified the Pursuit failure, IIML needed to determine how it would compensate the trust fund and consequently superannuation beneficiaries for the losses suffered. It said that no provision of the IPS Super trust deed negated the existence of IIML’s duty to get in and protect the trust property. In APRA’s words:

To the contrary, a range of provisions supported such a duty on the part of the trustee, namely:

(a) Cl 5.1 (CB 4/37, p. 675) requiring the Trustee to receive all moneys, rights and other property which are paid or receivable as income of the Fund;

(b) Cl 14 (CB 4/37, pp. 693-694) providing that the Trustee has power to deal with assets of the fund (cl 14.1) and general powers that included (cl 14.2) power:

14.2.2 to prosecute and as it may think fit to defend, answer, discontinue, compromise or settle any claims, actions, suits, or proceedings whatsoever and to refer and submit to arbitration any dispute or matter concerning any part of the Fund or relating to the trusts of this document;

14.2.5 to take and act upon the opinion or advice of any accountant, auditor, banker, lawyer, valuer or other expert or professional person or body and upon any information or documents received from a person on whom it is reasonable to rely (in any case, whether or not a shareholder or director of the Trustee)…

Cl 14.2.9 to compromise, compound, abandon, release, forgive, submit to arbitration or otherwise settle any debt, claim or thing whatsoever relating to the Fund or owing to the Trustee on any account whatsoever.

529 APRA repeated its submission, which I have not accepted above, that the decision to prosecute or compromise or abandon any claim against third parties was not a mere discretionary decision but was more akin to the kind of decision as to entitlement considered in *Finch v Telstra*. To the contrary, however, and as already explained, the decision whether to bring or not to make a claim against a third party or to bring proceedings necessarily involves an evaluative process about which reasonable minds may differ. It is not the kind of decision where there is one answer which may be categorised as right and another which may be characterised as wrong. The exposition in *Finch v Telstra* is dealing with a different kind of decision, being the formation of an opinion as to an entitlement for payment out of the trust fund on the basis of facts. The decision whether or not to pursue a claim for liability is of a different character. For the same reasons APRA’s proposition that when exercising its powers IIML was bound to seek relevant information does not have any particular significance for the circumstances of this case. The submission assumes the existence of reasonably arguable causes of action against IIML and IOOF Service Co when neither fact has been proved. Indeed, the submission goes further and assumes the existence of rights of recovery against IIML and IOOF Service Co when no such rights have been proved by APRA. Accordingly, APRA’s submission that it is “extremely important to beneficiaries of superannuation trusts that where the fund has rights against third parties to replenish losses suffered, that the exercise of those rights be properly considered and if possible, compensation recovered, from third parties rather than that the assets of the fund be diminished and its assets depleted” is of no assistance to it.

530 APRA contended that in 2014 when the issue of rectification and compensation arose in respect of the Pursuit Failures, IIML also had a statutory obligation to “give effect to” its risk management strategy in respect of loss and damage caused to the assets of the fund: s 52(8). In 2014, IIML’s risk management strategy was version 1.7 of that policy: CB 3/23E,   
p. 403\_0044. That provided the following:

(CB p.403\_0048): “The objectives of this Risk Management Strategy (RMS) are to:

* Document the measures and procedures which have been adopted and implemented by IIML to identify, monitor and manage material risks relating to IIML’s activities as an RSE Licensee”

(CB p. 403\_0053):

“The IIML Board of Directors can rely on the resources of the IOOF Group at their disposal for risk and compliance services, as a signatory to a Group Resources Deed.

The Deed governs the supply of human and technical resources to Group entities, including IIML.

IIML is able to enforce its rights under the Deed to a supply of resources if required by APRA. Further the Deed envisages that signatories such as IIML are bound to comply with superannuation regulations (which include adequate resources) and the Service Company agrees to support meeting such obligations”.

531 APRA said, and I accept, that the “Group Resources Deed” can only be a reference to the Services arrangements with IOOF Service Co.

532 The risk management strategy was updated in April 2016: CB 11B/254A. In the section dealing with “Operational Risk” it provided (CB 11B/254A, p. 3577\_0012):

The management of operational risk covers all activities undertaken by IIML, including the activities performed by IOOF Service Co pursuant to the Services and Resources Support Deed. This arrangement has been classified as a material outsourced arrangement and is managed in accordance with IOOF Group’s Vendor Management & Outsourcing Policy.

533 The IOOF Group’s Vendor Management & Outsourcing Policy required that at a “minimum” the contract with IOOF Service Co “contain liability and indemnity provisions”: CB 8/138,   
p. 2142.

534 APRA would have it, contrary to my conclusions, that there were two obvious sources of compensation available for the Pursuit Failures: IIML as operator of the Pursuit platform or IOOF Service Co as the entity actually responsible for providing the services and resources to process distributions. As I have said, on any meaningful analysis, neither was an obvious source of compensation.

535 APRA noted the following matters in the chronology of events, which have been taken from APRA’s submissions.

536 In its Pursuit Breach Notice, IIML had identified to APRA: “[T]he loss to IIML will be the compensation amount that it provides to affected clients”: CB 5/61, p.1360.

537 In that same document, Mr Riordan and IIML told APRA that the “IT, Finance and Operations departments” were at that time working to determine the appropriate methodology for determining any compensation “that will be in the best interests of members”. A similar statement was made to the IOOF Group Risk and Compliance Committee on 15 September 2014 by Mr Riordan’s team with the advice that the process “is expected to be complete by mid-October 2014”: CB 5/63, p.1368.

538 IIML’s Group Legal, Risk and Compliance Report to the board of IIML dated 17 October 2014 also contained a report on the Pursuit Failure. It was signed by five senior managers of that Group. They stated “we have determined that breach 1225 is significant”: CB 5/70A, p.1565\_0003. They indicated that a compensation plan was being developed and expected to be completed by November. On 27 October 2014, at a meeting of the board of IIML at which Mr Kelaher and Mr Venardos were present, that report was noted: CB 5/70B, p. 1565\_0009.

539 APRA said that these documents support a finding that IIML, Mr Kelaher, Mr Venardos and Mr Riordan knew by at least October 2014 that IIML had contravened its s 52(2)(b) covenant of due care and diligence and was exposed to liability to compensate for the losses. I disagree. The documents say nothing of this kind. Again, APRA’s reliance on internal IOOF documents as proving its case is misplaced for the reasons given above.

540 APRA continued with its chronology of events and related submissions in the following terms.

On 22 September 2014, 18 November 2014 and 3 December 2014, APRA was chasing IIML, Riordan (and later also Vine) for further information about the breach and compensation because of an absence of a substantive response: CB 5/71.

By October 2014, IIML had notified its insurer of a claim. The available inference is that Vine and Riordan were aware of that claim, given their responsibilities for Risk and Compliance, and that they are subsequently referred to in the insurance documents as intimately involved with the calculation of potential liability for the insurer:   
CB 6/129A, p. 2026\_0024.

On 4 December 2014, Riordan’s assistant emailed APRA, copying in Vine, attaching a letter from Riordan regarding the “Pursuit Reinvestment Distribution *Breach*” (emphasis added) and remediation measures: CB 5/73 That letter advised IIML’s “compensation solution” (p. 1574) involved the following (p. 1576):

2.3 Payment mechanism

We will be using the Operational Risk and Financial Reserve (ORFR) for superannuation accounts and IOOF Holdings Limited (IFL) will compensate the IDPS accounts. Using the 2.2% cash interest rate, total compensation would be $300,023, of which $51,400 would be funded by IFL and the remaining $248,623 would be funded through the ORFR.

541 The fact that Mr Riordan characterised the Pursuit failures as a “breach” does not prove APRA’s case for it. The existence of a breach was for APRA to prove by reference to facts. The fact that Mr Riordan held an opinion that the circumstances constituted a breach is an insufficient evidentiary foundation for APRA’s case in the circumstances identified above.

542 APRA’s chronology of relevant events continued in these terms:

On 9 December 2014, APRA responded to Riordan, copying Vine. APRA asked IIML to describe “the independent review process of the compensation methodology and outcome”, to explain the justification for why the ORFR reserve might be used when the issue pre-dated the introduction of the Prudential Standard SPS 114 which had introduced the ORFR such that “the IOOF Group is arguably responsible to compensate the superannuation accounts”, and raising the topic on which IIML’s letter had been entirely silent: IOOF Service Co’s exposure to liability to compensate the loss (6/83, p. 1693):

APRA understands IIML outsources the administration and processing services to IOOF Service Co through a service agreement. Your letter is silent on whether IIML is considering any action against IOOF Service Co for compensation consistent with the provisions of the service agreement and having regard to the trustee covenants of s 52(2) of the SIS Act.

Less than a week later, Vine asked internally for a copy of the agreement between “Service Co and the other IOOF entities”: CB 5/75A, p. 1594\_0001. The available inference is that at least Vine had not considered the possibility of IOOF Service Co being liable to compensate the trust and beneficiaries for the Pursuit losses until APRA raised it on 9 December 2014. However, from on or about the date of receiving it, he must have been aware of its contents, including its provisions for dispute resolution, the service standards required of IOOF Service Co, the requirements that IOOF Service Co have professional indemnity insurance such as to raise the possibility there would or may be monies available from an insurance claim were IOOF Service Co to make it, and the indemnity provided by Service Co in respect of loss and damage suffered by IIML in its capacity as licensee of IPS Super. In any event, having regard to the contents of IIML’s risk management strategy at this point which expressly dealt with the treatment that was to be applied when IOOF Service Co was exposed to liability or “APRA required it” (see CB3/23E, p. 403\_0053), IIML may be taken to have knowledge of its own contractual arrangements.

On 19 December 2014, Riordan responded to APRA on the points APRA had raised, copying in Vine: CB 6/83, p. 1691-1692. He confirmed there had been no independent review of the compensation outcome and IIML had relied on “experts in the Operation division” and discussion between the General Manager of Operations, the CFO (Coulter), Vine and Riordan who were “satisfied that the final approach is appropriate”. All of those persons were employees of IOOF Service Co. At least three of them were also officers of it. They were in an impossible position of conflict in making a decision on behalf of Questor [sic IIML] not to take steps to attempt to recover compensation from IOOF Service Co in respect of the losses.

543 I have indicated above that APRA’s assertions of conflict of interest are insufficient to found the existence of an actual conflict of interest, let alone one capable of having a significant impact on the relevant respondents’ capacities to prioritise the interests of the beneficiaries. In the present case, given the mutuality of the obligations of IOOF Service Co and IIML, and their common objective of ensuring that IIML satisfied its obligations under the SIS Act, I do not agree that the officers were subject to an impossible conflict of interest.

544 APRA’s chronology continued:

Riordan’s justification for using the ORFR which followed as the next item (6) in the email, recited the obligations of a trustee exercising a discretion whether to do so, but failed to apply those principles. None of the considerations involved the consideration that it was in the best interests of members that the assets of the fund, including the reserves, be preserved and the trustee first seek to vindicate the rights it held on trust against third parties or against the trustee personally (and to which an insurance policy responded): CB 6/83, p. 1692. It cannot be that Riordan and Vine did not know about such possibilities. APRA had asked about the possibility of a claim against IOOF Service Co and Vine had sought and obtained a copy of the contracts that might govern it. In addition, IIML had by this point already made a claim on its professional indemnity insurance policy: CB 5/70H, p. 1565\_0063.

545 APRA has assumed its case without proving the facts necessary to establish that it was in the best interests of beneficiaries for claims to be made against IOOF Service Co and IIML.

546 APRA said:

Riordan stated in his response that the compensation proposal that had been developed by him, Vine and others and notified to APRA was the “final approach”: CB 5/83,   
p. 1692. The conduct in developing it, and in considering the way in which the trustee would perform its duties and exercise its powers with respect to compensating the trust and its members, or exercising any power to access the general reserves for the purposes of “compensating” an event of trustee and service provider negligence or arguable negligence, fell far short of the standard required of superannuation trustees to act in the best interests of members, or to prioritise the interests of beneficiaries and ensure their interests were prioritised and the duties to them fulfilled despite the obvious conflict of interest involved between IIML’s desire not to use a professional indemnity insurance claim to compensate beneficiaries, or to recover compensation from IOOF Service Co.

Riordan’s answer as to whether IIML was considering any action against IOOF Service Co was equally problematic. Said Riordan (CB 6/83, p. 1692):

IIML is not currently considering any such action for a number of reasons, including the complex historical background involving ORION and product changes, legitimate use of the ORFR and the commercial reality of running a large group of companies where issues may not necessarily be realistically actionable or indeed require action in order for compensation to be made.

These were the reasons that were often repeated by IIML and its officers over the coming years. They display a fundamental misunderstanding of what the trustee’s best interests and conflicts covenants required. The first reason might be a justification for the allocation of responsibility as between IIML and its service provider, and hence between IIML’s professional indemnity insurer and an entity related to it. The best interests covenant might have been satisfied by a range of possible approaches by IIML to seeking to maximise the recovery of compensation from those two sources, but it was not satisfied by a course of conduct that took the view that members’ capital (in the form of the reserve) might be used as a first port of call instead of pursuing recovery from the service provider and the professional indemnity insurer. Further, Riordan’s assertion that the “legitimate use of the ORFR” included use of it as a first port of call, for the same reasons, did not satisfy IIML’s best interests covenant. Given the circumstances of conflict in which Riordan and Vine were in in respect of assessing any plan as to whether or not a claim ought be made against IOOF Service Co (of which they were employees and officers), Riordan’s justification was also not sufficient to discharge IIML’s duties with respect to the conflicts covenant either. And finally, the last justification – the “commercial reality of running a large group of companies when issues may not necessarily be realistically actionable or indeed require action in order for compensation to be made” was presumably based on the notion that no action was “required” because the compensation could be “paid” out of members’ reserves and the bill not footed by IIML’s insurer or the related entity IOOF Service Co. The justification itself raised the very conflict that infected the decision-making and its merits, whilst wholly failing to avoid the conflict or manage it in a way consistent with IIML’s conflicts covenant. To the extent the last justification was alluding to the potential costs of protracted litigation against a related entity, that was not a genuine consideration having regard to cl 17 of the service agreement and what it provided for in the event of dispute.

547 I do not accept these submissions. First, the use of Orion did involve a complex historical background which included the original development of the system, the involvement of the deregistered old Service Co, and the merger and the introduction of the new IOOF Service Co as service provider. Second, I do not accept that Mr Riordan was conveying what APRA seems to think. Mr Riordan was saying that if an entity within the group was considered to be liable for a loss then it would not be necessary for there to be litigation for the entity to reimburse beneficiaries. Third, and in any event, the ORFR was established for errors such as that in the Pursuit failure. APRA has not explained why its use in the circumstances was other than legitimate.

548 APRA continued:

From this point on until 2018, the persons through whom IIML acted continued to fail to discharge IIML’s obligations pursuant to its best interests and conflicts covenant.

On 2 March 2015, APRA met with Riordan and Vine about these matters: CB 6/102A (Vine’s notes), CB 6/105, p. 1771 (APRA’s notes, as reviewed by the participants at the meeting: CB 6/103-104). The speaking notes prepared by Vine for Riordan for the meeting appear at CB 6/100A, 100AA. The commentary given for use of the ORFR in the row “Compensation source” indicates that IIML’s senior legal, risk and compliance officers were myopically focussed on justifying its use by reference to the terms of the ORFR policy and failed to analyse the issue by reference to the best interests of members properly assessed. To the question “Members’ best interests” (see final page), the note records “We follow the policy”. The analysis fails to grapple with the obligations of a trustee in respect of seeking compensation from third parties, and instead wrongly presents the question as to whether a trustee “can”, within the terms of the policy, use the ORFR to “bring [members] back to a position had the operational event not occurred”. The obvious point that the ORFR is also an asset to which beneficiaries have an interest and forms part of the assets of the fund was not appreciated, or if it was, was ignored.

Vine’s own notes of the 2 March 2015 meeting record that APRA communicated to him and Riordan the view that IIML had not given proper consideration to the other sources of compensation that might be available – including from IIML personally and IOOF Service Co, and that there was a “*conflict b/w t/ee + service provider*”:   
CB 6/102A, p. 1768\_0002. See also CB 6/105, p.1773.

As APRA’s record of the meeting makes clear, it also communicated that the operational risk reserve could be used to mitigate timing difficulties between making a claim on a service provider and receipt of compensation monies from it, but could not be the first port of call (6/105, p. 1772, emphasis added):

APRA acknowledged that where compensation was sought from a service provider, it may be in members’ best interest to first make the payment to members from the ORFR whilst it pursues its service provider.

The logic of that explanation is the unremarkable proposition that having regard to what comprises the best interests of members of a superannuation fund (see the discussion of *Cowan v Scargill* and *Finch v Telstra*…above), it could only be in members’ best interests to use funds standing to the credit of the risk reserve where avenues existed to seek compensation from a service provider or insurer, if such avenues were first pursued and the ORFR monies used, in effect, as an advance on the proceeds of recovery from the wrongdoer. This was not IIML’s intention: IIML’s intention was to pay from the ORFR “in the first instance and that it would then consider options available to it in terms of seeking reimbursement”: CB 6/105, p. 1773. The problem, as APRA alerted Riordan and Vine to at that meeting, was that that course gave rise to obvious circumstances of conflict which would need to be managed carefully and appropriately.

They were not.

549 The distinctions that APRA draws here, between first using the ORFR and then pursuing other sources of compensation if available, and then using the ORFR, are unclear. It is apparent that Mr Vine and Mr Riordan had not ruled out compensation by IIML or IOOF Service Co if the view was taken that they were liable for the loss. They knew this was APRA’s position and there is no reason to infer that they proposed to do anything other than what they believed was consistent with APRA’s position. Again, APRA has not explained the “obvious” actual conflicts of interest it asserts existed. As employees of IOOF Service Co, Mr Riordan and Mr Vine were bound to assist IIML to act in the best interests of beneficiaries. In any event, APRA continued:

In fact, Riordan and Vine subsequently prepared speaking notes for the then Chairman of the IOOF Group to convey to APRA that APRA’s concern and questioning of “how the trustee had [made a decision on compensation] without considering other possible sources of recovery” was, in Riordan and Vine’s view (CB 7/130A):

“an unrealistic assessment of how things work in our business – our view is that our approach of internal management consideration then presentation to the trustee board is appropriate”

550 Again, I infer that the point that was being made was that no such thing as a formal claim would be necessary if the view was taken that any company in the group was liable for the loss.

551 APRA said:

On 25 March 2015, the Board of IIML met (each of Kelaher and Venardos were present) and discussed the Pursuit Failure: CB 7/118, p. 1875. The Legal, Compliance & Risk Report under consideration had informed the Board that APRA had requested on 2 March 2015 that IIML “further consider any potential alternative compensation sources”: CB 7/118B, item 2(a).

On 29 April 2015, the IOOF Risk and Compliance Committee (of which Venardos was a member, and which meeting was attended by Riordan and Vine as guests) noted a report tabled by Vine and his oral report that identified “Focus areas include APRA interaction on the ORFR and remediation of the Pursuit distribution breach (to be presented to the May Board)”: CB 7/126, p. 1997.

IIML’s Compensation Plan approved by the Board in May 2015 did not seek to fund compensation from either its own funds (indemnified by its insurer) or IOOF Service Co: CB 8/141, p. 2269\_006. The plan approved provided for beneficiaries affected by the Pursuit Failure to be compensated from IPS Super’s operational risk financial requirement reserve (ORFR) (the Pursuit Compensation Plan). This plan was endorsed by Vine and Riordan on 13 May 2015 (CN 8/138, pp. 2116-2120) and approved by the Board (including Kelaher and Venardos) on 27 May 2015: CB 8/141 pp.2263-2268. IIML, Questor, Vine and Riordan now each admit that the ORFR was trust property and that they, and Kelaher and Venardos, knew or ought to have known this at the time: Defences, [125(a)], [131(a)]. They each deny, however, that the Pursuit Compensation Plan was not in the best interests of beneficiaries: ASOC, [119]; Defences [119].

552 APRA explained its case in these terms:

APRA’s case is the that the Pursuit Compensation Plan was not in the best interests of beneficiaries and failed to prioritise their interests or meet the requirements of the conflicts covenants because (ASOC [118] – [121], in circumstances where there was conflict between the duties owed to and interests of the beneficiaries of IPS Super and the interests of the IOOF Group and other non-super investors as to the source of any compensation:

(a) IIML’s conduct and the plan itself did not recognise the conflict that existed in the formulation and adoption of the plan. The Board paper went to the Board acting in IIML’s capacity both as trustee of IPS Super and Operator of the Pursuit Investment services: CB 7/131, p. 2030. The conflict inherent between IIML’s interests in those two different capacities and the conflict between the members of the IDPS fund and the beneficiaries of IPS Super as to the use of any funds supplied by IIML (or its insurer) was manifest, and yet entirely overlooked by the members of the board and IIML’s senior officers proposing the plan;

(b) IIML’s conduct and the plan itself did not give adequate or genuine consideration to the sources of compensation other than the beneficiaries’ own reserves, including because it did not give adequate or genuine consideration to the prospects of pursuing IIML, or IIML’s professional indemnity insurer, or IOOF Service Co, to fund compensation;

(c) IIML’s conduct and the plan itself did not give adequate or genuine consideration to the appropriateness of a differential treatment of super beneficiaries and non-super beneficiaries;

(d) IIML’s conduct and the plan itself did not recognise, or give adequate or genuine consideration to the fact that the reserves were capital of IPS Super, and that use of the reserves to “compensate” IPS Super for the losses caused to its capital was in truth not “compensation” of the trust at all;

(e) IIML’s conduct and the plan itself did not give adequate or genuine consideration to IIML’s liability for the losses, the availability of insurance proceeds from a claim on IIML’s professional indemnity insurer for its liability for the losses caused to the assets of IPS Super and individual members’ accounts, or recognise the position of conflict in which IIML and the Board sat in making any decision not to pursue such a claim for the benefit of beneficiaries of IPS Super;

(f) IIML’s conduct and the plan itself did not appreciate, or give any adequate or genuine consideration to the fact that the proponents of the Pursuit Compensation Plan were themselves in a position of conflict, having regard to their role as officers and employees of IOOF Service Co. Nor did the Board of IIML, or Kelaher himself, identify his particular conflict as a director of IOOF Service Co, in making any decision in his capacity as responsible officer of IPS Super not to seek to vindicate IIML’s rights as against IOOF Service Co;

(g) IIML’s conduct and the plan itself did not involve IIML, in its capacity as trustee of IPS Super, seeking independent legal advice on its rights as against IIML in its personal capacity for failure to exercise due care and skill etc, or as against IOOF Service Co, or as to the proper use of the reserves to “fund” compensation to members out of the fund’s assets as a first port of call;

553 According to APRA:

While, in this instance, the board paper did include some commentary on why no action was being taken against IOOF Service Co (as the “fund administrator”) this consideration can only be described as perfunctory and not “genuine consideration” of the kind which the authorities require. Vine and Riordan recommended that no action be taken against IOOF Service Co because:

(a) the *“complex historical background”* of the breach means that it was *“difficult to attribute a breach of contract or negligence to the administrator”*;

(b) the *“commercial reality of running a large group of companies means that issues may not necessarily be realistically actionable or indeed require action in order for compensation to be made”*; and

(c) *“[l]egal action between the related bodies corporate would likely be contested”* and would require IIML to take steps to manage conflicts (including *“appropriate internal Chinese walls”*) which Vine and Riordan considered may be *“unnecessarily burdensome”.*

For the same reasons these explanations were inadequate when proffered to APRA on 19 December 2014 and in person on 2 March 2015, they remained inadequate in May 2015. They demonstrate that the issue was considered from the perspective of the IOOF Group as a whole, rather than by IIML in its capacity as trustee of IPS Super and the obligations it owed to beneficiaries. This should have been obvious to each of Kelaher, Venardos, Vine and Riordan. They also failed to give any consideration to the terms of the IOOF Service Co contractual arrangements, or the requirements of IIML’s risk management strategy where IOOF Service Co was exposed to liability. The first reason is not supported by the documents tendered in evidence in any event: whilst they might show some complexity in attributing responsibility to IOOF Service Co in respect of the initial design of the Pursuit processing systems, they indicate that from July 2009, IIML was responsible for the ongoing operation of that system, including its error detection processes. The Breach Notice IIML had submitted to APRA, the contents of which Riordan and Vine can be taken to have been well aware, included a detailed internal assessment by the Compliance team that the failure to detect the error for years and years was itself a contravention of IIML’s s 52(2)(b) covenant.

554 I have already explained above APRA’s reliance on internal IOOF documents, created for different purposes and often expressed at a high level of generality, is misplaced. The documents do not found the existence of contraventions of the SIS Act. The fact that a compliance officer believed there were such contraventions does not make APRA’s case for it.

555 APRA continued:

The “*commercial reality of running a large group of companies*” or the need to implement conflicts management procedures are not determinative considerations for a trustee required to act in the best interests of beneficiaries and to prioritise their interests above all others. The inherent conflict involved for Kelaher and Venardos, given their multiple roles in the IOOF Group, to be involved in making decisions as to whether IIML in its capacity as trustee ought to pursue related entities in that group without independent legal advice or some other risk treatment mechanism, ought to have been obvious to Kelaher and Venardos. They chose to rely on the internal advice of officers who were in a position of conflict that they themselves must have known existed. The unreasonableness of that reliance, and its inconsistency with IIML’s conflicts covenant and their own conflicts covenant and compliance covenants, ought to have been obvious to them. This answers the point made at Kelaher OS [18].

As with the CMT breaches addressed above, none of the explanations now given by the respondents in their defences for not pursuing IOOF Service Co appear in the materials before the Board in 2015, the minutes of that meeting, or in any other contemporaneous documents. Nor is there any evidence (in the board paper or otherwise) that consideration was given to the liability of IIML as the administrator of the Pursuit platform or trustee of IPS Super (despite the notification to APRA that IIML had breached s 52(2)(b)).

The flaw in IIML’s decision-making process for (i) the preservation of the trust’s property and the vindication of rights attaching to it (ii) the exercise of powers relevant to (i), and (iii) the application of its risk management strategy to the events of Pursuit, is revealed when the approach taken to superannuation beneficiaries is compared to the approach taken to non-superannuation investors affected by the Pursuit Failure. As recorded in the same board paper (CB 8/141), “[m]anagement recommends that the Operator compensates IDPS clients for loss incurred, given that the nature of the IDPS is contractual and there are no reserves maintained”. No explanation is given (or could be given) as to why non-superannuation investors had a viable claim against IIML (which it apparently did not intend to defend) but superannuation beneficiaries did not.

APRA understands that it may be some part of the respondents’ defence that at a meeting on 2 March 2015 with Vine and Riordan, APRA told IIML that the use of the ORFR was “appropriate”. The evidence (including Vine’s own notes of this meeting) does not show [sic] that what APRA communicated was that the ORFR may be used in the first instance to compensate beneficiaries, so long as other sources were considered to replenish the ORFR and conflicts appropriately managed. The evidence of Napolitano would give the Court comfort in the accuracy of APRA’s notetaking in respect of what was and was not said by APRA at this meeting: Napolitano 1, [12] – [26]. In essence, APRA was asking why IOOF Service Co was not being pursued for its role in failing to detect the error for multiple years and its role in the maintenance of the defective technological processes. Further, it was saying in respect of the ORFR specifically, that it could be used as an advance on third party compensation monies to ensure beneficiaries’ individual accounts were promptly compensated while IIML took steps to seek compensation from other sources (such as IOOF Service Co or an insurer). This is not what occurred. Instead, as noted above, on 27 May 2015 the IIML Board approved a plan that recommended the use of the ORFR reserve to compensate beneficiaries and that no further steps be taken to recover compensation from third parties or related entities. No document has been produced by the respondents indicating that this decision was ever revisited by the Board until September 2018.

556 APRA’s case continued by reference to some further emails between Mr Riordan and Mr Vine as to the drafting of the board paper for the meeting on 27 May 2015: CB7/130B, 130C, 132A1. According to APRA, these emails disclose that in the drafting of the board paper, Mr Vine and Mr Riordan were acutely conscious of the weakness of the justifications given for not pursuing IOOF Service Co. Mr Riordan noted on the original draft that it:

…looks a little weak in terms of enabling directors and APRA to raise questions so can we amplify a little further without locking us into a deeper issue I just think it needs some further textual work.

557 APRA said it was notable that “what was needed was some ‘further textual work’, not some independent legal advice as to the best interests of members or the management of the obvious conflicts that applied to advising IIML to adopt such a course, or in IIML adopting it”.

558 APRA continued:

After the 27 May 2015 meeting, IIML updated its insurer with the information that “The IIML Board has approved the remediation and rectification plan. Letters being drafted for affected clients. 869 IDPS clients with $120K compensation funded by IOOF. 4639 Super/pension clients with $696K funded through ORFR”: CB 7/129A, p. 2026\_0025. That update also indicated that “The split of funding of this claim between IOOF and the ORFR is to be reconfirmed once Paul Vine and Gary Riordan have resolved usage with APRA”: CB 7/129A, p. 2026\_0024. The available inference from the documents is that at all times when proposing the Pursuit Compensation Plan to the Board, and thereafter in attempting to implement it, Vine, Riordan and IIML was aware that another available source of compensation which had not been disclosed to APRA nor included in the board papers for 27 May 2015 was the possibility of insurance proceeds from its professional indemnity insurer.

In the event, following that approval of the plan, IIML delayed paying any compensation from the ORFR for over two years on the basis that the payment (coming, as it did, from beneficiaries’ own funds) could be considered by the ATO to constitute a concessional contribution. A private tax ruling was sought and IIML took no steps to compensate beneficiaries until that advice was received: CB 10/193A.

As Vine’s notification to APRA on 24 June 2015 of this development indicated, the board approval was still extant and IIML was not taking steps to pursue other sources of compensation in the meantime to fund the losses suffered by the TPS Super fund and its beneficiaries: CB 8/147E, p. 2306\_0006. The ruling sought from the ATO was to provide IIML with comfort that its compensation plan would not cause further losses to beneficiaries rather than with an assessment of whether it was in any event a plan in the best interests of beneficiaries for the losses they had already suffered.

The ATO provided its advice to IIML on 8 February 2017: CB 13/308A. It said that it would not treat payment from the ORFR as a concessional contribution on the basis that it had been informed by IIML that the ORFR would generally be used where the trustee had a right of action against itself or a third party, and would compensate the ORFR from those funds: CB 13/308A. This is the very course of action that APRA had urged IIML to take, but which it had failed to take until this point.

559 APRA said that:

To the extent that the above series of events is relied upon by the respondents to establish that there was no implementation of the Pursuit Compensation Plan, such reliance is misplaced. At all times until at least February 2017, the evidence shows that IIML was single-mindedly focused on using the ORFR to compensate for the Pursuit Failure. This was despite the delay in the availability of the ORFR meaning that the justification given to APRA for the use of the reserves in the first place, namely, the ability to promptly compensate beneficiaries, fell away. Up until mid-2017, beneficiaries remained uncompensated for losses that (at least some of them) had incurred more than ten years earlier.

560 APRA continued:

The policy has been added to the CB[3] at tab 32D1. Relevantly it provided insurance for (cl 1.1) “Breach of professional Duty” in the following terms:

Cl 1.1 Breach of Professional Duty

We agree to indemnify the Insured against any Claim for civil liability arising from a breach of professional duty owed in the conduct of the Professional Business fist made against the Insured during the Period of Insurance.

The limit of indemnity was $20 million.

…

…after the ATO had given its advice on 8 February 2017, IIML changed course. The insurer initially resisted the claim: tab 315A, 315B. After the ATO ruling, IIML was at pains to stress to its insurer its liability to pay compensation for the failure. On 18 April 2017, its broker wrote to the insurer explaining (tab 330A, emphasis added):

8. Clearly, in this case, the definition of Claim has been satisfied:

a. On numerous occasions Ms Stephen verbally relayed concerns she had with her account and demanded that IIML make good any loss caused as a result of errors. Ms Stephen’s email to the Insured also required the Insured to investigate a number of errors (and implies that the Insured must make good where there has been loss, as is IIML’s legal and fiduciary obligation).

b. The verbal conversations ant the email notice are both acceptable forms of notification under the Policy (see para 7. above).

c. The failure to reinvest distributions constitutes non-performance of financial, trustee and superannuation services; as evidenced by the breach notice lodged with ASIC and APRA as industry regulators.

9. IIML’s legal and fiduciary duties are to act fairly and equitably across all accountholders, compelling it to compensate all accountholders for loss, not just Ms Stephen. This is the nexus of its civil liability to accountholders and the very purpose of having civil liability in place.

…

11. IIML expected to be able to source part of the compensation amount from reserves but was preclude from doing so by law and APRA directives.

The response from the insurer was received on 12 July 2017: [CB14] tab 363A. The insurer accepted the Claim on the basis the error (at [26]) “arose out of the provision of ‘Professional Services’ by IIML (being, relevantly, fund management, asset management and/or superannuation services), and specifically, IIML’s administration of the Fund through the use of its computer software systems”. The insurer accepted that “on the information provided, IIML does have a legal obligation to compensate affected members by reason of the Error”: at [33.2]. The deductible was $250,000, in respect of which the insurer noted (at [36]):

“This means that IIML will be required to bear the first $250,000 towards the compensation paid to affected members”

561 APRA said that the evidence reveals that:

…only after sustained opposition from APRA and the correspondence from the ATO did IIML seriously pursue its claim on its professional indemnity policy with respect to the recovery of compensation for the benefit of beneficiaries of IPS Super. Further, that the claim itself was an admission by IIML that it was personally liable to compensate the fund for losses caused by the Pursuit Failure.

562 The chronology of events continued:

Insurance proceeds were received in around July 2017: CB 18/454. Those insurance proceeds did not cover the entire loss suffered by beneficiaries and in August 2017, IIML ultimately partially compensated beneficiaries from the insurance moneys and partially from the ORFR.

No steps were then taken to replenish the ORFR until October 2018. As noted above, this was only after increased pressure on IOOF from APRA and the Royal Commission, and the resignation of Kelaher from the Board. Despite the respondents’ assertion that this compensation was paid by IIML (Defences, [100]), the funds to compensate the ORFR were from IOOF Service Co’s account as the “party responsible for the error”: Board paper, 22 October 2018: CB, Tab 17/436, pp. 6293-6294; Email from Vine to APRA, 29 October 2018, confirming that IOOF Service Co paid the compensation: CB, 17/437C, p. 6300.

It is noteworthy that there was no resistance from IOOF Service Co at this point in time to paying this compensation and none of the difficulties anticipated in the May 2015 board paper existed.

###### 11.2 APRA’s case – IIML’s alleged Pursuit compensation contraventions

563 According to APRA, “IIML was in a position of conflict in considering, adopting and implementing the Pursuit Compensation Plan. It was a potential source of compensation, as was its related party IOOF Service Co. It also had potentially competing duties to MIS investors. Those conflicts were never acknowledged”.

564 APRA said that:

In circumstances where those other potential sources of compensation outside of the trust fund existed, APRA submits that it was not in the best interests of beneficiaries to approve and implement a compensation plan that used beneficiaries’ trust money (by means of the ORFR) to compensate them for losses without first at least exploring the possibility of making a claim against the IOOF Group companies involved, or making good the loss from the trustee’s funds. To the extent there was any indemnity available to the trustee (as to which, see above) that – as with the reserves – should have been a last resort after all other avenues of compensation had been exhausted. It is not in beneficiaries’ best interest for a trustee to indemnify itself from trust funds where it has other sources of indemnity (i.e. from IOOF Service Co) available to it. For the reasons explained above, IIML’s belated claim on its insurance does not cure its earlier breaches either. Until mid-2017, that claim was to cover any residual liability IIML may have had after use of the ORFR. It was not a claim that was made in the interests of beneficiaries; it was made in the interests of IIML’s own interests.

Accordingly, APRA submits that by considering, adopting and implementing the Pursuit Compensation Plan (including the use of beneficiaries’ reserves) until October 2018, without identifying conflicts of interest and taking steps to seek to recover compensation from itself or IOOF Service Co, Questor contravened the statutory covenants in s 52(2)(c) and (d) because it failed to act in beneficiaries best interests and prioritise those interests despite the conflict. Not only was this a breach of the statutory norm of conduct, but it was a breach of Questor’s own conflicts of interest management policy that, by means of SPS 521 and s 52(2)(d)(iv), informed the standard of conduct required.

###### 11.3 The respondents’ case - IIML’s alleged Pursuit compensation contraventions

565 The fourth to seventh respondents noted that APRA’s case was that in “developing, adopting and implementing the Pursuit Compensation Plan” IIML contravened s 55(1) of the SIS Act by failing to comply with its best interests covenant and no conflicts covenant under s 52(2)(c) and (d) of the SIS Act: ASOC [121]. The contraventions are said to be because:

(a) the plan was not in the best interest of the beneficiaries of IPS Super for the reasons referred [sic] at paragraphs [118] and [119];

(b) the plan preferred the profit interests of IOOF Service Co, IIML, IOOF Hold Co, the IOOF Group, Kelaher and/or the shareholders of IOOF Hold Co over the best interests of the beneficiaries of IPS Super;

(c) further to (b), the plan preferred the profit interests of IOOF Service Co and the IOOF Group, by not causing IIML to take steps to make a claim as against IOOF Service Co for IOOF Service Co’s Pursuit Exposure;

(d) further to (b), the plan preferred the profit interests of IIML, by not causing IIML to use its own funds to compensate the trust property and/or affected beneficiaries of IPS Super; and

(e) further to (b), the plan preferred the interests of non-superannuation investors in the MIS affected by the Pursuit Failure by using IIML’s own funds to pay those investors but not also or instead to compensate the beneficiaries of IPS Super.”

566 The fourth to seventh respondents said at para 121 of the ASOC thus picks up and is dependent upon the allegations that APRA makes at paras 118 and 119 of the ASOC. They continued:

At paragraph 118, APRA pleads that it was in the best interests of beneficiaries of IPS Super for compensation for the Pursuit Failure to have been recovered from IOOF Service Co, from IIML out of its own funds, or a combination of both. APRA also pleads at paragraph 118(c) that it would have been in the best interest for those beneficiaries for the compensation to have been met by IOOF Hold Co, however, it appears that this allegation is no longer pressed.

At paragraph 119 of the ASOC, APRA alleges that it was not in the best interests[of beneficiaries] for the loss and damage caused by the Pursuit Failure to be wholly paid for by funds taken from the IPS ORFR in circumstances where:

(a) IOOF Service Co was liable (or it was reasonably arguably that IOOF was liable) to compensate or indemnify IIML for the loss and damage caused by the Pursuit Failures under the Service Engagements;

(b) IIML was liable to make good the trust fund for the losses suffered by beneficiaries of IPS Super by reason of IIML’s Pursuit Breach;

(c) there was no practical difficulty in making a claim against IOOF Service Co; and

(d) the IPS ORFR was trust property and the superannuation beneficiaries of IPS Super had a beneficial interest in the money held in the IPS ORFR.

567 The fourth to seventh respondents made a series of propositions about these claims.

568 First, they said that paras 118 and 121 of the ASOC depend on the para 119 matters being established.

569 Second, it was said that “each of the matters referred to in paragraph 113 to 121 of the ASOC relate to the objective features of the compensation plans, the objective circumstances in which they were made and their alleged failure, as a matter of fact, to have served the best interests of beneficiaries. Accordingly, the subjective considerations and decision-making processes of IIML are properly seen as irrelevant to the case pleaded by APRA regarding the alleged compensation breach”.

570 Third, they submitted that “APRA’s case pivots on a misconception as to the nature and purpose of the ORFR and its characterisation as trust property. Whilst the ORFR is to be regarded as trust property it was constituted by a separate reserve in the accounts of IPS Super for the designated purpose of compensating members for losses arising from operational risk events. In other words, the interest superannuation beneficiaries had in this *sui generis* trust property was that it be used for their benefit for that purpose. Their interest was not that the ORFR be available to be allocated to their individual member account or to make payments of superannuation benefits under the trust deed”.

571 Fourth, they said that “on APRA’s own case, the ‘Pursuit Compensation Plan’ and its implementation must include all those steps directed at the ‘paying’ of compensation to affected beneficiaries. As explained further below, APRA wishes to run a case that now conveniently disregards the actual steps taken by IIML that resulted in the payment of compensation to affected beneficiaries”.

572 As to para 119(a) of the ASOC (IOOF Service Co was liable (or it was reasonably arguably that IOOF was liable) to compensate or indemnify IIML for the loss and damage caused by the Pursuit Failures under the Service Engagements), they submitted that “APRA bears the burden of establishing, by evidence, on the balance of probabilities, that IOOF Service Co was liable to IIML for the Pursuit Failure”, albeit noting that APRA’s case also involved the threshold of such a claim being “reasonably arguable”.

573 The fourth to seventh respondents submitted that:

…there is an obvious threshold difficulty with the proposition that IOOF Service Co was liable to IIML in respect of the Pursuit Failure: the events which caused the Pursuit Failure (namely the Orion configuration error) occurred in October 2006, more than two and half years before IOOF Service Co commenced providing services to IIML.

574 It was noted that APRA sought to avoid this by “alleging that IOOF Service Co was nevertheless liable for the loss and damage caused by the Pursuit failure because it failed to detect the Pursuit failure after 1 July 2009 (being the date IIML first became a party to the Service Engagements). The sole factual basis for this alleged liability is the conduct pleaded at paragraph 101(a) of ASOC:

(a) the Pursuit Failure continued, and was not detected, from 1 July 2009 to August 2014 because throughout that period IOOF Service Co:

(i) had failed to configure its IT system to process correctly beneficiaries’ re-investment instructions;

(ii) did not have an adequate framework in place to detect, prevent, mitigate or manage bugs in the IT system that could (and did) lead to the failure to reinvest distributions;

(iii) did not have appropriate controls and checks in place to detect that superannuation beneficiaries’ distributions were being held in cash and not re-invested or that beneficiaries’ express instructions were not being complied with.”

575 The fourth to seventh respondents said that:

It may immediately be observed that even if APRA were to succeed on its pleaded case, IOOF Service Co could only ever have been liable for part of the loss and damage arising from the Pursuit Failure. It clearly could not have been liable for any loss and damage attributable to the existence of the Pursuit Failure between October 2006 and July 2009. It could also only have ever been, at its highest, partially liable as a concurrent wrongdoer for any loss and damage attributable to the existence of the Pursuit Failure after July 2009, given that the events which brought about the Pursuit Failure in the first place (namely, the Orion configuration error) were, at the very least, an ongoing contributory cause of that loss and damage. APRA accepts this point.

Moreover, on APRA’s case IIML was also a concurrent wrongdoer for breach of the due care and skill covenant and would have thus been partly liable for the loss and damage arising post July 2009, adding to the complexity of any action against IOOF Service Co. Given any liability of IIML was excluded by the trust deed and IIML had a right of indemnity, these matters are highly significant in relation to APRA’s ultimate contention that IIML failed to act in the best interests of members by taking action to recover compensation from IOOF Service Co, especially given the size of losses (and hence any claim against Service Co) was less than $1 million in the context of a trust fund comprising assets of over $18 billion with more than 400,000 members.

576 I have explained above why I do not consider the rights of exclusion and indemnity applying to liability under s 55(3) of the SIS Act and that the materiality of any claim is not to be assessed merely by comparing the amount in issue with the total size of the fund. Apart from these observations, however, the fourth to seventh respondents’ submissions are sound.

577 Their submissions continued to the effect that if a claim had been made against IOOF Service Co it would have argued “that the real, substantial and effective cause of the loss and damage in respect of the Pursuit failure was the defect in the configuration of the reinvestment logic in Orion, for which IOOF Service Co bore no responsibility. Such an argument could have completely defeated, as a matter of causation, any liability of IOOF Service Co. In the very least, it would have been a matter substantially reducing its share of the loss of less than   
$1 million”.

578 The fourth to seventh respondents also made the point, as I have noted above, that the “factual foundation for IOOF Service Co’s putative liability, being the conduct of Service Co pleaded at [101] of ASOC, is unsupported by any evidence”. The fourth to seventh respondents dealt with APRA’s contentions as follows:

579 *IOOF Service Co “failed to configure its IT systems to process correctly beneficiaries’ re-investment instructions”*: “The obvious answer to this allegation is that the relevant IT system that was used to process beneficiaries re-investment instructions (that is, the Orion system) existed and was being used long before Service Co had any involvement with IIML’s business. That being so, it may reasonably be inferred, certainly in the absence of any evidence from APRA to the contrary, that it was not a system which IOOF Service Co owned, supplied to IIML or had any responsibility for configuring and was thus not a ‘Resource’ which was subject to the Service Co Resources Obligation under the agreements.”

580 *IOOF Service Co “did not have an adequate framework in place to detect, prevent, mitigate or manage bugs in the IT system” and did not have “appropriate controls and checks in place to detect that superannuation beneficiaries’ distributions were being held in cash and not re-invested or that beneficiaries’ express instructions were not being complied with”*: “APRA has wholly failed to identify with any precision, let alone adduce any evidence to substantiate, what framework, controls or checks IOOF Service Co could or should have had in place and that such a framework would have detected the Orion configuration error (an error which it will be recalled occurred more than two and half years before IOOF Service Co became involved in IIML’s business) or the resultant Pursuit Failure. Rather, and notwithstanding the seriousness of the allegations made in this proceeding, APRA merely invites the court to assume from the fact that an error occurred that there must necessarily have been ‘appropriate controls’ (unspecified) and ‘adequate frameworks’ (also unspecified) which would have prevented it. Such an approach is not only legally impermissible, but contrary to ordinary human and commercial experience.”

581 While I have said that I do not consider APRA needed to prove what a complying system would have been, it did need to prove that there was a system or systems reasonably available at the time (and not subsequently with the benefit of hindsight) which would have been capable of detecting the error. This APRA has not done. Further, as the fourth to seventh respondents submitted, the evidence is to the effect that there were no improvements to the systems that could be envisaged which would have been capable of detecting this particular error. Materiality is also a relevant concept which APRA has not considered (as to which see the next paragraph). The evidence suggests that one reason the problem was not detected was that the individual amounts involved were too small to detect. This suggests that there were systems in place to detect errors, but the details of these systems are unknown. All of these considerations would be relevant to any assessment of whether there was any failure to meet the applicable standard of care, yet all remain unknown on APRA’s case.

582 The fourth to seventh respondents said:

The evidentiary deficiencies, or more accurately the absence of any evidence, in APRA’s case are fatal to the allegation that IOOF Service Co was liable to compensate IIML for the loss and damage caused by the Pursuit Failure. To be sure, APRA could have sought to call evidence from an IT expert or an audit expert in internal control systems to assist it actually identify what framework and controls could have been sensibly and cost-effectively put in place to anticipate, detect, prevent and mitigate the kind of problem which eventuated. It has not done so.

It also must be kept steadily in mind that any assessment of IT internal control systems and frameworks IIML should have had in place to detect, prevent and mitigate IT errors (or “bugs”) quite appropriately should have regard to matters of materiality. No internal control system can detect and prevent all errors or at least the cost of building and putting in place such a fail-safe system would outweigh the benefits of doing so. Whilst the Pursuit Failure assumes prominence in these proceedings, its significance must be put into context. There is no suggestion the Pursuit Failure was indicative of a wider and systemic deficiency in IOOF Service Co’s IT internal systems for detecting and preventing errors. The Pursuit Failure represented [an] isolated problem, resulting from an unforeseen change in circumstances [distributions being paid and processed across two different accounting periods], that had an immaterial impact on the assets of the TPS Super Fund. Put another way, it is not a problem or incident that a reasonable external auditor, applying established principles of materiality, would consider sufficiently material to investigate and report in any audit report.

583 I agree with these submissions. The existence of reasonably arguable causes of action for loss against IOOF entities is central to APRA’s case yet it has not adduced the kind of evidence that would be necessary to prove that, objectively, any such causes of action existed. It has also not proved that if independent legal advice had been obtained the advice would have been to the same effect as APRA’s assertions, that the causes of action were reasonably arguable and the making of claims presented no practical difficulty. On the contrary, I infer that any such advice would have identified the fundamental difficulties which the respondents have noted.

584 Consistently with this reasoning, the submissions for the respondents continued:

It again bears emphasis that the kind of claim APRA postulates, but does not develop, against IOOF Service Co is not one of strict liability but contractual negligence. And all claims for negligence will be informed by foreseeability, materiality and costs of putting in place precautions to address the perceived risk. On the evidence, the claim asserted by APRA against IOOF Service Co was to address a problem or operational risk that could not reasonably have been anticipated and which, on any view, was immaterial to the asset position of the TPS Super Fund and the overall effective functioning of the internal control systems and processes of IOOF for the benefit and protection of members. Against that, there is no evidence from APRA as to the type of controls and frameworks that could have been put in place and the cost of doing so. There is not even any evidence from APRA as to the kind of computer software, with the requisite functionality, available at all relevant times to detect, prevent, mitigate and manage the kind of failure that occurred, let alone the attributes, cost, reliability and performance characteristics of any such computer software systems.

585 These submissions accord with the views I have already expressed that APRA appears to assume that liability is established by reason of the doctrine of *res ipsa loquitur* informed, perhaps, by a misunderstanding that the system as a whole was incapable of reinvesting distributions when, in fact, the error was far more confined and related to a circumstance described as not reasonably anticipated at the time the system was developed. All of these matters – reasonableness, foreseeability, practicality and materiality would be relevant to an evaluation of any failure to satisfy the applicable standard of care, yet APRA’s case does not deal with any of these matters.

586 The submissions also identified other legal obstacles as follows:

In order to successfully hold IOOF Service Co liable for the Pursuit Failure, IIML would have needed to formulate a nuanced and carefully articulated claim based on a detailed understanding of the facts. For example, any such claim would have needed to establish a factual basis as to:

(a) why the Pursuit Failure should be regarded as having been caused by IOOF Service Co’s failure to “adequately supervise Employees and Contractors” rather than a failure on the part of IIML to provide the Employees and Subcontractors with proper lawful instructions or directions to act;

(b) why the Pursuit Failure should be regarded as having been caused by IOOF Service Co’s failure to “have adequate audit, monitoring and assessment procedures in respect of the Services” rather than a failure on the part of IIML to have “kept adequate systems, procedures and processes” in circumstances where the Orion system contained the Orion Configuration Error;

(c) why the Pursuit Failure should be regarded as having been caused by IOOF Service Co’s failure to “exercise due care, skill and diligence in the performance of the Services” rather than a failure on the part of IIML to exercise due care, skill and diligence towards IOOF Service Co’s Employees;

(d) why the Pursuit Failure should be regarded as having been caused by IOOF Service Co’s failure to the best of its ability to ensure the Services complied with the agreements and legislative requirements rather than a failure on the part of IIML to the best of its ability to ensure that IOOF Service Co’s Employees complied with the agreements and legislative requirements;

(e) why the Pursuit Failure should be regarded as having been caused by a failure of IOOF Service Co, rather than IIML, to “do all such other acts and things as are necessary” to ensure that IIML complied with its statutory obligations (assuming there was in fact a breach of IIML’s statutory obligations, which is denied); and

(f) why, in any event, IOOF Service Co’s failure to detect and thus prevent Pursuit Failure should not be regarded as having been caused by IIML’s failure to notify IOOF Service Co of the existence of the Orion Configuration Error in breach of IIML’s notification obligation under clause 9(h).

It is highly doubtful that IIML would have been able to establish any of these matters in circumstances where the events initially giving rise to the Pursuit Failure had occurred more than seven years before they were first discovered, relevant documentation could not be located, IIML was unable to determine how the Orion configuration error arose, there was a “complex historical background”, and IIML did not consider that it had sufficient facts to make it clear that the Pursuit Failure was caused by fault or negligence on the part of IOOF Service Co.

It follows that APRA has not established on the balance of probabilities that IOOF Service Co was liable under the Services Agreements for the Pursuit Failure. It is difficult to see how a claim against IOOF Service Co would even have met the low threshold of being “reasonably arguable”. Accordingly, this aspect of APRA’s case must fail.

587 The fourth to seventh respondents identified another critical plank in APRA’s case as there being no practical difficulty in IIML making a claim against IOOF Service Co. This, they described as “misguided and blind to reality”, as:

APRA approaches its case as if it would have been sufficient to justify taking action against IOOF Service Co that the low threshold of a “reasonably arguable” claim was met. Quite to the contrary, given the cost and complexities associated with such a claim and the relatively modest amount of the claim, one would expect a prudent superannuation trustee would need a high degree of confidence to justify pursuing such a claim.

588 As to the dispute resolution procedure in cl 17, the fourth to seventh respondents said that:

…there is no basis for thinking it still would not have come at considerable cost. Messrs Riordan and Vine were no doubt correct to observe that such a process would have necessitated appropriate internal information barriers, independent litigation committees or “Chinese walls” within IOOF and, as a corollary, the engagement of separate, external lawyers to represent IOOF Service Co in a contested dispute. APRA adduces no evidence of the likely costs of such external legal representation or evidence as to the advice external lawyers would likely have given as to prospects of such a claim and the necessary evidence to be advanced in connection with such an expert determination. On any view, this kind of expert determination would still have required detailed and rigorous consideration of the real cause of the losses sustained, the kind of systems and procedures, if any, that could have been put in place to detect, prevent and mitigate the kind of error or problem that occurred and the range of difficult legal arguments as to the application of the negligence standard to the facts and attribution and division of legal responsibility. It would have required submissions from the parties, documents and witness statements and possibly expert evidence. Any decision of the expert adjudicator would also not have been binding on the parties if subsequently established in judicial proceedings to have been infected by manifest error of law, giving rise to the possibility of appeals.

589 They then identified a range of factors which would mean that pursuing IOOF Service Co would not have been in the best interests of the beneficiaries:

(a) the claim would have had, at best, highly uncertain prospects of success;

(b) IIML would have had considerable difficulty marshalling the evidence necessary to support the claim given the effluxion of time since the relevant events occurred and the multiple capacities which IOOF employees routinely acted (ie, for IOOF Service Co and for IIML);

(c) even if the requisite evidence could be obtained, the cost of investigating and establishing the potential claim would have been considerable;

(d) prosecuting and defending the claim would have involved considerable time and effort on the part of the management and employees of IIML and IOOF Service Co and to that extent distracted them from other activities for the benefit of beneficiaries (such as activities associated with the proper administration of the Fund)

(e) even if the claim was successful:

(i) only part of the loss and damage caused by the Pursuit Failure could have been recovered from IOOF Service Co as a contributory wrongdoer;

(ii) determining what proportion of the loss IOOF Service Co was liable for having regard to its relative contribution would have been an inherently difficult and uncertain exercise; and

(iii) there was therefore a reasonable prospect that, even if the claim was successful, only a small portion of the loss would be able to be recovered.

(f) insofar as APRA suggests IOOF Service Co’s professional indemnity insurance may have been relevant (ACS at [381]), difficult issues would likely have arisen as to the applicability of certain exclusions.

590 They submitted that Mr Vine and Mr Riordan, as experienced lawyers, would have been alive to these difficulties and aware of the principles that:

(a) First, “[a] trustee under the general law (such as IIML and Questor) must exercise judgment so as to save the estate unnecessary expenditure of money: see *Re Grimthorpe (Dec'd)* [1958] 1 Ch 615 at 623; *Re Whitley; Lloyds Bank Ltd v Whitley* [1962] 1 WLR 922 at 931; [1962] 3 All ER 45 at 53.”

(b) Second, an incident of this is that “[i]f there be one consideration again more than another which ought to be present to the mind of a trustee, especially the trustee of a small and easily dissipated fund, it is that all litigation should be avoided, unless there is such a chance of success as to render it desirable in the interests of the estate that the necessary risk should be incurred”: citing Bowne LJ in *Re Beddoe*. See also *Re England's Settlements Trusts; Dobb v England* [1917] 1 Ch 24 at 28,31.

(c) Third, where litigation is commenced by a trustee without sufficient prospects or is not reasonable having regard to the resources to be applied to it, questions arise as to whether the expense incurred by the trustee is properly incurred and within the trustee’s right to indemnity: *Adsett v Berlouis* (1992) 37 FCR 201 at 212; *Macedonian Church v Eminence Petar* (2008) 237 CLR 66 at 93-94 [69]-[72].

591 It was submitted that:

Importantly, the assessment of whether to advance uncertain, if not speculative, claims against a related entity, IOOF Service Co, is to be seen in a context whether there was otherwise an available source of compensation through the ORFR to restore beneficiaries’ positions and that source was put in place to protect beneficiaries and absorb losses arising from precisely the kind of operational risk associated with the Pursuit Failure.

Having regard to these matters, it could hardly be said that the decision by IIML not to take action against IOOF Service Co to recover compensation for the Pursuit Failure, but to instead have recourse to the ORFR, was a course of action incapable of reasonably being regarded as in the best interests of members. On the contrary, expending the assets of the trust fund to take action against IOOF Service Co, in all the circumstances, would have been difficult to reconcile with IIML’s duties, especially in the absence of any judicial directions justifying such a course.

592 As to IIML being an available source of compensation, the fourth to seventh respondents made the following propositions.

First, APRA has not established that IIML breached its due care and skill covenant in relation to the Pursuit Failure.

Secondly, even if such a breach could be established, it gave rise to no liability of IIML to pay compensation to superannuation beneficiaries. This is because, as explained above, by reason of clause 11.5 of the IPS Trust Deed IIML was exempted from any liability to beneficiaries under s 55(3) in relation to breaches of the Due Care Covenant.

Thirdly, if and insofar as IIML had any liability it was entitled to be indemnified out of the assets of the fund under clause 11.7 of the IPS Trust Deed (including the ORFR itself in the first instance as explained earlier). In other words, APRA’s case is entirely circular insofar as it pleads recovery should have come from IIML itself. Any liability of IIML would have resulted in a commensurate indemnity of IIML from the ORFR in the same amount as approved in May 2015 to immediately restore members’ accounts.

593 It will be apparent that I have accepted the first, but not the second and third of these propositions.

594 Apart from this, the fourth to seventh respondents addressed other reasons why they said APRA’s case must fail. They said:

APRA’s case appears to be one of locating a breach in respect of a “decision” as at 27 May 2015 and suggesting on and from that date IIML was in contravention of the SIS Act by “implementing” the compensation plan approved on 27 May 2015 (ASOC at [115] and [121]). Analysing the manner in which IIML addressed compensation of its beneficiaries for the Pursuit Failure in this way is wrong in fact and ignores that IIML’s compensatory response to the Pursuit Failure involved a continuous and evolving evaluation and re-evaluation throughout 2014 to 2017. The totality of IIML’s response must be considered. As already noted, IIML fully reimbursed the ORFR from its own funds and insurance proceeds. This position was arrived at having regard to the “observations and directives” of APRA. APRA wishes to gloss over this fact. APRA seeks to treat the steps in fact taken to implement the payment of its compensation to affected beneficiaries as “subsequent steps” disconnected from how IIML in fact addressed the payment of compensation from the Pursuit Failure in the best interests of members. APRA in its closing submissions (at [17] of the outline) treats the “course of conduct” in implementing the plan from 27 May 2015 through to 2018 as involving everything other than those steps dealing with the actual payment of compensation. Presumably APRA adopts this approach because it knows the compensation plan as approved by the Board on 27 May 2015 (as pleaded by APRA in the ASOC at [111] and [154]) was not “implemented” in that form because the ORFR was replenished through insurance proceeds (and as to the balance of $96,000 – which is properly regarded as an immaterial amount having regard to the size of IPS Super and its ORFR – through IIML’s own funds). By ignoring how in fact beneficiaries were ultimately compensated by IIML, APRA advances a case regarding “implementation” that is inconsistent with its pleading and what in fact happened.

595 The fourth to seventh respondents submitted that it was factually incorrect for APRA to frame its case in a way that precluded any further consideration of options to replenish the ORFR. The following contentions were made:

First, the May 2015 Pursuit Board Paper was preceded by a meeting on 2 March 2015 between APRA and Mr Vine and Mr Riordan. As already noted, at that meeting Mr Vine and Mr Riordan informed APRA that IIML intended to use the ORFR to fund the compensation to IPS Super members and would then give further consideration to other sources of funding to replenish the reserve. This of course is precisely what ultimately occurred.

Secondly, the May 2015 Pursuit Board Paper did not contain any final decision that the ORFR should not be replenished subsequently through other sources of funding. Nor did it contain a recommendation that IIML should give no further consideration to that issue… APRA considered that it was appropriate to use the ORFR to fund compensation to IPS members, provided that further consideration was given to other sources of compensation and that the ORFR was replenished to the extent other sources were properly available. That is precisely what IIML did.

596 As to the claim that the compensation plan preferred the profit interests of IOOF, there is no basis in the evidence for any such finding according to the fourth to seventh respondents. As they put it:

The amounts of money involved in relation to the Pursuit matter are properly seen as minor having regard to the size of IOOF group’s business. IOOF group’s total revenue for the year ending 30 June 2015 was $938 million. Its net profit after tax was $174 million. Any notion that the development and adoption of the Pursuit Compensation Plan was driven by desire to boost IOOF’s profits is therefore fanciful. This is not, with respect, an allegation that should have been made.

597 I have accepted a submission to this effect above.

598 As to the contention that the compensation claim impermissibly preferred the interests of   
non-superannuation investors, the non-superannuation investors had no interest in the trust fund or the ORFR and were thus entirely unaffected by the decision as to whether the compensation paid to superannuation beneficiaries was sourced from the ORFR or IIML or IOOF Service Co’s funds. There was a rational basis to treat these investors differently given that there was no dedicated fund to meet the kind of contingencies raised by the Pursuit failure for these investors.

599 The first respondent made certain additional points assuming there existed a reasonably arguable liability on the part of IIML or IOOF Service Co in relation to the Pursuit failure. They provided some background as part of these additional points noting, amongst other things, that Mr Riordan’s response to APRA of 19 December 2014 about action against IOOF Service Co was important. As noted, Mr Riordan had said:

IIML is not currently considering any such action for a number of reasons, including the complex historical background involving ORION and product changes, legitimate use of the ORFR and the commercial reality of running a large group of companies where issues may not necessarily be realistically actionable or indeed require action in order for compensation to be paid.

600 According to the first respondent:

a) First, there was a complex historical background involving ORION. That is true. As discussed above, ORION pre-dated the merger of Australian Wealth Management Limited and IOOF Holdings Limited. It was software that dated from a time when Old Service Co was providing services to IIML, not IOOF Service Co. Further, it was not clear whether fault lay with any person in regards to the Pursuit distribution reinvestment failure and there was certainly no evidence that fault lay with IOOF Service Co.

b) Secondly, Mr Riordan correctly identified that IIML could lawfully and legitimately use the ORFR. That assessment was correct for the reasons given…above.

c) Thirdly, Mr Riordan pointed to the fact that the “commercial reality” was that, if a view was taken that IOOF Service Co was in fact liable for the Pursuit incident, the IOOF Group would ensure compensation was paid without the need for a formal claim to be pursued against IOOF Service Co. Mr Riordan was saying that the fact that IOOF Service Co had a separate legal personality to IIML would not stand in the way if the true position was that it was at fault for the beneficiaries’ loss. That is a commendable position and one not strictly required by the law. At ACS [386], APRA wholly mischaracterises what Mr Riordan was clearly saying in circumstances where APRA knows what Mr Riordan actually meant because it was explained to APRA by Mr Riordan on 2 March 2015….

601 IIML had explained to APRA why it was not considering pursuing IOOF Service Co noting that APRA’s notes of a meeting on 2 March 2015 record that:

APRA asked IOOF to explain its specific reasons for not pursuing its service provider.

IOOF explained that:

The errors had occurred since 2007

It was unclear how the configuration issue came to be (i.e. was the service provider at fault/negligent?)

…

IOOF noted that they had not been able to find the Config Spec request from 2007 that would clarify who was at fault. IOOF also noted that the reason the issue developed was that fund managers had extended the time in which they paid distributions and that the system’s tight controls on backdating prevented the distributions from being reinvested. The amounts involved were small and thereby not detected by existing controls but upon investigation, IOOF did not believe that there was a control that could be introduced to detect these type of issues.

…

It was not clear that the service provider would be willing to foot the bill and the trustee did not want to get into a legal argument with its service provider resulting in an outcome that may not be in members’ best interest.

…

In respect to sources of compensation, IOOF noted that it was its intention to pay in the first instance and that it would then consider options available to it in terms of seeking reimbursement. IOOF noted that it was unlikely to advise APRA that it was pursuing its service provider as if it reached the conclusion that the fund should be reimbursed it would simply make it happen and would not be focused on where in the group that compensation was sourced.

602 The first respondent described this as a cogent and reasonable position. Nevertheless it said it is clear Mr Vine took APRA’s position seriously as he emailed Mr Tanner, Compliance Manager, on his return saying that APRA pressed the “issue around the trustee pursuing IOOF Service Co under the services agreement” to which Mr Tanner replied “Pursuit of action against IOOF Service Co is a question for legal – could not argue negligence or breach of contract for something not reasonably anticipated at the time. Also I think the legal entity that was a co at the time pre-merger was a different company”.

603 The first respondent’s submissions also noted, as is the fact, that Mr Kelaher knew none of this. What he knew was contained in the updates to the board including that on 13 March 2015 in which the board was informed:

We provided APRA with a full explanation of the proposed approach and met with them on 2 March 2015 to discuss this breach. APRA requested (1) further information on the testing we have conducted on the impact of the breach on particular categories of member and (2) following use of the ORFR as appropriate for compensation to members, that the trustee further consider any potential alternative compensation sources.

604 The submissions for the first respondent continued:

On 13 May 2015, Mr Vine and Mr Riordan prepared a memorandum to the Board of IIML with a recommendation regarding the compensation to be paid as a result of the Pursuit distribution reinvestment error. The paper began by noting:

Management ha[d] been in ongoing consultation with APRA in relation to the breach rectification process and compensation methodology for IPS members.

That was clearly true.

The recommendation made in the paper was that the breach be remedied by restitution, which management described as “placing clients in the financial position they would have been in had the error not occurred”. Compensation of that kind was clearly in the best interests of those that had suffered loss.

As to the source of compensation, the paper recommended that compensation be paid to non-superannuation clients by IIML, whereas compensation to superannuation beneficiaries would be paid from the ORFR reserve. The reason for this distinction was explained by Mr Vine and Mr Riordan in their memorandum. For non-superannuation clients, there was no equivalent reserve to the ORFR and so there was no dedicated fund to meet the sort of contingencies raised by the Pursuit incident.

605 The fact that non-superannuation clients were funded by IIML:

…shows that IIML was willing to fund losses from its own pockets where it was appropriate and necessary to do so to make clients whole. Where, on the other hand, IIML could properly call on a dedicated fund that had been established in accordance with the SIS Act to deal with losses of the very kind as those arising from the Pursuit incident, it properly did so.

606 The first respondent said the true position in May 2015, contrary to APRA’s case, was that:

a) IIML had self-reported the Pursuit distribution reinvestment failure to APRA and engaged in a deliberative process with APRA over some months in relation to the proposed compensation plan;

b) IIML had investigated the cause of the Pursuit incident but had not been able to determine who was at fault or whether it had a claim against anyone;

c) IIML had determined that the Pursuit incident commenced in 2007, at a time when Old Service Co was providing services to IIML and IOOF Service Co was not;

d) Old Service Co had been wound up;

e) Any claim against IOOF Service Co faced obvious difficulties, including that IIML had obligations under clause 9(g) of the AWM Services Deed and IOOF Services Deed to “keep adequate systems, procedures and processes”;

f) If IOOF Service Co was pursued, the likelihood was that IIML in its capacity as trustee would incur costs for which it would be indemnified out of trust assets; and

g) IIML itself had no exposure for the Pursuit failure because of the exclusion clause in the IPS Super trust deed, and in light of its rights of indemnity under that deed.

607 I have already explained why I would not agree with (f) and (g) of these propositions in terms of the operation of s 55(1) and (3) of the SIS Act but have also concluded, in any event, that APRA has not proved the existence of a reasonably arguable case for liability on the part of IOOF Service Co or IIML.

608 The first respondent, in common with the fourth to seventh respondents, said it would be wrong to characterise the IIML board’s resolution on 27 May 2015 to “approve the remediation strategy and the source of compensation” as foreclosing any possibility of pursuing compensation in the future to replenish the ORFR.

609 The second respondent, consistently with the submissions for the other respondents, said:

As to recovery from IOOF Service Co or IIML, as explained earlier, even if it was otherwise relevant, there is no evidentiary foundation for the allegation that either IOOF Service Co or IIML was liable for the original failure. In any event, the effect of the indemnity under cl 11.1 of the services agreement between IOOF Service Co and IIML was likely to render circular any arguments about liability as both IOOF Service Co and IIML had potential recourse to the indemnity. For example, IOOF Service Co might have claimed a breach by IIML of its obligation under cl 9.1(g) to “keep adequate systems, procedures and processes, whether technologically based or not (such as recording systems, compliance and monitoring systems or processes to ensure Service Company or its Employees or Subcontractors are being able to carry out their respective duties)”; IIML might have claimed that Service Co breached its obligation to exercise due care, skill and diligence under cl 8.1.

As indicated above, the board paper tendered by APRA includes the statement that management did not recommend action against IOOF Service Co for a number of reasons, the first of which was that “[t]he complex historical background involving Orion product changes makes it difficult to attribute a breach of contract or negligence to the administrator” (ie IOOF Service Co). That is a view expressed by lawyers familiar with the facts. That is evidence in for all purposes and contradicts APRA’s presumptive assertion of liability.

Management also considered that the issues may not be realistically actionable and legal action would likely be contested and costly. Contrary to ACS [399], these reasons do not demonstrate that the issue was considered from the perspective of the IOOF Group as a whole. Any legal action taken by IIML as the trustee would have had an obvious impact on the beneficiaries and the fund through, for example, the incurring of significant legal costs in circumstances where it was difficult to attribute a breach to IOOF Service Co. APRA has not adduced any evidence to the contrary. Furthermore, there is no reason to suppose that the legal advice being given was not genuine legal advice but commercial advice in the interests of IOOF. The persons expressing that view were responsible officers who had to assist IIML to give primacy to the interests of beneficiaries. There was no reason to suppose they were not doing so.

610 Otherwise, as to use of the ORFR:

(1) “The board was told that IIML’s ORFR reserves policy permitted IIML to use the ORFR reserve to compensate members for any loss arising from operational risk and explained that operational risk is ‘the risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events.’”

(2) “It is not alleged that IIML’s ORFR policy did not authorise the use of the ORFR reserve to compensate the IPS Super beneficiaries.”

(3) “It is not alleged that the loss arising from the original failure did not constitute an operational risk within the meaning of the policy or prudential standard SPS 114 – Operational Risk Financial Requirement.”

(4) “The board was also told of management’s view that ‘it is in members’ best interests to access the ORFR to ensure that loss is remedied on a timely basis’ and that ‘APRA agree with this position, subject to later consideration of sources of funding.’”

(5) “APRA was in complete agreement with management’s plan to use the ORFR in the first instance. At the meeting on 2 March 2015, APRA informed Mr Riordan and Mr Vine that ‘IOOF may proceed to use the ORFR to fund the compensation in the first instance whilst it pursued sources for reimbursement from within the IOOF Group.’”

(6) “The IPS Super beneficiaries were compensated from the ORFR reserve whilst an insurance claim was pursued. As acknowledged by APRA at ACS [376] and [383], that claim was first made in 2014 and was accepted by the insurer on 13 July 2017 and subsequently paid. A provision of $250,000 was recognised in IIML as payment of the deductible for the insurance claim. Following receipt of the insurance proceeds, the ORFR was replenished in August 2017 and APRA accepted, in its opening submissions, that this was so.”

611 The second respondent submitted that:

APRA’s position now appears to be that the ORFR reserve should not have been used as “a first port of call.” That is not what APRA said at the time, nor is it supported by law. As noted above, in March 2015, APRA informed IOOF representatives that the ORFR reserve could be used “in the first instance.” On 20 August 2015, Ms Napolitano wrote an email to Mr Vine in which she noted APRA’s view that the “ORFR may be used to compensate members in the first instance.” On 20 May 2016, APRA wrote to IOOF and stated that in the event of a loss resulting from an operational risk event, APRA expected “that the immediate remediation strategy would be to compensate members through drawing down the ORFR, which would place members in the same position they would have been in had the operational loss not occurred.” What occurred was entirely consistent with what APRA expected to occur. The super members were compensated from the ORFR whilst IIML pursued other sources, namely the insurance claim. The board was told that APRA agreed with IIML using the ORFR reserve “subject to later consideration of other sources of funding”. Once the insurance claim was paid, the ORFR reserve was replenished.

###### 11.4 Discussion

612 Except as otherwise indicated above I accept the submissions for the respondents. Given my conclusions about the Pursuit failure, that APRA has not proved liability or a reasonably arguable case for liability on the part of IOOF Service Co or IIML, it follows that it cannot succeed in its complaints about the Pursuit Compensation Plan.

613 Apart from this, APRA’s case on the Pursuit Compensation Plan is itself flawed. The case is amorphous and difficult to follow. The essence of the case, as orally submitted by APRA, appears to be that it was not in the best interests of beneficiaries to use the ORFR in the first instance without having exhaustively considered the prospects of claims against IOOF Service Co and IIML. The evidence discloses, however, that Mr Vine and Mr Riordan had given consideration to the practicalities of claims against IOOF Service Co and IIML and, rightly in my view, determined that such claims were impractical. Even had they done what APRA seems to consider was necessary, that is to obtain independent legal advice, on the evidence the position that would have been reached would have been no different from the position in fact reached. Claims against IOOF Service Co and IIML would be by no means straightforward and would face many practical and legal difficulties. Such claims would not meet the standard of being reasonably arguable for all of the reasons the respondents identified.

614 APRA has also not explained why what occurred involves any breach of the best interests and no conflicts covenants. The case seems to be, as the respondents suggest, that no regard may be paid to the fact that IIML was pursuing an insurance claim and the ORFR was replenished. Why the facts of what actually occurred may be disregarded is unclear. The respondents’ submission that the board of IIML never foreclosed the possibility of the ORFR being replenished from other sources must be accepted. But even if it had not been possible for the ORFR to be replenished, APRA’s case has not confronted the fact that the ORFR was established for the purpose of dealing with losses caused by operational risk. Using the ORFR for the purpose for which it was established cannot involve a failure to act in the best interests of members or, at the least, cannot amount to such a failure on the facts of the present case where there was no reasonably arguable case for liability on the part of any other entity.

615 APRA’s complaints about contravention of the no conflicts covenant also founder in the face of the facts of the present case. There was no material conflict of interest in existence between the interests of IIML or IOOF Service Co and the beneficiaries, as there was no reasonably arguable case for liability on the part of those entities. The evidence does not support the proposition that Mr Vine and Mr Riordan and the board of IIML approached the issue of compensation by reference to the interests of the IOOF Group as a whole and failed to give priority to the interests of the beneficiaries. The decision-making process reflects the giving of priority to the interests of the beneficiaries. In particular, I accept the submission that as experienced lawyers Mr Vine and Mr Riordan must have been alive to the practical and more obvious legal difficulties which any claim against IOOF Service Co or IIML would confront. I do not accept that in order to comply with the best interests and no conflicts covenants the respondents or any of them had to “exhaust” all possible other sources of compensation if, by this, APRA means that it was necessary to obtain independent legal advice and to bring claims if that advice suggested any possible argument for liability could be made irrespective of the prospects of success or potential costs. As I have said, even if such advice had been obtained the evidence supports the inference that it would have disclosed all of the legal and practical difficulties noted by the respondents with the consequence that “exhausting” all possible sources of compensation would have led to the same outcome in any event.

616 In its oral submissions APRA emphasised that the practical and legal difficulties to which any claims against IIML and IOOF Service Co would be subject did not form part of the decision-making process at the time and thus were irrelevant. It may be accepted that the level of detail into which the respondents have descended in this regard did not form part of the decision-making process at the time but that does not mean that the decision-making process involved no consideration of these matters. More to the point, however, APRA has failed to prove that the decision-making process, which it advocated was necessary in order to comply with the best interests and no conflicts covenants, would have led to any different result. This is fatal to APRA’s case.

617 APRA’s case, as the respondents submitted, repeatedly founders on the basis of lack of evidence. It is also conceptually flawed for the reasons the respondents identified. In particular, the case necessarily reduces to the failure to detect the error from 2009 onwards. Yet as the respondents submitted, APRA’s case fails to prove what the IT systems were and whether, in all of the circumstances, they were unreasonable or in breach of the relevant standard of care (a concept which APRA has not touched upon at all). APRA’s case gives no consideration to the concept of materiality or the cost-benefit evaluation that would be necessary to found any conclusion of contravention of the applicable standard of care.

618 I also do not accept that the insurance claim constitutes admissions of the kind necessary to establish liability on the part of IIML or a reasonably arguable case for such liability. The mere fact that an insurance claim was made on the basis of a genuine belief that IIML would be liable to compensate beneficiaries does not constitute an admission by IIML that it was so liable.

##### 12. MR KELAHER AND MR VENARDOS – ALLEGED PURSUIT COMPENSATION PLAN BREACHES

###### 12.1 APRA’s case

619 APRA’s case is that by their conduct in respect of IIML’s development, approval and implementation of the Pursuit Compensation Plan and failure to reverse it until 2018,   
Mr Kelaher and Mr Venardos contravened their ss 52A(b), (c), (d) and (f) covenants and thereby s 55(1) of the SIS Act: ASOC [125] - [129B].

620 According to APRA, Mr Kelaher, as managing director of IOOF Hold Co, IIML and IOOF Service Co had:

…a conflict between his duties to superannuation beneficiaries under s 52A in respect of (i) the preservation of IPS Super trust property, the vindication of rights in respect of it and the application of IIML’s risk management policy in respect of services provided by IOOF Service Co; (ii) the interests of the IOOF Group in relation to the decision as to how to compensate the Pursuit Failure, and (iii) duties to MIS investors affected by the same conduct.

621 Further, according to APRA, as a superannuation trustee director Mr Kelaher had to “bring a critical mind” to the Pursuit Compensation Plan that was presented to him on 27 May 2015 and determine whether that plan was in the best interests of beneficiaries, despite the conflict, before exercising his power as a director to vote in favour of the plan. Before so doing, according to APRA, Mr Kelaher knew or ought to have known:

(a) that the Pursuit Failure had occurred and the basal reasons for it;

(b) that the losses to beneficiaries flowing from the Pursuit Failure flowed directly from the actions and omissions of Questor and its service providers;

(c) accordingly, the proponents of the plan, Coulter and Vine, who were both senior executives of IOOF Hold Co and IOOF Service Co as well as acting as responsible officers of Questor, had a conflict of interest;

(d) that he himself, as Managing Director, had the conflict of interest mentioned above, and needed to make sure that his decision was not consciously or unconsciously swayed by interests other than those of the beneficiaries (which he was required to prioritise by reason of s 52A(2)(d)).

(e) that IIML was itself liable to make good the losses suffered by beneficiaries of IPS Super;

(f) that management had determined to address the loss suffered by IPS Super and its members differently to how it determined to address the loss suffered by IDPS investors;

(g) that in respect of IDPS investor losses, IIML was accepting liability to compensate, but was not proposing to compensate beneficiaries of IPS Super. The fact that IIML was proposing itself to compensate IDPS investors was a further indication, known to Kelaher at the time, that IIML was responsible for the errors and personally liable for the losses caused by them;

(h) that IIML was proposing to use the capital it held on trust for members in the form of the ORFR to “compensate” members of IPS Super; and

(i) that no compensation was to be sought from IOOF Service Co in respect of its involvement in the underlying conduct.

622 APRA said Mr Kelaher knew of the role that IOOF Service Co played in the group, namely providing all personnel and administration services required by each subsidiary (including IIML) to run their business and thus knew that the personnel who had responsibility from July 2009 to when the Pursuit failure was detected in 2014 for processing reinvestment instructions and the service provider of IIML’s systems for detecting errors of such kind were IOOF Service Co staff and IOOF Service Co systems. He also knew of the terms of the IOOF Service Co service obligations, the dispute resolution mechanism, and the indemnity it provided for the benefit of IIML.

623 Because of his conflicts, APRA said Mr Kelaher was “required to exercise ‘*special vigilance*’ and ‘*scrupulous concern*’ when considering the plan, particularly as it involved a discretionary decision by the trustee to dissipate trust funds to pay beneficiaries for losses that originated from conduct within the IOOF Group”.

624 According to APRA, armed with knowledge that Mr Kelaher had, a prudent superannuation trustee director exercising care, skill and diligence and performing his duties in the best interests of beneficiaries, would not have approved the Pursuit Compensation Plan. Rather, a prudent superannuation director would:

(a) have identified that IIML had a conflict of interest in approving a plan that treated IPS Super members differently from IDPS investors with respect to IIML’s personal liability to compensate;

(b) have identified and declared that he himself had a conflict of interest in approving the plan on behalf of IIML;

(c) have identified that the justifications management had given in support of the proposed Pursuit Compensation Plan did not explain why IIML itself was not an appropriate source of compensation for the loss suffered by the IPS Super fund and its beneficiaries, and required IIML to have available to it further information on that topic from a person who was not in a conflicted position to advise on it;

(d) have identified that the justifications given for not taking steps to seek contribution from IOOF Service Co were inadequate having regard to the services arrangements in place between IOOF Service Co and IIML, and that the paper did not give genuine consideration to members’ best interests or prioritise their interests and the performance of duties owed to them over others;

(e) not have accepted management’s conclusion that making a claim against IOOF Service Co was not practical, including because of the conflict applying to those personnel given their position as officers and employees of IOOF Service Co;

(f) have himself sought, or instructed management to seek, independent legal advice for IIML, it its capacity as trustee of IPS Super, on the liability of IIML and IOOF Service Co for the losses;

(g) have taken steps to manage conflicts of interest when considering the Pursuit Compensation Plan including, identifying all relevant conflicts and ensuring the Board’s decision-making recorded how those conflicts had been addressed;

(h) rejected the plan or alternatively adjourn the meeting so that proper enquiries could be made and genuine consideration be given to the plan by IIML consistently with its s 52 covenants.

625 It is because Mr Kelaher did not take these steps that he contravened ss 52A(2)(b), (c), (d) and (f) of the SIS Act. In response to submissions on Mr Kelaher’s behalf, APRA said that the board paper presented to the 27 May 2015 meeting was deficient. APRA submitted:

(a) …it [the board paper] is not detailed with respect to management’s consideration of other sources of compensation other than the reserves. There is no consideration in the paper of IIML’s own potential liability with respect to IPS Super, or IOOF Service Co’s potential exposure (as the service provider for 5 of the 7 years during which the Pursuit Failure was ongoing).

(b) It is not “well-reasoned and logical”. These submissions have made reference to the difficulty Vine and Riordan frankly acknowledged when drafting the paper of the fact it was “tricky” to justify not taking steps to seek compensation from IOOF Service Co: CB tab 132A1. Despite noting that the cause of the Pursuit Breach was various failures by IIML’s systems and in its service provision (which Kelaher would have known was principally provided by IOOF Service Co from 1 July 2009), the paper did not propose holding those responsible for those failures (namely, IIML and IOOF Service Co) accountable for the losses suffered by IPS Super whereas it proposed with no explanation to hold IIML accountable for the losses suffered by IDPS investors.

(c) It may have exhibited a “large degree of commercial common sense”, but only when considered from the perspective of the IOOF Group as a whole; not from the perspective of beneficiaries’ best interests. The same blind spot is apparent in Kelaher’s letter to APRA dated 19 April 2017 (CB 14/331, p. 4976 – penultimate paragraph). While it may have been an inconvenience to the IOOF Group to have had to pay money to beneficiaries for its own errors, that is no reason for a trustee to decline to make a claim for such compensation, or if it was to make such a decision, to do so only after adopting processes that complied with the requirements of its own Risk Management Strategy and Conflicts Policy.

626 According to APRA, adopting the same concept it has used elsewhere:

…a prudent director would have not approved the plan without undertaking further inquiries to ensure the plan was in beneficiaries’ best interests including, most importantly, determining whether all other avenues of compensation had been exhausted. The most prudent way to have done this would have been to seek advice from an independent (i.e. non-conflicted) lawyer.

627 APRA also said that Mr Kelaher did not comply with IOOF’s own conflicts management policy in making the decision as he did not identify the conflict and ensure that the minutes of the meeting addressed the conflict. This it was said was “not only a breach of an internal policy (which sounds in a failure to exercise care, skill and diligence) but a breach of his responsibilities under SPS 521, and therefore s 52(2)(d)(iv)” of the SIS Act.

628 APRA made the same submissions against Mr Venardos, albeit that he was not a director of IOOF Service Co, so APRA said the conflict arose from his dual position as a director of IOOF Hold Co and IIML (in each of its capacities).

###### 12.2 Discussion

629 Because APRA has failed to prove the foundation facts of liability or a reasonable argument for liability on the part of IOOF Service Co and IIML, its case against Mr Kelaher and Mr Venardos must fail. As prudent superannuation trustee directors Mr Kelaher and Mr Venardos were not required to “exhaust” consideration of obtaining compensation from these entities as an alternative to the ORFR. The evidence establishes, in any event, that had they done so the outcome would not have been any different.

630 As the first respondent pointed out there is no reason for Mr Kelaher (or Mr Venardos for that matter) to know any of the matters which APRA sought to attribute to them. None of the documents that came to the board identified any viable claim against IOOF Service Co, any liability on the part of IIML or any impediment to using the ORFR reserve. As the first respondent put it, the board “had expressly been told that APRA agreed that the ORFR reserve could be used provided that the company considered alternative sources of compensation”.

631 As the first respondent also pointed out, the memorandum of 13 May 2015 which Mr Vine and Mr Riordan prepared was not “perfunctory” given that the Pursuit error commenced in 2007, before the merger, and thus was unlikely to involve any liability of IOOF Service Co. To the contrary of the matters APRA said the directors knew or ought to have known, it may be taken that they knew this basic fact and, as the first respondent said, knew also that IIML and IOOF Service Co had reciprocal obligations under that deed, and that it was by no means clear contractually that IOOF Service Co had obligations to ensure that errors such as the Pursuit issue did not occur. As such, when they were told in the paper that any claim against IOOF Service Co was impeded by the “complex historical background” that was a statement which would have made good sense to Mr Kelaher and Mr Venardos.

632 I accept also the submission for the first respondent that the directors would have understood Mr Vine’s and Mr Riordan’s reference to a claim against IOOF Service Co not being “reasonably actionable” or “require[d]” to pay compensation. As the first respondent’s submissions said:

It is to be recalled that, from the time the Board was first made aware of the issue in October 2014, management was proposing that compensation would be paid and that non-superannuation investors would be paid by IIML. What that demonstrates is that IIML was willing to pay compensation itself if it thought it necessary and appropriate to do so, and that IIML would not regard a claim against IOOF Service Co as a necessary preliminary step to paying compensation if it thought it appropriate that compensation be paid by an IOOF company.

633 I accept the submissions for the first respondent, which apply equally to the second respondent, that the case against them is hopeless as nothing they were told suggested that a viable claim against IOOF Service Co or IIML existed and they had no reason to divine that some such claim might be conceivable. Further, the board’s resolution on 27 May 2015 did not preclude any subsequent steps for alternative sources of compensation if they later appeared viable.

634 I accept also the first respondent’s response to the allegations that Mr Kelaher (and Mr Venardos):

a) relied on the Pursuit compensation paper and did not ask management to attend the meeting to answer questions;

b) accepted management’s conclusion that making a claim against IOOF Service Co was not practical;

c) did not seek or cause management to seek independent legal advice as to whether there was a claim against IOOF Service Co or IIML; and

d) did not reject the plan or adjourn the meeting so that management could answer questions and legal advice could be obtains.

635 As to (a):

A director of a RSE is not required by ss 52 or 52A of the SIS Act to receive recommendations in person, nor required to ensure that management are available in person at Board meetings to answer questions. If the Board of IIML had questions regarding any matter proposed by management, they doubtless felt able to request further information. The absence of management from board meetings could not, of itself or in combination with any other matter, result in Mr Kelaher breaching his obligations under the SIS Act. In any event, APRA does not suggest that, had management attended, the decisions of the Boards would have been different. Indeed, it does not even suggest what information ought to have been sought from management that was not clearly addressed in the memoranda or known to Mr Kelaher.

636 As to (b), it is:

…premised on the proposition that the advice in the Pursuit compensation paper was self-evidently flawed but that is not the case. Moreover, even if the Court is of the view that the analysis in the compensation paper was incorrect, it is not obviously so and there is no reason to conclude that Mr Kelaher [or Mr Venardos] ought to have rejected it in the circumstances. It is to be recalled in this connection that this was a busy Board considering a relatively modest amount and the Board had been told and knew that members were being compensated. There is no reason why Mr Kelaher [or Mr Venardos] ought to have been moved by the compensation paper to demand further investigations.

637 As to (c), the proposition:

…ignores the substance of the advice in the compensation paper, being that there was no clear factual basis for the claims that APRA contends should have been made, and there were practical difficulties in bringing such claims in any event. Those are not obstacles that would be overcome by seeking independent legal advice - the identification of a theoretically available legal claim would not avoid the difficulties of proof, causation, risk and cost to which the compensation memoranda averted.

638 As to (d), the proposition adds nothing of substance.

639 It is also alleged that Mr Kelaher in approving the compensation plan did not identify the conflicts of interest pleaded by APRA (ASOC [129(a), (b), (c) and (d)]), did not require the minutes of the meeting to record the supposed conflicts (ASOC [129(e)]), approved the Pursuit Compensation Plan without identifying and minuting the conflicts (ASOC [129(f)]), and approved the compensation plan in circumstances where it was not in the best interests of beneficiaries and preferred other persons’ interests to their interests (ASOC [129(g), (h)].

640 As the first respondent submitted, in the circumstances, Mr Kelaher had no reason to suppose these conflicts existed and they did not in fact exist. The proposed conflicts are theoretical at best and APRA does not explain how or why they could be expected to have a significant impact on the giving of priority to the interests of beneficiaries.

641 I agree also that APRA has failed to explain how Mr Kelaher and Mr Venardos breached their director’s covenants under s 52A of the SIS Act, given the material the directors had as at 27 May 2015. Nor is there any evidence in support of APRA’s propositions of what a prudent superannuation trustee director would have done in the same circumstances (apart, that is, from the evidence of what their fellow directors did, which is to engage in precisely the same conduct as Mr Kelaher and Mr Venardos).

642 APRA also alleged that between 27 May 2015 and 25 October 2018 Mr Kelaher (and Mr Venardos) “did not take any or adequate steps to cause IIML to revoke or amend the Pursuit Compensation Plan” so that the compensation was “wholly recovered” from IOOF Service Co, IIML or related bodies corporate, or to ensure that the ORFR reserve was wholly compensated from such sources (ASOC, [129A]). It alleged that such failure was a breach of the s 52A covenants.

643 As the first respondent submitted, this allegation is not supported by the evidence. The first respondent’s summary of the facts relevant in this regard may be adopted and is set out below.

644 On 24 June 2015, Mr Vine wrote to APRA as follows:

We are currently considering an application to the Tax Commissioner for a ruling in relation to treatment of amounts paid to members via the ORFR. Applying a transfer from the ORFR may result in members breaching the concessional contribution cap, which would result in an unfair or unjust outcome. If we go ahead with this process, it would likely take about two months and the application may be unsuccessful.

Whilst the IIML and Questor boards approved our remediation and compensation proposals for these reported breaches, at this stage we do not intend to process the compensation pending a decision in relation to, and any outcome from, a tax ruling application. We will keep you informed.

645 The concern identified by Mr Vine was reasonable and prudent. Mr Vine’s 24 June email demonstrates that within a month of the 27 May 2015 board meeting the decision was made to delay the implementation of the compensation plan, pending the tax ruling. On 14 August 2015, the Board of IIML (including Mr Kelaher and Mr Venardos) was informed in a Legal, Compliance and Risk report that payment of compensation for the Pursuit error had been deferred until after the tax ruling was received. On 17 August 2015, Deloitte, on behalf of IPS Super, applied to the Commissioner of Taxation for the private ruling. The tax ruling took much longer than expected. The cause of the delay was the ATO, not IIML. The ATO did not produce a final response until early 2017. By letter dated 8 February 2017, the ATO issued a letter to the effect that the ORFR could be used to compensate members for operational risk events without such payments being treated as concessional contributions (an outcome which was in the best interests of the members).

646 On 21 March 2017, the board of IIML was informed in a Legal, Compliance and Risk Report as follows:

Management is continuing to engage with IOOF's PI insurer to finalise an insurance claim. In the meantime, the Rectification Committee and Finance are assessing the use of the ORFR to compensate accounts (which would then be reimbursed upon receipt of the insurance proceeds) circa $745,000. …

647 As the first respondent put it, by this time the board must have known that “IIML was not pursuing the compensation plan approved on 27 May 2015 simpliciter, but was also pursuing an insurance claim in relation to the Pursuit matter”. On 13 July 2017, IOOF’s insurer confirmed that it would accept the insurance claim in relation to the Pursuit matter. The amount paid by the insurer was $677,743.83, which was used to replenish the ORFR. Thus, the total amount used from the ORFR reserve and not replenished prior to 2018 was only $95,962.00, an immaterial sum.

648 These facts said the first respondent, with which I agree, meant that:

…the true position is that, contrary to the allegation in ASOC [129B], Mr Kelaher was aware from no later than June 2015 that the compensation plan approved by the Board on 27 May 2015 (or at least the form of that plan as alleged by APRA) was not being implemented as planned. In the period from June 2015 to February 2017, he knew the approach that IIML would take to compensation might change depending on the tax ruling. Then, from March 2017, he knew that insurance monies were being pursued to replenish the ORFR. In these circumstances, it simply does not accord with the facts to suggest Mr Kelaher was pursuing the 27 May 2015 compensation plan (as alleged) at all times between 27 May 2015 and 25 October 2018.

649 These propositions must apply equally to Mr Venardos.

650 The first respondent said, and I agree, that:

Finally, in relation to the Pursuit claim, the allegation that IIML “took steps to implement” the 27 May 2015 compensation plan (in the form alleged by APRA) is obviously not correct. The approach ultimately taken in relation to the Pursuit matter was that IIML funded the compensation almost entirely from insurance monies. That is an entirely different approach in substance to that allegedly approved by the Board on 27 May 2015.

651 The submissions for the second respondent also apply to the first respondent.

652 The second respondent said that the essential complaint against him is grounded in the alleged failure to consider “the possibility of making a claim against the IOOF Group companies involved, or making good the loss from the trustee’s funds”. As submitted for the second respondent, however:

…that is exactly what Mr Venardos and the whole board did, in fact, consider. The board paper explained that the loss in question arose from an operational risk event. The board was told that the ORFR reserve was available for use by IIML. The board paper set out management’s consideration of other available sources of funding including the reasons why management did not recommend pursuing legal action against IOOF Service Co. There was nothing “perfunctory” about that consideration. The minutes of the board meeting record that the board “noted the paper” and “the proposed remediation strategy and source of compensation”.

There was nothing before the board to suggest that it was not entitled to rely on the information and advice provided by management. The board paper was detailed. Both Mr Riordan and Mr Vine were qualified lawyers. They provided advice on the application of the ORFR reserves policy and whether legal action should be pursued against IOOF Service Co. APRA does not allege that the advice was wrong. APRA does not allege that independent legal advice would have rendered a different result. Indeed, in circumstances where APRA alleges that it was only “reasonably arguable” that IOOF Service Co was liable, it is difficult to see how the board’s reliance on advice from its in-house lawyers could give rise to a breach of the covenants, or why the board ought to have sought independent legal advice or called management in to explain. As was the case with the trustee in *Commonwealth Bank Officers Superannuation Corporation Pty Ltd v Beck* (2016) 334 ALR 692…, a director’s reliance on advice from its in-house lawyer amounts to proper consideration being given to the members’ best interests.

653 Further APRA has not proved that Mr Venardos knew that “personnel involved in the processing of reinvestment instructions and the risk detection systems used in administering the Pursuit platform were IOOF Service Co staff and services”. But even if this had been proved, as submitted for him, it does not follow that Mr Venardos knew or ought to have known that “IOOF Service Co had IOOF Service Co’s Pursuit Exposure as pleaded at paragraphs [101] to [104]” or that “there was no practical difficulty in making a claim against IOOF Service Co”. Nor is there any reason to suppose that Mr Venardos knew or ought to have known that by at least October 2014 that IIML had contravened its 52(2)(b) covenant of due care and diligence and was exposed to liability to compensate for the losses. The documents do not prove this fact by way of the alleged admissions. Further, the “Group Legal, Risk and Compliance Report of October 2014 informed the board of four key facts: there had been a software error; the error had now been fixed; the regulators had been notified; and management was taking steps to determine the appropriate compensation methodology. That is as far as the evidence goes”.

654 I also accept the following propositions of the second respondent:

(1) the fact that Mr Venardos admitted in his defence that Mr Riordan and Mr Vine were officers of IOOF Service Co does not constitute an admission that he knew or ought to have known, at the relevant time, that Mr Riordan and Mr Vine had a conflict (which, in my view, they did not);

(2) APRA’s case is that the conflict arises from the “exposure” of IOOF Service Co for the losses caused by the original failure. For the reasons already submitted, APRA has not established that IOOF Service Co was so exposed, nor has it established that Mr Venardos knew or ought to have known of that exposure;

(3) APRA’s positive assertion that Mr Venardos’ “fellow directors” all had a conflict highlights the fundamental problem with APRA’s case against Mr Venardos. The allegation is not pleaded. No other director, other than Mr Kelaher, has been given an opportunity to be heard on such an allegation. If all of the directors were in a position of conflict, it cannot seriously be suggested that Mr Venardos and Mr Kelaher were the only ones who were required to exercise “special vigilance”. In considering and approving the plan, Mr Venardos exercised his powers and performed his duties in his capacity as a member of the board, which acted in concert to approve the plan; and

(4) APRA’s claim of contravention based on Mr Venardos’ failure to take any or any adequate steps to revoke or amend the compensation plan should not be accepted. The claim cannot succeed where there was no underlying breach in approving and considering management’s plan. There can be no continuation of a breach, or a new breach, if there is no breach in the first place. In any event, APRA has never articulated any legal basis on which such a contravention would or could be founded, in circumstances where it neither submits nor particularises what such adequate steps could be taken by one director who holds one vote. APRA might try to characterise the replenishment of the ORFR reserve in September 2018 as one to which “Venardos ultimately agreed”, as though he was the only one, but that too was a decision of the IIML board (comprising Mr Walsh as Chairman, Ms Flynn, Mr Selak and Mr Venardos).

##### 13. FINDINGS SOUGHT AGAINST MR VINE AND MR RIORDAN

655 APRA said that it did not allege that Mr Vine or Mr Riordan breached any obligation of the SIS Act directly, as the covenants in s 52 and s 52A do not apply personally to them but sought certain findings of facts against them.

656 It follows from the conclusions above that APRA’s proposed findings cannot be made against Mr Vine or Mr Riordan. For example, they did not know and nor ought they to have known that “the facts giving rise to Pursuit failure including IIML’s role in the processing or reinvestment instructions and design of the system that was meant to do such a thing, and that the error was due, at least in part, to failures in IIML’s human and systems processes”. They knew that the source of the error could not be ascertained and the history was complex and thus could not have known the alleged matter. For the same reason they did not know and nor ought they to have known of “IOOF Service Co’s exposure by reason of it providing the administration and IT services that IIML relied upon for the purposes of administering and operating the Pursuit platform from 1 July 2009”. Given these circumstances they did not know and nor ought they to have known of any conflict of interest on their part.

657 Otherwise, the submissions of the fourth to seventh respondents may be adopted. Those submissions included that:

…there is no evidence that Mr Vine or Mr Riordan had a detailed understanding of the factual events that gave rise to the Pursuit Failure (including precisely what “human systems processes” had failed), the precise cause of the failure or whether the inability to detect it after July 2009 was attributable act or omissions of persons acting on behalf of Service Co or IIML. To the contrary, the evidence indicates that IIML (and Mr Vine and Mr Riordan) did not know any of those matters…

658 Further:

For the reasons set out in the respondents’ closing submissions, APRA’s allegations in respect of IOOF Service Co’s alleged liability are hopelessly flawed and suffer from a number of obvious deficiencies: CS at [282]ff. Given that Mr Vine and Mr Riordan recommended that no action should be taken against IOOF Service Co, and the reasons they gave for that recommendation (CS at [22]), it may be inferred that they were cognisant of these deficiencies without it being necessary or expedient for them to set them out in detail in the paper to the board (CS at [309]). There is, in any event, direct evidence that Mr Vine and Mr Riordan told APRA in March 2015 that they considered it was unclear whether IOOF Service Co was at fault or negligent and that Mr Vine, having made further enquiries as to that matter, was told the following day of the significant obstacles to any viable claim against IOOF Service Co: CS at [214(b)(iii)]; [217].

659 As to the proposition that Mr Vine and Mr Riordan knew or ought to have known of their own conflicts of duty and interest, I agree that the “proposed finding fails at the outset because it is premised on Mr Vine and Mr Riordan knowing of the supposed liability on the part of IIML and IOOF Service Co for the Pursuit Failure. It has already been pointed out that such a liability did not exist (CS at [270]ff, [282]ff). Nor is there any evidence that Mr Vine or Mr Riordan thought it existed. The evidence is in fact to the contrary”. Further:

…the SIS Act is only concerned with conflicts that have actually arisen in that some other interest or duty has a significant impact on the capacity of the responsible person to act in a manner consistent with the best interests of beneficiaries. APRA has not identified the interest or duty of Mr Riordan and Mr Vine that would have a significant impact on their ability to discharge their paramount duty to beneficiaries, keeping in mind also that that paramount duty expressly overrides their duties as directors of IOOF Service Co.

660 I see no purpose in addressing the other findings sought by APRA because all are founded on premise of arguable liability of IIML and IOOF Service Co which has not been proved.

661 APRA’s case against the respondents in relation to the Pursuit incident must be rejected for these reasons.

##### 14. THE SWEEP FAILURE

###### 14.1 APRA’s case – the Sweep failure

662 APRA recorded that in “around September 2011, the IOOF Group determined to close a series of funds known as the ‘United Funds’ and offered investors in those funds the option of transferring their investment to another IOOF fund known as the ‘Multimix Trust’ (of which IIML was the RE). Where beneficiaries of TPS Super or investors in the TPS MIS of which Questor was the RE selected this option, Questor undertook to transfer across the beneficiaries’ existing investment instructions including their automatic ‘sweep’ instructions: ASOC, [137]-[138]; admitted by each respondent Defences, [137]-[138]. Questor relied upon IOOF Service Co to effect this transfer of investment instructions, but IOOF Service Co failed to carry the instructions across: ASOC, [139]-[140]; substantially admitted IIML and Questor Defence, [139]-[140].” “A ‘sweep’ instruction in effect was an instruction that, if more than a minimum amount was sitting in a member's ‘Cash Management Account’ at the end of the month, it would be ‘swept’ into the member’s nominated investment profile: CB 5/47, p.1243”.

663 IOOF Service Co was Questor’s service provider at the relevant time.

664 The failure by Questor and IOOF Service Co to reinstate members’ sweep instructions upon the transfer to the Multimix Trust was not detected until December 2014. Investors and beneficiaries suffered losses totalling approximately $1,027,129.98: ASOC, [141]; substantially admitted IIML and Questor Defence, [141].

665 According to APRA, both Questor and its service provider, IOOF Service Co, were exposed to liability to pay compensation to beneficiaries, and/or to compensate the fund for the loss suffered by reason of the Sweep failure.

666 As to Questor’s exposure, APRA relied upon the following propositions.

667 Clients’ “sweep” instructions were fundamental to the Questor offering for TPS members. The PDS for “The Portfolio Service – Investment Essentials (Plan)” is at CB 6/47 and provides an indication of the importance of sweep instructions to Questor’s services to TPS Super beneficiaries and TPS MIS members.

668 On 21 January 2015, an “Issue Notification Form” was sent to IOOF’s Compliance Team about the Sweep failure: CB 6/82, p. 1685. According to APRA, this contains an admission that Questor assumed an obligation or duty to transfer across and reinstate any automatic investment plan (“sweep”) instructions previously made by clients, stating:

Where TPS clients chose to transfer, Questor Financial Services Limited (QFSL) undertook to reinstate any automatic investment plan (“sweep”) instructions previously made by clients.

669 A Compliance team member investigated the failure, and on 4 February 2015 completed an “Issue Assessment Form”: CB 6/80, p. 1662.

670 On 6 February 2015, Mr Riordan (on behalf of Questor) sent a breach notice to APRA about the Sweep Failure: CB 6/87, p. 1707, 1711. That form attached the Issue Notification Form and the Issue Assessment Form (p. 1711). It notified APRA that Questor considered the Sweep failure to be a significant breach of s 52(2)(b) of the SIS Act by Questor because:

(a) Questor had given clients with investments in the United Sector Leader Fund “a number of options – one being the option to be transferred into certain comparable IOOF MultiMix funds, plus have any regular investment sweeps in the United funds reinstated for the new MiltiMix investments”;

(b) subsequent to the transfer, the reinstatement of the previous sweeps “was not done”;

(c) the “automatic system report to detect failed sweep transactions” did not detect the issue because the sweeps for the United funds “had already been deleted” within the platform administration system;

(d) the identified “project task” to reinstate the sweeps “was not monitored to completion during, or after, the project”;

(e) the failure to sweep existed between September 2011 and December 2014;

(f) Questor’s failure “to accurately implement clients’ sweep requests, and also the inability to detect the error through internal review” (over a period of three years) fell “below the standard stipulated in s 52(2)(b)”;

(g) Questor “should have been vigilant in ensuring that their [sic] business systems accurately processed and reflected instructions of members”;

(h) the project associated with the wind-up of the United Funds “was not implemented sufficiently carefully and did not identify the failure to reinstate the sweeps” within the platform administration system;

(i) “[g]iven that the closure of the United Sector Funds was an internal project, affecting a large number of clients, [Questor] should have approached the task in a more systematic fashion, imposing a greater number of checks throughout the process to ensure that clients’ instructions (either to reinstate the sweeps or retain cash) were carried out efficiently”.

671 APRA said that the Issue Notification Form recognised that there was an obvious case of trustee negligence such that “[t]here is a financial impact for the business” (being Questor), and that loss was “[l]ikely, as the IOOF MultiMix funds have generally gone up in value since August 2011”: CB 6/82, p. 1685. The Issue Assessment Form similarly identified the breach which would require Questor (or its related entities) “to rectify the financial impact on TPS clients, where QFSL may be liable” and identified that this was a failure for which notification was required to Questor’s professional indemnity insurer (CB 6/80, p. 1665, 1667).

672 Despite this, APRA said that each of the respondents now denied that Questor breached s 52(2)(b) of the SIS Act with respect to the Sweep failure: ASOC, [147]; Defences [147].

673 As with the Pursuit failure, APRA said that it takes the view that the original internal assessment on behalf of the licensee, and the notification by Mr Riordan of the breach to APRA, was correct. According to APRA:

(1) Instructions from beneficiaries as to reinvestment or sweep instructions are fundamental to the nature of the service offering Questor was providing and the preservation and investment of the retirement savings of members.

(2) A failure by a superannuation trustee to ensure that it was actioning instructions from beneficiaries on such basic instructions as to how their financial savings were to be invested, or to detect an error of this kind within a reasonable period of it occurring, or to appropriately monitor a related-party service provider to ensure that adequate and sufficient processes were in place for the actioning and monitoring of reinvestment instructions, is a breach of the standard required by s 52(2)(b).

(3) Further, a failure to put in place appropriate checks and controls to ensure beneficiaries are not harmed when undertaking a major project is a further breach of s 52(2)(b).

(4) Questor’s own compliance team identified at the time what a reasonable trustee would have done, and that had it been done, it would have achieved the result for which APRA contends.

674 As to IOOF Service Co’s exposure, APRA relied on the following propositions.

675 Questor’s defence admits that Questor relied upon services by employees of IOOF Service Co to effect the closure of the United Funds and the transfer of investments to the MultiMix Trust, ensure that investment instructions by beneficiaries of TPS Super (including Sweep instructions) were being actioned; and assist Questor to comply with its obligations as trustee: Defence [139].

676 APRA submitted that on the basis of those admissions, the terms of the relevant service engagements, what is recorded in the breach notice and accompanying documents provided to APRA, there can be no doubt that IOOF Service Co had the exposure pleaded at ASOC [142]. It was thus reasonably arguable that IOOF Service Co was liable to compensate or indemnify Questor as trustee of TPS Super for the loss and damage caused by the Sweep Failure for the reasons there set out, and supported by the evidence as to the role IOOF Service Co in fact played in Questor’s business.

677 It was not necessary to adduce evidence from an IT expert because the evidence from Questor itself as to the deficiencies in the systems and processes adopted, and the human errors made, is sufficient to establish that they fell short of, or it was reasonably arguable that they fell short of, the standard of service which IOOF Service Co was required to meet. Alternatively, they engaged, or it was reasonably arguable that they engaged, the Service Co Indemnity: ASOC [142(d)].

###### 14.2 Discussion – the Sweep failure

14.2.1 Further facts

678 Some further facts which the respondents identified are relevant.

679 IOOF Group had in place a Project Management Policy which applied to all projects. The Project Management Policy required, amongst other things, that:

(a) a “Project and Change Management Plan” should be prepared for all “Significant Projects” (being projects nominated as significant by IOOF’s leadership group) setting out a “budget, risk matrix and other important tools necessary to manage the project”;

(b) relevant risks and issues be identified at the start of a project and managed on an ongoing basis throughout the project using appropriate tools;

(c) all projects be managed using “JIRA”, a project management software commonly used for “but tracking, issue tracking and project management”;

(d) all major tasks associated with the project and all action items, status updates and decisions be recorded in JIRA; and

(e) a post implementation review be conducted for all major projects.

680 On 15 May 2015, Questor sent a letter to APRA providing an update on the Sweep failure. In relation to the cause of the Sweep failure, Questor informed APRA that:

Despite significant investigation, the cause of this error has not been fully established. The sweep on the United Funds was cancelled and customers were advised that [Questor] would reinstate the sweep on the MultiMix Funds, however this was not actioned. The need to reinstate the sweep was not added to any project task list for reasons which are not identifiable.

681 On 15 May 2015, a paper was prepared for the Questor board which set out a summary of the Sweep matter and a proposed remediation strategy for the board’s approval. The proposal involved paying restitution to affected clients so as to put them in the financial position they would have been in had the Sweep failure not occurred. This amounted to a total compensation of $1,027,129.98 payable to TPS Members and $4,061.12 payable to IDPS Investors. The paper recommended that Questor pay the compensation to IDPS investors from its own funds and that Questor use the ORFR to fund the compensation payable to TPS beneficiaries. The former recommendation was made on the basis that “the nature of an IDPS is contractual and there are no reserves maintained in a wrap style product”. The recommendation to use the ORFR to fund the compensation payable to TPS Members was made on the basis that:

The Questor ORFR Policy permits the Trustee to use the ORFR to compensate members for any loss arising from operational risk. ‘Operational risk’ is the risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events. We have not yet heard back from APRA in relation to our approach, however would expect APRA to adopt a similar position to that seen with the Pursuit breach reported to the IIML May Board meeting.

682 In respect of IOOF Service Co, the paper said:

Under the ORFR policy, Questor is required to consider other sources for funding the compensation payable. APRA (as in relation to the Pursuit breach) are likely to suggest that Questor consider legal action against the IOOF Service Company, which is the fund administrator and Questor’s related body corporate.

Management does not recommend pursuing such legal action for the following reasons:

* Despite significant investigation, the cause of this error has not been fully established. The sweep on the United Funds was cancelled and customers were advised that we would reinstate the sweep on the MultiMix Funds, however this was not actioned. The need to reinstate the sweep was not added to any project task list for reasons which are not identifiable. These factual issues make it difficult to attribute a breach of contract or negligence to the administrator.
* As previously noted to APRA, the commercial reality of running a large group of companies means that issues may not necessarily be realistically actionable or indeed require action in order for compensation to be made.
* Legal action between the related bodies corporate would likely be contested, which would (a) require appropriate internal Chinese Walls; (b) consume significant management and employee time; (c) require internal and external legal and other advice; (d) incur potentially significant external legal fees; (e) depending on the length of the dispute, become unnecessarily burdensome.

Therefore, it is considered to be in the best interests of members to fund compensation via the ORFR, as set out in the ORFR Policy.

683 On 27 May 2015, the Questor board approved the remediation strategy proposed in the May Sweep board paper, including the recommendations referred to above.

684 The payment of compensation in respect of the Sweep failure was subsequently put on hold whilst IOOF awaited confirmation from the ATO as to the tax treatment of payments to members from the ORFR. That confirmation was not received until 8 February 2017.

685 On 17 June 2016, TPS Super was transitioned into IPS Super via a successor fund transfer. IIML subsequently took over responsibility for the remediation of the Sweep failure.

686 Having regard to APRA’s “observations and directives about where compensation should be sourced from”, IIML ultimately decided not to use the ORFR to fund any of the compensation for the Sweep failure. Instead, on or about 13 June 2017, IIML paid the compensation to all affected members out of its own funds.

14.2.2 Respondents’ answers to APRA’s case

687 Questor’s breach is said to arise from its alleged failure to exercise the care, skill and diligence required in monitoring and assessing whether IOOF Service Co was complying with beneficiaries’ instructions and alleged failure to exercise the care, skill and diligence required in assessing and testing the compliance attestations received from IOOF Service Co. In its submissions, however, APRA relied upon the mere fact of the Sweep failure as evidence establishing Questor’s failure to exercise the required degree of care, skill and diligence. The fourth to seventh respondents said this was inconsistent with the evidence which shows that Questor had in place a detailed project management policy with protocols intended to minimise the risk of errors such as the Sweep failure occurring.

688 APRA’s reliance on internal documents said to constitute admissions, the respondents submitted, was misplaced for the reasons already noted, namely:

(1) the statements are inadmissible to prove the legal conclusions as to breach of s 52(2)(b) of the SIS Act; and

(2) the opinions expressed by compliance officers, “in the conservative context of discharging reporting obligations, were, in any event, tentative and qualified and understandably were not the product of detailed legal analysis directed to the precise legal standard contained in s 52(2)(b) of the SIS Act”.

689 It followed, according to the fourth to seventh respondents, that APRA’s case again foundered for lack of evidence.

690 The first respondent submitted that “there is no clear evidence as to the cause of the issue and whether it arose as a consequence of Questor’s systems or those of IOOF Service Co” and, as to IOOF Service Co, APRA does not grapple with the reciprocal obligations in the services deeds. It was thus the case that:

…no claim could be said to be “reasonably arguable” against IOOF Service Co without a very close and detailed analysis of the causes of the Sweep issue. APRA has eschewed such an analysis...

691 The second respondent submitted that:

(1) “In the absence of evidence about IOOF Service Co’s IT systems or the adequacy of its controls and checks, there is no foundation for APRA’s allegation that IOOF Service Co breached its contractual obligations to Questor. The allegation that a breach was ‘reasonably arguable’ is also without substance for the same reason.”

(2) “Nor has APRA proved that Questor breached the s 52(2)(b) covenant as pleaded in ASOC [146]-[147]. The failure to make the sweeps does not, without more, establish a breach of the covenant. There is no evidence of the standard of care a superannuation trustee would have exercised.”

(3) “APRA’s reliance at ACS [463] on ‘Questor’s own compliance team’ as a proxy for ‘the reasonable trustee’ is no answer. The same objections to APRA’s reliance on the Sweep breach notice, the Issue Assessment Form and the Issue Notification Form as proof of negligence or as an admission that Questor breached the covenant apply equally here.”

(4) “In the absence of any recourse being available against IOOF Service Co and Questor (or any other company in the IOOF group), there was no conflict.”

692 I accept these submissions. APRA’s reliance on the internal documents of IOOF as the sole source of proof of its case is misconceived. Even if the statements in the documents are capable of constituting admissions, they cannot be admissions of law or legal conclusions. As admissions of fact, moreover they are statements made at a high level of generality in a particular context of self-reporting. They do not identify the cause of the error with any precision and, indeed, it appears that the cause was never able to be discovered. As such, they are of limited assistance as evidence directed towards the evaluation of the existence or otherwise of breach of the covenants on the part of Questor. The facts that if different steps had been taken the error would not have occurred or might have been detected earlier do not, of themselves, prove that Questor or IOOF Service Co failed to measure up to the requisite standards of care over time.

##### 15. THE SWEEP COMPENSATION PLAN

###### 15.1 APRA’s case

693 APRA pointed out that on 25 February 2015 the Sweep failure was reported to the board of IOOF Hold Co of which both Mr Kelaher and Mr Venardos were directors: CB 6/95.

694 APRA said that from no later than 27 February 2015, Mr Vine and Mr Riordan had detailed information about the Sweep failure, and it was Mr Vine’s view, as recorded in speaking notes prepared by him for Mr Riordan for a meeting with APRA on 2 March 2015, that (CB 6/100, 100A at p. 1755\_0002 - \_0003):

…better monitoring of project task execution, during and also after project implementation, would have revealed the failure to reinstate the Sweep instruction in a timely manner.

695 The problem with this for APRA is that when any error occurs it is nearly always possible, with hindsight, to identify that something could have been done to avoid the error. This does not mean that what was done was unreasonable or involved a reasonably foreseeable risk of the error occurring, or that the thing that could have been done to prevent the error was itself reasonable in all of the circumstances. APRA’s case (again) does not confront any of these complexities in seeking to establish its basal propositions of reasonably arguable claims of liability on the part of IOOF entities.

696 APRA noted that on 25 March 2015, at a meeting of the Questor board at which Mr Kelaher and Mr Venardos were present, the board discussed the breach, and described it in its minutes as “TPS failure to reinstate investment sweeps” and requested that it be added to business arising for the board to continue to monitor: CB 6/117, p. 1870

697 On 15 May 2015 Mr Vine notified APRA of the proposed rectification plan for the Sweep failure losses, saying:

We will be making a recommendation to the trustee in relation to the use of funds from the Operational Risk Financial Requirement (ORFR) in relation to superannuation accounts ($1,027,129.98) and Questor compensating the IDPS accounts ($4,061.12).

698 As APRA put it:

The circumstances concerning the development, approval and implementation of the Sweep Compensation Plan are relevantly the same as for the Pursuit Compensation Plan. Rather than seeking compensation from IOOF Service Co or itself for the failures to exercise due diligence in the closure of the United Funds and processing of beneficiaries’ instructions, Questor again defaulted to a compensation plan that involved the use of the beneficiaries’ ORFR…

699 The Sweep compensation plan, said APRA, was endorsed by Mr Vine and Mr Riordan on   
15 May 2015, and approved by the board (including Mr Kelaher and Mr Venardos) on 27 May 2015: CB 8/139, pp. 2198, 2200, 2243-2252; CB 8/142, p. 2270, 2272.

700 As APRA put it, the paper presented to the board was largely a carbon copy of the paper for the Pursuit Compensation Plan which was presented to the IIML board: CB 8/139, p. 2243-2248. It similarly recommended that non-superannuation beneficiaries be compensated by Questor itself (indicating that Questor did not intend to defend any such claim), but recommended that no claim be made against Questor or IOOF Service Co in relation to the beneficiaries’ loss for largely the same reasons as for the Pursuit Failure. It did not advert to the liability of Questor to compensate TPS Super for the Sweep failure losses, or as to the availability of professional indemnity insurance that might respond to a claim.

701 According to APRA:

The only additional reason given for this approach was that “the cause of this error has not been fully established”, a line that is echoed in IIML and Questor’s defence in this proceeding: Defences, para [141A(b)]. APRA disputes this assertion. It was first stated in the materials in Questor’s letter to APRA sent 15 May 2015 which was drafted after the IOOF Group had experienced significant push-back from APRA over its proposals to use the ORFR rather than pursue IOOF Service Co or itself fund the compensation. There is no support in the surrounding materials for any conclusion that Questor did not know that either it, or IOOF Service Co, or both, were responsible or arguably responsible for the error and liable to compensate the losses.

Indeed, the overwhelming inference on the materials that are in evidence is that Questor at all material times knew it was liable and that there was at least an arguable claim against IOOF Service Co for compensation. In circumstances where IIML and Questor admit that Questor and IOOF Service Co were responsible for ensuring that beneficiaries’ investment instructions were transferred following the closure of the United Funds, and those instructions were not followed, the cause of the error can only be that Questor and/or IOOF Service Co failed to exercise due care in carrying out their assigned tasks. Additionally, the failure to detect that the transfer had not occurred for three years after the event constitutes a further failure to exercise due care and was a further cause of the beneficiaries’ loss. This was the conclusion that Questor reached when it notified the breach to APRA in February 2015 and that conclusion was correct.

702 This submission again exposes APRA’s impermissible reasoning that as IOOF Service Co and Questor were responsible for ensuring that beneficiaries’ investment instructions were transferred following the closure of the United Funds, and those instructions were not followed, “the cause of the error can only be that Questor and/or IOOF Service Co failed to exercise due care in carrying out their assigned tasks”. In other words, every error is said to fall below the required standard of care, converting the trustee into an insurer against all loss. The facts of error and loss, however, are not sufficient to establish the conclusion of breach of the due care, skill and diligence covenant. The facts do not speak for themselves as APRA appears to assume.

703 APRA said the fact that the ORFR was never in fact used to compensate for the Sweep failure losses is immaterial. As APRA put it, it was only after the “ATO came back indicating that it required the ORFR to be replenished by a claim against a third party that other sources of compensation were considered” and in around June 2017 that IIML paid the compensation from its own account.

704 According to APRA:

APRA’s case is that the approval of the Sweep Compensation Plan by Questor, Kelaher and Venardos, and the failure to reverse that plan until June 2017, constituted a breach by each of them of their obligations under ss 52 and 52A of the SIS Act. The plan was not in the best interests of the beneficiaries and Questor, Kelaher and Venardos did not adequately identify and manage the conflicts of interest and conflicts of duties before approving its implementation. Vine and Riordan’s involvement in the plan and its implementation is also relied upon to establish their association with the contravening conduct.

705 According to APRA, the conduct of Questor and (from June 2016) IIML in approving and taking steps to implement the Sweep compensation plan was materially the same as its conduct in approving the Pursuit Compensation Plan. APRA thus relied on its submissions in respect of the Pursuit Compensation Plan to support its position in respect of Questor’s and IIML’s alleged Sweep compensation contraventions.

706 As against Mr Kelaher and Mr Venardos, APRA said that their reliance on the fact no money was paid out of the ORFR was misplaced because at all times until IIML decided to pay the compensation itself, Mr Kelaher and Mr Venardos knew that Questor (and then IIML) was taking steps to use the ORFR. However, it is not apparent to me that any step can be taken to use the ORFR other than the step of in fact taking money from the ORFR. As such, APRA is basing its case on an unimplemented decision. As a matter of principle, I am unable to see how an unimplemented decision can involve any contravention of the statutory covenants. As the respondents submitted, the SIS Act does not seek to prevent “thought-crimes”.

707 APRA also submitted that the same findings as made with respect to the Pursuit Compensation Plan ought to be made against Mr Vine and Mr Riordan with respect to the Sweep compensation plan.

###### 15.2 The respondents’ case

708 The fourth to seventh respondents noted that APRA sought a declaration that Questor’s approval and implementation of the “Sweep Compensation Plan” on and from 27 May 2015 contravened s 55(1) of the SIS Act by failing to comply with the best interests covenant and no conflicts covenant under s 52(2)(c) and (d) of the SIS Act (defined by APRA as “**Questor’s Sweep Compensation Breach**”). Further, APRA sought a corresponding declaration against IIML on and from 17 June 2016 (being the date of the successor fund transfer or SFT of TPS Super to IPS Super) which is premised on its alleged “failure to reconsider the Sweep Compensation Plan”, its alleged failure to seek compensation from IOOF Service Co, and its “continued implementation” of the plan after 17 June 2016.

709 As the fourth to seventh respondents put it, the “first core proposition upon which APRA’s case depends is the contention that IOOF Service Co was liable under the Services Agreements to compensate or indemnify Questor for the loss and damage caused by the Sweep Failure”. However, they said:

APRA’s case suffers from many of the same deficiencies as outlined previously in respect of the allegation that IOOF Service Co was liable for the Pursuit Failure.

710 In particular, they said:

APRA has not proved the factual matters it pleads at paragraph [142(a)] of the ASOC. It is uncontroversial that the Sweep Failure occurred; that is, that the Sweep instructions of clients were not transferred to the Multimix product after the closure of the United Funds as they ought to have been and that this resulted in some of those clients’ funds not being invested in accordance with their instructions. However, that fact of itself does not establish the matters alleged at paragraph [142(a)]. As has been noted, the burden was on APRA to establish the particular respects in which IOOF Service Co failed to meet the standard of care required of it and how these failures caused the Sweep Failure to occur. It has failed to discharge that burden.

711 Paragraph 142(a) of the ASOC alleges that the “Sweep Failure” continued, and was not detected, from 30 September 2011 to January 2015 because IOOF Service Co:

(i) did not configure its IT systems to process correctly the transfer instructions relating to the investments made by Questor on behalf of the 849 TPS Super beneficiaries and by the non-superannuation investors;

(ii) did not impose adequate controls and checks throughout the process of transferring investments from the United Funds to the MultiMix Trusts which were designed and adapted to action correctly and detect errors or failures relating to those instructions;

(iii) did not use a system, or configure it system, so as to make it capable of processing accurately instructions related to the investments made by Questor on behalf of the 849 TPS Super beneficiaries and by the non-superannuation investors;

(iv) did not have adequate controls and checks in place to detect and investigate in a timely way that:

(A) distributions were being held in cash above the minimum cash management account balance in circumstances where they should have been re-invested;

(B) beneficiaries of TPS Super and non-superannuation investors’ express instructions as to management of their investments or investments on trust for them were not being complied with;

Particulars

A. In supplying the Services to Questor in its capacity as trustee of TPS Super (including transferring beneficiaries’ investments from the United Funds to the Multimix Trust), IOOF Service Co relied on computer software and employees and subcontractors to audit, monitor and assess its own and Questor’s performance in processing and actioning beneficiaries’ instructions.

B. The software and human processes the subject of (A) did not constitute adequate controls and checks in that they were, individually and together, incapable of detecting, preventing, mitigating or managing:

1. a widescale failure in IOOF Service Co’s management of the project to close the United Funds and transfer beneficiaries’ investments from the United Funds to the Multimix Trust, in that that transfer did not include the transfer of existing Sweep instructions,

2. the failure to reinstate those instructions over a period of three years;

3. the incorrect accumulation of cash holdings in beneficiaries’ accounts.

712 The respondents are correct to submit that none of these matters have been proved. The high level conclusions in the IOOF documents, consistent with the reasoning already adopted, are not reliable evidence of the facts asserted therein. The documents were prepared for different purposes and are expressed at a high level of generality on the basis of hindsight without providing any details of the IT and other systems, controls and checks which were in place. As a result, it is not possible to reach a rational inference based on those documents that the facts alleged in para 142(a) of the ASOC are more likely to be true than not.

713 The respondents submitted also:

Similarly, the allegation that IOOF Service Co breached the Service Co Resources Obligation fails at the first hurdle because APRA has not identified what was the relevant “Resource” which IOOF Service Co owned or supplied to IIML that relevantly contained a “defect, error or impairment”. The closest APRA comes is the allegation in paragraph [142(a)] that IOOF Service Co “did not configure its IT systems to process correctly” clients’ sweep transfer instructions. No evidence has been adduced as to what was the relevant IT system which was not configured correctly and as to the ownership of that system. APRA has therefore failed to discharge its evidentiary burden in relation to the alleged breach of the Service Co Resources Obligation.

714 Further, they said:

APRA also has failed to address any of the obvious difficulties arising under the Services Engagements in relation to the attribution of liability to IOOF Service Co. These difficulties have been pointed out previously in the context of the Pursuit matter and it is unnecessary to repeat them. It is sufficient to note that substantially the same issues would have arisen with respect to any attempt by Questor to hold IOOF Service Co liable for the Sweep Failure.

715 They pointed out also that:

A further difficulty arises from the fact that APRA alleges that the Sweep Failure occurred as a result of an omission on the part of the “IOOF Group” project team responsible for the closure of the United Fund. It will be recalled that the United Fund was a MIS for which a separate IOOF entity, AET was the RE. Similarly, the Multimix Trust to which TPS members’ benefits were to be transferred following the closure of the United Fund was a MIS of which IIML was the RE. Each of IIML, AET and Questor were relevantly “Recipients” under the Services Engagements.

The relevant point is that, even if it may be accepted that the project team responsible for closing the United Fund comprised employees of IOOF Service Co, and that the work they performed in connection with that project was pursuant to the Service Engagements, there remained considerable doubt as to which capacity those employees were acting and to which entity they were providing the services. At least the following possibilities appear to be open on the evidence:

(a) the employees were acting on behalf of IOOF Service Co rendering the “Administration Services” to AET;

(b) the employees were acting on behalf of IOOF Service Co rendering the “Administration Services” to IIML;

(c) the employees were acting on behalf of IOOF Service Co rendering the “Administration Services” to Questor;

(d) the employees were rendering the “Personnel Services” (which, as has been noted, were not truly services but akin to a labour hire arrangement) to AET and were acting on AET, rather than IOOF Service Co’s, behalf;

(e) the employees were rendering the “Personnel Services” to IIML and were acting on IIML, rather than IOOF Service Co’s, behalf; or

(f) the employees were rendering the “Personnel Services” to Questor and were acting on Questor’s, rather than IOOF Service Co’s, behalf.

The capacity in which the relevant employees of IOOF Service Co were acting is highly significant to APRA’s ultimate contention that Questor failed to act in the best interests of TPS Members by not pursuing compensation from IOOF Service Co. That is because it is only on the basis of (c) or (f) referred to above that an act or omission on the part of the employees involved in managing the closure of the United Fund could conceivably have given rise to a right of action by Questor against IOOF Service Co in respect of the Sweep Failure.

716 As with the Pursuit failure, the fourth to seventh respondents submitted that:

Having failed to identify or address any of the above flaws in its claim, APRA essentially contends at paragraphs [465] to [466] of ACS that the fact of the Sweep Failure, coupled with the admission made by Questor at paragraph 139 of its Defence (to the effect that it relied upon services provided by employees of IOOF Service Co pursuant to the Services Engagements), is sufficient to established the alleged liability on the part of IOOF Service Co for the Sweep Failure.

It will be apparent from the matters already referred to that such a contention cannot be sustained. The mere fact that the Sweep Failure may have arisen as a result of acts or omissions on the part of employees of IOOF Service Co does nothing to overcome the inherent problems of attribution and delineation of liability which arise under the Services Engagements. One could only have overcome those problems by building a case against IOOF Service Co founded upon a nuanced and detailed exposition of the factual circumstances in which the Sweep Failure occurred, including at a minimum precise details as to how the failure arose, whether it was caused by human error or a technological error, to the extent it was caused by human error, which employee’s act or omissions caused the error, what role and duties that employee was performing at the relevant time and what instructions that employee had been given and by whom.

717 According to the fourth to seventh respondents, against this background “the conclusion reached by Mr Vine and Mr Riordan at the time that ‘[d]espite significant investigation, the cause of [the Sweep Failure] has not been fully established’ is significant”. They continued:

Contrary to the submissions made by APRA, there is no reason to doubt that this conclusion was bona fide. It is entirely plausible and unsurprising that, in circumstances where the error was first discovered more than three years after the relevant events occurred, Questor would not have been able to establish the factual circumstances relating to it with the level of precision that would have been required to make out a claim against IOOF Service Co.

718 For these reasons the fourth to seventh respondents said that APRA had failed to make out its allegation that IOOF Service Co was liable, or indeed that it was reasonably arguable that IOOF Service Co was liable, to compensate or indemnify Questor for any loss and damage suffered by reason of the Sweep failure. For the same reasons, as with the Pursuit failure, they said also that APRA had not proved that there would be no practical difficulty in making a claim against IOOF Service Co and the fact was the opposite would be the case.

719 I agree with these submissions. In common with the balance of APRA’s case, APRA does no more than rely on internal IOOF documents to prove various alleged failures to measure up to the requisite standard of care when the documents were prepared for another purpose and contain statements involving conclusions of law and otherwise operate at too high a level of generality to be useful evidence to prove the kind of facts APRA would need to prove to make good its case. APRA has not confronted the kind of evidence that would be required to prove the existence of a cause of action, or a reasonably arguable cause of action, in any aspect of its case. It has treated the bare facts of an error and loss or asserted loss, taken with the mixed statements of fact and law in the internal documents, as sufficient to prove its case when those documents are manifestly insufficient for that purpose.

720 In respect of alleged liability on the part of Questor, the fourth to seventh respondents said that this must fail as APRA has not established its case in respect of Questor’s alleged Sweep breach. I agree.

721 The fourth to seventh respondents continued saying that:

APRA’s pleaded case that Questor (and IIML from June 2016) breached their best interests covenant and “no conflicts” covenant in developing, adopting and implementing the alleged Sweep Compensation Plan must fail because the three critical integers to its case are not made out or are flawed. In short, the matters APRA relies on to contend that sourcing compensation from the ORFR was not in the best interests of beneficiaries are legally wrong or not made out on the evidence.

722 I again agree. The three critical integers are the alleged liability of IOOF Service Co for the Sweep failure, the lack of practical difficulty in making a claim against IOOF Service Co, and the alleged liability of Questor for the Sweep failure.

723 The fourth to seventh respondents said that the submissions they made with respect to the Pursuit allegations applied with even greater force to the Sweep allegations because in July 2017 IIML paid the compensation out of its own funds without any recourse to the ORFR. As those respondents put it, despite this:

…APRA has pressed ahead with a case which invites the Court to make serious findings of contravention against the corporate and individual respondents (and seeks disqualification of those individuals) on the basis of a course of action that was proposed more than four years ago which was never implemented and in circumstances where no superannuation beneficiaries have suffered any loss and the respondents, of their own volition more than a year and a half prior to the commencement of this proceeding, did precisely what APRA contends they ought to have done.

724 I agree also with these submissions. It is difficult to comprehend APRA’s case on the Sweep breach. The fact that at one time the ORFR was contemplated for use for a legitimate purpose does not give rise to any breach of the covenants of the superannuation trustee. If this were so, as the fourth to seventh respondents’ oral submissions put it, a trustee could be liable for every thought and decision, even if the thought or decision was never implemented. This does not strike me as a proper approach to the covenants which are concerned with conduct which is implemented.

725 The first respondent submitted that an important difference between the papers Mr Vine and Mr Riordan prepared for the boards to consider in respect of the Pursuit and the Sweep failures was that the latter paper provided relevant details as to why a claim against IOOF Service Co was not recommended, saying:

Despite significant investigation, the cause of this error has not been fully established. The sweep on the United Funds was cancelled and customers were advised that we would re-instate the sweep on MutliMix Funds, however this was not actioned. The need to reinstate the sweep was not added to any project for reasons which are not identifiable. These factual issues make it difficult to attribute a breach of contract or negligence to the administrator.

726 The first respondent said that APRA’s submission that this ought not to be believed should be rejected as there is no evidence to support it. I agree. There is nothing in the materials to suggest that this statement did other than reflect the genuine opinions of Mr Riordan and Mr Vine. The fact that they were dealing with a matter which dated back some years and in which they had no direct involvement supports the genuineness and accuracy of views they expressed.

727 The first respondent also dealt with APRA’s case that the Sweep compensation plan was not in the best interests of beneficiaries because:

a) there was a reasonably arguable claim against IOOF Service Co in relation to the Sweep issue (ASOC [158(a)]);

b) Questor as trustee was liable to make good the trust fund for the relevant losses (ASOC [158(b)]);

c) the ORFR was trust property (ASOC [158(c)]; and

d) there was no practical difficulty in making a claim against IOOF Service Co (ASOC [158(d)]).

728 The first respondent said:

In fact, there was no reasonably arguable claim against IOOF Service Co; Questor had no liability by reason of the exclusion clause in the trust deed and its rights of indemnity; the ORFR reserve was trust property but held on terms that permitted it to be used to compensate members for losses arising from operational risk events; and there were substantial practical difficulties in Questor pursuing a claim against IOOF Service Co. The allegations pleaded in ASOC [158] fail in their entirety.

729 Apart from the exclusion and indemnity point on the part of Questor, I accept these submissions. As to Questor, as I have said, there was no reasonably arguable case for liability on its part by reason of the lack of evidence of the kind which would be necessary to establish that it failed to measure up to the requisite standard of care in the particular circumstances of the case and that APRA had failed to adduce evidence of any kind sufficient for this purpose.

730 The first respondent said, and I accept other than in respect of (e) below, that the true position in relation to the Sweep failure in May 2015 was that:

a) Questor had investigated the cause of the Sweep issue but had been unable to determine who was at fault;

b) Mr Vine and Mr Riordan had informed the Board that they had considered the potential for a claim against IOOF Service Co but did not believe it had merit as it was factually “difficult to attribute a breach of contract or negligence” to IOOF Service Co;

c) Any claim against IOOF Service Co faced obvious difficulties, including that Questor had obligations under clause 9(g) of the AWM Services Deed and IOOF Services Deed to “keep adequate systems, procedures and processes”;

d) If IOOF Service Co was pursued, the likelihood was that Questor in its capacity as trustee would incur costs for which it would be indemnified out of trust assets; and

e) Questor itself had no exposure for the Pursuit failure because of the exclusion clause in the TPS Super trust deed, and in light of its rights of indemnity under that deed.

731 The first respondent noted that each of APRA’s five grounds to support Questor allegedly breaching the best interests and no conflicts covenant should be rejected:

(1) *The plan was not in the best interests of beneficiaries (ASOC [160](a)]*: when, for the reasons given, it could not be said that in the circumstances the plan was not in the best interests of beneficiaries. I agree.

(2) *The plan “preferred the profit interests” of the IOOF entities to the best interests of beneficiaries (ASOC [160(b)])*: but this claim is predicated on the erroneous assumption that there were viable claims against Questor and IOOF Service Co in respect of the Sweep issue. It also incorrectly assumes that it was not in members’ best interests to be compensated from the ORFR reserve. I agree and note also my general rejection of IOOF’s supposed profit motive above.

(3) *The plan preferred the profit interests of IOOF Service Co and the IOOF Group by not causing Questor to take action against IOOF Service Co (ASOC [160(c)])*: described as “simply a rehash of the same point and is to be rejected for the same reasons”. I agree.

(4) *The plan preferred the profit interests of Questor by not causing Questor to use its own funds (ASOC [160(d)])*: again, this is a reformulation of the same erroneous point. I agree.

(5) *The plan preferred the interests of non-superannuation beneficiaries over superannuation beneficiaries because Questor proposed to pay the former with its own funds but paid the latter from the ORFR reserve (ASIC [160(e)])*: it was said that the “hypothesis there is again the misguided proposition that members are injured when the ORFR reserve is used for the very purpose for which it was created”. I agree.

732 As to the alleged liability of Mr Kelaher and Mr Venardos, it follows from my conclusions that neither can have contravened their covenants as APRA proposed because the factual foundation necessary for such contraventions does not exist.

733 The submissions for the first respondent are that when the claim against Mr Kelaher at ASOC [161] - [166] is considered it must fail (noting the submissions for the first and second respondents apply equally to each of them).

734 As to ASOC [161]:

Mr Kelaher clearly did not have the pleaded level of knowledge. It is true that Mr Kelaher knew that APRA had indicated that Questor should consider claims against IOOF Service Co (see ASOC [161(e)]), but he had been told by Mr Vine and Mr Riordan that there was no viable claim against IOOF Service Co and that pursuing any such claim would involve difficulties and costs that would be borne by members and were therefore not in members’ best interests (cf. ASOC [161(a), (d)]). He had no reason to doubt their views in relation to those matters. Further, he would have known that there was no claim against Questor given the exclusion clause and rights of indemnity in the TPS Super trust deed (cf. ASOC [161(b)]). Mr Kelaher could rightly conclude that the ORFR reserve could be used to compensate trust beneficiaries, both because Mr Vine and Mr Riordan had said it could be used and because that was the true legal position (cf. ASOC [161(c)]).

As to ASOC [162], this is substantively the same allegation as made in ASOC [126] with respect to the Pursuit issue. The analysis at paragraphs [208]-[209] above applies with equal force to this allegation.

As to ASOC [165], the allegation collapses because the pleaded conflicts of interest did not exist and the assertion that the Sweep compensation plan was not in the best interests of members is not made out.

735 Apart from Mr Kelaher relying on the exclusion and indemnity provision (which he may well have subjectively done), I accept these submissions which are consistent with my findings above.

736 The submissions for the first respondent noted that APRA alleges that between 27 May 2015 and mid-2017, in breach of the director covenants in the SIS Act, Mr Kelaher “did not take any or adequate steps” to cause Questor to revoke or amend the Sweep compensation plan so that the loss and damage caused by the Sweep issue was “wholly recoverable” from IOOF Service Co, Questor, IOOF Hold Co or a combination of all three (ASOC, [165A]-[165B]). However, as pointed out above, the ORFR was never used to pay Sweep compensation. The first respondent also said APRA was incorrect to suggest the advice from the ATO led to a change of compensation plan. The first respondent said:

The IOOF Group Risk Compliance Report dated 3 February 2017 (five days before the ATO tax advice) records the following in relation to the Sweep issue:

The rectification of this error has been progressed this quarter and compensation calculations have been refreshed. Following earlier approval from the Board to source circa $1.0m compensation from the ORFR, further consideration has been given by the Finance and Legal Teams on the need to replenish the ORFR. This follows recent observations and directives from APRA about where compensation should be sourced from, taking into account such factors as whether a party is at fault and liable to compensate, as well as perceived conflicts of interest with related parties. A board submission will be available at the next meeting recommending a replenishment plan for the ORFR.

737 The first respondent said, and I accept, that the “true position is that Questor reconsidered its approach to the Sweep issue before the tax advice and before the Royal Commission and, of its own volition, elected to compensate members from its own pockets”.

738 The first respondent also said, and I accept, that:

Not only is that fact wholly destructive of the allegations in ASOC [165A]-[165B], it also destroys a key theme of APRA’s case. What the resolution of the Sweep episode demonstrates is that the IOOF Group was willing to fund compensation to members where, upon consideration, it formed the view that the IOOF Group as a whole was responsible for members’ loss. It did so notwithstanding that liability had not been established (by litigation or otherwise) and notwithstanding the exclusion of liability and indemnities in favour of members of the IOOF Group (as referred to above). Those are the actions of a responsible corporate actor and RSE licensee.

Furthermore, the conduct of the IOOF Group in relation to the Sweep issue provides a prism through which the other alleged breaches are to be viewed. The Sweep issue demonstrates that the IOOF Group was willing to pay money from its own pocket where it formed the view that it was at fault. The Court ought to draw the inference that the IOOF Group’s position was the same in relation to the Pursuit and CMT matters.

739 The second respondent submitted that the minutes of the Questor board meeting on 27 May 2015 show that the board “considered the proposed remediation strategy and source of compensation” before it resolved to approve the compensation plan. Further, the board paper clearly sets out the reasons why management was of the view that the plan was in the members’ best interests:

(a) it was “in members’ best interests to access the ORFR to ensure that loss is remedied on a timely basis”;

(b) APRA was “likely to agree with this position, subject to later consideration of other sources of funding”;

(c) Questor’s ORFR policy permitted the trustee to use the ORFR reserve for any loss arising from operational risk, being “risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events”; and

(d) management did not recommend pursuing legal action against IOOF Service Co for a number of reasons including the fact that despite “significant investigation, the cause of this error has not been fully established”, the “factual issues make it difficult to attribute a breach of contract or negligence” to Service Co, the issues may not be realistically actionable and legal action would be time-consuming, expensive and burdensome. That is evidence which contradicts APRA’s assertion that there was an IOOF Service Co exposure.

740 I agree with the submissions for the second respondent that the suggestion that the line in the report that the cause of the error has not been fully established and was a result of significant push-back from APRA and not a genuinely held view is a serious allegation which is not founded on the evidence. In any event, as the second respondent said, Mr Venardos was entitled to rely on the information in the board paper. The second respondent submitted that the board was also informed that APRA had been notified of the plan, and that management was waiting to hear back from APRA in relation to the proposed approach. This, it was said, is clear from the fact that:

(a) A copy of the letter sent by Mr Vine to APRA dated 15 May 2015 informing APRA of the compensation plan was attached as Appendix 2 to the board paper.

(b) In the ‘Background’ section of the paper, the board was told that:

Management has been involved in a number of communications with APRA in relation to the breach and the remediation proposals. The recommendations in this paper have been discussed with APRA.

(c) In the section of the board paper under the heading ‘Recommended source of compensation – Superannuation’, the board was told that:

We have not yet heard back from APRA in relation to our approach, however would expect APRA to adopt a similar position to that seen with the Pursuit breach reported to the IIML May Board meeting.

741 It was submitted that the plain inference as far as the board was concerned is that APRA was being kept informed of the plan, remained in discussions with management about it and based on the communications relating to Pursuit, was likely to be content with the course proposed. I accept this submission.

742 It was submitted that to the extent APRA seeks to impugn Mr Venardos’ conduct because he knew “the basal facts comprising the Sweep failure and Questor and IOOF Service Co’s exposure to liability”, the evidence does not prove this allegation. According to the submissions:

The Group Legal, Risk and Compliance Report of 13 February 2015 did not address the question of Questor’s and IOOF Service Co’s potential liability. It informed the board of four facts: (a) the nature of the error (namely, that the sweeps for a number of clients had not been reinstated on the transfer to MultiMix); (b) the issue had been reported to ASIC and APRA; (c) the client who first alerted Questor to the issue had been compensated; and (d) management was working on determining impacted clients and developing a compensation plan and approach to provide to APRA as soon as practicable. The fact that the minutes of the board meeting on 25 March 2015 described the matters as “TPS failure to reinstate investment sweeps” is neither here nor there.

743 In common with the other respondents, the second respondent made the point that, in the event, the Sweep compensation plan was never implemented and that this is fatal to APRA’s allegations. As I have said, I agree with this proposition.

744 It follows that APRA’s case against the respondents in relation to the Sweep incident is unsustainable in its entirety.

##### 16. THE ALLEGED BENDIGO BREACHES

###### 16.1 Basic facts on which APRA relied

745 APRA explained that:

Within IPS Super, the Bendigo and Adelaide Bank Ltd (BAB) had a defined benefit employee sub-plan (the Bendigo Plan). In around April 2015, BAB instructed IIML as trustee of IPS Super to sell certain surplus assets held for the Bendigo Plan. To effect the sale, IOOF Service Co (as service provider to IIML as trustee) was required to manually set the cash holding rate for the Bendigo Plan to avoid the automatic re-purchase of the assets being sold: ASOC, [179]-[182]; substantially admitted IIML and Questor, [179]-[182], [183A].

Twice, within the space of a few months, IIML and IOOF Service Co failed to carry out this procedure with due care and skill, causing loss to the trust assets of the Bendigo Plan.

The first error occurred on around 28 April 2015. To avoid IIML automatically re-purchasing the assets sold, IOOF Service Co manually set the cash holding rate for the Bendigo Plan at 10%. This control was unsuccessful and an unallocated buy for most of the Bendigo Plan’s cash amount occurred: CB 7/124, p. 1989. This transaction was reversed causing a small loss to the Bendigo Plan (approximately $10,000): CB 7/124, p. 1989. APRA does not allege this first failure was a breach of the SIS Act. APRA does say, however, that this failure should have put IIML and IOOF Service Co on notice that they needed to improve their checks and controls when manually adjusting the cash rate to effect asset sales from the defined benefit plan.

The second error occurred in around June 2015. This time, to facilitate a further transaction, IOOF Service Co set the cash holding rate to 99.9% with the intention of re-setting the rate back to 1.5% after the transaction had occurred. IOOF Service Co failed to do so. As a result, IIML automatically sold the entire investment held on behalf of the Bendigo Plan in a fund known as “Mercer Growth”: CB, 9/159 worth $8,205,361. The sale was detected about two weeks later and reversed. Due to changes in the value of the investment during that period, the Bendigo Plan suffered a loss of approximately $114,000: IIML and Questor Defence, [183]. This is the failure referred to as the “Bendigo Plan Failure” at ASOC [182].

IIML did not report either of these failures to APRA. IIML did, however, determine internally that the Bendigo Plan Failure constituted a breach of s 52(2)(b) of the SIS Act: 159, p. 9/2529. The root cause of the failure was identified by IIML as “inadequate training/lack of knowledge”. IOOF Compliance considered that the episode “indicates a lack of diligence around the processing and subsequent follow up of an irregular transaction, and also identified that a prior issue was not reported to compliance”.

APRA takes the view that this assessment by IIML’s compliance team was correct, and that the Bendigo failure was a breach by IIML of its due care, skill and diligence obligations under s 52(2)(b) of the SIS Act. A prudent superannuation trustee director, following the first failure, would have put in place controls to ensure that the same error did not occur again. A simply control would have been to put in place a procedure where by the cash holding rate was checked by another staff members (or by an automatic system) immediately after the transaction had occurred.

###### 16.2 APRA’s case – IOOF Service Co’s Exposure

746 APRA said that IIML had admitted that it relied upon the services provided by IOOF Service Co to administer the Bendigo Plan and assist IIML to comply with its obligations as trustee: IIML Defence, [179]. IIML further admitted that it was IOOF Service Co employees who failed to re-set the cash holding rate after the relevant asset sale: IIML Defence, [182(a)].

747 According to APRA, given that IOOF Service Co was required by the service agreements to provide the services to the standard required by IIML as trustee of TPS Super, the failure amounted to a breach by IOOF Service Co of the service agreement so that IOOF Service Co was prima facie liable for the loss.

###### 16.3 APRA’s case – The Bendigo Compensation Plan

748 APRA said IIML immediately moved the loss resulting from the Bendigo failure from the reserves of the Bendigo Plan to the investment trading reserve of IPS Super, which formed part of IPS Super’s general reserve (the **Bendigo Compensation Plan**).

749 On 16 December 2015, Mr Rossitto wrote that:

As the investment reserve (for statutory purposes it is rolled up into the general reserve and reported as such) no further action is required and no funding required by Trustee.

750 The Bendigo failure was reported to the IOOF Risk and Compliance Committee (**RCC**) in September 2015. Mr Venardos was a member of the RCC. The update to the RCC said:

Due to human error the cash holding % was not re-set and the entire Mercer Growth holding (2,785,633.2174 units worth $8,205,361) was sold into cash on 29/6/15. Upon detection the transaction was reversed and moved to the investment trading reserve on 9/7/15. This has removed the impact of the incorrect trade from the defined benefit reserve but any financial impact of market movements in the intervening period was effectively transferred to the investment trading reserve, which lost approximately $114,000 on this trade that needs to be reimbursed by IIML as Trustee.

In investigating the breach it was also noted that a prior similar error occurred however the financial impact of the earlier error was only $10,700.

751 The RCC noted this report. APRA said:

…there was no further discussion of the Bendigo Failure: CB 10/191A, p. 3155\_0002. There was no questioning by Venardos (either at this meeting or subsequent meetings of the Board or RCC) as to why the investment trading reserve had been used, or when it was proposed that IIML as trustee would reimburse the reserve.

Nor was there any consideration as to whether IOOF Service Co, as the relevant service provider, was liable to compensate beneficiaries for the loss. These are all matters that IIML and Venardos should have been acutely aware of at the time considering the ongoing discussions internally and with APRA regarding the CMT, Pursuit and Sweep Compensation Plans. The minutes in fact record that there was a discussion about the source of compensation for CMT at the very same meeting: CB 10/191, p. 3155\_0002.

No steps were taken to reimburse the reserve for the Bendigo Failure until October 2018. The reconsideration that happened around this time only occurred following a request from APRA to reconsider all uses of the general reserve since 31 January 2015: CB 18/444, p. 6376.

###### 16.4 APRA’s case – IIML’s alleged Compensation Plan breach

752 According to APRA, IIML had a conflict of interest when making the decision to use the beneficiaries’ reserve to compensate for losses suffered by reason of the Bendigo failure. The conflict arose from the fact that it or its related entity IOOF Service Co was potentially liable to repay the loss.

753 APRA said:

Considering the liability of IIML and the potential liability of IOOF Service Co, it was not in the best interests of beneficiaries for IIML to use the IPS Super general reserve to pay compensation for loss suffered. By adopting this course, IIML breached its covenants under s 52(2)(c) and (d). Mr Rossitto, as a senior member of the accounting team, is taken to have been acting for and on behalf of IIML in making this decision, and his conduct should be imputed to IIML.

###### 16.5 APRA’s case – Mr Venardos’ alleged Compensation Plan breach

754 APRA said that as a director of both of IOOF Hold Co and IIML, Mr Venardos also had a conflict of interest with respect to the approach that IIML had adopted to paying compensation for the Bendigo failure. The conflict arose from the fact that any money paid by IOOF Group entities to compensate beneficiaries would have an impact on the earnings of those entities and was therefore in conflict with Mr Venardos’ duty to shareholders. In this regard, it may be noted that there is again no evidence that would suggest the Bendigo issue could have had any impact on the share price; the alleged conflict remains one in theory only.

755 Further, by reason of the update at the RCC meeting on 23 September 2015, APRA contended that Mr Venardos knew or ought to have known:

(a) that, due to human error by IIML and its service provider IOOF Service Co, over $8m of assets held on trust for the Bendigo Plan had been sold inadvertently by IIML;

(b) the sale had been reversed but had caused losses to the trust assets of the Bendigo Plan;

(c) that loss had been transferred into the IPS Super trading reserve, effectively meaning that the loss had been paid from the trust money belonging to all IPS Super beneficiaries;

(d) the reserve needed to be reimbursed by IIML (suggesting an acknowledgment by the author of the paper, Ms Cristine Craig, that IIML was liable for the loss);

(e) the error that had occurred was not a one off event as a “prior similar event” had occurred.

756 APRA also said that Mr Venardos was aware at this time, “by reason of his prior approval of the Pursuit Compensation Plan and Sweep Compensation Plan and the updates he had received on the CMT issues, that using the reserves to compensate beneficiaries was an issue that needed to be carefully considered in light of his obligations under s 52A”.

757 APRA alleged that armed with this knowledge a prudent superannuation trustee director exercising care, skill and diligence and performing their duties in the best interests of beneficiaries would have “identified the conflicts of interest involved in the Bendigo compensation decision and taken steps to satisfy himself that management was proposing to make IIML reimburse the IPS General Reserve for the amounts taken out for the Bendigo Compensation Plan or, if they were not, that independent legal advice had been obtained to support management’s decision as trustee not to claim compensation from itself or IOOF Service Co”. According to APRA, Mr Venardos’ failures to do so continued from 23 September 2015 to 25 October 2018 when, belatedly, the issue of the use of the Bendigo compensation reserve was raised for consideration by the IIML board and compensation was paid.

758 APRA said that the fact that the report to the RCC on 23 September 2015 said the loss needed to be reimbursed by IIML as trustee was insufficient to discharge Mr Venardos’ duties. APRA said:

As for the nature of the proposal, all that the report recorded was that the trade “needs to be reimbursed by IIML”. It did not record that IIML was going to reimburse the trading reserve, or how it proposed to do so. It could have been proposing to do so from another reserve. In the circumstances, it was incumbent on Venardos to ask questions and make sure IIML’s conflicts were managed.

759 Further, APRA submitted that:

APRA does not allege that Venardos was being asked to do anything by management. APRA’s allegation is that, in light of the information presented to him, he was required to proactively consider beneficiaries’ best interests and satisfy himself that such interests were being properly pursued by the trustee and its management in circumstances where there was a real conflict of interest.

###### 16.6 The respondents’ case – IIML’s alleged Bendigo breaches

760 The fourth to seventh respondents submitted that APRA’s pleaded case in relation to IIML’s Bendigo Breach, as alleged, was focused on the causation of what it described as the Bendigo Plan Failure and the role played by the systems (including IT systems) and the processes that were in place at the time – what APRA described as the “policies, procedures and controls in place that a prudent superannuation trustee would have in place”. They summarised the pleaded case as follows:

(a) IIML breached the Due Care Covenant because it relied on IOOF Service Co to administer the asset sale in circumstances where the “Services” of IOOF Service Co were “defective, deficient and not fit for purpose” and where “IIML did not itself have adequate systems and processes to correct and detect errors” in the Services provided (ASOC [188](a) and [189]); and

(b) IIML breached the Due Care Covenant because it failed to exercise its rights under the Service Engagements to perform its own audit, monitoring or assessment of whether IOOF Service Co’s “IT systems were appropriate to provide the Services to IIML in its capacity as trustee of IPS Super” (ASOC [188(b)] and [189]).

761 The fourth to seventh respondents characterised APRA’s case as tantamount to submitting that the due care covenant insures against any form of error.

762 They submitted that the error in June 2015 was detected within 10 days and the transaction was moved into the investment trading reserve on that day.

763 The fourth to seventh respondents said the claim of IIML’s breach of the due care covenant must fail given the following matters:

(a) The conduct is to be viewed in context: The incident involved processing a unique client instruction, in respect of which external actuarial advice had been obtained. Given the unique nature of the instructions, and the relatively out-dated nature and declining use of defined benefit accounts generally (which accommodate only an increasingly smaller number of beneficiaries), an automated system to give effect to these instructions did not exist and manual processes needed to be applied. In all the relevant circumstances, these were reasonable arrangements to have in place, and to suggest otherwise is to impermissibly ignore these factors;

(b) Due care does not equate to insurance against all errors: While due care was taken, a ‘perfect storm’ of events coincided, such that the calculations that had been undertaken in order to correctly give effect to Bendigo's instructions did not take into account an unanticipated benefit payment to a member exiting the fund in the very narrow window of time during which this transaction was being executed. If the June Bendigo Incident amounts to a breach of the Due Care Covenant, then any error (which results also in loss or damage) will be actionable pursuant to s 55(3) of the SIS Act. This is patently not the intended scope of the duty. Furthermore, and more fundamentally, any 'lessons learned' from the April 2015 incident would not have prevented the error that occurred later in June 2015, as it was an entirely different issue that was involved;

(c) IIML acted quickly to redress the error: The error was detected promptly, and was reversed on the same day of detection. This is also relevant, by way of context, in relation to the predicate breach, given what APRA pleads in relation to the detection and correction of the error.

764 They noted that APRA also contended that IIML breached the best interests covenant and no conflicts covenant by its actions to address the loss by moving it to the investment trading reserve which forms part of the IPS general reserve. APRA’s pleaded case with respect to the Bendigo Compensation Plan was that:

(a) it would have been in the best interests of beneficiaries for the loss to have been recovered from IOOF Service Co, met by IOOF Hold Co, or a combination of the two (ASOC [196]);

(b) it was not in the best interests of beneficiaries for IOOF Service Co not to be pursued because IOOF Service Co was “liable to make good the trust fund for losses suffered by beneficiaries of IPS Super” and “there was no practical difficulty in making a claim against” Service Co (ASOC [197]); and

(c) the decision made on the day the error was detected to move the accidental sale from the account holding the defined benefit assets to the IPS General Reserve (which APRA describes as the “Bendigo Compensation Plan”) was an act taken in breach of the Best Interests and No Conflicts Covenants because it preferred a range of ‘profit interests’ ahead of the interests of beneficiaries (ASOC [199]).

765 According to the fourth to seventh respondents APRA’s case fails for these reasons:

(a) The alleged breach of the No Conflicts Covenant is misconceived from the outset: APRA fails in pointing to any interest that could have had a ‘significant’ impact on the manner in which IIML approached the question of compensation in light of the June Bendigo Incident. An ‘actual’ conflict has to have crystallised before consideration of the No Conflicts Covenant even arises. This aspect of APRA’s claim with respect to the June Bendigo Incident is misconceived;

(b) The loss was indirect and consequential: In addition, another reason for the absence of any conflict in light of the ‘potential’ of IOOF Service Co is the fact that the loss was indirect and consequential and IOOF Service Co was not liable to IIML for such loss;

(c) IIML’s initial approach to compensation was appropriate: The initial use of the IPS General Reserve (by means of the investment trading ‘sub-reserve’) was wholly permissible to account for this loss (and to remove any consequence from member accounts attached to the Bendigo Plan). The subsequent reimbursement of the IPS General Reserve by IIML does not detract from or alter the appropriate nature of this initial approach to compensation; and

(d) Internal assessments of breach are neither relevant nor determinative: ]It is not to the point that, internally, for its incident reporting purposes, the June Bendigo Incident was noted by IIML as a breach of s 52(2)(b) of the SIS Act by employees of IIML, who were not lawyers. That legal question is a matter for judicial determination in these proceedings.

766 The fourth to seventh respondents expanded on these contentions.

767 As to context, they explained that the Bendigo Plan is a sub-plan of IOOF Employer Super, which is a division (Division IV) of the IPS Trust. That is, Bendigo is a “Participating Employer” for the purpose of Division IV of the IPS Trust Deed. The investment management platform, or database, used to administer the Bendigo Plan is ASIS. The Bendigo Plan is comprised of a defined benefit section and an accumulation section (for non-defined benefit members, or “accumulation members”). The “accounts” that attach to the Bendigo Plan include the “DB Reserve”, or “Defined Benefits Reserve”, which is the account that holds the assets of the defined benefit section of the Bendigo Plan. The other members of the Bendigo Fund, being accumulation members, have individual accounts with their own member numbers and balances. There is also the “investment trading reserve”, which is part of the IPS General Reserve and which is attached specifically to the Bendigo Plan. Since at least 2007, the defined benefit section of the Bendigo Plan has been closed to new entrants. From that time forward, all new members joined the accumulation section of the fund.

768 There were three “cash holding” settings in the ASIS investment management platform in 2015:

(a) “Minimum” (or Low) cash holding: If the cash holding went below the minimum level, upon the next reweighting (which occurred twice weekly), assets were sold into cash in order to bring the cash holding up to the Standard Cash Setting of 1.5%, which is outlined below. (Minimum Cash Setting);

(b) “Standard level” cash holding: The standard level was typically set to 1.5%, in line with the Agreed Investment Strategy, which required 1.5% of the reserve to be held in cash. (Standard Cash Setting); and

(c) “Maximum” (or High) cash holding: The maximum cash rate was typically set at around 5 to 10%. If the cash holding went above the maximum level, upon the next reweighting (which occurred twice weekly), the system automatically purchased assets to bring the cash holding down to the Standard Cash Setting, outlined above. (Maximum Cash Setting).

If the cash holding was above the required level, or the Standard Cash Setting, the excess cash would be used to purchase units in Mercer Growth Option. Conversely, if the cash holding was below the required level, units in Mercer Growth Option would be sold in order to bring the cash holding back up to the required level. The re-weighting process was an automatic process in ASIS that occurred without any human intervention.

769 In response to APRA’s contention that the Bendigo incident in April 2015 should have put IIML and IOOF Service Co on notice that they needed to improve their checks and controls when manually adjusting the cash rate to effect asset sales from the defined benefit plan, the fourth to seventh respondents provided a detailed analysis of the events leading up to the April incident explaining the manual system that had to be used to achieve the objective of the relevant transaction. The fourth to seventh respondents submitted that APRA’s contention overlooked that there was no automated mechanism that could have been put in place during the short intervening period between the two incidents and no evidence to support the existence of any such system. They also submitted that while APRA asserted that IIML “did not have the policies, procedures and controls in place that a prudent superannuation trustee would have in place”, it did not explain “why such policies would be required in relation to the unique category of client instructions in issue, nor does APRA make any attempt to describe what those policies and procedures would have entailed in advance of these incidents”. Further, that “APRA is similarly at a loss to point to what more could have reasonably been done (without the benefit of hindsight) in all the relevant circumstances known to the trustee at the time”.

770 As the fourth to seventh respondents put it, to the extent that a more cautious approach could have been taken the second time around, the answer was “the relevant personnel were well and truly alive to the need to get the cash settings right”. But this did not prevent the incident occurring because of an unforeseen event (the payment out of the member) and it is “misconceived for APRA to contend that due care equates to a guarantee of perfect outcomes”. The fourth to seventh respondents made the following propositions in support of the additional care that was taken in respect of the second set of instructions from Bendigo.

771 On 12 June 2015, by email, Bendigo provided a second set of written instructions to IOOF outlining its desire to use the surplus funds again for a further SG (superannuation guarantee) contribution. Bendigo required this contribution to be made on the pay date of 25 June 2015.

772 On 15 June 2015, instructions were provided internally by Ms Richards to give effect to the further request of Bendigo. Ms Richards was alive to the processing requirements, and her instructions expressly included setting the “cash holding” to 99.9% to “avoid re-purchasing”. As such, on 17 June 2015 the minimum cash setting was set at 0.1%, the standard cash setting at 99.9% and maximum cash setting at 99.9%. On 17 June 2015 the specified assets were sold to make available sufficient cash for the intended SG contribution to members. On 19 June 2015 an unanticipated benefit payment to a member was made from the BD reserve in the amount of $207,650.55. This was because under the defined benefit scheme upon reaching the normal retirement age of 65, members are transferred from the defined benefit category into an accumulation account established in their name. The Investment Administration Team, given its functions, was not aware that this payment was to be made and did not allow for it in the setting that it applied in ASIS to give effect to Bendigo’s instructions. But for the payment of this benefit at this time, the automated sale in June of the Mercer Growth units would not have occurred. On 26 June 2015, the SG contribution in the amount of $1,200,902.20 ($1.02 million after tax) was made to members in accordance with the instructions of Bendigo. As the fourth to seventh respondents observed:

The SG contribution, combined with the 19 June 2015 member payment, caused the DB Reserve account balance to go in to the negative (in circumstances where this would not have happened in the absence of the unanticipated 19 June 2015 member payment). The balance of the account was -$172,467.75.

On 29 June 2015, upon the routine reweighting of the Bendigo assets, the system automatically applied the “99.9%” Standard Cash setting (which was still in place) by selling the entire Mercer Growth holding (2,785,633.2174 units to the value of $8,205,361) into cash (June Bendigo Incident).

773 They said further:

While due care was taken, a ‘perfect storm’ of events coincided, such that the calculations that had been undertaken in order to correctly give effect to Bendigo’s Second Set of Instructions – with express recognition of the need to correctly set the cash settings and avoid an automated transaction – did not take into account an unanticipated benefit payment to a member exiting the fund in the very narrow window of time during which this transaction was being executed.

Any ‘lessons learned’ from the April Bendigo Incident would not have prevented the error that occurred in June, as it was an entirely different issue that was involved. While APRA contends at paragraph [498] of its closing submissions that a simple control “would have been to put in place a procedure where by the cash holding rate was checked by another staff members [sic] (or by an automated system) immediately after the transaction had occurred”. It is patently clear that if such a process had been in place, it would not have addressed the issue of the unhappy timing of one of the 26 defined benefit members reaching the age of 65 in the very window of a week during which the settings had been adjusted in order to give effect to Bendigo’s Second Set of instructions.

774 In addition they submitted:

APRA overlooks the fact that the error involved in the June Bendigo Incident was detected promptly, and was reversed on the same day of detection to restore the DB Reserve to the correct position.

That is, on 9 July 2015, the automated sale was detected by the Defined Benefit administrator. The staff members who identified the error requested that the sale be ‘moved’ from the DB Reserve account (in which the vested benefits of defined benefits members of the superannuation fund were held, as noted above at paragraph [406]) to the investment trading reserve (being part of the IPS General Reserve). In moving the sale to the investment trading reserve, the staff members also had to account for the portion of the Mercer Growth units that would have been sold in the ordinary course. APRA deals with none of this complexity.

The movement of the sale out of the DB Reserve involved the following steps:

(a) Maintaining the portion of the sale that would have occurred in any event: First, a ‘sell’ of Mercer Growth units to the value of $363,217.63 was manually recorded against the Bendigo account as having occurred on 29 June 2015, retrospectively, in order to reflect the fact that that portion of the $8.2m sale would have correctly sold in any event.

(b) Repurchasing the balance using the IPS General Reserve: Secondly, in respect of the balance of the automated sale (being the units incorrectly sold), Mercer Growth units in the sum of $7,842.143.58 were repurchased using the investment trading reserve in the IPS General Reserve.

…

On 3 August 2015, IOOF identified the quantum of the loss in connection with the automated buy in July 2015 as being $114,206.00. This was a loss in connection with the investment trading reserve. In light of the reversal that took place as outlined above at paragraph [452], there was no loss to the Bendigo Plan in the manner described in APRA’s submissions at [496], and certainly no loss to the entitlements and underlying assets of the 26 defined benefit members.

775 The fourth to seventh respondents submitted further that the September 2015 compliance report stated, as was the fact, that Bendigo’s instructions involved “an unusual transaction request for which procedures to give effect were largely manual”. The report also said:

Upon detection the transaction was reversed and moved to the investment trading reserve on 9/7/15. This has removed the impact of the incorrect trade from the defined benefit reserve but any financial impact of market movements in the intervening period was effectively transferred to the investment trading reserve, which lost approximately $114,000 on this trade that needs to be reimbursed by IIML as trustee.

776 The fourth to seventh respondents submitted that the so-called Bendigo Compensation Plan was a decision made on 9 July 2015, when the error was detected, to move the accidental sale from the account holding the defined benefit assets (the DB Reserve) to the IPS General Reserve (or the investment trading reserve). This was a step taken to “remove any loss attributable to the assets held on behalf of the defined benefit members”.

777 As to the no conflicts covenant they submitted that:

APRA fails in pointing to any interest that could have had a ‘significant’ impact on the manner in which IIML approached the question of compensation in light of the June Bendigo Incident. An ‘actual’ conflict has to have crystallised before consideration of the No Conflicts Covenant even arises. This aspect of APRA’s claim with respect to the June Bendigo Incident is misconceived and rests on an incorrect premise.

…SPS 521 r 16 makes it plain that a “relevant duty or interest” for the purpose of identifying a conflict is “one that might reasonably be considered to have the potential to have a significant impact on the capacity of the RSE licensee… to act in a manner that is consistent with the best interests of beneficiaries”. This is an important indication of how the No Conflicts Covenant is to be construed. A conflict will only arise if – objectively – the particular interest or duty is likely to significantly impact on the capacity of the trustee to perform its duties consistently with the best interests obligation as specified in s 52(2)(d).

Put differently, a conflict only arises when there is a real and not remote possibility of undue influence – there must be a crystallised conflict. Where interests fall short of creating a conflict that will impair the performance of the duties of the trustee in accordance with members’ best interests, the No Conflicts Covenant is simply not engaged – s 52(2)(d) is not directed towards the avoidance of conflicts, but it is only engaged in the event of an actual conflict.

There is therefore no rigour in the allegation that APRA has made in this regard. The best that APRA can do is to suggest that the “conflict arose from the fact that [IIML] or its related entity IOOF Service Co was potentially liable to repay the loss”…

778 Further, they submitted that APRA has not made good its claim that “there was no practical difficulty in making a claim against” IOOF Service Co. APRA, they said, does not “elaborate on why it was preferable to engage in costly, potentially protracted litigation, rather than to immediately and on the same day restore the DB Reserve account to the state it was in prior to the accidental sale”.

779 As to the nature of the loss, they submitted that it was plainly indirect and consequential loss, excluded from the scope of IOOF Service Co’s indemnity, according to the fourth to seventh respondents. As they explained:

The June Bendigo Incident resulted in the unintended sale of assets from the DB Reserve on 29 June 2015 – that was the relevant consequence. However, the loss arose from the repurchase out of the IPS General Reserve on 9 July 2015, for the balance of the sale that needed to be ‘reversed’.

The repurchase on 9 July 2015 very well could have been made at a gain, but such a windfall would not have been attributable to the June Bendigo Incident. In the language of *Macmahon Mining Services v Cobar Management* [2014] NSWSC 731 at [19], here there is an ‘intervening cause’ which makes the loss indirect and consequential, so as to engage clause 11.2 of the Service Agreement…

780 The fourth to seventh respondents said that the use of the IPS general reserve was “wholly permissible to account for this loss and to remove any consequence from the reserve account attached to the Bendigo Plan”. They said:

It was an action that immediately and without delay removed any consequence from the account attached to the Bendigo Plan in which the vested benefits of members of the superannuation fund were held, and it was thus a step that was in the best interests of the beneficiaries at the time the action was taken. It was permitted by the trust deed and IOOF’s Reserves Policy…

The subsequent reimbursement of the General Reserve by IIML – in light of the steps taken in October 2018 – does not detract from, or alter, the appropriate nature of this initial approach to compensation.

781 The fourth to seventh respondents also submitted that:

…it is not to the point that, internally, for its incident reporting purposes, the June Bendigo Incident was noted as a breach of s 52(2)(b) of the SIS Act by employees of IIML, who were not lawyers. Contravention of s 55(1) by means of a breach of a covenant is uniquely a matter for the court’s determination.

782 The second respondent’s submissions also addressed the Bendigo case. It was noted that the allegations pleaded against Mr Venardos were all said to arise from him “considering the Bendigo Compensation Plan” and “not taking adequate steps to revoke or amend the Bendigo Compensation Plan”.

783 It was submitted that a critical fact is that on the evidence Mr Venardos was informed that the loss would be reimbursed by IIML and not by way of the pleaded Bendigo Compensation Plan. This was because “on 23 September 2015 Mr Venardos attended the RCC meeting with two other non-executive directors, Mr Allan Griffiths and Ms Harvey. Mr Griffiths was the Chairman of the RCC at this time. The Group Compliance Report tabled for noting at the meeting included a section titled ‘Bendigo Staff Defined Benefit (DB) reserve error’. That section reads (emphasis added)”:

Bendigo Staff Defined Benefit Plan has built up considerable surplus and the Bank requested that this be reduced by paying SG contributions for broader DC membership for paydays 30/4/15 and 26/6/15. The contribution amount for 26/6/15 was $1.2million ($1.02million after tax). This is an unusual transaction request for which procedures to give effect were largely manual.

It was agreed with the employer that asset sales would be performed before the contribution date so that the agreed investment strategy of the reserve account was maintained. Sufficient assets were to be retained in cash until the contributions were processed.

To ensure assets were not re-purchased before allocation, it was necessary to temporarily and manually set the cash holding to 99.9%. This should have been manually set back to the standard 1.5% once complete. Due to human error the cash holding % was not re-set and the entire Mercer Growth holding (2,785,633.2174 units worth $8,205,361) was sold into cash on 29/6/15. Upon detection the transaction was reversed and moved to the investment trading reserve on 9/7/15. This has removed the impact of the incorrect trade from the defined benefit reserve but **any financial impact of market movements in the intervening period was effectively transferred to the investment trading reserve, which lost approximately $114,000 on this trade that needs to be reimbursed by IIML as Trustee.**

784 The second respondent submitted that having been so informed it was clearly unnecessary for Mr Venardos to consider the liability of IOOF Service Co for the loss. APRA’s contention that the report was ambiguous should be rejected, as the report was clear that IIML as trustee would be paying the reimbursement. It was said APRA’s ambiguity submission, underlying its contention that Mr Venardos had to do more than note the report should be rejected because:

(a) The Group Compliance Report did more than “suggest” that IIML was going to reimburse any loss – that is plainly what was stated in the Group Compliance Report and what must have been understood by the members of the RCC. There is no other inference or conclusion available based on the words in the Group Compliance Report.

(b) The submission that the words “needs to be reimbursed by IIML as Trustee” may mean “needs to be reimbursed by IIML as Trustee from the general reserve” or that “IIML could have been proposing to do so from another reserve” (or any similar submission) is contrived and nonsense, particularly when one appreciates that the investment trading reserve is part of the general reserve (as APRA acknowledges at ASOC [193]).

(c) In all other instances considered in this case, reports from management concerning the actual or proposed use of a reserve in relation to compensation expressly and clearly identified the use of a specific reserve.

(d) APRA’s own submission at ACS [508] which states that Mr Venardos should have asked “when it was proposed that IIML as trustee would reimburse the reserve” itself acknowledges that the statement in the Group Compliance Report was clear.

785 The submissions for the second respondent also noted that:

In opening and in the ACS [505], APRA relies upon emails between management personnel between 24 September 2015 and 17 December 2015. In the first email in that chain on 24 September 2015, Ms Tanner (Compliance Manager) asked Mr Rossitto (Head of Investment & Accounting Services – Finance) “whether the Trustee has compensated the investment trading reserves of IPS for the financial impact”. This is consistent with the Group Compliance Report to the RCC on 23 September 2015. In later emails, Ms Tanner remained of the view that IIML as trustee was to reimburse the fund (see her email of 3 December 2015 in the chain), but it appears in the subsequent emails other management personnel decided not to take any further action in respect of losses associated with the Bendigo matter (contrary to what was reported in the Group Compliance Report to the RCC earlier on 23 September 2015). There is no evidence, or any allegation, that Mr Venardos was aware of this until late 2018.

On 15 August 2018, in response to questions asked by Mr Venardos (who by this time had been appointed as the Chairman of IOOF Hold Co), Mr Vine sent Mr Venardos an email informing Mr Venardos that the general reserve had been used to compensate losses in respect of the Bendigo matter. There is no evidence that, prior to this email, Mr Venardos was aware that IIML may not have reimbursed the loss as he was informed would occur by the Group Compliance Report to the RCC on 23 September 2015.

Subsequently, Mr Riordan prepared a paper to the IIML board dated 23 October 2018 confirming that “the investment loss for this matter remains in the investment trading reserve account and needs to be cleared through the payment of a good value claim (GVC), to be funded from IIML’s corporate account.” On 25 October 2018, the board of IIML (which included Mr Walsh as Chairman, Ms Flynn, Mr Selak, and Mr Venardos) resolved that IIML would reimburse the reserve in relation to the Bendigo matter.

786 The second respondent’s submissions relied on these matters to state that:

Accordingly, even if there was a Bendigo Compensation Plan as alleged by APRA (which is not admitted and has not been established), the evidence is clear that Mr Venardos was not aware of the alleged Bendigo Compensation Plan and therefore did not consider it, and could not have been required to take any steps to revoke or amend it. Shortly after it was identified in late 2018 that IIML had not reimbursed the loss (despite all contrary indications in the Group Compliance Report), the board of IIML resolved that IIML would replenish the reserve.

This is a complete answer to the claims against Mr Venardos in relation to the Bendigo matter.

787 It was further submitted that even if Mr Venardos had been informed of the Bendigo Compensation Plan on 23 September 2015, APRA’s claims against him would fail. This was because the RCC had limited powers and, in particular, no power to revoke or amend decisions made by management. This is why the Group Compliance Report was for noting rather than decision. The submissions continued:

Consistent with the decisions relating to the Bendigo matter being made without any approval or decision of the board of IIML (or the RCC, which could not have made such a decision in any event), the amount of $114,000 was well within the delegated authority of management for compensation claims.

Viewed in their proper factual context as outlined above, the allegations at ASOC [207] that Mr Venardos should have caused management to seek independent legal advice as to whether IOOF Service Co or IIML was liable for the loss or instructed management to cause IIML to replenish the reserve should be dismissed (even leaving aside the fact that as far as Mr Venardos was aware IIML was to reimburse the loss, making these allegations misconceived from the outset).

###### 16.7 Discussion

788 It is difficult to say more than that I accept the entirety of the respondents’ submissions about the alleged Bendigo breaches.

789 APRA’s case again appears to assume that it is sufficient to establish the fact of an error and loss. Without any detailed analysis of the relevant context and circumstances, APRA proceeds on the apparent assumption that the fact of an error and loss necessarily involve a breach of the due care covenant. APRA then relies on internal reporting documents which identify a cause of the error as admissions, but these documents are invariably also expressed at a high level of generality, without any detailed consideration of the context. APRA also relies on the legal conclusions expressed by the authors of those documents to the effect of breach of the due care covenant. However, as the respondents submitted, evidence to this effect cannot prove the fact of breach of any of the covenants. At best it proves that the author of the document considered there to be a breach but it is not apparent that the opinion of the author can constitute an admission. Even if it could constitute an admission, the documents are expressed at such high levels of generality that they are not reliable evidence of the existence of breach of the due care covenant which requires a detailed factual analysis of why it is said, in the particular circumstances of the case, the trustee failed to measure up to the relevant standard of care. APRA has never provided an analysis of that kind. Its case is free from the kind of detail one would expect to prove breach of the statutory covenants including proof of the details of the systems in place, the reasonableness of those systems, the foreseeability or otherwise of the kind of error that was made, the materiality of the error, and what measures could have been taken reasonably at the time to prevent the error. As the respondents submitted, APRA’s approach is tantamount to imposing a standard of perfection on the trustee so that, in effect, it becomes an insurer for all loss. This approach is wrong in principle.

790 Without repeating the respondents’ submissions the following points can be made.

791 APRA’s case depends on the contentions that the services provided by IOOF Service Co were defective, deficient and not fit for purpose and IIML did not have adequate systems and processes to correct and detect errors. APRA, however, provided no detailed analysis of the systems that were in place relevant to the Bendigo transaction. It did not explain why the services were defective, deficient and not fit for purpose. Instead, it relied on the fact of the error as if that fact alone established its case for it. A case of the kind APRA brings cannot be proved in this way.

792 As the respondents pointed out, APRA gave no consideration to the context of the Bendigo transactions. That is, that they were transactions out of the ordinary course which required manual calculations, inputs and adjustments. APRA did not explain why the specific failure that occurred, that the calculations did not allow for the payment of a defined benefit to a member during the window within which the transaction was being processed, made the system defective, deficient and not fit for purpose. APRA’s reliance on the earlier April Bendigo incident, as the respondents said, provides no support to APRA’s case because the officers were alive to the need for due care and caution but were caught out by an unforeseen event. The real issue would be whether that specific event (the pay out to one member at the time of the transaction) was reasonably foreseeable in all of the circumstances and should have been foreseen by the prudent superannuation trustee. This, however, is a question which APRA’s submissions did not address. APRA’s submissions operate at a much higher, and unhelpful, level of generality.

793 APRA’s case also treated the step taken to move the accidental sale from the defined benefits assets to the IPS general reserve as if it were a compensation plan. It was a decision taken on the day to remove any loss attributable to the assets held on behalf of the defined benefit members. That is, the step was taken immediately in the best interests of those members. As such, APRA’s case that the actions taken on the day the error was discovered were in breach of the best interests and no conflicts covenant is misconceived. As the respondents submitted, APRA also did not explain how any fact or matter could have given rise to an actual conflict of interest capable of having a significant impact on the way in which IIML approached the issue of compensation for the Bendigo incident in June. I accept the respondents’ submissions that the no conflicts covenant is necessarily about actual conflicts of interest which objectively exist and which are capable of having a significant impact on the performance of the duties of the trustee in accordance with members’ best interests. APRA’s approach to the no conflicts covenant, however, involves mere assertion of the existence of conflicts in theory without any of the analysis required to establish the existence of an actual conflict of the requisite kind.

794 APRA’s case about there being no practical difficulty in making a claim against IOOF Service Co faces all of the usual complexities which have been explored elsewhere in these reasons for judgment including the existence of the mutual obligations of IIML and IOOF Service Co and the mutual indemnities, as well as the characterisation of the loss as direct or indirect and consequential. The respondents’ case that the loss is clearly indirect and consequential is persuasive, thereby placing another practical and legal difficulty in the path of any claim against IOOF Service Co. As the respondents also submitted, APRA has not explained why a response of a potentially difficult claim against IOOF Service Co would be seen as being in the best interest of members as against the immediate restoration of the members’ position using the general reserve in an entirely permissible manner.

795 APRA’s case again appears to involve the proposition that all potential claims against entities who might have had some responsibility for the error had to be “exhausted” before there could be recourse to the general reserve in order to comply with the best interest covenant. I do not accept that approach as a matter of principle. The respondents have well and truly proven the legal difficulties which would have bedevilled any attempt to hold IOOF Service Co liable for any error given the complex terms of the service arrangements. In those circumstances it could not be said that anything would be gained by exhausting consideration of potential claims against IOOF Service Co before accessing the general reserve which was available for the purpose for which it is used and immediately rectified the loss.

796 The case against Mr Venardos in respect of the Bendigo incident, it has to be said, is hopeless. The RCC (and thus Mr Venardos) was clearly and unambiguously informed that IIML as trustee would be reimbursing the loss. Having been told that, Mr Venardos had no reason to believe otherwise or to consider a claim against IOOF Service Co or to take any steps to revoke or amend the Bendigo Compensation Plan. The proposition that Mr Venardos had to do more and ask when IIML as trustee would reimburse the loss goes too far. A clear statement was made that it needed to be done and Mr Venardos had every right to rely on the report as clear evidence that IIML as trustee would be reimbursing the loss. Accordingly, Mr Venardos did not consider the Bendigo Compensation Plan or know anything about it until 2018. To the contrary, Mr Venardos was told and must have believed that the Compensation Plan would involve reimbursement by IIML as trustee. The circumstances that existed provided no basis calling for Mr Venardos to second-guess what he had been told.

797 APRA’s case on the Bendigo breaches of the statutory covenants must fail.

##### 17. THE OPTUS SFT ALLEGED BREACHES

###### 17.1 APRA’s case – background facts

798 APRA explained that the alleged breach concerned a decision by Mr Kelaher as a delegate of IIML to reject a proposed successor fund transfer (**SFT**) of Optus’ employee default superannuation arrangements from IPS Super to AMP Superannuation Savings Trust (**AMP**) in February 2015 without giving genuine consideration to whether the proposal may have been in the best interests of beneficiaries.

799 APRA explained that:

An SFT involves the transfer of members and assets of one superannuation fund into another superannuation fund. At the time, the Superannuation Industry (Supervision) Regulations 1994 (Cth), r 1.03 (“successor fund”) and 6.29(1)(c) provided that a successor fund transfer could only occur where:

(a) The successor fund conferred on the member equivalent rights to the rights that the member had under the original fund in respect of the benefits; and

(b) Before the transfer, the trustee of the successor fund had agreed with the trustee of the original fund to confer upon the member equivalent rights to the rights that the member had under the original fund in respect of the benefits.

While these provisions allowed for SFTs, the power to transfer member benefits ultimately derived from the terms of the trust deed. Clause 18 of the IPS Trust Deed dealt specifically with transfer of beneficiaries’ benefits to a new fund: CB 4/37 (p. 699). Those provisions allow for the termination of an employers’ participation in the fund (cl 18.2) and gave IIML a discretion as to whether to transfer the beneficiaries’ benefits to the successor fund “in any other circumstances the Trustee determines” (cl 18.4).

800 According to APRA, Mr Kelaher, as in *Finch v Telstra* at [30], was required to form an opinion as an ingredient in the performance of a trust duty. APRA continued:

For such purposes, he was required not to knowingly exclude relevant information from consideration in the performance of the trust duty, and where there was conflicting bodies of material or insufficient material, his duties of care skill and diligence required that relevant information be sought: *Finch v Telstra Super Pty Ltd* (2010) 242 CLR 254; [2010] HCA 36 at [30], [43], [55]-[56], [66]. As their Honours observed in *Finch*, “the duty of trustees properly to inform themselves is more intense in superannuation trusts in the form of the Deed than in trusts of the *Karger v Paul* type”: at [66].

801 Further, in forming that opinion, APRA said Mr Kelaher was bound to comply with his s 52A covenants and to manage “the obvious conflicts of interest”.

802 According to APRA, the relevant background facts are these, taken from APRA’s written submissions.

803 In late 2014, Optus put its default employee superannuation arrangements out to tender: CB 5/54B, p. 1329\_0012.

804 At the time, Optus was IPS Super’s largest employer plan in terms of total member benefits: ASOC, [290]; admitted IIML and Questor Defence, [290].

805 By January 2015, it was apparent IOOF was unlikely to win the tender. Mr Kelaher told the IOOF Hold Co board that:

…the impact is not financially material, rather the ability to reference Optus, a brand name, as one of our clients…there would not be a successor fund transfer rather a move member by member.

806 In a paper created in February 2015 within IOOF it was said that:

It was disappointing to be notified during the month that we lost both Optus ($600m) and…

Despite the loss, it is not expected that we will see any bulk transfer of funds. Optus have requested a bulk transfer of their plan (SFT) however we are not legally obliged to comply with this request. Our focus now turns to engaging with those members and ensuring they are fully aware of the implications of any move to AMP.

807 On 2 February 2015, Optus wrote to IIML requesting an SFT of its employees’ default super arrangements to AMP: CB 6/85 (p. 1704). That letter said:

…we confirm we have decided to transfer our default superannuation arrangements from IOOF to AMP, via a successor fund transfer. Our expectation is that all parties will work together to ensure the transfer occurs as soon as practicable, at a time which is mutually agreed upon, with minimal impact on the Plan’s members.

We understand that you intend to move all Accrued Default Amounts (ADAs) to the MySuper option with effect from mid May 2015….

We request that you do not move Optus member assets into the MySuper option, as we believe our members will suffer from the multiple significant short term charges to their investment strategy.

808 On 10 February 2015, IIML replied to Optus’ letter: CB 6/88 (p. 1714). In that letter, IIML said:

IOOF Investment Management Limited as Trustee declines to accept your request to successor fund transfer (SFT) member accounts.

As we have always done over the past 13 years for Optus employees, the Trustee places paramount importance on protecting the rights of its members and acting in their best interests. Transferring superannuation accounts without member consent is a matter of utmost sensitivity for the Trustee and requires careful attention.

It is, inter alia, for these reasons that the Trustee has decided to allow Optus members to choose for themselves which fund they prefer for their ongoing employer superannuation contributions, as is their statutory right.

We are of the opinion that Optus members will only be able to make a fully informed decision once in possession of the necessary comparison information from both the Trustee and AMP about the respective superannuation plans.

Any individual transfer requests that the Trustee receives from Optus members will be processed in accordance with our standard transfer procedures.

Finally, please note we have decided to delay the transfer of the Optus Plan ADAs to IOOF MySuper until around August 2015. We trust this will give our members more time to properly assess their options with regard to their super arrangements.

809 APRA said that three things should be noted about this letter:

First, it did not request further information from Optus regarding AMP’s offering so that it could complete its equivalency of rights assessment; it rejected the proposed SFT. Second, IIML proposed to allow beneficiaries to make their own decision as to whether to leave the IPS Super. Considering these were default superannuation arrangements, that is, the fund that Optus employees were put into if they did not make a choice as to which fund they wanted to use, it was likely that the upshot of this proposal would be that IIML maintained most existing Optus employees within its fund. This is why Kelaher told the Board the “impact is not financially material”. Third, it did not acknowledge that the effect of not transferring beneficiaries’ existing balances would be that beneficiaries who did not nominate to remain with IIML would end up with multiple superannuation balances (and potentially incur additional fees because of this). As recognised in cl 18.3 of the IPS Trust Deed, once Optus withdrew as a participating employer, it could no longer make contributions to IPS Super (cl 18.3.2: CB 4/37, p. 700).

810 APRA noted that in their defences, Mr Kelaher and IIML have each admitted that the decision to decline the Optus SFT proposal was made by Mr Kelaher as delegate of IIML on or around 10 February: Kelaher and IIML Defences, [293].

811 APRA continued:

On 24 February 2015, APRA sought a copy of any paper setting out the reasons for not agreeing to the SFT and was told by Vine that there was no such paper: CB 6/93 (p. 1725). It was suggested at this time, and may still be part of IIML and Kelaher’s defence, that the reason for rejecting the SFT was because of the capital gains tax (CGT) implications for beneficiaries. The only document recording any CGT advice that has been produced, however, is an email from Ms Pam Roberts, IOOF Technical Services Manager, to Mr Mark Mittleman and Ms Clarke on 11 February 2015:   
CB 6/89A (p. 1715\_0001). That was one day after Kelaher rejected the SFT. The analysis in that email was also inconclusory. It concluded: “It is doubtful rollover relief would not apply to the transfter [sic] of the default members MySuper account and their ADAs”. Nor is there any evidence that, to the extent this was a relevant consideration taken into account, that that consideration was weighed against the detriment to beneficiaries of potentially having multiple accounts.

At a further meeting with Riordan and Vine on 10 March 2015, APRA queried IIML as to why the Optus SFT had been declined. When asked why IIML had not asked for additional information, APRA was told that it was not IIML’s responsibility to do so: CB 6/110 (pp. 1790-1791).

Considering that unsatisfactory responses it was receiving from IIML as to the reasons for the rejection of the Optus SFT, APRA issued a notice to produce any documents relating to the decision pursuant to s 255 of the SIS Act. IIML responded on 31 July 2015: CB 9/158 (p. 2517). In response to the category seeking:

“Documents and records recording the discussions within IIML concerning the Optus request between 2 February 2015 and 10 February 2015”

IIML responded:

“…there are no relevant documents and records recording internal discussions. This is because, as explained in our covering letter, IIML declined Optus’ initial request on the basis that relevant information had not been made available for IIML to consider and enable it to perform the required equivalency analysis. IIML remains open to considering Optus’ request if appropriate information is forthcoming. IIML is currently awaiting that information.”

In response to another category seeking:

“Documents and records that were reviewed by IIML in order to make a decision on the Optus request”

IIML enclosed the email from Ms Roberts dated 11 February 2015 and responded:

“No additional documents and records were reviewed.”

In light of the fact that the email from Ms Roberts was sent after IIML had notified Optus of its decision, the effect of this response to APRA’s notice to produce was that no documents had been reviewed prior to IIML rejecting the SFT, and no documents had been created recording the reasons for why that decision was made at the time.

On 12 September 2015, Vine wrote a further letter (on behalf of IIML) to APRA disputing any inappropriate conduct with respect to the Optus SFT proposal:   
CB 10/185C (p. 3106\_0004). In that letter (at p. 3106\_0005), Vine asserted that:

“The decision referred to was made on behalf of IIML by Christopher Kelaher, Managing Director of the IOOF group, and he was acting within the scope of his authority as a director and delegate of the IIML Board in making that decision. Therefore, the making of this decision did not require Board minutes or records recording internal discussion on the issue.”

###### 17.2 APRA’s case – Mr Kelaher’s alleged breaches

812 APRA said that its case is that Mr Kelaher:

…breached his obligations under ss 52(2)(c) and (d) of the SIS Act by making the decision as delegate of IIML without ensuring beneficiaries’ best interests were promoted, in circumstances of clear and obvious conflict. That conflict was the conflict between Kelaher’s interest (as shareholder) and duty (as Managing Director of the IOOF Group) in promoting the financial interests of the IOOF Group. Kelaher’s duty to consider the Proposed Optus SFT solely from the perspective of beneficiaries’ best interests, as required by s 52A, was in conflict with these interests and duties.

813 At ASOC [301] APRA pleaded that Mr Kelaher did not comply with his obligations under s 52A because he:

(a) was aware or ought to have been aware of IIML’s and his own conflicts of interest in making the decision;

(b) did not identify IIML’s or his own conflicts of interest in making the decision;

(c) did not manage the conflicts in accordance with the IOOF COI Policy by ensuring that the decision was not made solely by him without reference to the Board of IIML and was properly documented;

(d) did not acknowledge that beneficiaries of a default superannuation fund have not made a choice to be in that fund and that accordingly allowing such beneficiaries to choose which fund to join was not necessarily in their best interest;

(e) did not assess the comparative benefits of IPS Super and AMP to determine whether the transfer was in the best interests of members;

(f) to the extent that he formed the view that he had insufficient information to make the assessment in the preceding paragraph, did not request further information from Optus or AMP about the proposed superannuation arrangements to make that assessment;

(g) did not document any consideration or analysis to support the decision to approve or decline the proposed transfer.

814 APRA said that it had clearly pleaded that the process by which Mr Kelaher had made the decision was deficient and founded the breach of the s 52A best interests and no conflicts covenants. It said that given the paucity of documents and the fact that Mr Kelaher had not given evidence, the Court would not infer that he had made the decision in the best interests of members but should find instead that he made the decision “without taking any of the steps required by s 52A(2)(d), SPS 521 or IOOF’s own COI Policy (which Kelaher was required to ensure was complied with in accordance with SPS 521)”.

815 APRA said:

(1) “APRA’s case is not that Kelaher should have agreed to the SFT. Its case is that in making the decision to decline it, he should have complied with the conflicts covenants in s 52A(2)(d).”

(2) “APRA’s concern is not the speed of the decision; it is the complete absence of any consideration of the conflicts of interest involved and of the taking of any steps to ensure the decision was made in beneficiaries’ best interests despite the conflict.”

(3) “…the options available to IIML and Kelaher in February 2015 were not limited to Kelaher deciding to either accept or refuse the request, but included the options (which would have been in the best interests of beneficiaries, and which are expressly pleaded at ASOC [297]) of (a) seeking further information from Optus before making the decision, and (b) using a different decision-making process that was not compromised by the same kinds of conflicts which vitiated the process in fact used by IIML and Kelaher’s involvement in it. APRA’s case is that there was a range of possible conduct in respect of the Proposed Optus SFT which might have been capable of meeting the description of being in the ‘best interests of beneficiaries’, but the option IIML and Kelaher took was not one of them.”

816 APRA also said that Mr Kelaher’s conduct is to be imputed to IIML so that if the Court finds a breach of the s 52A covenants by Mr Kelaher, it follows that IIML breached the s 52 covenants.

###### 17.3 The respondents’ case

817 The fourth to seventh respondents submitted that the Optus’ request was misconceived because:

(a) it incorrectly assumed that there was power in the IPS Trust Deed for IIML to do what it was asking;

(b) it incorrectly assumed that IIML was obliged to act upon the request, including in the absence of any participating employer agreement; and

(c) it overlooked or ignored that, assuming there was in fact power to conduct an SFT, a trustee is required to undertake a detailed analysis of the “successor” fund as part of acting in the best interests of beneficiaries and in compliance with the SIS Regulations.

818 They submitted that the trustee’s conduct was not to be judged by reference to Optus’ misguided approach from the outset. In support of this proposition they said by way of summary:

(a) No relevant power, or duty: There was no power under the IPS Trust Deed to comply with Optus’ Request and, even if there was such power under the deed, there was no duty operating to require IIML to automatically agree to conduct a SFT, either under statute or contract. While the question of power is to be viewed objectively – did IIML as Trustee have power under the IPS Trust Deed to effect an SFT in the manner requested by Optus? –it is significant that the Board later received independent legal advice that the IPS Trust Deed would require amendment to give effect to Optus’ Request;

(b) Equivalency of rights analysis is required: The power, or capacity of IIML to conduct an SFT was conditioned upon being satisfied that the ‘successor’ fund had the requisite characteristics of conferring on members “equivalent rights to the rights that the member had under the original fund in respect of the benefits”. In practical terms, this requires the incumbent trustee (IIML) to engage in a comprehensive “equivalency of rights” analysis between the benefits its fund confers, in comparison with the benefits of the successor fund (AMP). APRA’s claim that IIML “rejected the Proposed Optus SFT” in its letter dated 10 February 2015 is thus a fundamental mischaracterisation of this exchange of letters, and it ignores the requirements imposed upon IIML under the regulatory regime;

(c) SFTs occur in the absence of member consent: If a SFT is permitted by a particular trust deed and is to be considered, the rationale for the imposition of the heavy onus and responsibility on IIML by the statutory regime is made plain when one has regard to the fact that the transfer is to occur in the absence of members’ consent. In a SFT, in place of individual member consent, what the trustee is effectively doing is making the choice for members as a whole as to what will be in their best interests. “Best interests” in this context are likely to be synonymous with “best financial interests”. The trustee is authorised under the statutory regime to make this important choice on behalf of members;

(d) IIML’s demonstration of what was in fact required in order to consider an SFT: What was in fact required in order for IIML to appropriately consider whether a SFT was both (i) permitted under the deed and the SIS Regulations; and (ii) additionally, in the best interests of members in all the relevant circumstances, is clearly reflected in the Board papers, which were provided to APRA by email dated 4 November 2015. This makes it plain that IIML was acting consistently with its responsibilities as trustee in the events leading up to its response to Optus’ Request in February 2015 (and throughout the process, culminating in the submission to the Board in October 2015). It also makes it plain that Optus was completely unaware of what those responsibilities were and that the approach set out in Optus’ Request was wholly misconceived from the beginning;

(e) Statutory scheme contemplates the co-existence of SFTs and compliance with the no conflicts covenant: The statutory regime makes provision for SFTs, which will – by their very nature – always raise issues of a potential conflict of interests. The regime nevertheless makes provision for such a “bulk” transfer, conditioned upon the satisfaction of the incumbent superannuation trustee as to the equivalency of the successor fund. The covenants in s 52 of the SIS Act are cumulative (not discrete), and in determining any particular course of action, one or more covenants may be engaged, particularly considering the ‘umbrella’ nature of the Best Interests Covenant. In the present case, IIML simultaneously acted consistently with its duties under the Best Interests Covenant and the no conflicts covenant in its approach to considering the proposed Optus SFT. In circumstances where the trustee is mandated to have the beneficiaries’ interest as its paramount concern, the law has predetermined the resolution of any potential conflict; and

(f) No ‘actual’ conflict relevantly arises: APRA fails in pointing to any interest that could have had a ‘significant’ impact on the manner in which IIML approached Optus’ Request. An ‘actual’ conflict has to have crystallised before consideration of the no conflicts covenant even arises.

819 In response to APRA’s proposition that Mr Kelaher (and thus IIML) were bound not to knowingly exclude relevant information and in the event of conflicting or insufficient information had to seek out relevant information, by reference to *Finch v Telstra*, the fourth to seventh respondents submitted that cl 18 of the trust deed, and the steps it requires if an employer leaves the fund, are not analogous to the core trust duty considered in *Finch v Telstra* of the making of a distribution to a beneficiary. The submission continued:

An examination of the origins of the principle that a superannuation trustee must give properly informed consideration to a beneficiary’s claim for benefits makes it plain that the proposition arises in respect of trustee duties directed towards determining the benefits to be accorded to beneficiaries under the terms of the trust:

(a) In *Kerr British Leyland (Staff) Trustees Ltd* (*British Leyland*), decided by the Court of Appeal on 26 March 1986 and reported in [2001] WTLR 1071, it was held at 1079 that in considering a claim for a disability payment, in circumstances where the trustee did not have the relevant medical evidence before it, “the power of the trustee to decline acceptance of the claim cannot simply be an uncontrolled discretion”, but rather that “the duty of the trustee was to give properly informed consideration to the application”, where the information “might materially have affected their decision”.

(b) In *Stannard v Fisons Pension Trust Ltd* [1992] IRLR 27 (*Stannard*), citing *British Leyland*, it was held that in determining the amount to transfer in respect of exiting beneficiaries the trustees “should … have given consideration to the current value of the trust fund and its implications”. The trustees owed a duty both to the transferring members and the contributing members. A failure to consider the value of the fund as at the transfer date and its implications for the quantum of the transfer amount was a failure to “give properly informed consideration” (at 31).

(c) In *Finch*, by reference to both *British Leyland* and *Stannard* at [66] (and footnote 55), the High Court noted that the decision of a trustee may be “reviewable” in the absence of “properly informed consideration”. In that context, the High Court observed at 280 [66] that it “is extremely important to the beneficiaries of superannuation trusts that where they are entitled to benefits, those benefits be paid” and, further at 281 [66] that a “beneficiary is entitled as of right to a benefit provided the beneficiary satisfies any necessary condition of the benefit”. In the context of the particular deed in issue in Finch, the High Court also noted at [66] that there was both a power and a duty to take into account “information, evidence and advice the Trustee may consider to do so”.

(d) In *Alcoa of Australia Retirement Plan Pty Ltd v Frost* (2012) 36 VR 618 at [60] (Nettle JA; Redlich JA agreeing at [74] and Davies AJA agreeing at [76]), the Court of Appeal of the Supreme Court of Victoria held, including by reference to *British Leyland* and *Stannard*, that “[s]uperannuation fund trustees are bound to give properly informed consideration to applications for entitlements and, if that necessitates further inquiries, then they must make them”. The Court of Appeal acknowledged the qualification at [60] that it may be that “a trustee is not required to undertake any inquiries until and unless a claimant puts forward sufficient material to show that there is a case to be investigated”. Justice Nettle regarded it as an open question whether *Finch* “decided no more than that the trustee was under a duty to seek relevant information in order to resolve conflicting bodies of opinion” (at [41], and see also [47]).

820 According to the fourth to seventh respondents, APRA made no submissions as to why the principle should be extended beyond a duty to be properly informed when considering an application for a beneficiary’s entitlement in accordance with the terms of the trust. In particular, they said APRA “does not point to any feature of cl 18 of the IPS Trust Deed which identifies an obligation to conduct a wholesale SFT such that there is any duty comparable to the duty to make a payment to a beneficiary…[t]he principles in *Finch* address an entirely different set of considerations, and are not relevant in assessing the conduct of the trustee in relation to its response to Optus’ Request”.

821 Further, when IIML received the Optus letter on 2 February 2015 it was not faced with any conflicting material – it had no material bar the request whatsoever.

822 **As to IIML’s statutory duty**: APRA’s claims assumed that if IIML receives a request to bulk transfer members it:

(a) must not decline the request, in the absence of first initiating and engaging in a detailed consideration of all of the rights and benefits of a member, clause by clause, under the terms of each fund (Equivalency of Rights Analysis);

(b) must, if the party requesting the transfer fails to provide the necessary information to enable a SFT to occur, point that deficiency out and inform the other party as to what information it needs to provide.

823 This, said the fourth to seventh respondents, is not the position which applies under superannuation law. However:

[r]ather than requiring a trustee to consider and facilitate a SFT, the regulations provide that a SFT “must not” occur unless certain detailed and specific conditions are met in order to ensure the “successor” fund offers equivalent rights and that members (whose consent is not a requirement for this process) are not disadvantaged. Only upon the satisfaction of these requirements does the regulatory regime permit a SFT to take place.

824 As the fourth to seventh respondents’ submissions explained:

The term “successor fund” is defined in r 1.03 of the *Superannuation Industry (Supervision) Regulations 1994* (Cth) (**SIS Regulations**) in the following terms (emphasis added):

“successor fund, in relation to a transfer of benefits of a member from a fund (called the original fund), means a fund which satisfies the following conditions:

(a) the fund **confers on the member equivalent rights** to the rights that the member had under the original fund in respect of the benefits;

(b) before the transfer, the trustee of the fund has agreed with the trustee of the original fund that the fund **will confer on the member equivalent rights** to the rights that the member had under the original fund in respect of the benefits.”

825 Accordingly, an equivalency of rights analysis is necessary in order to decide whether a prospective superannuation fund meets the statutory test of a “successor fund”.

826 The fourth to seventh respondents continued:

With the definition of “successor fund” set out in s 1.03, r 6.29 of the SIS Regulations then sets out “general rules” for a SFT. Regulation 6.29 falls within Division 6.4 (“*General Rules for Rollover and Transfer Of Benefits in Regulated Superannuation Funds and Approved Deposit Funds*”) in Part 6 (“*Payment Standards*”) of the Regulations.

Within this framework, r 6.29 relevantly provides that these “general rules” are as follows:

Except as otherwise provided by the [SIS Act], the Corporations Act 2001, the Corporations Regulations 2001 or these regulations, a members’ benefits in a fund must not be transferred from the fund unless:

(a) the member has given to the trustee the member’s consent to the transfer; or

…

(c) the transfer is to a successor fund.”

827 The fourth to seventh respondents said:

Taken together, rr 1.03 and 6.29 impose restrictions or conditions which, unless satisfied, prohibit a trustee from undertaking a SFT. These provisions do not, on any view, oblige a trustee to undertake a SFT upon receipt of such a request, without more. APRA’s attempt to convert these conditions, which govern the capacity to undertake an SFT, into positive obligations to commence the Equivalency of Rights Analysis at any time a request is received is not supported by the legislative framework for SFTs, and would be an unworkable process which the legislators have not adopted.

828 **As to IIML’s contractual duty**: Optus and IIML were agreed as to the fact that there was no contractual obligation upon IIML to agree to and process the SFT.

829 **As to IIML’s power under the trust deed**: the fourth to seventh respondents said:

IIML was not empowered by cl 18 of the IPS Trust Deed to conduct an SFT in accordance with Optus’ Request. As APRA acknowledges at ACS at [522], while the SIS Regulations allow for SFTs, one has to look to the terms of the trust deed for any relevant power.

Consistently with this capacity conferred under the SIS Regulations, cl 18 of the IPS Trust Deed provides for a ‘Successor Fund transfer’, defining ‘Successor Fund’ in clause 28.1 of the Deed in the same way as r 1.03 of the SIS Regulations, such that the same conditions apply in relation to equivalency.

However, cl 18 deals with the transfer of benefits to a new fund on the basis of two different scenarios:

(a) upon a member’s request (thus, evidently, with their consent) (cl 18.1); and

(b) upon the withdrawal of an employer from the fund (cl 18.2).

In relation to the second scenario, cl 18.3 addresses the effect on members in the event of such a withdrawal and it expressly contemplates that: (i) the member “may remain a Member of the Fund”; or (ii) may request to “transfer the remaining part of the Member’s Benefit in accordance with clauses 18.4”. It is only then – after such an election by the member has been made – that the IPS Trust Deed contemplates the transfer of any remaining benefits to “a Successor Fund”, by way of a bulk transfer. This might be described [as] the power to conduct a partial or residual SFT.

830 In this regard the fourth to seventh respondents noted that “IIML ultimately received legal advice, before its submission was put to the Board on 29 October 2015, that the IPS Trust Deed did not in fact permit the method of successor fund transfer that Optus had demanded, and that amendments to the Trust Deed would be required in order to facilitate any such SFT”. As summarised in the board minutes, “the Optus Plan division rules would need to be amended in order to facilitate an SFT in these circumstances”. Evidently, “this is not a matter which had stopped IIML from giving due consideration to whether the proposed SFT was in the best interests of Optus members and should be undertaken (which would have required amendments to the trust deed) when it received from AMP the information it required to consider that issue).”

831 As a result the fourth to seventh respondents submitted:

Accordingly, in light of the position under the statutory scheme, the absence of any contractual obligation and the lack of power under the IPS Trust Deed, IIML denies that it could lawfully have undertaken the SFT in the circumstances. Objectively, there can be no breach in respect of a failure to exercise a power that the trustee simply did not possess. There can certainly be no “trust duty”, upon which might hinge a requirement to be properly informed. APRA’s claim can go no further.

Even assuming IIML might otherwise have been entitled to carry out the SFT (which IIML denies for all the reasons set out above), neither Optus nor AMP had provided IIML with the necessary information to enable IIML to determine whether an SFT could be carried out consistently with the SIS Regulations and the detailed guidance provided in Circular I.C.4. Whether this is characterised as an improper request, or insufficient to enliven any “duty” to enquire, there was simply nothing more for IIML to act upon at that stage.

The kind of information that would have been necessary to identify the advantages and disadvantages to Optus members of the SFT proposed in Optus Request, would have included the following information:

(a) details of the proposed AMP fund;

(b) information as to the rights and benefits Optus members would receive in the proposed AMP fund;

(c) a copy of the relevant trust deed for the proposed AMP fund;

(d) a copy of insurance policies relating to the proposed AMP fund;

(e) product disclosure statements and associated reference guides; and

(f) fund audit reports and risk management plans relating to the proposed AMP fund.

Accordingly, IIML says that, as at 10 February 2015, IIML did not have sufficient information to enable it to determine and be satisfied as to whether the proposed SFT would be permissible and in the best interests of beneficiaries. This is particularly so in circumstances where the little information that was in fact known to IIML at the time, indicated that members would not have been better off with AMP.

832 Further, in its defence IIML contended that as at 10 February 2015 it had:

(a) formed the view that it was likely that an SFT would cause many Optus members to incur a material CGT liability which they would not otherwise incur if a SFT was not undertaken; and

(b) formed the view that it would not be in the best interests of Optus members to undertake an SFT unless the identified adverse consequences to Optus members were outweighed by other benefits of the SFT.

833 Before 10 February 2015 IIML had corresponded to Optus:

(a) that IIML could only undertake a SFT if it was in the best interests of members to do so and if IIML had first undertaken an equivalent rights analysis and was satisfied that the transferee fund would confer equivalent rights to the rights conferred on members by the IPS Super fund; and

(b) that the effect of regs 1.03 and 6.29(1)(c) of the SIS Regulations was to restrict the circumstances in which an SFT could occur, and to require consideration of various matters before an SFT could be undertaken.

834 The fourth to seventh respondents provided a chronology of the communications between IIML and Optus before February 2015 in which, amongst other things, Optus was advised on 10 September 2014 that:

Under super law, the trustees must act in the best interest of members. S. 52. Decisions must be made in the best interest of members. The decision the trustees will need to make is “is a transfer out of OPSSF of member’s benefits in the best interests of the members’ as a whole”. Where transferring out would incur the realisation of capital gains it is not in their best interests unless the damage is outweighed by other factors. Reduced costs. Cap gains is material because otherwise clients could transfer their benefits to pension phase and no CGT would apply. You have to model it. That is why it is so difficult to SFT out of a platform.

835 This, said the fourth to seventh respondents, undermined APRA’s suggestion that capital gains tax implications were a mere afterthought by IIML.

836 On 11 September 2014, IIML had explained in a further communication to Optus that:

Under super law, the trustees must act in the best interest of members. S. 52. Decisions must be made in the best interest of members. The decision the trustees will need to make is “Is a transfer out of the IOOF Portfolio Service Superannuation Fund (this incorporates Lifetrack and IOOF Employer Super) of member’s benefits in the best interests of the members’ as a whole.” Where transferring would incur the realisation of capital gains (this will be likely for many Optus members) it is not in their best interests unless the damage is outweighed by other factors i.e. reduced costs. As IOOF Employer Super and Lifetrack invest “direct” and not into PST’s, tax is calculated at an individual and not at a fund level. This is why an individual assessment needs to be made. Capital Gains is material because if the client stayed with IOOF they could transfer their benefits to pension phase and no CGT would apply.

This requirement applies to all members in the plan both – choice and MySuper classified. However the trustees have heightened responsibility in relation to MySuper members. Section 29VN applies and each director of IOOF Investment Management Limited (IIML) Would have sign off on it 29VO. 29VN is about the financial interests of the beneficiaries on an individual basis. Very high step. Requires a lot of lawyers. 29VN Each trustee of a regulated superannuation fund that incudes a MySuper product must:

* (a) promote the financial interest s of the beneficiaries of the fund who hold the MySuper product, in particular returns to those beneficiaries (after the deduction of fees, costs and taxes);

The actual equivalent rights test for SFTs of a potential transition will be easier and less time consuming than insuring the transfer is in the best interests of the client.

What this means is that in addition to all equivalent rights analysis for each MySuper member we will have to look individually at each member to insure the transfer to another fund is in their financial interests and have this approved and signed off by our lawyers and trustees before the transition can occur. This will incur extra costs to many parts of our business involved in the transition over and above the $130,000 fixed fee you have requested.”

837 The fourth to seventh respondents also said that documents after 10 February 2019 disclosed that no final determination had been made and also cast light on the 10 February 2015 letter. Thus, they referred to:

(a) An email from Paul Vine to Kathleen Holloway (APRA), dated 5 March 2015, which made it patently clear that a final determination, on a best interests analysis had not yet been made, and that “[t]o date, we [IIML] have seen no information on the rights and benefits that will be conferred on members in the new AMP fund”;

(b) A letter from IOOF to APRA, dated 31 July 2015, which clearly stated that “IIML declined Optus’ request to successor fund transfer member accounts to AMP because no information had been made available to IIML to perform the equivalency analysis which it is duty bound to undertake in order to be able to assess whether the successor fund transfer was appropriate and in the best interests of members”; and

(c) A letter from IOOF to APRA, dated 21 September 2015, which again clearly reiterated the point that the “February Response was given because the SFT Request was not accompanied by sufficient information to justify the proposed SFT”.

838 The fourth to seventh respondents thus said that the deficiency existed in Optus’ request, and not IIML’s reply. That this is so is evident from subsequent events involving IIML, Optus and AMP. As the fourth to seventh respondents put it:

Optus and AMP re-engaged with IIML and provided the detailed information which was necessary to allow the parties to consider the proposed SFT in compliance with the regulatory requirements and conformably with the duties imposed on IIML as the incumbent trustee.

In their correspondence, Optus and AMP acknowledged that a SFT could only occur if that information was provided and analysed and an agreement reached about equivalency between the two funds. This was an implicit, but clear, recognition that the Optus Request was not made in circumstances that would have permitted IIML to consider, let alone undertake, a SFT.

When AMP and Optus in fact provided a proper SFT request with sufficient information to IIML, IIML engaged in a rigorous process to undertake the Equivalency of Rights Analysis. That process involved comparing equivalent rights and benefits under the terms of each fund, and identifying areas where the “successor” fund, being AMP, did not provide equivalent rights and benefits to members. This analysis was then subjected to external review by Holding Redlich. While Holding Redlich’s assessment reached different conclusions on some of the comparisons, the view that was ultimately formed was that there would need to be negotiation with AMP “to ensure equivalency” and that there was some uncertainty about how to manage the identified issues about “equivalency of investment options”, such that, if that issue could not be resolved, “then many of the remaining investment offerings through the AMP Fund may not be equivalent”.

That assessment ultimately established that IIML was not able to undertake a SFT, as the equivalency assessment demonstrated that members would not enjoy equivalent rights with AMP.

Following this exchange of material between Optus and AMP, on the one hand, and IIML on the other, the proposed Optus SFT was submitted to the IIML Board for consideration on 29 October 2015. The detailed Board Pack considered at that meeting and the minutes of the meeting recording the Board’s decision were provided APRA in an email from Gary Riordan to Kayleen Holloway on 4 November 2015. The IIML Board decided not to undertake the proposed SFT on the basis that it was not in the best interests of Optus Members.

839 **As to the alleged breach of the no conflicts covenant**: the fourth to seventh respondents submitted that the “statutory regime makes provision for SFTs, which will - by their very nature - always raise issues of potential conflict of interests”. They continued:

The regime nevertheless confers this power, which is conditioned upon a satisfaction of equivalency, on the incumbent superannuation trustee. The trustee is to make this decision on behalf of members, in the absence of their consent, and in their best interests.

The covenants in s 52 of the SIS Act are cumulative and not discrete, and in determining any particular course of action, one or more covenants may be engaged, particularly considering the “umbrella” nature of the Best Interests Covenant.

In the present case, IIML simultaneously acted consistently with its duties under the Best Interests Covenant and the No Conflicts Covenant in responding to Optus’ Request, and in its conduct thereafter (which, it is noted APRA does not challenge). IIML’s subsequent conduct demonstrates how it advanced the interests of the beneficiaries, notwithstanding any relevant interests of IIML or its related entities. This is succinctly captured in the Board Paper submitted by Vine and dated 16 October 2015:

“We note that the Trustee’s decision in respect of the SFT will be closely scrutinised by APRA and could result in further regulatory investigation. We also note the risk of legal proceedings being initiated against IIML by Optus in the event of a determination by the board that the SFT to AMPSS should not proceed. Neither of these matters should go towards compromising IIML’s duty as trustee to act in the best interests of members.”

In other words, it was in the face of anticipated problems (adverse to IIML’s own interests) that it considered the SFT and recommended that – in light of members’ financial interests being better served by remaining in the original fund with IOOF – the Optus SFT should not be approved.

840 Further, APRA had again failed to identify any interest that could have had a “significant” impact on the manner in which IIML approached Optus’ request. The fourth to seventh respondents said:

An “actual” conflict has to have crystallised before consideration of the No Conflicts Covenant even arises.

Critically, APRA does not grapple with the fact that as at February 2015, no power or duty had been enlivened in respect of which any conflict could relevantly arise. Similarly, APRA’s submissions do not take into account that when, after formal consideration of a properly framed request, the board did come to consider the SFT proposal, which was informed by independent legal advice and an Equivalency of Rights analysis, the Board considered this matter on 29 October 2015, the minutes record the following:

“The Chairman noted the potential for conflict of interest in that IIML being the trustee for the Optus Plan division of the IOOF Fund has common directors with its parent and holding company, IOOF Holdings Limited and the chairman requested that the Board consider the Proposal based on the recommendations of General Counsel and acknowledge the conflict and confirm that while acting as directors of IIML, directors must only consider the interests of Optus Plan and IOOF Fund members and no other interest, including the interests if IOOF Holdings Limited and its shareholders.

Resolved that the Board acknowledge the conflict of interest as between IIML as trustee of the IOOF Fund and IOOF Holdings Limited as its parent entity and further that the directors will only consider the interest of Optus Plan and IOOF Fund members and no other interest including the interest of IOOF Holdings Limited and its shareholders.”

841 The submissions for the first respondent also relied on the full chronology of the events in respect of the Optus SFT. The first respondent said by way of overview that:

The Optus SFT part of the case is hopeless and should never have been brought. Even up to the stage of final written submissions, APRA refuses to lay out the full narrative. The “decision” identified by APRA, upon a full understanding of the facts, was no more than an interim stance and was clearly subject to review upon receipt of further information. When that further information was received and considered a decision was made which is not suggested by APRA to be wrong. Indeed, as far as one can tell, it seems to be accepted by APRA that it was the correct decision. Its complaint is that the “decision” was not documented (which is obviously wrong because the “decision” is recorded in the letter advising of the decision) and that instead of declining the request Mr Kelaher ought to have asked for more information. This in circumstances where there is no obligation under the statute to request such information and, as the evidence shows, AMP acknowledged that IOOF did not have sufficient information in the first instance.

842 The first respondent submitted that:

…a surprising and troubling aspect of APRA’s case in relation to the Optus SFT is its attempt to analogise a request by an employer to complete a SFT with requests by members to the trustee to pay superannuation benefits in accordance with the terms of the trust. The latter is a fundamental duty of a superannuation trustee and at the core of that particular trust relationship. The former is a highly unusual request by a stranger to the trust, acting in its own economic interest. The two circumstances are not the same.

843 The relevant provisions of cl 18 (which APRA disputed operated in the way the respondents contend) are as follows:

**Effect on Employee Members**

18.3 In the event of the termination of the participation of an Employer in the Fund:

18.3.1 no further persons who are employed only by that Employer shall be admitted as Members;

18.3.2 no further contributions shall be made by that Employer except contributions that were due on or before the date of withdrawal;

18.3.3 subject to any insurance cover that may apply where a Member elects to transfer to division II, insurance cover shall cease for each Member employed by the Employer at the end of the period for which contributions made by that Employer are last made;

18.3.4 the Member may remain a Member of the Fund, in which case the Member will transfer to division II;

18.3.5 the Member may contribute to the Fund unless the Fund is not a public offer superannuation fund; and

18.3.6 the Member may request:

(a) payment of any part of the Member’s Benefits that may be paid in accordance with the Rules for Payment of Benefits; and

(b) transfer the remaining part of the Member’s Benefit in accordance with clauses 18.1 to 18.5.

**Transfer to Successor Fund**

18.4 Any other moneys and assets comprising the benefit of a Member that are not dealt with in accordance with clause 18.3 on a person ceasing to be a Member of the Fund or in any other circumstance the Trustee determines shall be transferred to a Successor Fund.

844 The first respondent noted that by the terms of cl 18 of the trust deed where an employer in the fund terminates its participation:

a) no new employees of that the employer will be admitted as new members (clause 18.3.1);

b) the employer ceases making financial contributions to the fund in respect of existing members (clause 18.3.2);

c) a member employed by that employer “may remain a Member” at their election, and make contributions to the fund (clauses 18.3.4, 18.3.5); and members employed by that employer “may request” transfer to a successor fund proposed by the employer (clause 18.3.6(b)); and

d) any other monies and assets comprising the benefit of a member that are not dealt with in accordance with clause 18.3, may be transferred to a Successor Fund.

845 The first respondent submitted that the proper construction of cl 18.3 and cl 18.4 of the IPS trust deed meant that members must be given the choice to remain in the fund in accordance with cl 18.3.4. As such, there was no power under the trust deed to complete the SFT as Optus requested. The trust deed required that members be given a choice as to whether to be transferred to AMP or not.

846 In respect of APRA’s disputation of this construction, I both prefer the respondents’ approach to the provision and note that, in any event, the position that was taken (and that was subsequently supported by legal advice) was objectively reasonable in all of the circumstances. Given this latter fact, it could not have been a breach of any of the statutory covenants for IIML to have proceeded on the basis that Optus’ request could not be actioned as proposed.

847 According to the first respondent, “that is the end of APRA's case in relation to the Optus SFT issue”.

848 The first respondent also made similar submissions to the fourth to seventh respondents about the question whether IIML was permitted by law to complete the Optus SFT. On the same basis the first respondent said that IIML was also prohibited by law from completing the Optus SFT until the equivalence requirement was satisfied.

849 The first respondent continued:

As noted above, APRA seeks to characterise a decision by a trustee to make a SFT as akin to a decision to whether or not a member is entitled to benefits, such as disability benefits, in accordance with the terms of trust (ACS [532]). That was a submission advanced by APRA in closing by reference to *Finch* and the decision of the Victorian Court of Appeal in *Alcoa of Australia Retirement Plan Pty Ltd v Frost* [2012] VSCA 238 (T154.37 – 157.10).

Like *Finch*, *Frost* was a case concerning the payment of total and permanent disability benefits. A decision by a superannuation trustee as to whether or not a member qualifies for such benefits is an incident of the superannuation trustee’s fundamental duty to pay member benefits as and when required in accordance with the terms of trust: see *Frost* [2012] VSCA 238 at [57].

A decision in relation to a SFT proposed by an employer is of an entirely different kind. It is a request made by a stranger to the trust who has no duty to act in members’ best interests. It is also a request fundamentally to change the terms on which members’ benefits are held. If a SFT is completed, members’ funds will be held on new terms by a new trustee. Unlike the decisions at issue in Finch and Frost, a decision in relation to a proposed SFT is not one with respect to a fundamental entitlement conferred by the terms of trust; it is unusual and exceptional decision which, if made in favour of granting the SFT, can radically alter the terms of trust.

Most critically, unlike the decisions in *Finch* and *Frost*, which were decisions that the trustee was compelled to make having regards to its obligations under the trust deeds, there was no obligation on IIML under either the SIS Act or the IPS Super trust deed to make a decision in relation to the proposed Optus SFT. The effect of r 6.29(1)(c) was that IIML could not make the SFT unless satisfied of certain matters but it was under no obligation to consider Optus’ request or to attempt to satisfy itself of those matters.

It is for this reason that the further observations of Nettle JA in *Frost* regarding the obligation on a trustee in certain circumstances to make further inquiries are inapplicable in this context: cf [2012] VSCA 238 at [58]ff. Those comments were made in relation to the trustee’s fundamental duty to determine if a member has an entitlement to claimed benefits. Nettle JA was not suggesting that, whenever a trustee is faced with a decision affecting the administration of a trust, the trustee is required to make further inquiries.

Indeed, in the SFT context, the obligation to make further inquiries would make no sense. Regulation 6.29(1)(c) operates where the trustee intends to make a SFT. In those circumstances, the default position is that a trustee cannot make a SFT unless satisfied of equivalency. There is no need for an obligation to inquire because a decision to complete a SFT simply cannot be made until the requisite degree of satisfaction is reached (whether by inquiry or otherwise). In this way, the legislation has an understandable default bias against a SFT being made.

Once these aspects of the law are recognised, APRA’s case with respect to the Optus SFT issue fails because IIML was not required by law to consider Optus’ request and was prohibited by law from completing it unless satisfied of equivalency. There is no dispute that IIML was never so satisfied and APRA appears to accept that IIML was correct in that regard (ACS [544]).

IIML had no duty to make inquiries or actively to seek to satisfy itself of equivalency. That is because there is no legal obligation requiring a trustee to consider making a SFT. If Optus wished to procure a SFT it was incumbent on Optus to provide IIML with such information as was necessary to meet the equivalency requirement in   
r 6.29(1)(c).

850 In providing the full chronology of events the first respondent referred to the report Mr Kelaher gave to the IOOF Hold Co board on 29 January 2015 recorded in the minutes as follows:

The Managing Director advised one low is the loss of the Optus account (Corporate Super) to AMP. It was noted the impact is not financially material, rather the ability to reference Optus, a brand name, as one of our clients. The Board noted Heron was appointed by Optus as their broker to facilitate the tender. The Managing Director stated management will conduct an examination to conclude the process. The Managing Director advised there would not be a successor fund transfer, rather a move member by member.

851 The first respondent submitted that while APRA sought to make much of the last sentence to prove some kind of pre-determination by Mr Kelaher, in fact:

a) First, at this point in time, Optus had not, in fact, requested a SFT. As a result, the most natural reading of Mr Kelaher’s statement is that he was reporting his understanding at the time. APRA made the mischievous submission in opening that the statement that the loss of the Optus account was not “financially material” might have been predicated on the fact that Mr Kelaher had predetermined not to approve a SFT (T63.4). That submission is repeated in APRA’s closing but the only evidence cited is a February 2015 Board paper (ACS [528]). That document was evidently prepared after Optus’ request for a SFT was made on 2 February 2015. There is no basis to infer from that later-in-time document that Mr Kelaher had predetermined the position in January.

b) Secondly, Mr Kelaher’s statement is entirely consistent with the requirements of clause 18.3 of the IPS Super trust deed, which required that members be given a choice as to whether to move to a new fund and which prevented IIML from simply completing a SFT without members’ consent; and

c) Thirdly, even if IIML had formed a view that a SFT would not be made if requested, the available inference in light of Mr Ferguson’s 11 September 2014 email is that such a decision was based on an appreciation of the fact that members would incur significant CGT liabilities if a transfer occurred.

852 As to the Optus request itself the first respondent noted that:

No further information was provided by Optus with this request. It did not identify the proposed new fund to which members were to be transferred. It did not identify the provider. It did not identify the terms of the new fund. And it did not address Mr Ferguson’s point regarding the CGT implications for fund members.

Notwithstanding all of these matters, Optus demanded an “urgent” response “by return email”. Given the terms of r 6.29(1)(c) of the SIS Regulations, the only lawful response that IIML could have given was “no”. That is because it could not possibly have been satisfied of equivalency in the circumstances. Any other “urgent” response would breach the law.

853 Further, the first respondent submitted that:

The very same day that Optus sent its formal request to IIML, and before IIML had responded, Ms Secombe [of Optus] called APRA. She told APRA that she was concerned that “IOOF would be difficult to deal with” in relation to the SFT. In that call, Ms Secombe frankly told APRA that “the equivalency of rights assessment has not been undertaken as yet”, and noted (as was the fact) that “IOOF had flagged a possible tax issue”.

The file note of Ms Secombe’s call to APRA is further contemporaneous evidence that IIML was already aware of the potential tax implications for members arising from the proposed SFT and that IIML had expressly raised that concern with Optus. It is also irrefutable evidence that IIML did not have sufficient information to enable it lawfully to comply with Optus’ urgent request. Ms Secombe told APRA that in terms.

854 The first respondent noted that:

Ms Secombe called APRA again on 4 February 2015 expressing “further concerns”. The APRA file note records that IIML advised Mr Secombe verbally that it was “not required to agree to an SFT and consider that the proposed SFT is not in members’ best interest”, but that Ms Secombe disagreed with that position because IIML had “yet to be provided with any information on which to form its view that the SFT was not in members best interest”. If Ms Secombe was right, the legal position was clear — IIML could not complete the SFT without contravening the SIS Regulations.

855 According to the first respondent:

IIML, of course, was completely correct that it was “not required to agree to an SFT” if it did not consider it in members’ best interests. Indeed, it was prohibited from doing so. Furthermore, by reason of the CGT issues it had raised with Ms Secombe, IIML had a firm basis to believe that the proposed SFT would harm members (as was ultimately shown to be the true).

856 The 10 February 2015 letter from Mr Kelaher needed to be viewed in this context. It was submitted for the first respondent that the letter represented the “only lawful response that IIML could give to Optus’ ‘urgent’ request. Optus had not said in its letter that it would permit time for IIML to consider the issue, obtain information and complete an equivalency analysis. It asked that IIML ‘accept our request’ and do so ‘by return email’.”

857 The first respondent noted that APRA made three points in relation to the 10 February 2015 letter:

a) First, IIML did not request further information from Optus regarding the AMP fund that was proposed to be the destination fund for the transfer;

b) Secondly, IIML proposed that beneficiaries be allowed to make their own decision as to whether to leave IPS Super, which APRA says was not in beneficiaries’ interests because these were default superannuation plans where members had not made a choice as to their super fund; and

c) Thirdly, it did not recognise that the effect of not transferring members would be that members might end up with multiple superannuation plans and incur additional fees.

858 The first respondent responded to each of these matters as follows:

a) IIML was under no obligation to request further information from Optus. Optus had requested an “urgent” response “by return email”. The only response IIML could urgently give was to decline the request. Moreover, for the reasons given …above, IIML was not under any obligation to make further inquiries. Optus was a stranger to the trust between IIML and the superannuation beneficiaries and had no lawful entitlement to demand a SFT. If it wished to procure that outcome, it was incumbent on Optus to provide IIML with the necessary information to complete an equivalency analysis.

b) Permitting members to make their own decision whether to stay with IPS Super was required by clause 18.3.4 of the IPS Super trust deed. Moreover, there is no proper basis to infer that members who adopt an employer’s default superannuation plan are persons who are not thoughtful or who are careless in their superannuation arrangements. It is surprising and disappointing that APRA would make such a submission.

c) It is unclear why APRA says that IIML should have noted this fact. APRA does not contend that this risk, when properly considered and assessed, was material to the equivalency analysis. The much more pertinent risk was the CGT risk which IIML had already identified and notified to Optus and Ms Secombe.

859 The first respondent also made the point that nothing in the 10 February 2015 letter suggested that IIML had made a “once and for all” decision in relation to the proposed SFT or had closed its mind to the proposal. Rather, Optus had requested an urgent response and received one. The subsequent events showed that IIML was open to further discussions.

860 The chronology of subsequent events shows IIML on the next day, 11 February 2015, giving further consideration to the CGT implications of the proposal. According to the first respondent, this showed that IIML had not closed its mind to the proposal.

861 Further, as the first respondent identified in its chronology of subsequent events:

(1) on 23 February 2015, for the first time, Optus provided IIML with information regarding the proposed destination fund by supplying IIML with contact details for the relevant individuals at AMP;

(2) “[o]n 24 February 2015, Mr Vine informed APRA that the reason that Optus’ urgent request for a SFT had been refused was because of the CGT concerns. APRA contends that the only document recording such concerns was Ms Roberts’ 11 February 2015 email (ACS [533]). That is not correct. The CGT issues were first raised by Mr Ferguson in September 2014. What is worse, though, is that APRA was told by Ms Secombe on 2 February 2015 that IIML had raised tax concerns and that is recorded in APRA’s own file note of that call.”;

(3) on 5 March 2015, Mr Vine wrote to APRA regarding the CGT issues. APRA does not suggest Mr Vine’s analysis of the issues is incorrect and given the detail of the analysis it is impossible to “conclude that this was a reason manufactured by IIML for rejecting the Optus SFT after the event”. Rather, the Court would conclude that the letter reflected IIML’s state of mind at the time;

(4) on 16 March 2015, IIML wrote to Optus again, saying:

I refer to your letter of 26 February 2015 and our recent meeting in relation to the transfer of member accounts in the Optus Group Superannuation Plan.

I confirm that IOOF investment Management Limited (Trustee) has declined Optus’ request to successor fund transfer (SFT) member accounts, particularly in the absence of a Participating Employer Agreement between the parties.

In order for the Trustee to consider an SFT, we need to be satisfied that Optus members will receive equivalent rights to those they currently have in respect of their benefits in the IOOF Employer Super Fund.

To date, the Trustee has received no information on the rights and benefits that will be conferred on members in the new AMP fund in order to conduct the necessary equivalency analysis. Although from our past experience in conducting SFTs, we know there will be capital gains tax implications for members as well as a potential loss of insurance benefits given the arrangements with the new insurer will be different.

To ensure the Trustee does not risk breaching its statutory duties in relation to the protection of members’ rights, we have taken the position that Optus members should be given an opportunity to consider the relevant comparative information from both the Trustee and AMP, before choosing for themselves which fund they prefer for their ongoing employer superannuation contributions.

As I mentioned in our meeting, we are working hard on the transfer of the Optus Plan ADAs to IOOF MySuper. So until the parties are able to agree on the transfer position for member accounts, we do not intend to provide you with the information requested in your letter about different transfer scenarios that may or may not happen.

As the first respondent said, “the Court would infer from the opening paragraph of this letter that IIML and Optus had been in ongoing discussions in relation to the proposed SFT. This confirms that the 10 February 2015 letter was not regarded by anyone as a final position.”;

(5) on 2 April 2015, AMP wrote to IIML:

We acknowledge receipt of your letter dated 16 March 2015 where you noted that IOOF Investment Management Limited (IOOF Trustee) would need to be satisfied that Optus Group Superannuation Plan members (Plan Members) would receive equivalent rights in an AMP superannuation fund to those they enjoy in respect of the benefits currently provided to them in the IOOF Employer Super Fund before the IOOF Trustee could agree to a transfer by way of successor fund.

We also acknowledge your statement that to date the lOOF Trustee has not been provided with sufficient information in respect of the rights and benefits that will be conferred on these Plan Members in the relevant AMP superannuation fund to allow it to make such a determination.

AMP understands the duties and responsibilities of the lOOF Trustee and will provide the lOOF Trustee with a comprehensive and appropriate proposal for the transfer by way of successor fund of the relevant Plan Members Proposal.

The first respondent said this letter is “powerful evidence that the position taken by IIML throughout the Optus SFT process was appropriate. AMP frankly conceded that IIML had not been provided with sufficient information to assess equivalency. As AMP recognised, the effect was to prevent IIML from agreeing to the proposed SFT”;

(6) on 28 April 2015, AMP provided its proposed equivalency analysis to IIML for the first time;

(7) on 16 October 2015, Mr Vine prepared a paper to the IIML Board regarding the proposed Optus SFT. The paper included an independent opinion from Holding Redlich. Holding Redlich’s conclusion was:

If the CGT impact of the successor fund transfer will financially disadvantage Transferring Members and this is not sufficiently compensated for by any potential costs savings and other benefits in the AMP Fund, the IOOF Trustee could form the view that the proposed successor fund transfer is not in the best interests of members, and that to agree to it would be a breach of its trustee duties under common law and legislation;

The board paper concluded with the statement that:

We note that the Trustee’s decision in respect of the SFT will be closely scrutinised by APRA and could result in further regulatory investigation. We also note the risk of legal proceedings being initiated against IIML by Optus in the event of a determination by the Board that the SFT to AMPSS should not proceed. Neither of these matters should go towards compromising IIML’s duty as trustee to act in the best interests of members.

The first respondent said this is clear evidence of IIML acting in members’ best interests despite expecting regulatory scrutiny of its conduct.

(8) on 29 October 2015, the Board of IIML considered the 16 October 2015 Board paper. The minutes record:

The Board considered and discussed the documents tabled at the meeting and the discussion by Mr Riordan. It was noted that the estimated CGT impact Optus Plan members would realise on transfer and implementation of the Proposal were materially detrimental to them, such that IIML would not be acting in their best interests if it were to approve the Proposal.

The Board also noted that individual members within the Optus Plan may choose to transfer their account to the AMP Fund at any time.

Resolved (unanimously) that:

(a) the Board is satisfied that the AMP Fund will not currently be a ‘successor fund’ within the meaning of SIS;

(b) the expected realised CGT impact on Optus Plan members means it is not in the best interests of those members to implement the Proposal; and

(c) having regard to the matters discussed at the meeting and noting that individual Optus Plan members may at any time make their own choice to transfer their account to the AMP Fund the Board is satisfied that it is not in the best interests of the Optus Plan members that they and the Optus Plan assets be transferred to the AMP Fund.

The first respondent noted that APRA does not suggest that this was anything other than a responsible and prudent decision in accordance with the SIS Act and SIS Regulations.

862 The first respondent submitted that:

The Court would infer from this chronology that IIML did not conclusively decide to reject the proposed Optus SFT on 10 February 2015. IIML gave the only response it could lawfully give “by return email”, but thereafter engaged with Optus and AMP in relation to the proposed SFT. Moreover, when the merits of the proposal were considered, including by an independent law firm, the advice was that the concerns raised by Mr Ferguson as far back as September 2014 were valid.

863 The first respondent noted that APRA alleged that IIML breached the best interests and no conflicts covenants on 10 February 2015 by rejecting the Optus proposal without:

a) “identifying” and “managing” the relevant conflicts of interests (ASOC [297(a), (b), (c)]);

b) acknowledging that “beneficiaries of a default superannuation fund have not made a choice to be in that fund and that accordingly allowing such beneficiaries to choose which fund to join was not necessarily in their best interests” (ASOC [297(d)]);

c) assessing the comparative benefits of IPS Super and AMP to determine whether the transfer was in the best interests of members (ASOC [297(e)]);

d) requesting further information from Optus or AMP if required to assess equivalency (ASOC [297(f)]); and

e) documenting any consideration or analysis to support the decision (ASOC [297(g)]).

864 The first respondent submitted that:

The first and complete response to this allegation is that there was no permanent “rejection” of the Optus SFT on 10 February 2015 (cf. ASOC [293]). What occurred in fact was that IIML provided the only response it could lawfully give to what Optus had insisted was an urgent request. When Optus thereafter afforded appropriate time to consider its request, and provided the relevant information, IIML considered it.

In addition to that answer, the responses to the allegations referred to …above are as follows (using corresponding paragraphs):

a) The “conflicts” only existed if there was a divergence between members’ best interests and IIML and Mr Kelaher’s interest, but no such conflict in fact existed. The CGT concerns, coupled with the fact that IIML was prohibited by law from agreeing to the Optus SFT on 10 February 2015 meant the “conflicts” did not arise in fact;

b) The proposition that members of a default superannuation plan have not consciously turned their mind to their superannuation arrangements is obviously wrong, as is the paternalistic submission that such individuals would not be able to make a decision in their own interest as to whether to stay with IPS Super or transfer to AMP;

c) IIML cannot be faulted for failing to assess the comparative benefits of IPS Super and AMP on 10 February as, by Ms Secombe’s account, it had not been provided with the requisite information;

d) IIML was not obliged by law to request further information for the reasons addressed …above.

e) There is no obligation on a trustee to record decisions in relation to a proposed SFT in a document. In any event, IIML’s position was recorded in the 10 February 2015 letter to Optus.

865 The first respondent said that the Court would reject APRA’s case on the alleged Optus SFT breach against IIML entirely and would reject the whole of the case against Mr Kelaher in respect of that matter as well for the same reasons.

###### 17.4 Discussion

866 I again find the submissions for the respondents compelling.

867 APRA has sought to pluck out of a lengthy and highly regulated process, two communications and, by examining those communications entirely divorced from their context, has alleged that IIML and Mr Kelaher breached their respective best interests and no conflicts covenants. However, when the entirety of the context is considered, both factual and legal, it is apparent that APRA’s allegations are without factual foundation. There was no actual conflict between the interests of IIML and Mr Kelaher and those of its members capable of having any significant impact on the decision-making process at the time of the 10 February 2015 letter. At that time there was no divergence between the relevant interests because IIML was legally prohibited from complying with Optus’ request. Optus’ request was misconceived. In demanding an urgent response to a request that could not be fulfilled, Optus received the only response that was permissible at the time. To attempt to found alleged contraventions of the statutory covenants on this flimsy foundation is itself also misconceived.

868 The facts and circumstances of the present matter bear no meaningful relationship to the decision of a trustee to pay out of the trust fund to a beneficiary. As the respondents submitted, the payment to a beneficiary involves a core trust function whereas the Optus request for an SFT involved a stranger to the trust requesting an exercise of power by the trustee to change the terms on which the beneficiaries’ assets are held without the consent of the beneficiaries to the trust. Accordingly, APRA’s case that IIML was bound to request further information rather than responding as it did on 10 February 2015 is unsustainable as a matter of principle. It is also unsustainable on the facts. This was not a case of a trustee deciding a beneficiary’s entitlement without proper information. The statute mandated a particular process which had to be fulfilled before any consideration could be given to the requested SFT. It is difficult to accept that APRA’s case amounts to nothing more than a complaint that the letter of 10 February 2015 should have pointed out to Optus that unless the statutory requirements were satisfied (which they had not been) nothing could be done, yet APRA’s case does seem to involve nothing more than this.

869 Accordingly, in the circumstances as they existed at 10 February 2015, the answer that IIML gave Optus was the only legally permissible answer that could be given. Such an answer, in such circumstances, necessarily was in the best interests of the members and could not give rise to any actual conflict of interest. As the respondents put it, APRA has again failed to identify any actual conflict of interest that could have had a significant impact on IIML’s response to Optus’ request.

870 In my view it is entirely misconceived for APRA to focus on two pieces of correspondence in a chain of events and to consider those communications in isolation as if the first represented a request that could be lawfully actioned (when it could not) and the second represented an irrevocable decision to refuse the request under all circumstances irrespective of the best interests of members (which it did not). To frame its case in this way is the height of artificiality on APRA’s part.

871 I also agree with the first respondent that the fact that the IPS trust deed, by cl 18, required that members be given the choice is fatal to APRA’s case on the alleged Optus breaches. However, the full factual circumstances are also equally fatal to APRA’s case, as is the fact that, right or wrong, IIML’s view of the legal position was reasonable in the circumstances. Once those full factual circumstances are considered, nothing emerges other than a trustee acting in the best interests of its members cognisant of any actual conflict of interest capable of having a significant impact on the required decision. That was the decision made by the board on 29 October 2015, not the communication of 10 February 2015, which was nothing more than a response along the way to a misguided request by Optus that could not be fulfilled but nevertheless sought an urgent response.

872 APRA’s case on the alleged Optus breaches must be rejected in its entirety.

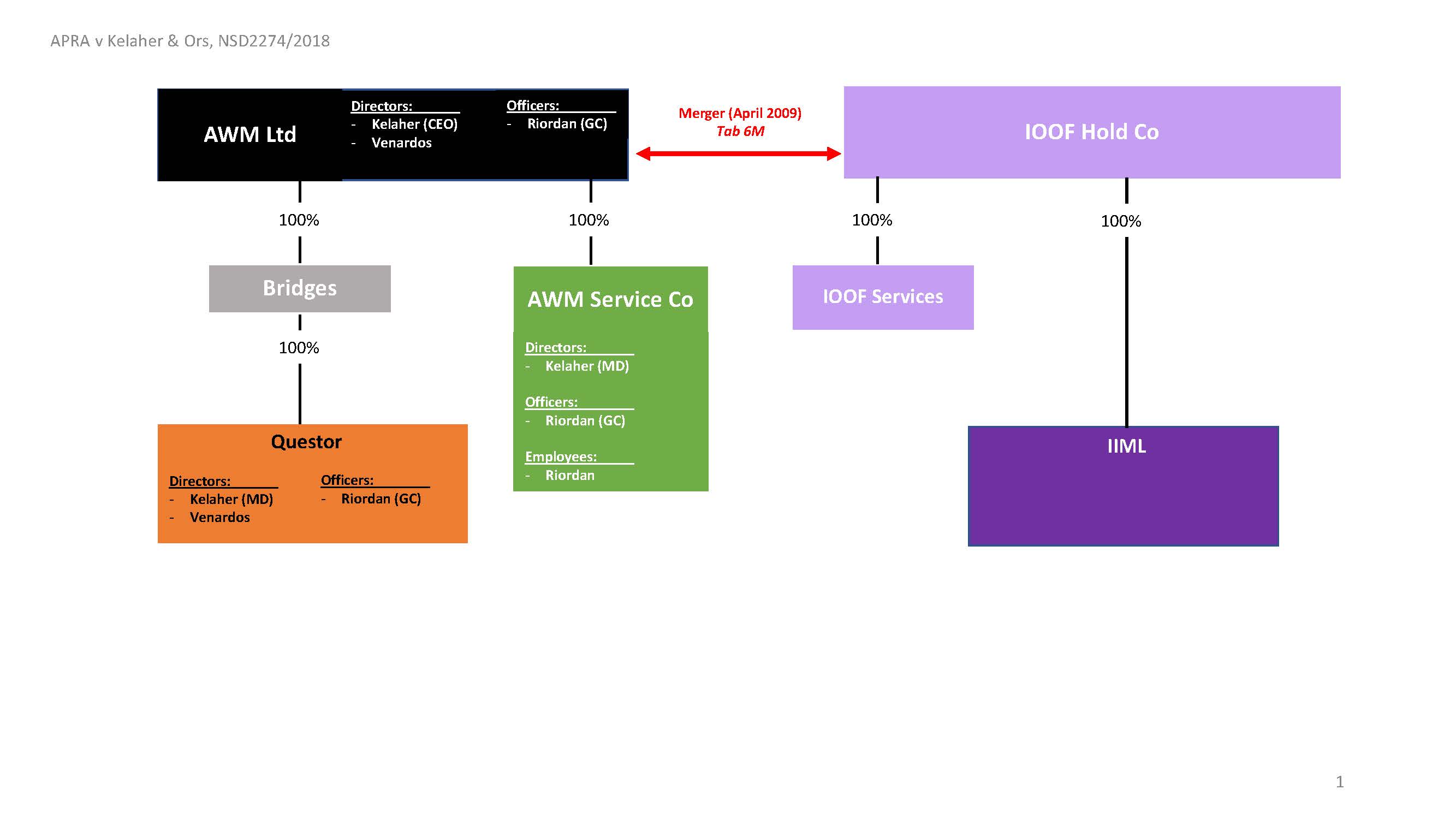
##### 18. CONCLUSION

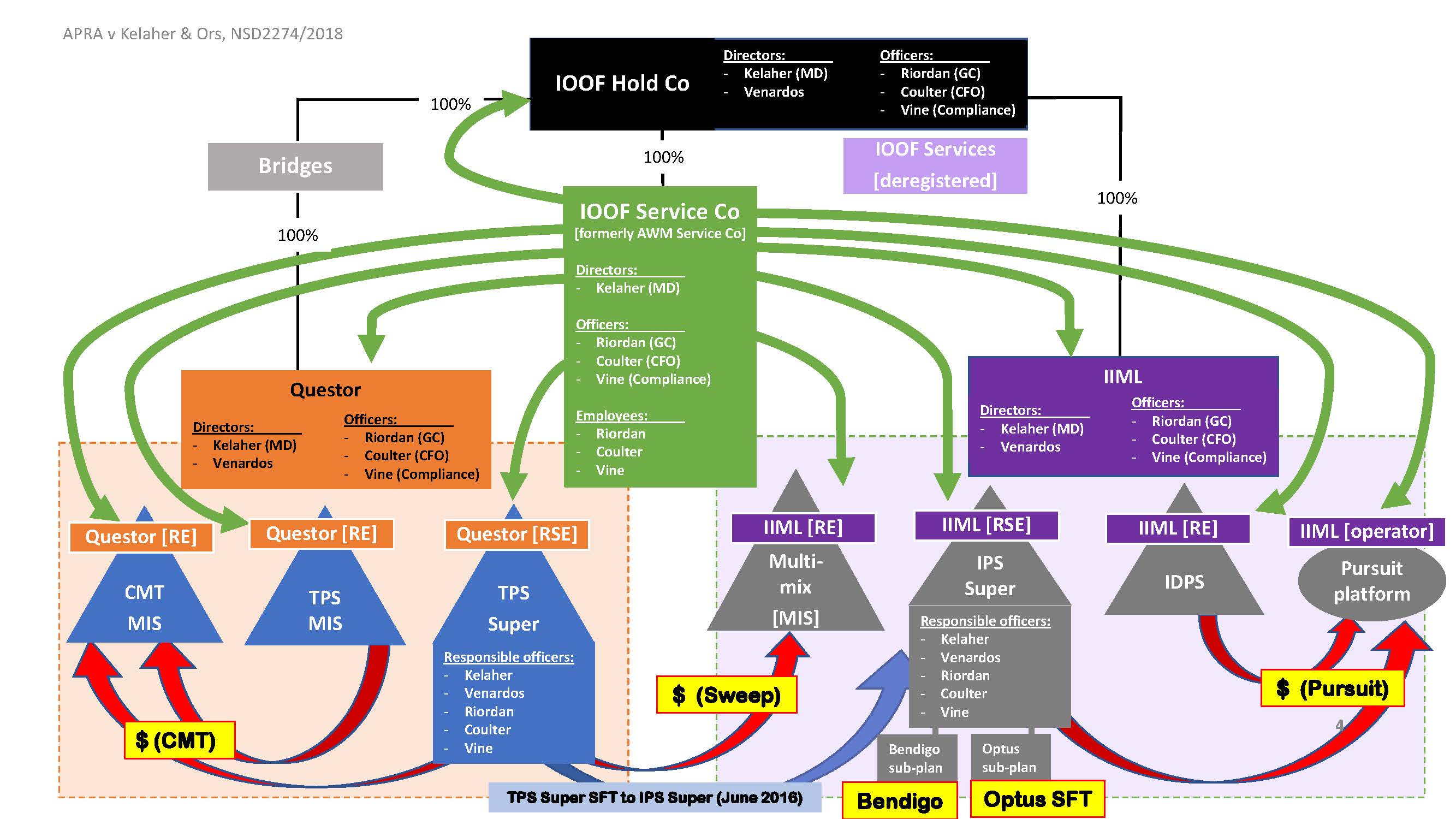
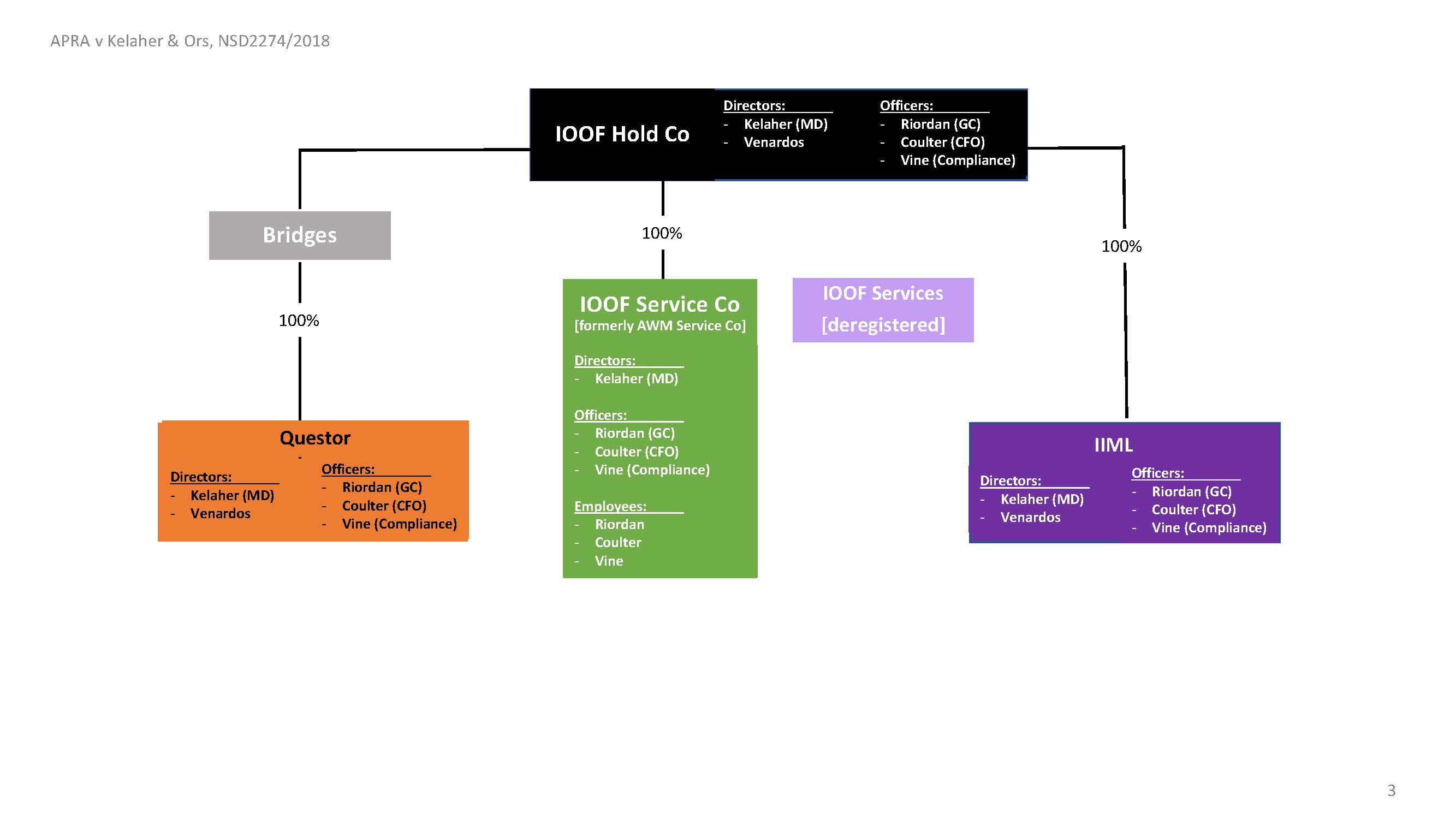
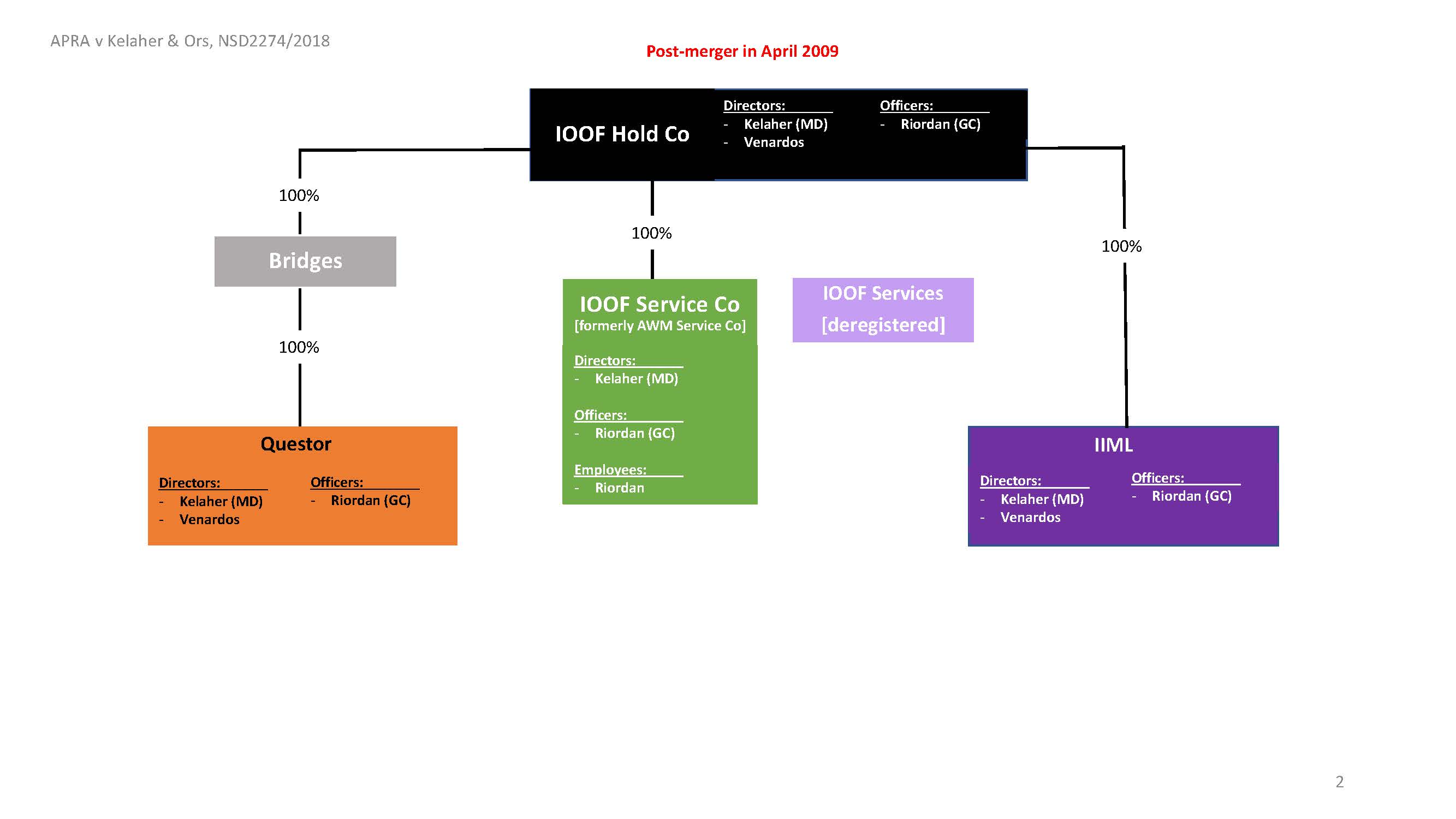
873 For the reasons given, APRA has failed to prove any of the contraventions of the SIS Act alleged against the respondents. It follows that APRA’s application should be dismissed with costs.

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| I certify that the preceding eight hundred and seventy-three (873) numbered paragraphs are a true copy of the Reasons for Judgment herein of the Honourable Justice Jagot. |

Associate:

Dated: 20 September 2019

ANNEXURE A



ANNEXURE B

**APRA response to pleading points**

APRA CS = APRA Closing Submission

APRA OCS = APRA Outline of Closing Submissions

K CS = Kelaher Closing Submissions

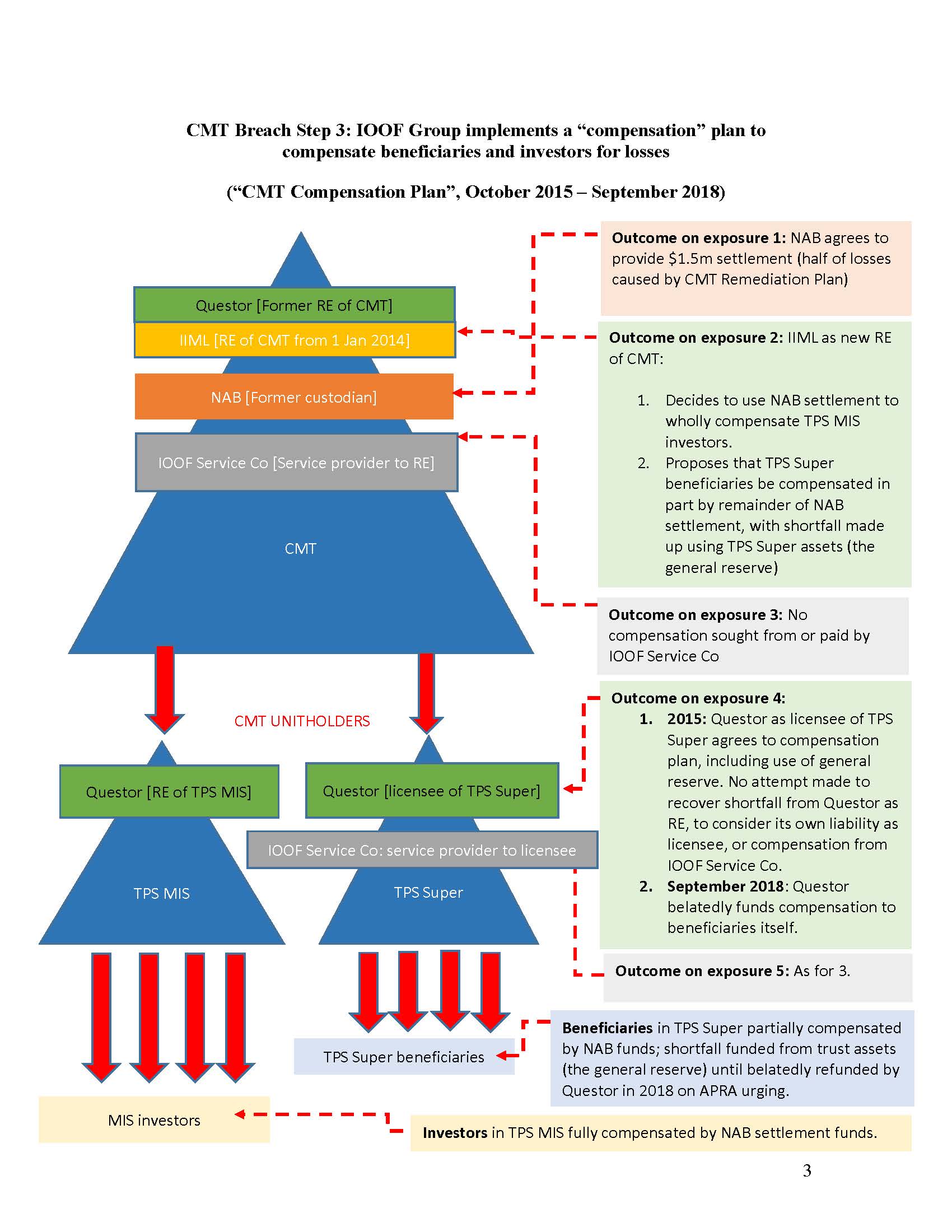
V CS = Venardos Closing Submissions

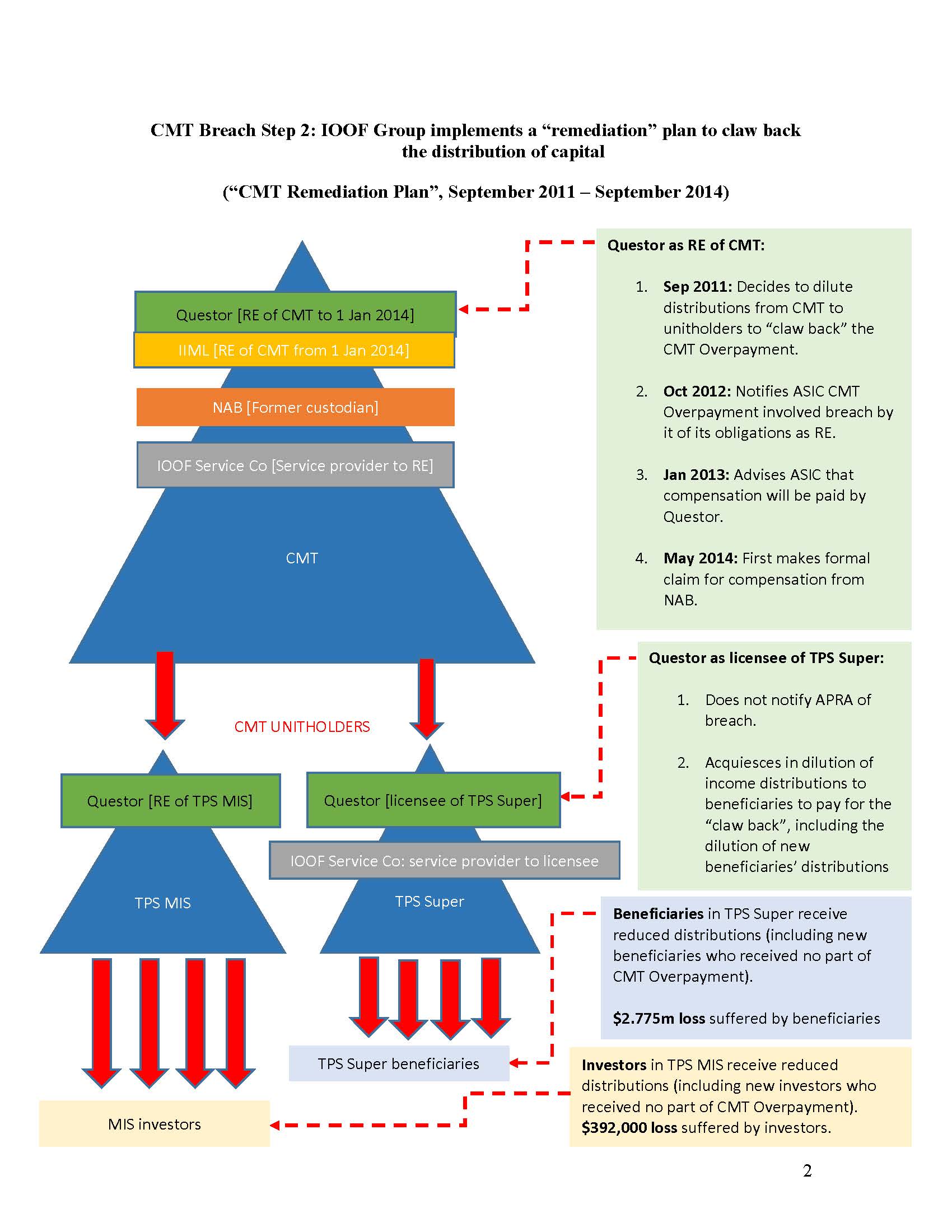
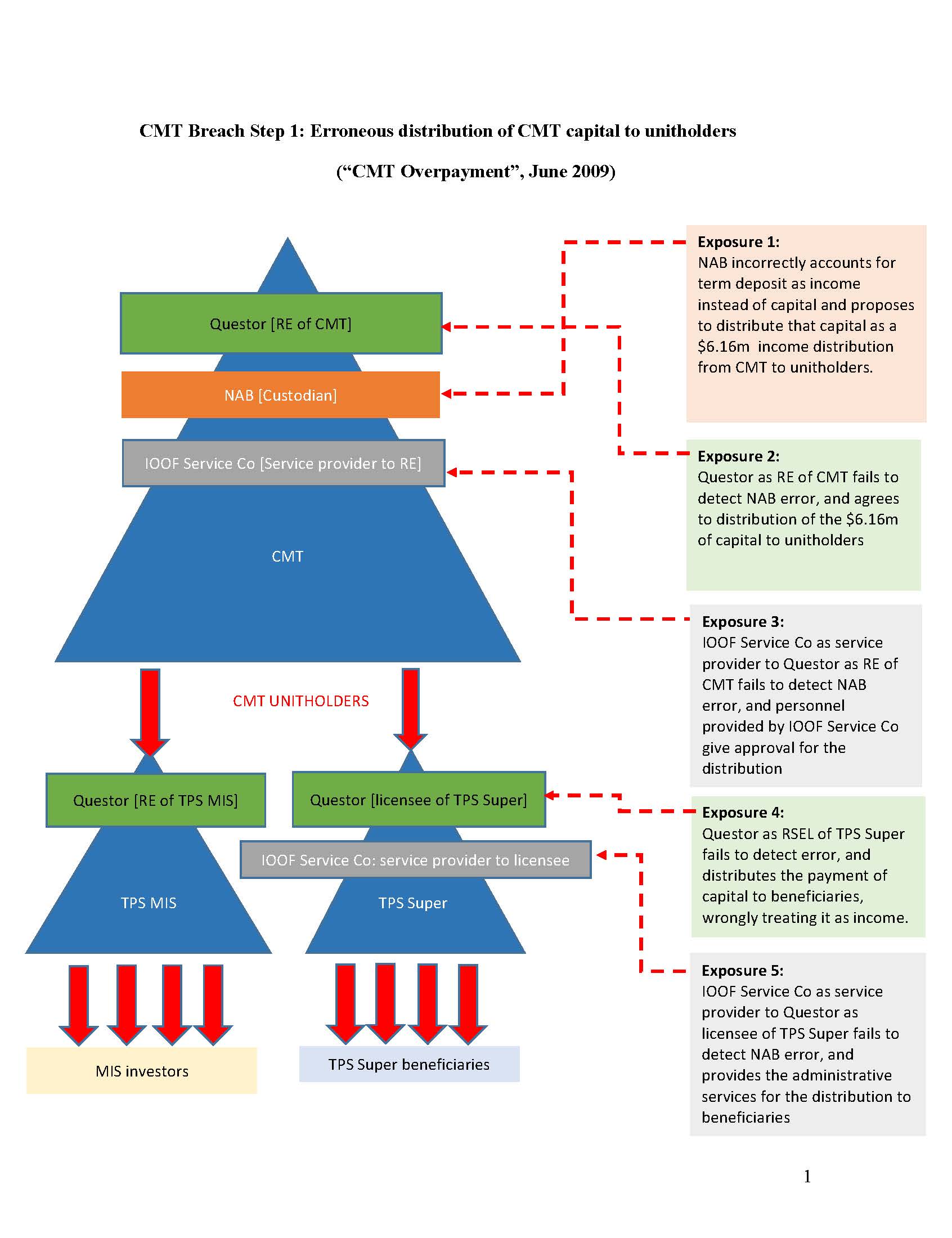
C CS = Coulter Closing Submissions

4-7 CS = 4-7th Respondents Closing Submissions

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | **Respondents pleading complaint** | | | | **APRA response** |
|  | Allegation | Matter allegedly not pleaded | Closing subs | Transcript | Response |
| 1. | General | Duty to preserve trust property and vindicate rights attaching to it | K CS, [19]  4-7 CS, [14(c)], [37(c)] | T369.4 (Hutley) | Pleaded at ASOC, [74(a)(ii), (iv), (v)], as integer of conflicts pleaded at [74]-[77] (i.e. conflict between this duty and interests of IOOF Group). Conflicts then relied upon for each alleged contravention. |
| 2. |  | Knowing exclusion of relevant information from consideration and seeking relevant information (*Finch*) | K CS, [31]  V CS, [148]  4-7 CS, [14(c)], [37(c)-(d)] |  | Knowledge of individuals pleaded at ASOC, [125], [131] (Pursuit), [161], [167] (Sweep), [206] (Bendigo), [247], [253], [270], and [276] (CMT). Then pleaded at ASOC, [126], [132] (Pursuit), [162], [168] (Sweep), [207] (Bendigo), [248], [254], [271] and [277] (CMT) that, despite this knowledge, they did not seek further information from management or independent lawyer.  Pleaded at ASOC, [119] (Pursuit), [158] (Sweep), [239] and [267] (CMT) that compensation plans not in best interests because no practical difficulty in seeking compensation from other sources.  Pleaded at ASOC, [297(e)-(7)] and [301(f)-(g)] in relation to Optus that IIML and Kelaher required to assess comparative beneficiaries and seek further information if required. |
| 3. |  | Contravention based on “process” rather than “outcome” | 4-7 CS, [14(c)] | T360.24; T362.25 (Hutley) | Process and outcome in issue: pleaded at ASOC, [121] (Pursuit), [160] (Sweep), [199] (Bendigo), [239] and [267] (CMT) that IIML/Questor contravened by developing, adopting and approving relevant compensation plans, in light of information pleaded at [119] (Pursuit), [158] (Sweep), [197] (Bendigo), [239] and [267] (CMT).  Pleaded at ASOC, [126], [129], [132], [135] (Pursuit), [162], [165] [168], [171] (Sweep), [207], [210] (Bendigo), [254], [248], [274] and [277] (CMT) that individuals failed to take relevant steps to ensure best interests promoted and conflicts managed (e.g. identify conflicts and seek independent advice). |
| 4. |  | Delay in paying compensation | K CS, [32] |  | Pleaded at ASOC, [122]-[124], [129A] (Pursuit) |
| 5. |  | “Pattern of conduct” submission | K CS, [35] |  | Relevant to penalty hearing; not findings of contravention: ASOC, Part XII. |
| 6. |  | Failure to comply with SPS 521 | V CS, [105] |  | SPS 521 pleaded at ASOC, [27(d)] as informing conflicts covenant (including by requiring conflicts policy).  Pleaded at ASOC, [80(d)] and [81(e)] that Kelaher and Venardos were required to comply with prudential standards in relation to conflicts.  Pleaded at ASOC, [129] (Pursuit), [165] (Sweep) [210] (Bendigo) and [274] (CMT) that Kelaher and Venardos breached this duty (by cross-reference to [80]-[81]) |
| 7. |  | Implementation of compensation plans | 4-7 CS, [14(d)] |  | Pleaded and particularised at ASOC, [117] (Pursuit), [156] (Sweep) |
| 8. |  | That respondents failed to gather information concerning sources of information in accordance with ORFR policy | - | T371.43 (Hutley) | Relevant information to be gathered was “sources of compensation”. Pleaded at ASOC, [126], [132] (Pursuit), [162], [168] (Sweep), [207] (Bendigo), [248], [254], [271] and [277] (CMT) that further information concerning sources of compensation not sought from management or independent legal advice. |
| 9. | **Pursuit Breach** | Failure by IIML to exercise care, skill and diligence, other than by failing to supervise IOOF Service Co. | 4-7 CS, [253], [257] | T381.23 (Owens) | Pleaded at ASOC, [106] which incorporates [100]. See also ASOC, [105(a1)], failure by IIML to have “adequate systems”. |
| 10. |  | IIML contraventions prior to 2009 | 4-7 CS, [257] |  | Pleaded at ASOC, [106] which incorporates [100]. |
| 11. |  | Allegation that IIML did not do what it represented to its clients it would do (“quasi-misrepresentation” case). | K CS, [160] |  | Mischaracterisation of APRA’s case. Pleaded case and basis of submission is that IIML did not have system and procedure in place to process instructions or detect failure to do so: ASOC,[100], [106]. |
| 12. | **Pursuit Compensation Plan** | IIML’s subjective decision-making processes or considerations constituted a breach | 4-7 CS, [173], [182], [278] |  | Mischaracterisation of APRA’s case. APRA’s case is that, objectively assessed, conduct of respondents (including decision-making process) did not comply with covenants: see item 3 above. |
| 13. |  | Venardos knew that Vine and Riordan were conflicted | V CS, [155] |  | Pleaded at ASOC, [77] and [89] that Vine and Riordan had relevant conflicts; failure to identify conflicts pleaded at ASOC, [129]. |
| 14. |  | Implementation of Pursuit Compensation Plan | 4-7 CS, [321] |  | Pleaded and particularised at ASOC, [117]. |
| 15. |  | Riordan and Vine failed to considered the issue of compensation from the perspective of the IOOF Group and failed to consider the terms of the IOOF Service Co contract | 4-7 CS, [223] |  | Factual findings are to be made on the evidence before the Court; proposed findings are consistent with material facts pleaded at ASOC, [131], [135]. |
| 16. |  | Vine and Riordan knew that IIML had notified its insurer | 4-7 CS, Annex D [26] |  | Factual findings are to be made on the evidence before the Court; insurance claim related to allegation of knowledge of IIML’s liability: ASOC, [131(b)]. |
| 17. | **Sweep Breach** | Failure by Questor to exercise care, skill and diligence, other than by failing to supervise IOOF Service Co. | 4-7 CS, [354] | T389.21 (Owens) | Pleaded at ASOC, [146(a1)] that Questor did not itself have adequate systems and processes to undertake relevant tasks. Forms basis of alleged contravention at ASOC, [147]. |
| 18. |  | Questor did not do what it represented to its clients it would do (“quasi-misrepresentation” case). | K CS, [238] |  | Mischaracterisation of case. Pleaded case and basis of submission is that Questor did not have system and procedure in place to process instructions or detect failure to do so: ASOC,[140], [146], [147]. |
| 19. |  | Questor’s subjective decision-making processes or considerations constituted a breach | 4-7 CS, [173], [182] |  | Mischaracterisation of APRA’s case. APRA’s case is that, objectively assessed, conduct of respondents (including decision-making process) did not comply with covenants: see item 3 above. |
| 20. |  | Sweep breach notice falsely alleged that the cause of the Sweep issue had not been fully established | K CS, [239] |  | Mischaracterisation of submission, which is to the effect that it was possible for Questor to determine who was responsible: APRA CS, [476] |
| 21. | **Bendigo** | Failure by IIML to exercise care, skill and diligence, other than by failing to supervise IOOF Service Co. | 4-7 CS, [392] |  | Pleaded at [189] that IIML contravened by reason of [179], [181], [182], [184(a)] and [188]. Pleaded at ASOC, [188(a)] that IIML did not have its own adequate system and processes, and relied wholly on IOOF Service Co. |
| 22. |  | Breach was due to failure to put in place controls to ensure the April 2015 error did not occur |  | T394.15 (Owens) | Pleaded at ASOC, [184(a)(iv)]. |
| 23. |  | Venardos should have given Bendigo particular attention considering similarity to other alleged matters | V CS, [196] |  | Pleaded at ASOC, [206(e)] that Venardos ought to have been aware that Bendigo Failure and Pursuit Failure relevantly similar. |
| 24. |  | Venardos should have taken positive steps to raise the issue at a subsequent meeting | V CS, [197] |  | Pleaded at ASOC, [209A] that Venardos did not take adequate steps from September 2015 to October 2018 to ensure compensation for Bendigo Failure was sourced otherwise than from reserves. |
| 25. |  | Uncertainty in language of the Group Compliance Report should have caused Venardos to ask questions | V CS, [198] |  | Relevant to pleading that Venardos did not query management concerning compensation plan: ASOC, [207]. |
| 26. | **CMT Overpayment** | Losses suffered by Questor form CMT Overpayment. | V CS, [226]  4-7 CS, [496(a)] | T324.15 (Bannon) | Pleaded at ASOC, [221]-[222] that loss and damage suffered at each level. Specific losses identified at APRA, CS [180] are examples of this loss – i.e. reduction in amount of capital due to taxes and fees as it is distributed. |
| 27. |  | Application of various provisions of the *Corporations Act 2001* (Cth) to Questor as RE | 4-7 CS, [496(a)], [548] |  | Pleaded at ASOC, [232]-[233] that Questor as RE of CMT had exposure, by reason of failures in its systems and processes and reliance on NAB and IOOF Service Co. No particulars sought of pleading. Relevant *Corporations Act* provisions inform basis of liability. |
| 28. |  | *Corporations Act* (Cth), ss 601FC(1) (c), (j) and (k) |  | T332.17 (Bannon) | Section 601FC(1)(b) obligation particularised at paragraph [233], [224(b)(ii)]. APRA does not need to rely upon the other provisions of s 601FC. |
| 29. | **CMT**  **Remediation** | Questor could have sought to recover the overpayment and pay compensation for incidental losses, with such compensation sourced from claims against relevant entities. | K CS, [356]  V CS, [8], [207], [249] | T322.30 (Bannon) | Pleaded at ASOC, [233] and [239(h)-(i)] which allege that Questor as RE caused CMT Overpayment and was potentially liable for loss (pleaded and particularised as loss of capital). This encapsulates potential restitutionary claim.  Liability of other entities for potential compensation further pleaded at ASOC, [239]. |
| 30. |  | Questor as TPS Super trustee had a cause of action against Questor as CMT RE in relation to the CMT Overpayment | V CS, [232] | T296-297; T341.23 (Bannon) | Pleaded at ASOC, [233] and [239(h)-(i)] that Questor as RE had exposure to liability. |
| 31. |  | Questor had a defence to a claim for restitution of the CMT Overpayment | V CS, [280] |  | Pleaded at ASOC, [239(l)] that Questor should have considered availability of defence. |
| 32. |  | Questor as RE’s decision to make diluted distributions was not exercised in good faith | V CS, [234] |  | APRA does not allege lack of good faith. Respondents have alleged in defence that CMT Remediation Plan was authorised by CMT Constitution. In reply, APRA has identified that power relied upon was limited: APRA CS, [214]. |
| 33. |  | Venardos had a duty to oversee management of Questor and apply an enquiring mind to the matters brought before the Board in relation to the CMT Remediation Plan. | V CS, [271] |  | Pleaded at ASOC, [245(e)] that Venardos should have questioned management about the CMT Remediation Plan. |
| 34. |  | Venardos should have taken steps to manage conflicts when considering the CMT Remediation Plan | V CS, [281] |  | Pleaded at ASOC, [248(b)-(e)] that Venardos did not identify conflicts and take steps required by Conflicts Policy (which is pleaded as contravention of duties in [81], including compliance with prudential standard: see item 6 above). |
| 35. |  | Venardos should not have accepted the CMT Remediation Plan until satisfied that conflicts had been managed and the decisions made in beneficiaries’ best interests | V CS, [283] |  | Pleaded at ASOC, [248(f), (g), (h)] that Venardos contravened by accepting plan without taking steps set out and in circumstance where plan not in best interests. |
| 36. |  | Findings with respect to Coulter’s conduct in relation to the CMT Remediation Plan | C CS, [137] | T411.33 (Studdy) | Factual findings are to be made on the evidence before the Court; proposed are consistent with material facts pleaded at paragraph: ASOC, [250]-[245]; |
| 37. | **CMT Compensation Plan** | Questor as TPS trustee had a claim against Questor as RE for the reduced distribution | V CS,  [260] |  | Pleaded at [267(b)] that Questor remained liable by reason of involvement in CMT Overpayment. |
| 38. |  | Venardos ought to have known that “advice” given by Vine was not legal advice | V CS, [321] |  | It is not APRA’s case that the advice was legal advice, that is a contention put forward by Venardos. APRA denies it. |
| 39. |  | Coulter approved the use of the NAB settlement to compensate non-superannuation beneficiaries | C CS, [185] |  | Factual findings are to be made on the evidence before the Court; proposed are consistent with material facts pleaded at paragraph: ASOC, [276]-[279]. |
| 40. |  | Coulter (and others) failed to act with due care, skill and diligence in developing and approving plan | C CS, [178] | T414.30 (Studdy) | Reference is to APRA CS, [241], intended as general statement. No specific finding sought against Coulter. |
| 41. |  | Coulter (and others) failed to act in beneficiaries’ best interests in developing and adopting plan | C CS, [179] | T414.30 (Studdy) | Reference is to APRA CS, [241], intended as general statement. No specific finding sought against Coulter. |
| 42. |  | Findings with respect to Coulter’s conduct in relation to the CMT Compensation Plan | C CS, [193] | T415/5-25 (Studdy) | Factual findings to be made on the evidence before the Court; proposed findings are consistent with material facts pleaded at paragraph: ASOC, [276]-[279]. |
| 43. |  | ~~Coulter did not take any steps to revisit, or have the Board revisit, the decision~~ | ~~C CS, [195]~~ |  | ~~Factual findings to be made on the evidence before the Court; proposed findings are consistent with material facts pleaded at paragraph: ASOC, [276]-[279].~~ Withdrawn. |
| 44. |  | Coulter and Vine were making decisions on what they thought they could get past APRA | C CS, [184] | T414.40 (Studdy) | APRA withdraws this submission. |
| 45. |  | ~~Vine sought to distract the Board (and potentially APRA’s) attention~~ | ~~4-7 CS, Annex D, [45]~~ |  | APRA has withdrawn this submission. |
| 46. | **Optus** | Duty to inquire | 4-7 CS, [575] |  | Pleaded at ASOC, [297(e)-(7)] and [301(f)-(g)] in relation to Optus that IIML and Kelaher required to assess comparative beneficiaries and seek further information if required. |

ANNEXURE C





SCHEDULE OF PARTIES

|  |  |
| --- | --- |
|  | NSD 2274 of 2018 |
| Respondents |  |
| Fourth Respondent: | ANDREW PAUL VINE |
| Fifth Respondent: | GARY WILLIAM RIORDAN |
| Sixth Respondent: | I.O.O.F INVESTMENT MANAGEMENT LTD ACN 006 695 021 |
| Seventh Respondent: | QUESTOR FINANCIAL SERVICES PTY LTD ACN 078 622 718 |