Questions on Notice – Storm

A significant number of submitters to this inquiry into the performance of ASIC referred to aspects of the Storm Financial case,[1] including:

1. the perception or understanding that ASIC gave approval to the Storm model and failed to identify flaws in the model;

1.1 Australian Financial Services licensing is a minimum threshold. When processing an application for an Australian Financial Services Licence (**AFSL**) ASIC assesses whether the entity applying for the licence is competent to carry out the kind of financial services business it is applying for; if it has sufficient financial resources to carry on the business it is proposing; and if it can meet its other obligations as a licensee.

1.2 ASIC cannot refuse a licence on the basis of the licensee's proposed and apparently lawful business model . Under section 913B of the *Corporations Act* 2001 (**Corporations Act**), ASIC must grant an AFSL if the applicant meets the five criteria set out in subsection (1) of section 913B. If the applicant does not meet those criteria, ASIC must not issue an AFSL. ASIC cannot refuse to issue an AFSL because it does not agree with the applicant's business model. ASIC has previously addressed the licensing regime (as it was at the relevant times) in its submission to the PJC Inquiry Into Financial Products and Services in Australia dated August 2009 (see Part C).

1.3 At most, the licensing process seeks to ensure that an entity is confined to providing financial services that it is competent to provide and has adequate resources to provide those services at the time of the application. It does not involve an endorsement of business models adopted by the applicant. The relatively low threshold for obtaining an AFSL and the relatively high threshold for removing a licence is not well understood by some retail investors. There is a perception amongst some consumers that an AFSL means that the licensee's business model has been approved by ASIC or that it guarantees delivery of high quality financial services by the licensee. This is not what licensing by ASIC involves.

1.4 The issue of an AFS licence does not certify that ASIC approves the licensee's business model or that ASIC has endorsed the quality of the advice provided or the investment strategies adopted by the licensee. ASIC granted Storm an AFS licence, as it was required to under law, because Storm met the relevant statutory criteria.

1.5 Neither the complaints received about Storm nor ASIC's subsequent surveillance of Storm disclosed misconduct that, under existing law, would have enabled ASIC to cancel Storm's licence. We do not have any record of ASIC officers informing prospective Storm clients that Storm's investment strategy was sound.

[1] Submissions 18, 41, 42, 44, 82, 84, 87, 88, 90, 106, 149, 172, 236, 256, 278, 301, 311, 318, 387.

ASIC does not regulate or provide advice upon the merits of investments or investment strategies and ASIC staff have always understood that to be the case.

1.6 As a result of the Future of Financial Advice (**FOFA**) reforms, which commenced on 1 July 2012, and with which compliance was mandatory from 1 July 2013, ASIC has been given expanded powers to cancel or suspend an AFS licence and to ban authorised financial representatives.

2. ASIC's last minute settlement with CBA, one submitter termed this act as 'the mother of all back-flips' (submission 41);

2.1. ASIC's settlement with CBA was not done at the last minute, nor was it a "back-flip". ASIC's position in relation to its attempts to settle claims against the banks involved in Storm, as articulated in its media releases, was consistent and public. See for example:

(a) ASIC's media release dated 19 March 2010 (10.56AD), where ASIC stated that, having completed its investigation, it would be moving into confidential discussions with the individuals and entities which had been the subject of its investigations "*to see if a commercial resolution can be reached which will be acceptable to ASIC and which ASIC would be prepared to recommend to investors. ASIC considers a commercial resolution, if it can be achieved, will be preferable to protracted litigation.*"

(b) ASIC's media release dated 26 November 2010 (10.250MR), where ASIC announced that it intended to commence legal proceedings against various persons and entities in relation to Storm, including against Commonwealth Bank of Australia Limited (**CBA**), Bank of Queensland Limited (**BoQ**) and Macquarie Bank Limited (**MBL**) alleging that the banks had been knowingly involved in Storm's operation of an unregistered managed investment scheme (**UMIS Proceeding**). That media release stated that a short further period would be allowed, before proceedings were filed, for the commercial resolution discussions to continue. ASIC's then Chairman, Tony D'Aloisio, said, "*We have not, to date, been able to reach an acceptable commercial resolution with key parties on compensation which ASIC was prepared to recommend to investors. In the circumstances, it was not possible for ASIC to continue to defer the decision to commence legal proceedings. However, ASIC remains of the view that a commercial resolution is the preferable course*".

(c) ASIC's media release dated 22 December 2010 (10.281MR), where ASIC confirmed that it had filed legal proceedings against various parties, including against CBA, BoQ and MBL, and that since announcing its intention to issue legal proceedings on 26 November 2010, it had continued confidential commercial discussions with some key parties but those discussions had not resulted in an acceptable commercial resolution on compensation. ASIC's then Chairman Tony D'Aloisio said, "*ASIC is bringing these actions to seek compensation for investors who have suffered losses. ASIC has maintained that a commercial resolution is the preferred*

approach. Unfortunately discussions did not result in a satisfactory outcome and it has been necessary for ASIC to bring these proceedings."

(d) ASIC's media release dated 14 September 2012 (12-227MR), where ASIC announced that it had settled its claim in the UMIS Proceeding against CBA, and would continue its claims against BoQ and MBL. ASIC's Chairman Greg Medcraft stated: *"ASIC's objective of obtaining compensation for Storm investors has been achieved today for CBA customers, without the need for a long, costly legal process that brings with it a level of uncertainty. 'Today's compensation deal is a timely, fair and certain outcome for Storm investors who borrowed from CBA. 'Storm investors can be confident we would not have agreed to a settlement unless we thought the compensation was appropriate.*"

2.2. In addition to its media releases, ASIC created a Storm dedicated website to keep Storm investors informed of developments in relation to its investigation into Storm and the legal proceedings that ASIC had undertaken. From 17 September 2012, that website contained a "Frequently Asked Questions" document which set out why ASIC had entered into the settlement with CBA and which provided a detailed explanation of the terms of the settlement, the way in which investor losses and compensation had been calculated and allocated between banks, and its effect of the settlement on investors who used monies borrowed from CBA to invest through Storm.

2.3. ASIC reached a settlement with CBA of ASIC's UMIS Proceeding, on terms acceptable to ASIC, on 14 September 2012 (**ASIC/CBA Settlement**). The ASIC/CBA Settlement was not done at the last minute. It was the culmination of ASIC's commercial resolution discussions which began in the first half of 2010 and which continued at various intervals, after ASIC issued the UMIS Proceeding. Ultimately, ASIC was able to achieve an acceptable settlement with CBA.

2.4. In considering whether to settle with CBA, ASIC had to assess the prospects of success of its legal proceedings against CBA and the level of compensation that might be awarded if the litigation were successful. ASIC was also very conscious of the benefit of Storm investors receiving compensation sooner, rather than after a prolonged legal process that could include awaiting the trial judgment, the outcome of likely appeals to the Full Court of the Federal Court and the High Court, and the necessary assessment of loss by a court on an investor by investor basis. Such a process could have taken three to four years, or more, from the end of the trial at first instance in early 2013.

2.5. ASIC developed a compensation model (in conjunction with a firm of external forensic accountants) to calculate Storm investors' loss, based upon investor data derived from Storm's database, banks and fund managers (**ASIC compensation model**). The ASIC compensation model calculates the estimated loss for each investor (or investor group, where two or more investors invested jointly in the Storm scheme) by calculating the profit or loss for each investment made, based upon the income and realisation proceeds received on the investment and the cost of financing or otherwise acquiring the investment. The model allocated each

investor's loss between the banks who funded that investor's investments through Storm.

2.6. The ASIC/CBA Settlement involved CBA agreeing to pay up to $136 million in compensation, plus other benefits, to CBA customers who had borrowed from CBA to invest through Storm. This was in addition to the approximately $132 million, plus other benefits, CBA had previously provided to Storm investors under its CBA Resolution Scheme. The combined amount of $268 million available as compensation from CBA is approximately 72% of the amount of $373 million which represents the total loss of Storm investors that is allocated to CBA under the ASIC compensation model.

2.7. This settlement meant that participating CBA customers who borrowed monies from CBA to invest through Storm and suffered loss as a result were eligible to receive compensation at least equal to 55% of that part of their loss allocated to CBA under ASIC's compensation model (and, in many cases, more than 55% of their loss). Because the basis upon which CBA paid compensation under its earlier Resolution Scheme (a scheme created by CBA in 2009 to provide compensation to investors) (**CBA Resolution Scheme**)was different from the basis of loss calculation under the ASIC compensation model, some Storm investors received compensation from CBA under its Resolution Scheme in excess (and, in some cases, substantially in excess) of the 55% level described above.

2.8. ASIC considers the ASIC/CBA Settlement to be a timely, fair and certain outcome for Storm investors who borrowed from CBA. ASIC would not have agreed to a settlement unless it thought the compensation was appropriate.

2.9. Further, it is not uncommon for litigation to settle shortly before the commencement of a trial. This is sometimes because the work of a plaintiff in prosecuting and preparing for trial persuades a defendant that there is a serious case to be answered and that the defendant has a real prospect of losing at trial. Settlement with CBA does not indicate that ASIC's preparation for trial was wasted, rather it may demonstrate that the trial preparation work undertaken by ASIC assisted in achieving a settlement under which CBA agreed to pay an additional compensation amount of $136 million to Storm investors.

2.10. ASIC considers that it acted consistently with the public interest, and in particular in furtherance of the statutory objective of the confident and informed participation of investors and consumers in the financial system, in bringing ASIC's Storm UMIS Proceeding and in entering into the settlement with CBA.

3. Suggestion that ASIC prevented Storm clients from obtaining information about their financial situation from Storm—attempted imposition of an enforceable undertaking;

3.1. ASIC sought to negotiate an enforceable undertaking (**EU**) with Storm around 18 December 2008, well after Storm had begun to experience problems. At that point, the damage had already occurred in that total investor equity was far less

than total margin loans. The purpose of the EU was to address ASIC's concerns that Storm may have been providing conflicted and incorrect advice to Storm clients who were in negative equity, to the effect that Storm clients did not need to meet their margin calls and should not communicate with the lending banks. ASIC was concerned that this advice may have been influenced by the collapse of the Storm model and it was ASIC's view that it was preferable for Storm clients to seek and have the benefit of independent advice about their affairs. The EU would have facilitated Storm clients being transferred to other financial advisers without the need to go through a lengthy court process. Furthermore, ASIC was concerned that Storm could not have given their clients adequate advice pursuant to their AFS licence conditions and the relevant provisions of the *Corporations Act 2001* - that is, advice relating to each person's individual financial circumstances. ASIC was concerned that Storm, which had 120 employees, may not have been sufficiently resourced to give appropriate advice to the approximately 3,000 investors or investor groups who were its clients and who had used margin loans to invest through Storm in a short time frame.

3.2. It is common practice in a proposed EU for the parties to negotiate the terms of the proposed EU which would be acceptable to both parties. In those negotiations, ASIC indicated the terms of the EU that would be acceptable to protect Storm clients.

3.3. However, Storm did not ultimately offer an EU that was acceptable to ASIC. Around 19 December 2008, Storm voluntarily undertook that it would cease contact with all its clients over the Christmas period. This undertaking was not solicited by ASIC.

3.4. Storm subsequently went into administration on 9 January 2009. Former Storm clients who contacted ASIC after this time may have been referred to the Financial Planning Association for assistance in seeking independent advice about their affairs.

4. ASIC's intervention in the class action (submission 90); and

4.1. On 22 December 2010 ASIC commenced proceedings against Macquarie Bank (Macquarie), CBA and Bank of Queensland (BoQ) based on the operation by Storm of an alleged unregistered managed investment scheme in which the banks were knowingly concerned (the UMIS Proceeding).

4.2. In addition to ASIC's UMIS Proceeding, a class action was commenced by lead applicant Tracey Richards on 24 December 2010 against Macquarie, seeking compensation for losses suffered in respect of investments made through Storm (the **Richards Proceeding**). Levitt Robinson Solicitors acted for Ms Richards in the class action.

4.3. The Richards Proceeding initially claimed that an unregistered managed investment scheme was operated by Storm and Macquarie in contravention of the Corporations Act. In August 2011 and December 2011 the claims in the Richards

Proceeding were amended to pick up and replicate the claims brought by ASIC in its proceedings against the banks.

4.4. The trial of ASIC's UMIS Proceeding (which proceeded against Macquarie and BoQ after ASIC had settled with CBA) and the trial of the Richards Proceeding were heard together with most of the evidence being presented by ASIC.

4.5. In March 2013 Ms Richards agreed to settle the Richards Proceeding with Macquarie for $82.5 million, inclusive of costs and interest. As the lead applicant, she did so on behalf of herself and all group members. ASIC was not a party to, nor invited to participate in, the settlement negotiations between Ms Richards and Macquarie.

4.6. Under the settlement, the 317 group members who were clients of Levitt Robinson and who had made a contribution, in varying amounts, to the costs of the proceedings ("funding group members') were to receive reimbursement of the legal costs that they had contributed plus a compensation amount representing 42% of their estimated losses from investing through Storm. However, the majority of group members, about 733 people, were to receive an amount representing only about 17.6% of their losses. This difference was attributable to the payment to the funding group members of a "funder's premium" of $28.875 million, being 35% of the total settlement pool. At no time was it asserted by Macquarie or Levitt Robinson that there was any difference between the underlying legal merits of the claims against Macquarie of the funding group members and the other group members.

4.7. On 26 April 2013 ASIC intervened in the application for approval of the settlement by the Federal Court of Australia. ASIC's decision to intervene was prompted by concerns about the distribution of the settlement money and by the significant fact that ASIC had been so closely involved in the legal and factual issues underlying the allegations against Macquarie also made in the Richards Proceeding. ASIC's concerns centred on:

(a) the distribution of the compensation money, and in particular the disparity between the compensation outcomes for the majority of class action members (who were not clients of Levitt Robinson and were not legally represented) who were to recover approximately 18% of their lost 'net equity' and the minority of class action members (clients of Levitt Robinson) who were to recover approximately 42% of their lost 'net equity';

(b) the quality of disclosure to class action members of the effect of the settlement and the extent of prior disclosure of the prospect of disparate outcomes under a settlement; and

(c) the uncertainty under the settlement of the rights of class action members to pursue claims against other banks.

4.8. On 3 May 2013, Justice Logan of the Federal Court approved the settlement of the Richards Proceeding, despite concerns expressed by ASIC about the funders' premium.

4.9. ASIC appealed the decision of Justice Logan to approve the settlement. ASIC's appeal related to:

(a) the distribution of the settlement money, which was not in proportion to losses suffered by class action members;

(b) whether the funders' premium for class action members who funded the action amounted to an unfair advantage for those members at the expense of the remaining 70% of class action members;

(c) whether inadequate notice was given to class action members of the prospect of payment of a funders' premium; and

(d) whether class action members who were not clients of Levitt Robinson had the same opportunity to become members of the group funding the action as did those class action members who were clients of Levitt Robinson.

4.10. The Full Court unanimously upheld ASIC's appeal.

4.11. The Full Court decided that the distribution of the settlement sum was not fair and reasonable to all group members. It said that the unfairness arose in two ways: first, the lack of opportunity afforded to class members who were not clients of Levitt Robinson to share in the premium proposed to be paid to those funding the class action; and secondly the inappropriate calculation of the premium by reference to success fees obtained by commercial litigation funders.

4.12. The Full Court said: "*In the circumstances outlined, the settlement cannot be said to be fair and reasonable to all group members. A substantial wrong has occurred which the Court is obliged to correct."*

4.13. In discussing the funders' premium aspect of the settlement, Justices Jacobson, Middleton and Gordon said:

> *"In the present case, not only was there inequality of opportunity afforded to group members to share in the Funders' Premium but advantageous terms were offered, after the settlement was reached at the mediation, and those terms were available only to clients of Levitt Robinson. If there is an analogy, it is that a small number of group members (who were also clients of Levitt Robinson) were able to place a bet on a horse race after the race had run and knowing the result of the race."*

4.14. Subsequent to the Full Court judgment, Macquarie and Ms Richards held further discussions and agreed to a second settlement proposal which was approved by the Court on 13 December 2013.The settlement provides for the same total settlement amount of $82.5 million, but the basis on which that amount is to be distributed amongst the group members has materially changed. The settlement amount will now be distributed to group members principally in proportion to the losses they have suffered. Group members who had contributed to funding the costs of the class action remain entitled to receive reimbursement of the legal costs they have contributed but otherwise have the same entitlement to the settlement funds as non funding group members.

5. ASIC's involvement in the negotiated compensation deal for the Doyles and not other victims.

5.1. The ASIC Doyle Proceeding was brought in the public interest, in part, to compensate Mr and Mrs Doyle who could not afford to bring their own proceedings and, more importantly, to provide indirect assistance to other Storm investors in a similar position to mount similar claims. Through proceedings such as these, other potential claimants are informed of the types of causes of action that may be available, how they can be pleaded and what degree of legal and factual support they may have. In this regard it should be noted that the class actions brought by Levitt Robinson against Macquarie (the Richards Proceeding) and the CBA (the **Sherwood Proceeding**), were amended to include both ASIC's UMIS case and the ASIC Doyle causes of action. The later class actions brought against BoQ and Westpac also included claims similar to those raised in the ASIC Doyle Proceeding.

5.2. The claims made in the ASIC Doyle Proceeding require assessment by reference to the distinct circumstances of each investor of matters such as liability , causation of loss and amount of loss. Mr and Mrs Doyle were chosen for representation in the public interest because ASIC believed that their personal circumstances provided a suitable factual background against which to test the causes of action in the ASIC Doyle Proceeding and because ASIC considered that they had reasonable prospects of success. By prosecuting claims on behalf of Mr and Mrs Doyle, ASIC hoped to establish a path to compensation that would be followed by other lawyers on behalf of other Storm investors. To a large extent this occurred with the inclusion of claims similar to those made in the ASIC Doyle Proceeding in class actions brought against banks connected to the Storm investment model.

6. Commonwealth Bank settlement

In a letter to ASIC, Mr Ron Jelich, (submission 172) noted that in December 2010, ASIC commenced legal proceedings against the Commonwealth Bank arising out of its involvement in an alleged unregistered Managed Investment Scheme operated by Storm Financial. He wrote:

> *It's incongruous to believe that literally hours, taking into account the weekend, before the commencement of this trial that ASIC can announce all charges have been dropped against the CBA…This was an opportunity for ASIC to follow through on its publicly stated commitments to raise the standard of future corporate behaviour. Why would ASIC drop these charges at the 11th minute of the 11th hour?*

6.1 There were no "charges" brought by ASIC against CBA. The UMIS Proceeding did not involve criminal charges, nor claims for a civil penalty. The UMIS Proceeding was an attempt to obtain compensation for customers of CBA, BoQ

and Macquarie who had used monies borrowed from those banks to invest through Storm, and who had suffered loss as a result. As is set out in the answer at paragraph 2, ASIC was always clear that it wished to obtain compensation for investors, if possible through a negotiated settlement. ASIC did achieve such a settlement with CBA, which saw eligible investors receive at least (and in many cases more than) 55% of their loss as calculated by the ASIC compensation model and as allocated to CBA.

6.2 See response above to the Question "ASIC's last minute settlement with CBA, one submitter termed this act as 'the mother of all back-flips' (submission 41)" at paragraph number 2.

7. Another submitter (submission 88, name withheld) similarly argued that ASIC agreed that CBA would not have to answer any charges providing they made some obtuse offer to investors. Mr Peter Dunell (submission 90) also argued that ASIC had *'the mandate to pursue the CBA and had considerable evidence to support its case…but 'chose to sit behind closed doors with its protagonist and strike out a deal which was never agreed to by investors.'*

Has ASIC explained to the victims of Storm Financial the reasons for not taking CBA to trial?

7.1. On 17 September 2012, ASIC published a document titled "Frequently Asked Questions" on its dedicated Storm Financial website, which provided detailed information about the settlement reached with CBA. The following information regarding the reasons ASIC had entered into the settlement was contained in that document:

Why is ASIC settling with CBA now?

- *2.1 ASIC recognises that CBA's Resolution Scheme was a constructive response by CBA to the financial hardship faced by some of CBA's customers arising from their investment with Storm.*

  2.2 The provision of additional compensation by CBA under the agreement reached between ASIC and CBA resulted from continuing negotiations between CBA and ASIC about whether it was appropriate to provide additional compensation for some CBA customers who borrowed to invest through Storm, over and above that already provided under the CBA Resolution Scheme.

  2.3 The provision of the additional compensation obtained pursuant to the settlement agreement reached between ASIC and CBA is positive for Storm investors who borrowed from CBA to invest in Storm and, recognizing the compensation already provided under the CBA Resolution Scheme, produces a timely, fair and certain outcome for CBA customers.

  2.4 ASIC welcomes CBA's approach to resolving this matter and sees it as an example of a responsible approach by a bank to

dealing with its customers.

2.5 ASIC's end objective in commencing the legal proceedings has always been to obtain compensation for investors for losses incurred as a result of investment through Storm. This has been achieved without the need for a long, drawn out legal process. Legal proceedings can often be uncertain. Investors can be confident that we would not have agreed to a settlement of this matter unless we regarded the amount of compensation to be appropriate.

7.2. ASIC also issued a media release on 14 September 2012 (the day the settlement with CBA was reached), which stated, in part, as follows:

- *CBA's $136 million of additional compensation is intended to ensure that each CBA investor (or investor group) who takes part in the settlement will get compensation of approximately 55% of that part of their total loss allocated to CBA under the ASIC compensation model. This calculation takes into account the compensation CBA already provided to investors under its Resolution Scheme. In determining the aggregate amount of compensation, allowance has also been made for the period that has elapsed between the time that Storm investors suffered loss and the time of receipt of compensation. Today's agreement provides other benefits to Storm investors who borrowed from CBA:*
  - *if, after compensation is applied to an investor's outstanding Storm-related margin loan, the investor is still in negative equity on their margin loan, the balance of the loan will be written off, and*
  - *an investor granted an interest-payment moratorium by CBA will have that moratorium interest written off.*
- *Subject to the Court dismissing ASIC's claim against CBA, this agreement will bring to a close the legal action against CBA in ASIC's unregistered managed investment scheme proceedings which were brought in the Federal Court of Australia in Brisbane in December 2010. Today's agreement was reached as a culmination of discussions between CBA and ASIC about whether it was appropriate to provide additional compensation, over and above that already provided under the CBA Resolution Scheme, and was reached without any admission of liability by CBA. ASIC will request the Court to dismiss its proceedings against CBA and the agreement will become effective upon that occurring.*
- *ASIC will continue the unregistered managed investment scheme proceedings against Storm, Bank of Queensland and Macquarie, which are scheduled to start on Monday 17 September 2012. ASIC estimates the total loss suffered by all investors who borrowed monies from banks to invest through Storm to be approximately $830 million.*
- *Mr Medcraft said today, 'ASIC's objective of obtaining compensation for Storm investors has been achieved today for CBA customers, without the need for a long, costly legal process that brings with it a level of uncertainty. "Today's compensation deal is a timely, fair and certain outcome for Storm investors who borrowed from CBA. Storm investors can*

be confident we would not have agreed to a settlement unless we thought the compensation was appropriate."

7.3. Further, ASIC issued a media release on 16 April 2013 (13-214MR) providing a general response to a number of similar letters which ASIC had received from some Storm investors asking about the settlement with CBA. The media release (and the letters in response which ASIC sent to Storm investors who had written to ASIC) also set out the reasons that ASIC entered into the settlement with CBA.

7.4. In addition to ASIC's media releases, letters to those investors who had written to ASIC, and the information on ASIC's website, ASIC's Storm investor liaison team has communicated with a large number of investors who have contacted ASIC directly and explained the reasons for ASIC's settlement with the CBA.

7.5. It should be recognised that if ASIC had not settled with CBA and had instead proceeded to trial, it may have lost at trial and the additional $136 million compensation payable by CBA would not have been available to Storm investors.

8. Was it ever ASIC's intention 'to test the legality of CBA's involvement'?

8.1. ASIC sought compensation from CBA for Storm investors. ASIC's UMIS Proceeding alleged, amongst other things, that an unregistered managed investment scheme was operated by Storm in contravention of s.601ED(5) of the Corporations Act, and that each of the bank respondents, including CBA, were knowingly involved in that contravention. A Court finding of that nature then provided a basis under section 1325 of the Corporations Act for ASIC to seek compensation form CBA on behalf of investors.

8.2. As is set out in paragraph 2, ASIC was ultimately able to achieve a settlement with CBA on terms which it regarded as acceptable, and which resulted in CBA customers who had borrowed from CBA to invest in Storm receiving compensation equal to at least 55% (and, in many cases, more than 55%) of their loss as calculated by the ASIC compensation model and allocated to CBA.

8.3. It should be recognised that if ASIC had not settled with CBA and had instead proceeded to trial, it may have lost at trial and the additional $136 million compensation payable by CBA would not have been available to Storm investors.

8.4. The ASIC/CBA Settlement is documented in a Settlement Agreement between ASIC and CBA which was executed on 14 September 2012. ASIC entered into the ASIC/CBA Settlement because ASIC believes that the settlement reached was a timely, fair and certain outcome for Storm investors who borrowed from CBA. ASIC also believes that the compensation obtained for CBA investors was appropriate, and met ASIC's objective of obtaining compensation for Storm investors who borrowed from CBA, without the need for a long, costly and uncertain legal process.

8.5. See response above to the Question "ASIC's last minute settlement with CBA, one submitter termed this act as 'the mother of all back-flips' (submission 41)" at paragraph number 2. .

9. What was the catalyst that drove ASIC to seek a settlement with the CBA?

9.1. It has always been ASIC's position that a settlement on the right terms could provide a better outcome than the uncertainty and delay involved in litigation. As is set out in the response to the Question "ASIC's last minute settlement with CBA, one submitter termed this act as 'the mother of all back-flips' (submission 41)" at paragraph number 2, ASIC's position was stated in its public statements about the UMIS Proceeding.

9.2. In considering whether to settle with CBA, ASIC had to assess the prospects of success of its legal proceedings against CBA and the level of compensation that might be awarded if the litigation were successful. ASIC was also very conscious of the benefit of Storm investors receiving compensation sooner, rather than after a prolonged legal process that could include awaiting the trial judgment, the outcome of likely appeals to the Full Court of the Federal Court and the High Court, and the necessary assessment of loss by a court on an investor by investor basis. Such a process could have taken three to four years, or more, from the end of the trial at first instance in early 2013.

9.3. Ultimately, through the ASIC/CBA Settlement, ASIC was able to achieve compensation for Storm investors who had borrowed from CBA to invest in Storm that was at least equal to (and in many cases exceeded) 55% of their loss which was allocated to CBA, as calculated by the ASIC compensation model.

9.4. ASIC considered, and considers, the ASIC/CBA Settlement to be a timely, fair and certain result for CBA customers who borrowed monies from CBA to invest through Storm.

9.5. See the response to the above Questions "ASIC's last minute settlement with CBA, one submitter termed this act as 'the mother of all back-flips' (submission 41)" at paragraph number 2 and "Has ASIC explained to the victims of Storm Financial the reasons for not taking CBA to trial?" at paragraph number 7.

10. How many investors received compensation as a result of the CBA compensation scheme?

10.1. There were approximately 2,025 CBA investors or investor groups (where more than one person used monies borrowed from CBA to invest through Storm). Of those 2,025 investors or investor groups:

(a) some 1,845 investors or investor groups received compensation or an offer of compensation from the CBA Resolution Scheme and/or the ASIC/CBA Settlement;

(b) some 1,195 investors or investor groups had previously accepted an offer of compensation under the earlier CBA Resolution Scheme;

(c) some 1,395 investors or investor groups received compensation or an offer of compensation under the ASIC/CBA Settlement;

(d) of the 1,395 investors or investor groups who received compensation or an offer of compensation under the ASIC/CBA Settlement, 745 had also received compensation under the earlier CBA Resolution Scheme, and 650 had not previously received compensation from CBA.

10.2. Approximately 630 CBA investors or investor groups did not receive compensation or an offer of compensation under the ASIC/CBA Settlement, either because:

(a) in aggregate, and over the life of their Storm investments funded by CBA, they made a profit from their investments in Storm, and not a loss; or

(b) in a small number of cases, they are persons who were excluded from the ASIC/CBA Settlement because they were closely associated with the design, implementation or promotion of the Storm investment model, or invested in the Storm scheme jointly with a person who was; or

(c) they had already received, under the earlier CBA Resolution Scheme or another previous settlement with CBA, compensation equal to or higher than 55% of their loss as calculated by the ASIC compensation model and allocated to CBA. Because the basis upon which CBA paid compensation under its earlier Resolution Scheme was different from the basis of loss calculation under the ASIC compensation model, some Storm investors received compensation from CBA under its Resolution Scheme in excess (and, in some cases, substantially in excess) of the 55% level described above.

10.3. The ASIC/CBA Settlement involved CBA agreeing to pay up to $136 million in compensation, plus other benefits, to CBA customers who had borrowed from CBA to invest through Storm. This was in addition to the approximately $132 million, plus other benefits, CBA had previously provided to Storm investors under its CBA Resolution Scheme. This settlement meant that participating CBA customers who borrowed monies from CBA to invest through Storm and suffered loss as a result received compensation at least equal to 55% of that part of that part of their loss allocated to CBA under ASIC's compensation model equivalent to at least 55% of that part of their loss allocated to CBA (and, in many cases, more than 55% of their loss), as calculated by the ASIC compensation model.

10.4. The combined amount of $268 million available as compensation from CBA is approximately 72% of the amount of $373 million which represents the total loss of Storm investors that is allocated to CBA under the ASIC compensation model.

10.5. See the response to the above Question "ASIC's last minute settlement with CBA, one submitter termed this act as 'the mother of all back-flips' (submission 41)" at paragraph number 2.

11. Why did ASIC act to secure 100% compensation for two investors, but only 55% for another group? Are the two investors significantly better off as a result of this decision than any other Storm investor? On reflection, does ASIC consider this is fair?

11.1. ASIC brought the ASIC Doyle Proceeding, a representative proceeding under s 50 of the *Australian Securities and Investments Commission Act* 2001 (**ASIC Act**), against Macquarie, BoQ and Senrac Pty Ltd (a franchisee of BoQ's North Ward branch). The ASIC Doyle Proceeding was not brought against CBA. Unlike ASIC's UMIS Proceeding (which alleged the banks' knowing involvement in the operation by Storm of an unregistered managed investment scheme), the claims made in the ASIC Doyle Proceeding were claims peculiar to the individual circumstances of the claimants, and it was likely that the strength of those claims and the compensation recoverable as a result of them would vary accordingly. This is in contrast to the claims in ASIC's UMIS Proceeding, where the grounds for establishing legal liability (as distinct from quantum of loss) of the banks is likely to be the same or similar for all Storm investors.

11.2. ASIC was of the view that the best way to bring claims of the type brought in the ASIC Doyle Proceeding was on behalf of individuals, in the hope that the presentation of that claim would assist others to bring claims. In this test case, ASIC, unsurprisingly, endeavoured to select plaintiffs who it believed would present a strong case. Mr and Mrs Doyle were chosen for representation in the public interest because ASIC believed that their personal circumstances provided a suitable factual background against which to test the causes of action in the ASIC Doyle Proceeding and because ASIC considered that they had reasonable prospects of success. By prosecuting claims on behalf of Mr and Mrs Doyle, ASIC hoped to establish a path to compensation that would be followed by other lawyers on behalf of other Storm investors.

11.3. To a large extent, this occurred. ASIC stated in its media release dated 29 May 2013 (13-122MR), "*…the allegations against BoQ and Macquarie of breach of contract, unconscionable conduct and liability as linked credit providers of Storm, which were first raised in these proceedings, have provided a template for similar allegations that have been raised in class actions brought on behalf of investors against BoQ, Macquarie and CBA.*" Similar allegations have also been raised in a Storm-related class action against Westpac Banking Corporation Ltd.

11.4. Because the UMIS Proceeding (which was settled, as against CBA, as a result of the ASIC/CBA Settlement) and the ASIC Doyle Proceeding were based upon different causes of action, a like for like comparison on the respective settlement outcomes is not possible nor accurate. ASIC considers that both settlements achieved a fair, reasonable, certain and timely outcome for the CBA borrowers and the Doyles. Settlement of any litigation involves a compromise between the parties.

11.5. See the response to the above Questions "ASIC's last minute settlement with CBA, one submitter termed this act as 'the mother of all back-flips' (submission 41)" at paragraph number 2, "ASIC's involvement in the negotiated

compensation deal for the Doyles and not other victims" at paragraph number 5, and "Has ASIC explained to the victims of Storm Financial the reasons for not taking CBA to trial?" at paragraph number 7.

12. Did the Commonwealth Bank admit any liability as part of its settlement? [If the answer is no] Given the significance of the Storm case, why was a settlement without an admission of liability agreed to? & Mr Medcraft advised that the Storm Financial case has cost ASIC $50 million. Given that amount of taxpayer money already spent on an investigation, why was the CBA case settled rather than pursued through the courts?

12.1. In settling the ASIC UMIS Proceeding brought against it by ASIC, CBA did not admit liability in relation to ASIC's allegations and the terms of the agreement reached between ASIC and CBA reflect this.

12.2. ASIC is aware of criticism from some Storm investors that ASIC should not have accepted a settlement from the CBA without an admission of liability, and that indeed ASIC should have continued to litigate against CBA to set a precedent. As is explained in the response to Question 2 (see paragraph 2), a primary purpose of ASIC in bringing the UMIS Proceeding was to obtain compensation for Storm investors. The ASIC/CBA Settlement resulted in CBA customers who used monies borrowed from CBA to invest through Storm receiving an amount of compensation that was at least equal to (and in many cases more than) 55% of the loss suffered by the investor or investor group as calculated by the ASIC Compensation Model and allocated to CBA. ASIC believes that the ASIC/CBA Settlement resulted in a timely, fair and certain outcome for CBA customers.

12.3. It should be recognised that if ASIC had not settled with CBA and had instead proceeded to trial, it may have lost at trial and the additional $136 million compensation payable by CBA would not have been available to Storm investors.

12.4. The amount of $50m stated at the time by ASIC's Chairman, Mr Medcraft, was a reference to the total cost incurred by ASIC to that date, in undertaking its investigations into the collapse of Storm. This includes investigating the conduct of Storm, its directors and advisers and the conduct of the banks, preparing and prosecuting the ASIC UMIS Proceeding, the ASIC Doyle Proceeding and ASIC's civil penalty proceedings against Mr and Mrs Cassimatis and the intervention in the court approval of the settlements in the Richards Proceeding (and appeal).

12.5. See the response to the above Questions "ASIC's last minute settlement with CBA, one submitter termed this act as 'the mother of all back-flips' (submission 41)" at paragraph number 2, "Has ASIC explained to the victims of Storm Financial the reasons for not taking CBA to trial?" at paragraph number 7, and "What was the catalyst that drove ASIC to seek a settlement with the CBA?" at paragraph number 9.

Macquarie Bank and Bank of Queensland settlement

In response to the collapse of Storm, ASIC initiated compensation proceedings against the Bank of Queensland, Senrac and Macquarie on behalf of two investors (Barry and Deanna Doyle). Mr Peter Dunell (submission 90) also noted that in the case brought by ASIC for Doyle v CBA, ASIC was able to gain compensation acceptable to the investors but this was not a case of precedent. He asked, *'Why did they do this when so many other poor souls could have benefited.*

13. Could ASIC offer explanations to the submitters above and the numerous others who wrote to the committee deeply unhappy about ASIC's actions in respect of the Commonwealth Bank, Macquarie Bank and Bank of Queensland settlements?

13.1. See the response to the above Question "ASIC's involvement in the negotiated compensation deal for the Doyles and not other victims" at paragraph number 5, and "Why did ASIC act to secure 100% compensation for two investors, but only 55% for another group? Are the two investors significantly better off as a result of this decision than any other Storm investor? On reflection, does ASIC consider this is fair?" at paragraph number 11 above.

14. As asked by Mr Jelich—Why did ASIC not use this settlement framework as a matrix for settlement of the other thousands of claims against the lending institutions?

14.1. See the response to the above Question "ASIC's involvement in the negotiated compensation deal for the Doyles and not other victims" at paragraph number 5, and "Why did ASIC act to secure 100% compensation for two investors, but only 55% for another group? Are the two investors significantly better off as a result of this decision than any other Storm investor? On reflection, does ASIC consider this is fair?" at paragraph number 11 above.

15. Did ASIC confer with the victims or their legal representatives before pursuing the settlements? If not why not?

15.1. Negotiations with the CBA that resulted in the Settlement Agreement were confidential between the parties. This is a common feature in the settlement of litigation. ASIC had undertaken significant work in understanding and evaluating the causes and quantum of losses suffered by Storm investors and the potential liability of the banks. It was simply not possible for the large number of Storm investors who borrowed from the CBA to be parties to any settlement.

15.2. ASIC informed investors and SICAG of the agreement reached between ASIC and CBA as soon as the agreement was reached.

15.3. The proceedings on behalf of Mr and Mrs Doyle were settled following negotiations between ASIC, Mr and Mrs Doyle, Macquarie and BoQ. These negotiations were also, and unsurprisingly, confidential. These proceedings were not a class action, unlike the Richards and Sherwood proceedings. Mr and Mrs Doyle had independent legal representation and advice in the settlement negotiations.

16. Did ASIC consider fairness when it, according to a submitter, *'negotiated a deal for the Doyles which left every other Storm Financial (Macquarie Bank) investor out of any consideration for compensation even though they suffered a similar fate to the Doyles*'

16.1. As is explained at paragraph 11, the ASIC Doyle Proceeding was based upon Mr and Mrs Doyle's personal circumstances which gave rise to claims against BoQ and Macquarie.

16.2. ASIC had a responsibly to the Doyles to settle their claim on a basis that reflected the strength of their claim, once the opportunity to do so arose. The Doyles also had the benefit of independent legal advice in the settlement negotiations.

16.3. As is also explained in paragraph 11, ASIC hoped that, in bringing the ASIC Doyle Proceeding, it would establish a path to compensation that would be followed by other lawyers on behalf of other Storm investors. To a large extent this occurred with the inclusion of claims similar to those made in the ASIC Doyle Proceeding in class actions brought against banks connected to the Storm investment model.

16.4. See the response to the above Question "ASIC's involvement in the negotiated compensation deal for the Doyles and not other victims" at paragraph number 5, and "Why did ASIC act to secure 100% compensation for two investors, but only 55% for another group? Are the two investors significantly better off as a result of this decision than any other Storm investor? On reflection, does ASIC consider this is fair?" at paragraph number 11 above.

17. Is ASIC able to state the number of investors that were left out of 'consideration for compensation even though they suffered a similar fate to the Doyles'? & Why did ASIC take compensation proceedings on behalf of only two Storm investors? Why were the two investors selected? Was their experience any different to that of other investors?

- What has ASIC done to assist the investors that were left out?

17.1. It is not correct to say that ASIC took compensation proceedings on behalf of only 2 investors. ASIC's UMIS Proceeding sought compensation for all investors who had borrowed from CBA, BoQ or Macquarie to invest through Storm.

17.2. In relation to CBA customers, ASIC was ultimately able to enter into the ASIC/CBA Settlement, which saw CBA make available a total of $268 million as compensation, which equates to approximately 72% of the amount of $373 million which represents the total loss of Storm investors that is allocated to CBA under the ASIC compensation model. Those investors were eligible under the ASIC/CBA Settlement to receive compensation that equated to at least 55% (but in many cases more) of their loss as calculated by the ASIC compensation model and allocated to CBA. ASIC refers to its response to the Question "ASIC's last minute settlement with CBA, one submitter termed this act as 'the mother of all back-flips' (submission 41)" at paragraph number 2.

17.3. In relation to ASIC's UMIS Proceeding against BoQ and Macquarie, judgment remains outstanding. In the event ASIC is successful then this will provide the basis for pursuing compensation for those who borrowed from BoQ. The Richards class action was settled in a way which is likely to preclude ASIC seeking further compensation from Macquarie on behalf of Storm investors who borrowed from Macquarie to invest through Storm

17.4. As is explained at paragraph 11, the claims made against BoQ and Macquarie in the ASIC Doyle Proceeding were based upon the individual circumstances of Mr and Mrs Doyle. It is therefore not possible to state what proportion of investors may be able to make similar claims against financiers.

17.5. ASIC refers to its response to the Question "ASIC's involvement in the negotiated compensation deal for the Doyles and not other victims" at paragraph number 5, and "Why did ASIC act to secure 100% compensation for two investors, but only 55% for another group? Are the two investors significantly better off as a result of this decision than any other Storm investor? On reflection, does ASIC consider this is fair?" at paragraph number 11, and "Did ASIC consider fairness when it, according to a submitter, 'negotiated a deal for the Doyles which left every other Storm Financial (Macquarie Bank) investor out of any consideration for compensation even though they suffered a similar fate to the Doyles" at paragraph 16 above.

18. How many customers did the Bank of Queensland and Macquarie have from Storm Financial?

18.1. 322 investors (or investor groups) borrowed from BoQ to invest through Storm. 1045 investors (or investor groups) borrowed from Macquarie to invest through Storm.