

## Chapter 12

### Commonwealth Financial Planning Limited: Recent developments and committee conclusions

12.1 This chapter outlines the developments that occurred in the final two months of the committee's inquiry that led to ASIC and the CBA correcting key evidence about the compensation process that both organisations gave to the committee. This chapter also contains the committee's overall conclusions on the CFPL matter.

#### Developments in May 2014

12.2 As noted in Chapter 9, following a request from the committee at a public hearing on 10 April 2014, ASIC provided the committee with a copy of the letter it sent to CFPL on 29 February 2008.<sup>1</sup> The content of the letter revealed that ASIC's surveillance project focused on the operations of another CBA subsidiary, Financial Wisdom Limited (FWL), in addition to CFPL.

12.3 The content of this letter is troubling for several reasons. First, the letter indicates that ASIC's surveillance was directed towards advice provided by two CBA subsidiaries, not just CFPL. The fact that FWL was subject to surveillance was not revealed in ASIC's summary of the surveillance project in its written submission,<sup>2</sup> nor had ASIC referred to its concerns regarding FWL at any prior point in the inquiry. The issues relating to FWL, and in particular with regard to adviser Mr Rollo Sherriff, were not widely revealed until Fairfax Media published allegations regarding FWL and Mr Sherriff on 3 May 2014. Subsequently, ASIC provided the committee with a supplementary submission which explained that ASIC had conducted an investigation into Mr Sherriff's conduct, but decided against taking any enforcement action against him. ASIC also noted that its 'work on this matter led to CBA reviewing all advice given by Mr Sherriff to his clients and FWL paying compensation totalling \$7.3 million to 98 of Mr Sherriff's clients'.<sup>3</sup>

12.4 Since that letter was provided to the committee, further revelations and significant developments have occurred. On the evening of Friday, 16 May 2014, both ASIC and the CBA provided the committee with statements correcting evidence previously given during this inquiry. According to the CBA, some elements of the compensation process described in its submission were not applied consistently. The primary differences were:

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1 ASIC, letter to Commonwealth Financial Planning Limited and Financial Wisdom Limited, 29 February 2008, *Additional Information* 7.

2 ASIC, *Submission 45*, pp. 12–13.

3 ASIC, *Submission 45.8*, p. 1.

- not all CFPL and FWL customers were offered \$5,000 to obtain independent advice to review their compensation offer;
- not all CFPL and FWL customers received all the written correspondence described in the CBA's submission including upfront communication with affected customers to advise them of concerns about the quality of advice provided; and
- an independent accountancy expert did not endorse and oversee the remediation process for FWL clients as FWL was not subject to the CFPL enforceable undertaking.<sup>4</sup>

12.5 The CBA advised that where it discussed total compensation payments and the remediation process in its submission or at a public hearing, this applied to both CFPL and FWL customers. ASIC provided a further supplementary submission that noted some of the information ASIC put to the committee about the compensation process was inaccurate because it was based on the CBA's submission.<sup>5</sup> ASIC's previous submissions reported that the compensation paid to affected clients of CFPL totalled \$51 million. The total compensation is now \$52 million; of that amount, \$10.5 million was paid to affected clients of advisers of FWL and \$41.5 million was paid to affected clients of advisers of CFPL.<sup>6</sup>

12.6 Since becoming aware of anomalies in CBA's advice, ASIC informed the committee that it would impose, by agreement with the CBA, conditions on the AFS licences of CFPL and FWL. The revised conditions follow concern that customers of other high-risk advisers in CFPL and FWL were disadvantaged because their compensation process was different from the clients of Mr Nguyen and Mr Awkar—that compensation arrangements were applied inconsistently cross all affected customers of the businesses. The new conditions require CFPL and FWL to apply the conditions agreed to under Project Hartnett to all clients who did not originally receive the benefit of those measures.<sup>7</sup> This includes offering up to \$5,000 to seek independent advice from an accountant, lawyer and/or licensed financial adviser; and allowing all affected clients to reopen the question of compensation.<sup>8</sup>

12.7 The committee was not satisfied with the information contained in ASIC's late supplementary submission or the CBA's correspondence. Although both documents were supposed to correct misinformation provided to the committee, they only added to the confusion already surrounding the compensation process. The committee then wrote to CBA seeking clarification. For example, the committee sought to establish the meaning of 'not all CFPL and FWL customers were offered \$5,000 to obtain

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4 CBA, *Additional Information 10*.

5 CBA, *Additional Information 10*.

6 ASIC, *Submission 45.6*, p. 5.

7 See paragraph 11.4.

8 ASIC, *Submission 45.6*, p. 5.

independent advice to review their compensation offer'. The advice received is now clear that 'none' of the customers under the Past Business Review or three other CFPL advisers received this offer.<sup>9</sup>

12.8 Information provided to the committee shows that:

- under the Past Business Review 2,287 cases were considered and 403 offered compensation; and
- of the three other CFPL advisers, 573 cases were reviewed of which 55 cases were offered compensation.<sup>10</sup>

12.9 The clients of FWL were not part of the Past Business Review but, according to CBA, FWL 'adopted a remediation policy that was very closely based on the Past Business Review'. Thus, the committee concludes that these customers (of the 793 cases where advice was provided, 258 cases were offered compensation) similarly did not receive the \$5,000 offer to assist them obtain independent advice.

12.10 It also turns out that not one of the above clients received an initial letter stating that the CFPL/FWL had concerns about the advice provided. According to the CBA:

Communications to clients of advisers in the Past Business Review were made when further information was required from the customer in order to assess the case and/or there was an assessment of inappropriate advice and compensation was assessed as payable.

The communication with respect to the FWL clients was similar to those in the Past Business Review.<sup>11</sup>

12.11 For months the committee had been led to believe that all clients, not only those of Mr Nguyen and Mr Awkar, had received equal treatment under the compensation schemes. In part, this discrepancy may explain why some people have written to the committee completely confused and distressed by recent correspondence from the CBA.

12.12 This obfuscation by the CBA has further undermined the committee's confidence in the integrity of the process.

12.13 The committee wants to make two final points about the compensation offered: the amounts were substantial and, in a number of cases, the difference between the CBA's first and final offers was significant. The committee has cited a few cases already. For example, Maurice Blackburn referred to one of its clients who, before he sought legal representation, 'was offered one-tenth of what Maurice

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9 CBA, answer to question on notice, no. 18, p. 13.

10 CBA, answer to question on notice, no. 18, p. 7.

11 CBA, answer to question on notice, no. 18, p. 15.

Blackburn ultimately negotiated'.<sup>12</sup> In order to obtain some sense of the gap between the first and final offers, the committee obtained from the CBA in confidence a sample from the highest to the lowest. The figures have been rounded and approximate but they included an initial offer of \$230,000 to a final offer of around \$657,000 (a difference of about \$427,000), an initial offer of \$29,000 to a final offer of \$101,500 (a \$72,500 difference) and an initial offer of \$5,500 to a final offer of \$33,900 (a difference of around \$28,000). On the lower end of the scale they ranged from an initial offer of \$49,000 to a final offer of \$50,000 (a difference of just over \$1,000). From the indicative sample provided, the other differences recorded between the initial offer and the final offer involved sums of \$23,800, \$13,600, \$12,700, \$10,800, \$6,900, \$2,000, \$184 and zero.

### **Committee view**

12.14 The preceding chapters have outlined the committee's concerns about ASIC's response to the seriousness of the problems at CFPL. The committee also has significant concerns about the process for providing restitution to affected clients. From the very beginning of the inquiry, the committee has been troubled by the CBA's attitude and the information it has provided.

12.15 Firstly, the committee believes that the CBA's bland suggestion that clients received 'inappropriate advice' ignores the very real distress experienced by CFPL clients as a result of the calculated deceit by their financial advisers. The committee has little doubt that the pain and suffering experienced by the CFPL clients who gave evidence was almost certainly experienced by countless other CFPL clients.

12.16 Secondly, the FWL matter was not disclosed to the committee, either by ASIC or the CBA, until April 2014 when the committee obtained from ASIC a letter it sent to the CBA on 29 February 2008. The letter indicated that ASIC's surveillance was not only directed toward the advice being provided by the CFPL, but also the advice from another CBA subsidiary, FWL.

12.17 Finally, there were the developments in May 2014 that led to licence conditions being imposed on CFPL and FWL and both ASIC and the CBA providing statements to the committee correcting their evidence. This shows that, for some time, both the committee and ASIC had not been kept fully or properly informed of the compensation process for clients affected by serious misconduct within two of the CBA's businesses. Until ASIC and the CBA provided corrections to their evidence, the committee had not been provided with accurate information on the total amount of compensation or the process for remediation. The imposition of licence conditions on CFPL and FWL show that ASIC has finally begun to hold the CBA to account. Nevertheless, ASIC continues to maintain that the compensation process, as originally devised, 'was fair and robust'.<sup>13</sup>

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12 Mr John Berrill, Maurice Blackburn Lawyers, *Proof Committee Hansard*, 10 April 2014, p. 16.

13 ASIC, *Submission 45.6*, p. 5.

12.18 Notwithstanding the recent developments, the committee is deeply concerned by both the number of clients that were potentially affected by serious misconduct who have not received fair compensation and the processes put in place by the CBA to reconstruct incomplete client files and compensate CFPL clients. The committee is particularly concerned by the apparent asymmetries of knowledge and negotiating power inherent in the compensation process, wherein vulnerable clients without expert financial knowledge or legal representation (including clients without the means to access legal representation) were largely forced to rely on the CBA's assurances about the integrity of the process. The evidence received from the law firm Maurice Blackburn that suggested CFPL clients without legal representation may have received inadequate compensation was telling in this regard. There was a clear incentive for CFPL to minimise the amounts it repaid clients; clients that challenged the compensation offered and had copies of their documentation had their payments substantially increased.

12.19 The committee considers that there are potentially many more affected clients that have not been fairly compensated. The clients that the committee invited to give evidence at a public hearing were exceptional in that they were willing to voice their concerns publicly and were able to fight for compensation because of their circumstances, either because they had a family member determined to assist them with their case or because the next CFPL adviser they dealt with after a rogue adviser was Mr Jeffrey Morris, one of the whistleblowers, who gave them a copy of their original file.

12.20 The committee notes that the CBA made (or will make) \$5,000 available to each affected CFPL client to help pay for an independent review of the compensation offered. The CBA, however, controlled which accountants or lawyers could be selected. In any case, the committee believes this \$5,000 is inadequate for its intended purpose. In this connection, the committee points to the evidence received from Maurice Blackburn suggesting that the reviews it conducted of client files cost somewhere in the order of \$35,000 per client (this cost being covered in the eventual settlement between Maurice Blackburn's clients and the CBA). While the committee does not believe that Maurice Blackburn's charges are necessarily indicative of the amount other law firms (or other suitably qualified professionals) might charge for this service, it would nonetheless strongly suggest that the \$5,000 offered by the CBA was inadequate.

12.21 The committee has carefully weighed the evidence received about the file reconstruction process, including evidence from ASIC and the CBA suggesting the process was fair and proper, and evidence from Mr Jeffrey Morris and Ms Marilyn Swan suggesting the process involved the manipulation of client files to reduce compensation payable. The committee believes that serious questions remain unanswered on this score. A more comprehensive, independent review of both CFPL client files and the file reconstruction process is necessary to remove doubts about the integrity of the process. The committee believes that such a review should include a forensic re-examination of the files of each client potentially affected by misconduct

within CFPL, and assess whether the compensation made available to CFPL clients was adequate.

12.22 To the committee, it appears that the following five options are available:

- (a) the arrangements in place as a result of the licence conditions ASIC recently imposed on CFPL's and FWL's AFS licences are left to run their course;
- (b) the above arrangements or a separate review process agreed to by ASIC and the CBA, and funded by the CBA, with the addition of a client advocate appointed as part of the review process to ensure client interests are properly represented;
- (c) a complete review of the compensation arrangements for all clients of financial advisers suspected of providing bad advice, to be undertaken by an independent law firm or other expert appointed by the government, again with a client advocate appointed;
- (d) an independent inquiry established by the government and headed by an eminent and knowledgeable person, such as a retired judge; or
- (e) a Royal Commission.

12.23 As noted above, the committee is not satisfied with option (a), that is, the current arrangements. It is acknowledged that the process has the advantage of compensation potentially being determined in a timely fashion. It is also acknowledged that an ASIC-appointed independent expert will now oversee the compensation process. However, the committee notes that the independent expert was not appointed to act as an advocate for client interests. The absence of a client advocate in the compensation process is, in the committee's view, a key deficiency in that process. The compensation arrangements are also supposed to comfort affected clients; yet, the committee has been contacted by several clients now anxious and confused by the CFPL's communications with them. Another key concern is that the CBA is still determining the compensation amounts based on files that contain documents claimed to be fraudulent or that are 'missing' key documents. The scheme also applies only to a limited number of clients, whereas the committee has received evidence indicating that the problems with CFPL were far more widespread.

12.24 Options (b) and (c) aim to improve on the current arrangements by requiring a client advocate. These processes may still result in relatively timely determinations. They also have other advantages such as greater independence from the CBA and, unlike a public inquiry, the cost of the review could be borne entirely by the CBA. However, both options (b) and (c) only deal with instances of misconduct that have currently been identified. The committee has no reason to believe that the cases on the public record to date represent the entirety of the serious misconduct that took place within CFPL.

12.25 The committee's confidence in ASIC's ability to get the process right this third time is severely undermined and the committee is not convinced that the regulator

should be left to manage this matter any longer. ASIC has shown that it is reluctant to actively pursue misconduct within CFPL and FWL; rather, it appears to accept the information and assurances the CBA provides without question. The committee is also strongly of the view that the CBA's credibility in the CFPL matter is so compromised that it should not be directly involved in future arrangements for investigating the misconduct or reviewing the compensation process.

12.26 There were fundamental and widespread problems within CFPL. It is essential that:

- all rogue advisers are identified and that any conduct that may amount to a breach of any law or professional standard pursued; and
- all clients who have suffered as a consequence of the serious misconduct that occurred receive just compensation.

12.27 Given the seriousness of the misconduct involved and the need for all client files to be reviewed, the committee believes that a review with sufficient investigative and discovery powers should be established by the government to undertake this work. To resolve this matter conclusively and satisfactorily, the inquiry would need the powers to compel relevant people to give evidence and to produce information or documents. The committee is of the view that a judicial inquiry is warranted. The CFPL scandal needs to become a lesson for the entire financial services sector. Firms need to know that they cannot turn a blind eye to rogue employees who do whatever it takes to make profits at the expense of vulnerable investors. If this matter is not pursued thoroughly, there will be little incentive for Australia's major financial institutions to take compliance seriously.

### **Recommendation 7**

**12.28 The committee recommends that the government establish an independent inquiry, possibly in the form of a judicial inquiry or Royal Commission, to:**

- **thoroughly examine the actions of the Commonwealth Bank of Australia (CBA) in relation to the misconduct of advisers and planners within the CBA's financial planning businesses and the allegations of a cover up;**
- **identify any conduct that may amount to a breach of any law or professional standard;**
- **review all files of clients affected or likely to be affected by the misconduct and assess the appropriateness of the compensation processes and amounts of compensation offered and provided by the CBA to these clients; and**
- **make recommendations about ASIC and any regulatory or legislative reforms that may be required.**

