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Kenneth Hayne must traverse a legal quagmire

By [Chanticleer](#)

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The complexity of the legal reform task facing [banking royal commissioner Kenneth Hayne](#) is laid bare in the first rigorous and detailed analysis of all the corporate collapses and fraudulent financial activity that hit consumers and ended up in court between 1981 and 2018.

David Millhouse, who was awarded a PhD by the faculty of law at Bond University for his thesis on the systemic and cultural failures in Australian financial services, says unless there is substantial law reform systemic deficiencies in regulation will remain.

A key part of Millhouse's analysis was to first quantify the financial losses incurred by investors in non-bank financial entities in Australia over the 38 years to 2018. He drew upon senior court judgments and disclosures by royal commissions, parliamentary inquiries, regulators, liquidators' reports and selected third party judgments. His thesis has 2490 references and analysis of 320 court cases.



Banking royal commissioner Kenneth Hayne is faced with a legal minefield for consumer protection. **David Rowe**

He concludes that investors in entities owned by the big four banks suffered losses of about \$14.7 billion while investors in a range of other non-bank entities suffered losses of about \$38 billion. The heaviest losses of all were borne by investors in managed investment schemes targeting agriculture, property and debentures. Combined losses in MIS products were \$17.2 billion.

A stunning finding, which ought to be brought to the attention of Hayne, is the 90 per cent correlation between related party transactions and people being found guilty in court of misleading and deceptive conduct, breaches of fiduciary duties, breaches of good faith and conflicts of interest.

He also found a 75 per cent correlation between those involved in related party transactions and being found guilty of fraud or dishonesty. Millhouse says this is good reason to keep a close eye on industry super funds, which have high levels of related party transactions.

Four failings

Millhouse argues that Hayne must address four strategic failings in the financial system in order to put an end to the "systemic creeping corruption" in some financial services and financial products sold by non-bank financial entities.

He says Australian law permits the contracting out of fiduciary obligations. The Corporations Act subsumes general law fiduciary obligations beneath regulatory



process and in superannuation statutory intervention excludes access to the general law relating to conflict of interest

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Millhouse says people responsible for overseeing investments, whether they are a super trustee or a director of a company, need to take fiduciary to mean absolute loyalty to the interests of the consumer.

Financial collapses and frauds, 1981-2018

NBFE* category	NBFES with data**	Funds lost/ permanently impaired (\$m)	Beneficiaries/ investors impacted
Financial conglomerates	15	14,731	112,634
Government rescued entities	5	6,502	7
Insurance entities	6	957	69,292
Hedge funds	3	738	1,745
MIS/debenture schemes real estate	56	10,423	291,517
MIS forestry & agribusiness	23	6,826	169,590
Companies similar business model	6	178	2,324
MIS infrastructure	2	2,924	850
Securities broking & leveraged lending	8	1,105	2,304
Securities trading platforms	12	226	5,647
Wealth management/financial planning	43	4,018	423,741
Retail superannuation	3	372	31,076
Industry superannuation	5	2,918	291,458
Workers entitlement funds	2	146	24,730
Other superannuation entities	3	105	1,370
Finance companies	7	81	487,323
Total sample	199	52,251	1,915,608

* Non-bank financial entities. ** Authoritative empirical data. SOURCE: DAVID MILLHOUSE

He says Hayne needs to avoid recommending the passage of more laws given that the "Age of Statutes" over the past 25 years resulted in a large compliance industry with attendant increased costs borne by investors.

In Australia, the best interests of consumers have often been contractually overridden by parties with conflicts of interest who have failed to meet requirements of a fiduciary position.

The three other areas of reform identified by Millhouse are: harmonisation of best interest duty, eliminating conflicts of interest, and market conduct regulation for the 21st century.

Millhouse says there are multiple differing interpretations of best interests in the Corporations Act, SIS Act and Fair Work Act and general law interpretations, fiduciary or otherwise, add to the confusion.

Millhouse discloses at the front of his 500-page thesis that he was a director of Trio Capital from November 2003 to October 2005. He entered into an enforceable undertaking with the Australian Prudential Regulation Authority in October 2013. He undertook not to act as a trustee or as a responsible officer of a body corporate that is a trustee, investment manager or custodian of an APRA-regulated superannuation entity for a period of 10 years.

Tony Boyd



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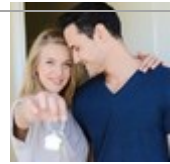
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