

Enforceable Undertaking

Australian Securities & Investments Commission Act 2001

Section 93AA

The commitments in this undertaking are offered to the Australian Securities and Investments Commission ("ASIC") by:

NATIONAL AUSTRALIA FINANCIAL MANAGEMENT LTD (ACN 000 176 116)

Company Secretarial G MLC

105-153 Miller Street

North Sydney NSW 2060



NATIONAL AUSTRALIA SUPERANNUATION PTY. LTD. (ACN 006 972 309)

Company Secretarial G MLC

105-153 Miller Street

North Sydney NSW 2060

MLC NOMINEES PTY LTD (ACN 002 814 959)

Company Secretarial G MLC

105-153 Miller Street

North Sydney NSW 2060

1 Background

- 1.1 On 16 August 2002 MLC Limited announced that approximately \$60 million in compensation would be provided to members of National Australia Financial Management Ltd ("NAFiM") superannuation, pension and investment bond products who had been adversely affected by a unit price adjustment on 30 and 31 October 2001 ("UPA"). The UPA related to investment portfolios in statutory funds worth \$4.285 billion and affected approximately 235,000 investors.

The parties

- 1.2 NAFiM's ultimate holding company is National Australia Bank Limited ("NAB"). NAFiM is a registered life company under the *Life Insurance Act 1995* and is also the manager of superannuation plans pursuant to service agreements with National Australia Superannuation Pty Ltd ("NAS") and MLC Nominees Pty Ltd ("MLC Nominees").
- 1.3 NAS is a wholly owned subsidiary of NAFiM. NAS' ultimate holding company is NAB. NAS was trustee of the National All In One Superannuation Fund ("NAIOSF") until 30 June 2001 and remains trustee of the National Australia Personal Superannuation Fund.
- 1.4 MLC Nominees is a wholly owned subsidiary of MLC Limited. MLC Nominees' ultimate holding company is NAB. MLC Nominees is trustee of The Universal Super Scheme ("TUSS"). Since 1 July 2001, the sub-plans or "products" within NAIOSF have been sub-plans or "products" within TUSS.
- 1.5 Both NAS and MLC Nominees are approved by the Australian Prudential Regulation Authority ("APRA") as superannuation trustees under the *Supervision Industry (Supervision) Act 1993* ("SIS Act").
- 1.6 National Wealth Management Holdings Limited ("NWMH") is a wholly owned subsidiary of NAB. It was incorporated on 1 August 2000 as the holding company of the wealth management business of the merged National and MLC group ("National Group"). NWMH assumed the functions of the "Global Wealth Management Business Board" on 6 September 2000.
- 1.7 Global Wealth Management or Wealth Management as it was later termed is a division within the National Group. It is comprised of employees of NAB and certain of its subsidiaries who are part of the wealth management businesses within the National Group.

Superannuation Integration and Closure

- 1.8 On 30 June 2000, NAB acquired the MLC group of companies.
- 1.9 On 6 September 2000, the "Global Wealth Management Business Board" and NAFiM approved an Integration Master Plan ("IMP"). The IMP was a report on the "design phase" of integration of the wealth management businesses of the merged National Group. The IMP recommended the integration of, among other

things, the superannuation funds of NAS and MLC Nominees. The IMP set out, in brief terms, a number of steps that were necessary to achieve integration of these funds ("**Superannuation Integration**"), including the closure of certain products within NAIOSF to new members and the transfer of those products to existing (or shortly to be created) MLC products.

- 1.10 Some of the recommendations for Superannuation Integration were subject to, among other things, relevant trustee company approvals. The NAS and MLC Nominees boards were informed of the proposal for Superannuation Integration in November 2000.
- 1.11 Ultimately, the steps involved in Superannuation Integration included:
 - (a) closure to new members of the remaining open products of NAIOSF;
 - (b) a successor fund transfer of members and assets from NAS as trustee of NAIOSF to MLC Nominees as trustee of TUSS on 30 June 2001, which involved:
 - (i) an amendment to the TUSS Trust Deed to replicate the NAIOSF products under TUSS;
 - (ii) an amendment to the NAIOSF Trust Deed to remove the requirement for employers of employer sponsored funds to consent to any transfer of the members' funds, being a requirement that did not exist for individually invested funds;
 - (c) "trade-up" of members and assets of the replicated NAIOSF products within TUSS to existing MLC products.

However, not all products that have been subject to the successor fund transfer have yet been traded-up as was envisaged as part of Superannuation Integration or are part of a current plan for trade up.

- 1.12 Contributions made by investors into the products of NAIOSF were invested by NAS into one or more life products issued by NAFiM.
- 1.13 On 12 March 2001, NAFiM, in conjunction with NAS, announced to financial advisers within the National Group that certain of its life products, including Personal All in One Super ("**PAIOS**"), Business All In One Super ("**BAIOS**") and National Flexible Pension Plan ("**FPP**") would be closing to new investors on 31 May 2001 in order to move to a single suite of investment products and a single administration system. Other life products were also closed to new investors on 30 June 2001.
- 1.14 Closure of PAIOS, BAIOS and FPP to new members occurred on 31 May 2001. These three products were the only remaining "open" products of NAIOSF and constituted approximately 85% of the \$4.7 billion of funds under management in NAIOSF.
- 1.15 In April 2001, as part of Superannuation Integration, NAS and MLC Nominees approved a successor fund transfer of all members and assets from NAIOSF to TUSS ("**SFT**"). A SFT, pursuant to the SIS Act and its regulations, permits the transfer of members and assets from one superannuation fund to another without the need to obtain member consent, where the recipient fund confers on members

equivalent rights as the members received under the original fund. If equivalent rights are not conferred, member consent to the transfer must be obtained.

- 1.16 In the case of a SFT, the NAIOSF Trust Deed required employers of employer-sponsored funds, but not individuals, to consent to any transfer of members and assets. On 12 April 2001 the NAS Board resolved to remove the requirement for employer consent from the NAIOSF Trust Deed in order to facilitate the SFT. Employer consent to the SFT was consequently not obtained.
- 1.17 On 30 June 2001, all members and assets of NAIOSF were transferred to TUSS in replicated NAIOSF products via a SFT.
- 1.18 Trade up was, and is, the final step of Superannuation Integration. Trade up involves transferring members from the replicated product within TUSS into an existing TUSS product (with additional features to the NAIOSF product), thereby altering members' terms and conditions. The power to trade-up is provided for in the TUSS Trust Deed. Before the trustee can approve a trade-up, it must be satisfied that the trade-up is in the members' best interests.
- 1.19 MLC Nominees resolved (subject to certain conditions, which were subsequently satisfied) that the two trade-up proposals put to it were in the members' best interests and, accordingly, approved them in July-August 2001. As a result:
 - (a) approximately 30,000 members of PAIOS and their assets were traded up to MLC MasterKey on 1 December 2001; and
 - (b) approximately 90,000 members of FlexiSuper were traded up to The Employee Retirement Plan on 1 January 2002.
- 1.20 In relation to these two trade-ups, MLC Nominees was of the view that:
 - (a) PAIOS members who expressed dissatisfaction with the terms of the trade-up, through the internal complaint handling process, should be informed of their ability to leave the fund without cost; and
 - (b) such PAIOS members wishing to exercise their right to exit prior to the day of trade-up must have their entry fee refunded on an equitable pro rata basis (for entry fee members) or without exit fee (for no entry fee members), with NAFiM to bear the costs of this right,(collectively, the "Decision").
- 1.21 NAFiM waived exit fees for 11 PAIOS investors totalling \$29,500.
- 1.22 Due to an internal misunderstanding, NAFiM did not, in some circumstances, implement the Decision.
- 1.23 NAFiM has, during the course of ASIC's investigation, recently identified:
 - (a) 8 PAIOS members who were dissatisfied with trade-up and charged exit fees totalling approximately \$17,000 – NAFiM has written to each of those persons seeking to reimburse them;
 - (b) 12 PAIOS members who were dissatisfied with the trade-up, did not withdraw their funds, or only partially withdrew their funds, and who still

have an exit fee payable – NAFiM has also written to each of those persons offering to allow them to withdraw now at no cost.

- 1.24 NAFiM is of the view that there are no other affected PAIOS members but has agreed to provide the undertaking in paragraph 2.9 below. This is to ensure that all PAIOS members who registered a complaint in relation to the terms of the trade-up during the period 1 August 2001 to 1 December 2001 ("**Dissatisfied PAIOS Members**") are informed of their ability to leave the fund without cost.

Unit Price Adjustment

- 1.25 On 30 October 2001, NAFiM reduced the unit prices of certain of its investment portfolios by approximately \$60 million. The reductions affected approximately 21 NAFiM life insurance products that invested in certain investment portfolios in NAFiM statutory funds 2, 4 and 5 and reduced the account balance of approximately 235,000 investors. A list of affected products is contained in schedule 2.
- 1.26 Investment-linked life insurance products buy and sell assets with investors' money. Costs are incurred when assets are bought and sold. Unitised life insurance products seek to ensure that transaction costs incurred in the buying and selling of assets by the products are borne equitably. For NAFiM's products, this was usually done by incorporating an allowance for transaction costs into the unit price.
- 1.27 For growing investment portfolios, some of the money from new investors is used to pay exiting investors, and the balance is used to purchase new assets. However, when a portfolio is contracting, assets must be sold in order to pay out exiting investors as there is not enough new investors' money to meet the needs of exiting investors. This purchase or sale of assets incurs transaction costs. In the circumstances of a growing portfolio, the transaction costs factor should generally be set to raise the unit price so that new investors pay their share of transaction costs. Similarly, in the circumstances of a contracting portfolio the transaction costs factor should generally be set to lower the unit price so that exiting investors receive less money for their investment in order to pay their share of transaction costs.
- 1.28 Historically, the NAFiM investment portfolios had generally been growing and the transaction costs factors for the portfolios were set on this basis. However, closure of the PAIOS, BAIOS and FPP products in May 2001, contributed to the contraction of some of the investment portfolios and as such the transaction costs factors had to be adjusted to lower the unit price. This was done by NAFiM on 30 October 2001 as an interim measure until further information on the appropriate setting of the transaction costs factors was obtained.
- 1.29 Disclosure of the UPA was intended to be provided, within three months, to approximately 150,000 of the 294,000 investors then considered to be affected by the UPA, on the basis NAFiM considered those investors to be materially affected by the UPA. The disclosure was to be made by way of a flyer inserted in the "National Perspective" magazine in January / February 2002. Due to a breakdown in communication within NAFiM, only 30,000 investors actually received the flyer. Those investors not considered to be materially affected by the UPA were to

be informed of the UPA through the annual reports. The annual reports were issued in September 2002.

ASIC's Investigation

- 1.30 ASIC has been making enquiries into the circumstances surrounding the UPA since July 2002 and since September 2002 has been investigating suspected contraventions of the Australian Securities and Investments Commission Act 2001 ("**ASIC Act**"), the Corporations Act 2001 ("**Corporations Act**") and the SIS Act in relation to:
- (a) the integration of members and assets on or around 30 June 2001, from superannuation funds for which NAS act or acted as trustee to superannuation funds for which MLC Nominees act as trustee;
 - (b) the monitoring and valuation of statutory funds established by NAFiM; and
 - (c) the disclosure of information concerning these matters.
- 1.31 On 15 April 2003, ASIC provided to APRA a detailed formal referral of matters arising from ASIC's investigation and relevant to APRA's jurisdiction. On 16 May 2003, ASIC wrote to NAS, MLC Nominees and NAFiM specifying its concerns and the remedial action it required to address those concerns. This letter was also provided to APRA. NAS, MLC Nominees and NAFiM responded to that letter on 27 May 2003 denying those concerns, but offering certain remedial actions.
- 1.32 ASIC acknowledges that the National Group has co-operated with ASIC during its investigation and demonstrated a commitment to fully compensate affected investors.
- 1.33 ASIC's investigation has now concluded.
- 1.34 As part of its compensation commitment, and during ASIC's investigation, NAFiM engaged Trowbridge Deloitte, an external independent actuary ("**Trowbridge Deloitte**"), and received a report in writing dated 23 May 2003 indicating that, based on best estimates from the information provided, the compensation offered and paid (or to be paid) by NAFiM will be sufficient to compensate investors directly affected by:
- (a) the UPA; and/or
 - (b) the unit pricing errors (described in paragraph 1.56 below).
- 1.35 ASIC and the APRA requested NAFiM to instruct Trowbridge Deloitte to undertake some further work following their review of Trowbridge Deloitte's report of 23 May 2003. Further work was, as a result, undertaken by Trowbridge Deloitte. The results of that work are contained in further reports that have been consolidated into a report by Trowbridge Deloitte dated 29 August 2003 (the "**Trowbridge Deloitte Report**").

- 1.36 Trowbridge Deloitte based their reports on certain assumptions referred to in paragraph 1.53 below because of an absence of certain records relating to unit pricing for significant times during the period 1987 to 2001.
- 1.37 ASIC, having obtained its own independent actuarial advice, considers that, in these circumstances, Trowbridge Deloitte's approach is an appropriate way to calculate the compensation payable to the investors affected by the UPA and/or the unit pricing errors.
- 1.38 Trowbridge Deloitte calculated that in order to compensate investors for the unit pricing errors, and for the effect of the UPA, compensation in the amount of \$67.2 million would need to be paid.

ASIC's concerns and Companies' response

- 1.39 ASIC has, in the course of its investigation, identified some issues of concern. Those concerns are set out at paragraphs 1.41 to 1.48 and paragraph 1.58 below.
- 1.40 NAS, MLC Nominees and NAFiM (together the "Companies") do not agree with those concerns. The Companies' response, to each of ASIC's concerns, is set out at paragraphs 1.52 to 1.55 and paragraph 1.58 below.

ASIC's concerns - disclosure

- 1.41 ASIC is concerned that disclosure by NAS, NAFiM and MLC Nominees to investors, financial advisers and employers in relation to Superannuation Integration, closure of the NAFiM and NAS products, the trust deed amendments to NAIOSF, the SFT and the UPA was deficient in the following material aspects:
- (a) Superannuation Integration was not disclosed to investors when NAFiM approved and NAS and MLC Nominees were informed of the proposal for Superannuation Integration in late 2000;
 - (b) closure of the NAFiM and NAS products, the NAIOSF trust deed amendments and the SFT were not disclosed to investors prior to these events occurring;
 - (c) when disclosure of these events was made, it was not made in the context of Superannuation Integration. Had such disclosure been made, the NAIOSF members would have been informed of the plan to further transfer their investment from the replicated NAS products in TUSS to existing TUSS products and would have been able to consider whether to:
 - (i) exit their current investment prior to the proposed changes;
 - (ii) resist the proposed changes;
 - (iii) accept the proposed changes;
 - (d) the UPA was not disclosed to 90% of affected investors in January/February 2002. The 10% that did receive notification in January / February 2002 were not told:
 - (i) the size of the UPA;
 - (ii) the degree to which the UPA affected investors; or

- (iii) all of the causes of the UPA;
 - (e) Investors and advisers were also told that in relation to the UPA;
 - (i) the National Group did not benefit from the UPA, whereas in ASIC's view a contributing cause of the UPA, being closure of the products, was necessary to achieve Superannuation Integration, which was expected (amongst other things) to deliver significant cost savings to the group;
 - (ii) the UPA was made to ensure investors were treated equitably, whereas in ASIC's view the unit price should have been adjusted prior to 31 October 2001 to achieve equity;
 - (iii) unit pricing assumptions are regularly reviewed and externally audited, whereas in ASIC's view adequate regular reviews or audits had not been performed in relation to the transaction costs factor of the unit price since 1993;
 - (f) PAIOS members received an exit statement in January 2002 with an annual account balance that incorporated the effect of the UPA under "investment performance", which in ASIC's view misled members to believe that the effect of the UPA was actually a result of the performance of their investment;
 - (g) a number of statements were also made to investors, employers and advisers about future events when in ASIC's view there were no reasonable grounds for making those statements at the time they were made. These included that:
 - (i) closure would have no effect on members' investments;
 - (ii) the adjustment would have been necessary regardless of closure;
 - (iii) all affected investors would be informed of the UPA;
 - (iv) a further adjustment to the unit price was not expected.
- 1.42 ASIC considers that these deficiencies constitute contraventions of section 12DA of the ASIC Act, section 1041H of the Corporations Act (misleading or deceptive conduct) and section 34 of the SIS Act (in relation to the SIS Regulations governing significant event reporting) by NAFiM, NAS and MLC Nominees in a number of significant respects. ASIC has commenced proceedings in the Federal Court of Australia. NAFiM, NAS and MLC Nominees have defended those proceedings. The parties have agreed to settle those proceedings, without admissions, on the basis that:
- (a) NAFiM, NAS and MLC Nominees give undertakings to the Federal Court of Australia to take certain remedial actions. The form of the undertakings are attached to this Enforceable Undertaking (at Schedule 1) and can be found on ASIC's website www.asic.gov.au;
 - (b) the proceedings are dismissed with no order as to costs.
- 1.43 The Companies' response to ASIC's concerns in relation to disclosure is at paragraph 1.52 below.

ASIC's concerns - corporate governance and due care and diligence

- 1.44 ASIC also has concerns about a number of aspects of corporate governance within the superannuation and life businesses of the National and MLC groups. These concerns derive from the fact that NAS and MLC Nominees are subsidiaries within a wider group of companies in circumstances where group interests will not always coincide with the interests of superannuation fund investors for which the trustees are responsible. They include:
- (a) the flow of detailed and considered information to trustees from business areas within the group was inadequate;
 - (b) the attribution of personnel and their actions to "Wealth Management", making it difficult to assign responsibility and accountability to any particular entity, and in particular to NAS and MLC Nominees;
 - (c) the obtaining of legal advice by "Wealth Management" on behalf of the trustees and NAFiM, creating possible conflicts of interest in the provision of instructions.
- 1.45 The Companies' response to ASIC's concerns in relation to corporate governance and due care and diligence is at paragraph 1.53 below.

ASIC's concerns - closure, the trust deed amendments and the SFT

- 1.46 ASIC is concerned that:
- (a) neither of the boards of NAFiM or NAS considered the effect of closure of the NAFiM and NAS products to investors;
 - (b) had these boards done so, the need for the UPA may have been foreseen;
 - (c) the NAS board approved of the SFT and the amendment to the NAIOSF Trust Deed on 12 April 2001:
 - (i) without (in ASIC's view) the benefit of detailed analysis of the advantages and disadvantages of the SFT or contemplated trade-up being provided to the NAS Board;
 - (ii) without (in ASIC's view) considering or adequately taking into account that the provision in the trust deed requiring employer consent for an SFT, afforded beneficiaries of employer sponsored funds a measure of protection and the amendment removed that protection;
 - (d) the NAS board approved the amendments to the NAIOSF Trust Deed without giving employer sponsors or employee beneficiaries of employer sponsored funds prior notice of the amendment before it occurred;
 - (e) the NAS board was informed of the proposal for Superannuation Integration in late 2000 but was not otherwise provided with sufficient information in relation to Superannuation Integration to enable it to properly consider the effect on investors of closure, the NAIOSF Trust Deed amendments and the SFT and how these matters should be disclosed;
 - (f) if investors and employers of employer sponsored funds of the NAFiM and NAS products had been informed of Superannuation Integration, closure of the NAS and NAFiM products, the trust deed amendments and

the SFT, investors and employers would have been able to consider whether to:

- (i) exit their current investment prior to the proposed changes;
- (ii) resist the proposed changes;
- (iii) accept the proposed changes.

1.47 The Companies' response to ASIC's concerns in relation to closure, the trust deed amendments and the SFT is at paragraph 1.54 below.

ASIC's concerns – UPA

1.48 ASIC also has concerns about the UPA, including the following:

- (a) the NAFiM board did not approve the UPA. The UPA was made following a decision by senior staff within "Wealth Management";
- (b) the MLC Nominees board was not made aware of the UPA until it received a presentation on 29 November 2001. That presentation did not, but should have, informed the board of:
 - (i) the monetary impact of the UPA on investors;
 - (ii) the number of investors affected;
 - (iii) the number of products affected;
 - (iv) any disclosure proposed in relation to the UPA;
- (c) MLC Nominees' complaint handling system did not detect that investors had not received any or adequate information in relation to the UPA, despite the lodgement of complaints in this regard;
- (d) neither NAFiM nor MLC Nominees understood the unit pricing methodology of the NAFiM products at the time of the UPA, causing:
 - (i) a delay in making the unit price adjustment; and
 - (ii) an inability to determine what the appropriate transaction costs factor should be;
- (e) NAFiM was not able to identify all of the products affected by the UPA until October 2002, and in the case of one of the 21 affected products, NAFiM was not able to finally confirm whether or not it was affected until April 2003.

1.49 The Companies' response to ASIC's concerns in relation to the UPA is at paragraph 1.55 below.

Companies' Response to ASIC's concerns

1.50 ASIC has, in the course of its investigation, identified the issues of concern as set out at paragraphs 1.41 to 1.48 above and paragraph 1.58.

1.51 NAFiM, NAS and MLC Nominees do not agree with ASIC's concerns as noted in paragraphs 1.52 to 1.55 and paragraph 1.58 below, but acknowledge all of those concerns.

Companies' response – disclosure

- 1.52 NAS, NAFiM and MLC Nominees do not agree with, but acknowledge, ASIC's concerns in relation to disclosure, as set out in paragraphs 1.41 to 1.42 above. The Companies also do not agree with the conclusions drawn by ASIC with regard to alleged contraventions of the ASIC Act, the Corporations Act and the SIS Act. In particular, and without being exhaustive, NAS, NAFiM and MLC Nominees assert that:
- (a) the integration of the businesses of the National and MLC groups was announced in general terms to the public shortly after the acquisition in 2000, and in the Companies' view this created in the minds of investors an awareness of superannuation integration, and therefore, in the circumstances, the Companies now say that the disclosures that were made (as referred to in sub-paragraphs 1.52(c) and 1.52(d) below) were sufficient and appropriate;
 - (b) there was no obligation to disclose "Superannuation Integration" to investors in late 2000 and, in fact, to have so disclosed at that time may have misled investors as:
 - (i) Superannuation Integration was part of a high level plan, approved of by NAFiM for implementation and noted by NAS and MLC Nominees for their information only;
 - (ii) implementation of some aspects of Superannuation Integration was subject to, among other things, relevant trustee approvals;
 - (iii) some details of Superannuation Integration were subsequently amended; and
 - (iv) a number of aspects of Superannuation Integration, in particular relating to trade-up, have not been implemented;
 - (c) the closure of products to new investors, the NAIOSF Trust Deed amendments and the SFT were disclosed to investors in the annual reports for the PAIOS and FPP products for the year ended 30 June 2001, based on various considerations, including external legal advice obtained by Wealth Management. The covering letter to those annual reports referred to the integration of NAFiM and MLC;
 - (d) PAIOS and FlexiSuper members were informed of the decision to trade-up their products in August - September 2001, shortly after that decision was made and more than three months in advance of the trade-ups occurring. Detailed information was provided at that time as to the effect of the trade-ups, and reference was made to the earlier steps of closure and the SFT;
 - (e) while the particular unit pricing errors were not detected, various extensive internal and external audits and other reviews were conducted for NAFiM throughout the period;
 - (f) financial advisers were informed of the UPA on the day immediately following the UPA and were provided with further information following complaints raised by those advisers about the UPA and the communication of it;

- (g) disclosure of the occurrence of the UPA was intended to be made three months after the UPA, to those investors that NAFiM considered would be materially affected by the UPA and to the balance of investors, in the annual reports provided to them in September 2002;
- (h) at the time of disclosure of the UPA, the unit pricing errors were not disclosed as NAFiM and MLC Nominees did not have knowledge, at that time, of those unit pricing errors;
- (i) NAS and MLC Nominees have in place various principles, processes, risk management frameworks (including compliance systems) and controls in relation to compliance with their disclosure obligations.

Companies' Response – corporate governance and due care and diligence

1.53 NAS and MLC Nominees do not agree with, but acknowledge, ASIC's concerns in relation to corporate governance (as set out in paragraph 1.44 above). In particular, NAS and MLC Nominees assert that:

- (a) they are aware of the statutory and fiduciary obligations that, as trustees, they owe to their members, and do not believe that their position as subsidiaries within a wider group of companies adversely affects in any way their ability to meet those obligations;
- (b) the corporate structure within which NAS and MLC Nominees operate is common to the industry, in particular to all of the major financial institutions with superannuation offerings;
- (c) they have a services agreement with NAFiM and are of the view that they insist upon the provision of detailed and timely information;
- (d) in the case of MLC Nominees, it is comprised of an even number of non-executive and executive directors who meet regularly – in the financial year 2002/03, the Board met on 18 separate occasions;
- (e) they have received legal advice from external law firms engaged on their behalf by Wealth Management in relation to significant decisions (such as the SFT and trade-ups);
- (f) they have in place various principles, processes, risk management frameworks (including compliance systems) and controls in relation to compliance with their trustee duty obligations.

Companies' Response – closure, the trust deed amendments and the SFT

1.54 NAS and NAFiM do not agree with, but acknowledge, ASIC's concerns in relation to closure, the NAIOSF Trust Deed amendments and the SFT (as set out in paragraph 1.46 above). In particular, and without being exhaustive, NAS and NAFiM assert that:

- (a) NAFiM had the power to close its life products to new investors pursuant to the relevant policy documents, and NAS had the power to close the NAIOSF products to new members pursuant to the NAIOSF Trust Deed;
- (b) it is common in the life insurance and superannuation industries for life insurance and superannuation products to be closed to new investors;
- (c) NAS had the power to amend the NAIOSF Trust Deed;

- (d) NAS considered that the NAIOSF Trust Deed amendments and the SFT were in the best interests of its members, based on various matters, including external legal advice obtained on its behalf by Wealth Management;
- (e) NAS informed members of closure, the NAIOSF Trust Deed amendments and the SFT in the annual reports for the PAIOS and FPP products for the year ended 30 June 2001, based on various considerations, including external legal advice obtained on its behalf by Wealth Management. The covering letter to those annual reports also described the SFT and referred to the integration of NAFiM and MLC.

Companies' response - UPA

1.55 NAFiM and MLC Nominees do not agree with, but acknowledge, ASIC's concerns in relation to the UPA (as set out in paragraph 1.48 above). In particular, NAFiM and MLC Nominees assert that:

- (a) unit pricing was a matter for NAFiM as life insurer, and was therefore not the responsibility of MLC Nominees;
- (b) the UPA involved the application of the unit pricing methodology in the relevant life policy documents and, as such, management did not at the time consider the UPA required the approval of the NAFiM Board;
- (c) as a general matter, the wealth management businesses within the National Group have in place processes and practices in relation to the handling of customer complaints, including the employment of 15 full-time complaints handlers;
- (d) in the case of the UPA, as noted in paragraph 1.52(f) above, further information was provided to advisers in response to complaints by them about the UPA and the communication of it;
- (e) no investors will be adversely affected by the UPA, as a result of the compensation commitment announced by MLC Limited in August 2002.

Unit pricing errors – Trowbridge Deloitte Report

1.56 In its report, Trowbridge Deloitte referred to two unit pricing errors that were discovered by NAFiM during NAFiM's consideration of the circumstances of the UPA. These are:

- (a) the application of the wrong unit price methodology in relation to 5 of the 21 affected products:
 - (i) for 4 of the 21 affected products, two sets of policy documents were distributed by NAFiM to investors, each referring to different unit pricing methodologies. As such, an incorrect unit price methodology was applied to some of those products;
 - (ii) for one of the affected products, a different unit pricing methodology was applied compared to that contained in the product policy document;
- (b) NAFiM incorrectly set the transaction costs factor of the unit price too high for most investment portfolios for significant periods since at least

1993 and possibly since 1987, without detection by NAFiM, NAS or MLC Nominees.

1.57 Those products affected by the unit pricing errors described in sub-paragraph 1.56(a) are noted in Schedule 2 as part of the list of affected products.

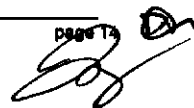
1.58 In relation to the unit pricing errors:

- (a) ASIC is concerned that NAFiM may have benefited from setting the transaction costs factors too high as this may have led to increased management fees being paid to NAFiM by some investors;
- (b) in relation to 1.58(a), Trowbridge Deloitte estimate that very few (if any) investors will be affected. In any event, NAFiM has now committed to refunding these fees by 31 December 2003 (or, if that is not possible, as soon as practicable thereafter);
- (c) ASIC is concerned that NAFiM could only locate data points in respect of 270 days for transaction costs factors between 1987 and 31 October 2001. Additionally, NAFiM did not maintain records of actual transaction costs during this period (consistent with industry practice);
- (d) given the matters referred to in sub-paragraph 1.58(c) Trowbridge Deloitte based its findings on the reconstruction of what it considered would have been NAFiM's transaction costs and compared this to the data points available;
- (e) given the matters referred to in sub-paragraphs 1.58(c) and 1.58(d), NAFiM has erred on the side of caution in favour of investors in its assessment of compensation in order to ensure that affected investors are fully compensated for the UPA and/or the unit pricing errors;
- (f) NAFiM asserts that it has in place various principles, processes, risk management frameworks (including compliance systems) and controls in relation to, among other things, investment valuation and unit pricing. NAFiM asserts that it also has in place various initiatives aimed at improving those principles, processes, frameworks and controls.

Setting of transaction costs – disclosure

1.59 Trowbridge Deloitte has prepared a report for NAFiM dated 8 August 2003 that concurs with NAFiM's view that the current setting of the transaction costs factor is fair. The current setting means that no allowance is made in the unit price for transaction costs, given that these costs are now borne by the underlying asset pools that NAFiM invests in. NAFiM has also received legal advice that the current setting of the transaction costs factor is permitted by the relevant product policy documents.

1.60 As the transaction costs associated with redeeming assets are borne by the underlying asset pools, this creates a negative "drag" on the performance of an investor's units. While the drag has a minimal impact on investors presently, its cumulative effect will increase in significance over time. Trowbridge Deloitte conclude that, based on current net outflows, this effect is immaterial.

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- 1.61 ASIC has formed the view that this change in approach and its effect on investors requires disclosure to investors.

Acknowledgements of concerns and resolution

- 1.62 While NAFiM, NAS and MLC Nominees do not agree with all aspects of ASIC's concerns as set out in this Enforceable Undertaking, they acknowledge those concerns and have instituted a number of further actions in order to ensure best practice in complying with their various legal obligations.
- 1.63 In addition, NAFiM, NAS and MLC Nominees have undertaken to ASIC to take the further steps identified in paragraph 2.11 to 2.39 below to ensure that there are appropriate practices and processes to address ASIC's concerns.
- 1.64 By accepting:
- (a) the undertakings identified in paragraph 2 below offered by NAFiM, NAS and MLC Nominees in this Enforceable Undertaking; and
 - (b) the undertakings made by NAFiM, NAS and MLC Nominees to the Federal Court of Australia (pursuant to paragraph 2.2 below), in resolution of Court proceedings instituted by ASIC,

ASIC concludes its investigation into the matters the subject of this Enforceable Undertaking and will not take any other action against the parties to this Enforceable Undertaking (or their past or present officers) or any other related entity (or their past or present officers), subject to paragraph 3.3 below.

2 Undertakings

- 2.1 NAFiM, NAS and MLC Nominees have offered, and ASIC has agreed to accept, an enforceable undertaking in the terms set out below.

Disclosure

- 2.2 Each of NAFiM, NAS and MLC Nominees have, without admissions, provided the undertakings contained in Schedule 1 of this Enforceable Undertaking to the Federal Court of Australia to resolve the proceedings commenced by ASIC.

Compensation

- 2.3 NAFiM undertakes to compensate investors affected by the UPA and/or the unit pricing errors referred to in paragraphs 1.25 and 1.56 respectively (together the "Affected Investors") by 31 December 2003 (or, if that is not possible, within such time as is reasonably practicable thereafter) such that, based on the Trowbridge Deloitte Report, no Affected Investor is adversely affected by either the UPA or the unit pricing errors.
- 2.4 NAFiM and MLC Nominees must ensure all Affected Investors are provided with information that relates specifically to their compensation and the calculation of it, at the time of payment of compensation to them.

- 2.5 The compensation referred to in paragraph 2.3 must not be paid out of, nor shall reimbursement or indemnification be sought from, assets of any funds managed for or on behalf of any investor.
- 2.6 NAFiM, NAS and MLC Nominees must ensure that:
- (a) within 35 days, they use their best endeavours to jointly send a disclosure statement in the form contained in Schedule 2 to each current Affected Investor (other than those Affected Investors who are to receive a disclosure statement pursuant to undertakings provided to the Federal Court as referred to in paragraph 2.2);
 - (b) as soon as reasonably practicable, but in any event by 31 December 2003, they use their best endeavours to jointly send a disclosure statement in the form contained in Schedule 2 to exited Affected Investors (other than those exited Affected Investors who are to receive a disclosure statement pursuant to undertakings provided to the Federal Court as referred to in paragraph 2.2).
- 2.7 In the case of any Affected Investor for whom NAFiM, NAS and MLC Nominees do not possess a current address or means to contact the Affected Investor, NAFiM, NAS and MLC Nominees will be taken to have complied with paragraphs 2.3, 2.4 and 2.6 if NAFiM, NAS and MLC Nominees satisfy the procedure set out in Schedule 3 to this Enforceable Undertaking.
- 2.8 NAFiM, NAS and MLC Nominees undertake to provide ASIC with monthly reports detailing progress in relation to the:
- (a) payment of compensation to Affected Investors as referred to in paragraph 2.3;
 - (b) provision of the disclosure statement to Affected Investors pursuant to this Enforceable Undertaking as referred to in paragraph 2.6;
 - (c) provision of the disclosure statement to Affected Investors pursuant to the undertakings provided to the Federal Court of Australia as referred to in paragraph 2.2.

Trade-up

- 2.9 NAFiM undertakes that:
- (a) by 31 December 2003 (or if that is not possible, as soon as reasonably practicable thereafter), any Dissatisfied PAIOS Member who has exited the fund and who was charged an exit fee or not reimbursed an entry fee (as relevant), will be:
 - (i) reimbursed any exit fee charged or entry fee that should have been reimbursed, consistent with the Decision;
 - (ii) provided with information about their reimbursement and the reasons for it at the time of reimbursement to them;
 - (b) by 31 December 2003, it will:
 - (i) notify all Dissatisfied PAIOS Members who:
 - (A) remain members of TUSS; and

- (B) either:
- (I) would be subject to an exit fee if they now chose to exit the fund; or
 - (II) entered the fund less than four years ago and paid an entry fee,
- of their ability to exit the fund without cost; and
- (ii) waive exit fees or reimburse entry fees (as relevant), if requested to do so by any Dissatisfied PAIOS Member in response to such notification; and
- (c) by 31 January 2004, it will provide a final report to ASIC on its performance of the obligations in sub-paragraphs 2.9(a) and 2.9(b) above, which report will specify the method used to identify Dissatisfied PAIOS Members and the content and timing of the notifications provided.

Unit pricing - disclosure

- 2.10 NAS, MLC Nominees and NAFiM undertake to explain the circumstances surrounding the change in approach to unit pricing as outlined in paragraphs 1.59 and 1.60 above and the effect it will have on relevant investors. The form and means of this disclosure must be approved by ASIC and sent to investors affected by the change by 31 December 2003.

Unit pricing - review

- 2.11 Within 4 months of the date of execution of the Enforceable Undertaking by ASIC ("**Operational Date**"), NAFiM must:
- (a) review the manner (including the processes, practices, internal controls, risk management framework, compliance systems, supervision, training, service agreements and resources) with respect to unit pricing (the "**Unit Pricing Compliance Program**"), by which NAFiM seeks to achieve the following objectives in relation to all unitised products issued by NAFiM:
 - (i) that all unit prices are monitored, maintained, calculated and set in accordance with the applicable unit pricing formulae contained in the relevant life policy documents;
 - (ii) that transaction costs at all times are allocated as between investors in accordance with the applicable unit pricing formulae contained in the relevant life policy documents; and
 - (iii) that any discretion permitted within the relevant life policy documents in relation to the setting, monitoring, maintaining and calculating of unit prices is appropriately exercised to achieve equity as between investors within each unitised product issued by NAFiM,
- (together sub-paragraphs (i) to (iii) constitute the "**Unit Pricing Obligations**");

- (b) document the Unit Pricing Compliance Program (the **"Unit Pricing Compliance Documentation"**); and
 - (c) use its best endeavours to implement the Unit Pricing Compliance Program.
- 2.12 Within 4 months of the Operational Date, NAFiM must engage an external independent unit pricing expert (the **"Unit Pricing Expert"**), on terms to be approved by ASIC to:
- (a) review the Unit Pricing Compliance Program and the Unit Pricing Compliance Documentation to ascertain whether they are appropriate to enable NAFiM to comply with the Unit Pricing Obligations;
 - (b) determine whether the Unit Pricing Compliance Program has been implemented.
- 2.13 Within 7 months of the Operational Date, the Unit Pricing Expert must provide to NAFiM and ASIC a report on the review conducted by the Unit Pricing Expert pursuant to paragraph 2.12 (the **"Initial Unit Pricing Expert Report"**). The Initial Unit Pricing Expert Report must either:
- (a) confirm that:
 - (i) the Unit Pricing Compliance Program and the Unit Pricing Compliance Documentation are appropriate to enable NAFiM to comply with the Unit Pricing Obligations; and
 - (ii) the Unit Pricing Compliance Program has been implemented; or
 - (b) if the Unit Pricing Expert is unable to provide the confirmation referred to in sub-paragraph 2.13(a) set out the deficiencies:
 - (i) in the Unit Pricing Compliance Program and/or the Unit Pricing Compliance Documentation identified and recommend changes to the Unit Pricing Compliance Program and/or the Unit Pricing Compliance Documentation; and/or
 - (ii) in the implementation of the Unit Pricing Compliance Program and specify the steps to be taken to rectify the deficiencies.
- 2.14 If the Initial Unit Pricing Expert Report identifies deficiencies in the Unit Pricing Compliance Program and/or the Unit Pricing Compliance Documentation, within 2 months of receipt of the Initial Unit Pricing Expert Report, NAFiM must provide a report to ASIC setting out the action it has taken or proposes to take, and in what timeframe, to rectify the deficiencies (the **"Unit Pricing Remedial Action"**).
- 2.15 NAFiM must use its best endeavours to implement the Unit Pricing Remedial Action.
- 2.16 NAFiM must maintain and annually update (for two subsequent anniversaries of the Operational Date) the Unit Pricing Compliance Program and the Unit Pricing Compliance Documentation to ensure that they continue to be appropriate to enable NAFiM to comply with the Unit Pricing Obligations.

- 2.17 On or before the date of the two subsequent anniversaries of the Initial Unit Pricing Compliance Report, NAFiM must ensure that the Unit Pricing Expert has conducted a review of the implementation of the Unit Pricing Compliance Program, the Unit Pricing Remedial Action (or Subsequent Unit Pricing Remedial Action as defined in paragraph 2.18 below) (if any) and the Unit Pricing Compliance Documentation. The Unit Pricing Expert must, after doing so, provide to NAFiM and ASIC a report on the review conducted by the Unit Pricing Expert pursuant to this paragraph 2.17 (the **"Subsequent Unit Pricing Expert Report"**). The Subsequent Unit Pricing Expert Report must either:
- (a) confirm that:
 - (i) the Unit Pricing Compliance Program and the Unit Pricing Remedial Action (or Subsequent Unit Pricing Remedial Action as defined in paragraph 2.18 below) (if any), have been implemented and complied with; and
 - (ii) the Unit Pricing Compliance Program and the Unit Pricing Compliance Documentation remain appropriate to enable NAFiM to comply with the Unit Pricing Obligations; or
 - (b) if the Unit Pricing Expert is unable to provide the confirmation referred to in sub-paragraph 2.17(a), set out the deficiencies:
 - (i) in the Unit Pricing Compliance Program and/or the Unit Pricing Compliance Documentation identified and recommend changes to the Unit Pricing Compliance Program and/or the Unit Pricing Compliance Documentation; and/or
 - (ii) in the implementation of the Unit Pricing Compliance Program and the Unit Pricing Remedial Action (or Subsequent Unit Pricing Remedial Action as defined in paragraph 2.18 below) (if any) and specify the steps to be taken to rectify the deficiencies.
- 2.18 If the Subsequent Unit Pricing Expert Report identifies deficiencies in accordance with sub-paragraph 2.17(b), within 2 months of the date of receipt of the Subsequent Unit Pricing Expert Report, NAFiM must provide a report to ASIC setting out the action it has taken or proposes to take, and in what timeframe, to rectify the deficiencies (the **"Subsequent Unit Pricing Remedial Action"**).
- 2.19 NAFiM must use its best endeavours to implement the Subsequent Unit Pricing Remedial Action.

Corporate Governance

- 2.20 The undertakings contained in paragraphs 2.21 to 2.29 below confer obligations severally upon each of NAS and MLC Nominees. A reference to "Trustee" in those paragraphs is taken to be a reference to each of NAS and MLC Nominees.
- 2.21 Within 4 months of the date of the Operational Date, the Trustee must:
- (a) review the manner (including the processes, practices, internal controls, risk management framework, compliance systems, supervision, training, service agreements and resources) (the **"Governance Program"**) by which the Trustee seeks to comply with its trustee duty obligations under

the SIS Act and to support the directors in the discharge of their duties under the Corporations Act (the "**Governance Obligations**");

- (b) ensure that it has in place appropriate written agreements ("**Service Agreements**") with all entities within the National Group that provide services to the Trustee ("**Service Providers**"). Any such agreement must:
 - (i) contain terms that ensure the Service Providers give to the Trustee sufficient, appropriate and timely information to enable the Trustee to comply with its Governance Obligations; and
 - (ii) require the Service Providers to properly train and supervise their staff in the provision of information to the Trustee in a manner that will assist the Trustee in the discharge of the Governance Obligations;
- (c) document the Governance Program (the "**Governance Documentation**" which reference, for the avoidance of doubt, includes the Service Agreements);
- (d) use its best endeavours to implement the Governance Program.

2.22 Within 4 months of the Operational Date, the Trustee must engage an external independent governance expert (the "**Governance Expert**"), on terms to be approved by ASIC to:

- (a) review the Governance Program and the Governance Documentation to ascertain whether they are appropriate to enable the Trustee to comply with the Governance Obligations; and
- (b) determine whether the Governance Program has been implemented.

2.23 Within 7 months of the Operational Date, the Governance Expert must provide to the Trustee and ASIC a report on the review conducted by the Governance Expert pursuant to paragraph 2.22 (the "**Initial Governance Expert Report**"). The Initial Governance Expert Report must either:

- (a) confirm that:
 - (i) the Governance Program and the Governance Documentation are appropriate to enable the Trustee to comply with the Governance Obligations; and
 - (ii) the Governance Program has been implemented; or
- (b) if the Governance Expert is unable to provide the confirmation referred to in sub-paragraph 2.23(a), set out the deficiencies:
 - (i) in the Governance Program and/or the Governance Documentation identified and recommend changes to the Governance Program and/or the Governance Documentation; and
 - (ii) in the implementation of the Governance Program and specify the steps to be taken to rectify the deficiencies.

2.24 If the Initial Governance Expert Report identifies deficiencies in the Governance Program and/or the Governance Documentation, within 2 months of receipt of the Initial Governance Expert Report, the Trustee must provide a report to ASIC

setting out the action it has taken or proposes to take, and in what timeframe, to rectify the deficiencies (the "**Governance Remedial Action**").

- 2.25 The Trustee must use its best endeavours to implement the Governance Remedial Action.
- 2.26 The Trustee must maintain and annually update (for two subsequent anniversaries of the Operational Date) the Governance Program and the Governance Documentation to ensure that they continue to be appropriate to enable the Trustee to comply with the Governance Obligations.
- 2.27 On or before the date of the two subsequent anniversaries of the Initial Governance Expert Report, the Trustee must ensure that the Governance Expert has conducted a review of the implementation of the Governance Program, the Governance Remedial Action (or Subsequent Governance Remedial Action, as defined in paragraph 2.28 below) (if any) and the Governance Documentation. The Governance Expert must, after doing so, provide to the Trustee and ASIC a report on the review conducted by the Governance Expert pursuant to this paragraph 2.27 (the "**Subsequent Governance Expert Report**"). The Subsequent Governance Expert Report must either:
- (a) confirm that the:
 - (i) Governance Program and Governance Remedial Action (or Subsequent Governance Remedial Action as defined in paragraph 2.28 below) (if any) have been implemented and complied with; and
 - (ii) Governance Program and Governance Documentation remain appropriate to enable the Trustee to comply with the Governance Obligations; or
 - (b) if the Governance Expert is unable to provide the confirmation referred to in sub-paragraph 2.27(a), set out the deficiencies:
 - (i) in the Governance Program and/or the Governance Documentation identified and recommend changes to the Governance Program and/or the Governance Documentation; and
 - (ii) in the implementation of the Governance Program and the Governance Remedial Action (or Subsequent Governance Remedial Action as defined in paragraph 2.28 below) (if any) and specify the steps to be taken to rectify the deficiencies.
- 2.28 If the Subsequent Governance Expert Report identifies deficiencies in accordance with sub-paragraph 2.27(b), within 2 months of the date of receipt of the Subsequent Governance Expert Report, the Trustee must provide a report to ASIC setting out the action it has taken or proposes to take, and in what timeframe, to rectify the deficiencies (the "**Subsequent Governance Remedial Action**").
- 2.29 The Trustee must use its best endeavours to implement the Subsequent Governance Remedial Action.

Complaints Handling

- 2.30 The undertakings contained in paragraphs 2.31 to 2.38 below confer obligations severally upon each of NAS and MLC Nominees. A reference to "Trustee" in those paragraphs is taken to be a reference to each of NAS and MLC Nominees.
- 2.31 Within 4 months of the Operational Date, the Trustee must:
- (a) review the manner (including the processes, practices, internal controls, risk management framework, compliance systems, supervision, training, service agreements and resources) (the "**Complaint Handling Program**") by which the Trustee seeks to comply with its complaints handling obligations under the SIS Act and the Corporations Act ("**Complaint Handling Obligations**");
 - (b) document the Complaint Handling Program (the "**Complaint Handling Documentation**");
 - (c) use its best endeavours to implement the Complaint Handling Program.
- 2.32 Within 4 months of the Operational Date, the Trustee must engage an external independent complaints handling expert (the "**Complaint Handling Expert**"), on terms to be approved by ASIC to:
- (a) review the Complaint Handling Program and the Complaint Handling Documentation to ascertain whether they are appropriate to enable the Trustee to comply with the Complaint Handling Obligations; and
 - (b) determine whether the Complaint Handling Program has been implemented.
- 2.33 Within 7 months of the Operational Date, the Complaint Handling Expert must provide to the Trustee and ASIC a report on the review conducted by the Complaint Handling Expert pursuant to paragraph 2.32 (the "**Initial Complaint Handling Expert Report**"). The Initial Complaint Handling Expert Report must either:
- (a) confirm that:
 - (i) the Complaint Handling Program and the Complaint Handling Documentation are appropriate to enable the Trustee to comply with the Complaint Handling Obligations; and
 - (ii) the Complaint Handling Program has been implemented; or
 - (b) if the Complaint Handling Expert is unable to provide the confirmation referred to in sub-paragraph 2.33(a), set out the deficiencies:
 - (i) in the Complaint Handling Program and/or the Complaint Handling Documentation identified and recommend changes to the Complaint Handling Program and/or the Complaint Handling Documentation; and
 - (ii) in the implementation of the Complaint Handling Program and specify the steps to be taken to rectify the deficiencies.

- 2.34 If the Initial Complaint Handling Expert Report identifies deficiencies in the Complaint Handling Program and/or the Complaint Handling Documentation, within 2 months of receipt of the Initial Complaint Handling Expert Report, the Trustee must provide a report to ASIC setting out the action it has taken or proposes to take, and in what timeframe, to rectify the deficiencies ("**Complaint Handling Remedial Action**").
- 2.35 The Trustee must use its best endeavours to implement the Complaint Handling Remedial Action.
- 2.36 The Trustee must maintain and annually update (for two subsequent anniversaries of the Operational Date) the Complaint Handling Program and the Complaint Handling Documentation to ensure that they continue to be appropriate to enable the Trustee to comply with the Complaint Handling Obligations.
- 2.37 On or before the date of the two subsequent anniversaries of the Initial Complaint Handling Report the Trustee must ensure that the Complaint Handling Expert has conducted a review of the implementation of the Complaint Handling Program and the Complaint Handling Remedial Action (or Subsequent Complaint Handling Remedial Action as defined in paragraph 2.38 below) (if any). The Complaint Handling Expert must, after doing so, provide to the Trustee and ASIC a report on the review conducted by the Complaint Handling Expert pursuant to this paragraph 2.37 (the "**Subsequent Complaint Handling Report**"). The Subsequent Complaint Handling Report must either:
- (a) confirm that the:
 - (i) Complaint Handling Program and the Complaint Handling Remedial Action (or Subsequent Complaint Handling Remedial Action as defined in paragraph 2.38 below) (if any) have been implemented and complied with; and
 - (ii) Complaint Handling Program and Complaint Handling Documentation remain appropriate to enable the Trustee to comply with the Complaint Handling Obligations; or
 - (b) if the Complaint Handling Expert is unable to provide the confirmation referred to in sub-paragraph 2.37(a), set out the deficiencies:
 - (i) in the Complaint Handling Program and/or the Complaint Handling Documentation identified and recommend changes to the Complaint Handling Program and/or Complaint Handling Documentation; and
 - (ii) in the implementation of the Complaint Handling Program and the Complaint Handling Remedial Action (or Subsequent Complaint Handling Remedial Action as defined in paragraph 2.38 below) (if any) and specify the steps to be taken to rectify the deficiencies.
- 2.38 If the Subsequent Complaint Handling Report identifies deficiencies in accordance with sub-paragraph 2.37(b), within 2 months of the date of receipt of the Subsequent Complaint Handling Report, the Trustee must provide a report to ASIC setting out the action it has taken or proposes to take, and in what timeframe, to rectify the deficiencies (the "**Subsequent Complaint Handling Remedial Action**").

- 2.39 The Trustee must use its best endeavours to implement the Subsequent Complaint Handling Remedial Action.

External Experts

- 2.40 Each of NAFiM, NAS and MLC Nominees must, in relation to the Unit Pricing Expert, the Governance Expert and the Complaint Handling Expert (together the "External Experts"):
- (a) permit the External Experts, as reasonable, to have access to their respective books, to interview any present employee or to consult with ASIC;
 - (b) give the External Experts any information or explanation reasonably requested by the External Experts of any matter in any way connected with the reports required to be prepared by the External Experts under this Enforceable Undertaking ("Expert Reports");
 - (c) otherwise reasonably assist the External Experts in conducting the reviews and producing the Expert Reports.
- 2.41 The External Experts will be engaged on the basis that the External Expert will provide an Expert Report that will:
- (a) set out the steps that the External Expert has taken to fulfil his or her task, including but not limited to:
 - (i) the personnel that have assisted the External Expert and in what way;
 - (ii) the personnel that have been interviewed;
 - (iii) the documents that have been reviewed;
 - (b) set out any limitations or qualifications to the Expert Report;
 - (c) list those documents or extracts of documents most relevant (in the view of the External Expert) in producing the Expert Report;
 - (d) otherwise comply (to the extent relevant) with those paragraphs of the Federal Court of Australia Practice Direction entitled "Guidelines for Expert Witnesses in proceedings in the Federal Court of Australia", that fall under the sub-heading "The form of the expert evidence";
 - (e) set out any amendments that were made by the Companies, to the relevant compliance program and compliance documentation during the course of the External Expert's review of that compliance program and compliance documentation, and the reasons for any such amendments

Costs

- 2.42 NAFiM, NAS and MLC Nominees must bear the cost of complying with the obligations in this Enforceable Undertaking, including the engagement of the External Experts and the Expert Reports and must not seek reimbursement of those costs from assets of any funds managed for or on behalf of any investor or member of a superannuation fund.

- 2.43 NAFiM must pay ASIC, within 7 days of the Operational Date, the sum of \$250,000 representing the disbursements associated with ASIC's investigation and with the Federal Court proceedings.

Reporting obligations and assistance

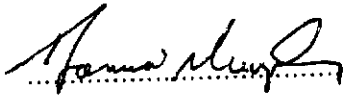
- 2.44 Without derogating from any other obligation upon NAS, NAFiM and MLC Nominees to report to ASIC, in the event that one of those entities forms a view that they have breached a term of this Enforceable Undertaking, that entity must notify ASIC in writing within 1 business day of it forming the view that a breach has occurred and provide particulars of that breach.
- 2.45 NAS, NAFiM and MLC Nominees agree to provide to ASIC information it may reasonably require in relation to the performance of the undertakings contained in this Enforceable Undertaking.
- 2.46 Any report or notification to be provided to ASIC in accordance with this Enforceable Undertaking is to be delivered to:
- Director Enforcement (South/West)
Australian Securities and Investments Commission
Level 13
485 LaTrobe Street
Melbourne VIC 3000.

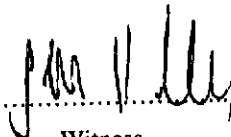
3 Acknowledgments

- 3.1 NAS, NAFiM and MLC Nominees acknowledge that ASIC:
- (a) may issue a media release on execution of this undertaking referring to its terms and the concerns of ASIC which led to its execution;
 - (b) may from time to time publicly refer to this undertaking; and
 - (c) will make this undertaking available for public inspection.
- 3.2 NAS, NAFiM and MLC Nominees acknowledge that this undertaking in no way derogates from the rights and remedies available to any other person or entity arising from any conduct described in this undertaking.
- 3.3 NAS, NAFiM and MLC Nominees acknowledge that ASIC's acceptance of this undertaking does not affect ASIC's power to investigate a contravention arising from future conduct.
- 3.4 NAS, NAFiM and MLC Nominees acknowledge that ASIC may provide the Expert Reports it receives from NAS, NAFiM or MLC Nominees to APRA and that APRA may use and rely on these reports as it sees necessary in the performance of its functions.
- 3.5 ASIC acknowledges that nothing in this Enforceable Undertaking constitutes any admission by NAS, NAFiM or MLC Nominees.

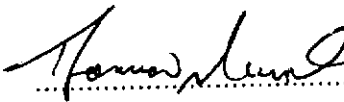
3.6 NAS, NAFIM and MLC Nominees acknowledge that this undertaking has no operative force until accepted by ASIC.

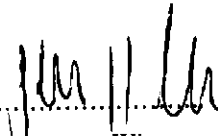
Executed by NATIONAL AUSTRALIA FINANCIAL)
MANAGEMENT LTD (ACN 000 176 116) by its duly)
authorised representative on 2nd September 2003 in the)
presence of:)


.....
Authorised representative

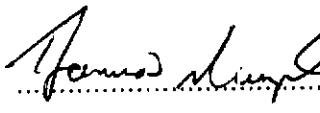

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Witness

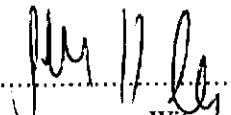
Executed by NATIONAL AUSTRALIA)
SUPERANNUATION PTY. LTD. (ACN 006 972 309) by)
its duly authorised representative on 2nd September 2003 in)
the presence of:)


.....
Authorised representative


.....
Witness

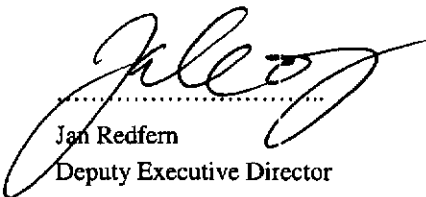
Executed by MLC NOMINEES PTY LTD)
(ACN 002 814 959) by its duly authorised representative)
on 2nd September 2003 in the presence of:)


.....
Authorised representative


.....
Witness

Accepted by the Australian Securities and Investments Commission pursuant to section 93AA of the *Australian Securities and Investments Commission Act* by its duly authorised delegate.

Date this 31 day of September 2003


Jan Redfern
Deputy Executive Director
Enforcement

**Schedule 1 to Enforceable Undertaking -
Undertakings provided to the Federal Court of Australia**

**IN THE FEDERAL COURT OF AUSTRALIA
NEW SOUTH WALES DISTRICT REGISTRY**

No N of 2003

IN THE MATTER OF:

NATIONAL AUSTRALIA SUPERANNUATION PTY LTD (ACN 006 972 309)

**NATIONAL AUSTRALIA FINANCIAL MANAGEMENT LTD (ACN 000 176
116)**

MLC NOMINEES PTY LTD (ACN 002 814 959)

B E T W E E N:

AUSTRALIAN SECURITIES AND INVESTMENTS COMMISSION

Plaintiff

**NATIONAL AUSTRALIA SUPERANNUATION PTY LTD (ACN 006 972
309)**

First Defendant

**NATIONAL AUSTRALIA FINANCIAL MANAGEMENT LTD (ACN 000
176 116)**

Second Defendant

MLC NOMINEES PTY LTD (ACN 002 814 959)

Third Defendant

MINUTE OF UNDERTAKINGS AND CONSENT ORDER

UPON UNDERTAKINGS TO THE COURT, WITHOUT ADMISSIONS, BY THE FIRST, SECOND AND THIRD DEFENDANTS THAT:

1. As soon as reasonably practicable, but in any event within 35 days, the Defendants will use their best endeavours to jointly send a disclosure statement in the form of Schedule 1 to every person recorded in the Defendants' records as being a current member of The Universal Super Scheme ("TUSS") (together with any current employer sponsor of that member) provided that the member was a member of:
 - (a) any superannuation plan of the National All In One Super Fund ("NAIOSF") at any time during the period 20 December 2000 to 30 June 2001 inclusive; or
 - (b) any superannuation plan of NAIOSF, as replicated under TUSS, at any time during the period 1 July 2001 to 31 October 2001 inclusive,and do so in compliance with the requirements set out in Schedule 2.
2. As soon as reasonably practicable, but in any event by 31 December 2003, the Defendants will use their best endeavours to jointly send a disclosure statement in the form of Schedule 1 to every person recorded in the Defendants' records as being, as at the date of this undertaking, an exited member of NAIOSF or TUSS (together with any employer sponsor of that member at the time the member exited, whether that employer sponsor is current or not) provided that the member was a member of either:
 - (a) NAIOSF at any time during the period 20 December 2000 to 30 June 2001 inclusive; or
 - (b) NAIOSF, as replicated under TUSS, at any time during the period 1 July 2001 to 31 October 2001 inclusive,and do so in compliance with the requirements set out in Schedule 2.
3. Within 3 days of the giving of these undertakings, the Defendants will, at their expense, cause a disclosure statement in the form of Schedule 1 to be published on the internet accessible by the public in the following manner until 31 January 2004:
 - (a) On the website www.national.com.au by one or other of the following means:
 - (i) If any media release relating to this proceeding is published by or on behalf of the Defendants on that website and given equal prominence to

all other media releases, by a prominent one click link attached to that media release; or

- (ii) by a prominent one click link on the home page; and
 - (b) On the website www.mlc.com.au, by a prominent one click link on the homepage;
 - (c) On any website introduced after the date of this undertaking in substitution for www.mlc.com.au or www.national.com.au, by a prominent one click link on the homepage.
4. The Defendants will each implement a disclosure compliance program in compliance with the requirements set out in Schedule 3.

PURSUANT TO ORDER 35 RULE 10A, THE COURT ORDERS BY CONSENT THAT:

1. There be no order as to costs.
2. The proceedings be otherwise dismissed.

DATED: September 2003.

.....
Australian Securities and Investments Commission

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Solicitors for the First, Second and Third Defendants

SCHEDULE 1 TO COURT UNDERTAKINGS

FORM OF DISCLOSURE STATEMENT

Compensation for October 2001 Unit Price Reductions to certain NAFiM Superannuation, Pension and Investment Bond Products

Explanatory Booklet for Investors

Introduction

On 16 August 2002, MLC Limited, on behalf of National Australia Financial Management Limited ("NAFiM"), announced that it would compensate investors in a number of NAFiM products who had been affected by reductions in unit prices in October 2001 ("affected investors").

A leading firm of actuaries, Trowbridge Deloitte, has independently assessed NAFiM's commitment to compensate investors and confirmed that as a result of that compensation, no investor will be adversely affected by the unit price reductions of October 2001 and the unit pricing errors referred to below. Compensation is explained later in this booklet.

This booklet has been prepared by NAFiM, National Australia Superannuation Pty Limited ("NAS") and MLC Nominees Pty Limited ("MLC Nominees") in consultation with the Australian Securities and Investments Commission ("ASIC") and following the settlement of Court proceedings commenced by ASIC.

The purpose of this booklet is to provide affected investors with:

- an overview of the circumstances leading to the unit price reductions in October 2001, including the relevant events arising from the integration of NAFiM with the MLC Group (the integration followed National Australia Bank Limited's acquisition of the MLC Group on 30 June 2000);
- detail of the reasons for the unit price reductions in October 2001;
- an overview of the reasons for the compensation announcement in August 2002; and

- a description of the enhanced procedures that are being put in place to address the issues identified in this booklet.

This booklet was foreshadowed to affected investors at the time of the compensation announcement in August 2002 and, relevantly, through the annual reports issued in 2002.

NAFiM, NAS and MLC Nominees are collectively referred to as the "Companies" in this booklet. NAS and MLC Nominees are superannuation trustees.

ASIC's concerns and action

ASIC commenced enquiries into the circumstances surrounding the October 2001 unit price reductions in July 2002. In September 2002, ASIC began investigating suspected contraventions of the law by the Companies in relation to:

- the integration of the personal and business superannuation products offered by NAS with those offered by MLC Nominees ("superannuation integration");
- unit pricing by NAFiM; and
- the disclosure of information in relation to these matters.

ASIC's investigation has now concluded. ASIC acknowledges that the Companies co-operated throughout ASIC's investigation and demonstrated their commitment to fully compensate investors.

However, ASIC believes that some of the disclosures made to investors about the unit price reductions and superannuation integration were misleading or deceptive and did not meet the disclosure obligations under the *Superannuation Industry (Supervision) Act 1993*. As a result, ASIC commenced proceedings against the Companies in the Federal Court of Australia. The Companies do not agree with ASIC's view but acknowledge that the investor communication processes around the unit price reductions and the closure of certain products as part of superannuation integration were not satisfactory.

The Companies defended the claims made by ASIC in the proceedings.

The proceedings were settled, without admissions, by the Companies giving undertakings to the Federal Court that:

- this booklet be distributed to affected investors; and
- the Companies take certain remedial action to prevent a recurrence of some of the issues identified in the investigation,

on the basis that:

- the proceedings be dismissed;
- there be no order as to costs.

The Companies have also offered an Enforceable Undertaking to ASIC, which ASIC has accepted, under which they have agreed to take certain steps to ensure there are proper and improved processes and procedures in place in relation to:

- the setting and monitoring of unit prices;
- governance within NAS and MLC Nominees; and
- complaint handling.

Further details of the Federal Court action brought by ASIC and the Enforceable Undertaking can be found on ASIC's website www.asic.gov.au.

Relevant events concerning integration and the unit price reductions

It has been agreed with ASIC that the following events represent the key matters to be explained to affected investors about the unit price reductions and superannuation integration.

Superannuation integration involved the following steps:

- approval in September 2000 of a plan to integrate the operations of NAS and MLC Nominees, and their various products, including the affected NAFiM products;
- closure of certain NAS products in May and June 2001 to new investors;
- a successor fund transfer, and associated trust deed amendment, in June 2001;
- trade-ups to existing MLC products in December 2001 and January 2002.

An unintended consequence of closure, as part of superannuation integration, was its contribution to the unit price reductions in October 2001.

Each of these events are outlined below.

Integration – September 2000

On 30 June 2000, National Australia Bank Limited acquired the MLC group of companies. At that time, the National Group was essentially operating two distinct wealth management businesses. For example, in relation to superannuation, NAS

offered a range of superannuation products, and MLC Nominees offered a range of different superannuation products.

The integration of the businesses of the National and MLC groups was announced in general terms to the public shortly after the acquisition in 2000.

The integration of the superannuation businesses of NAS and MLC Nominees achieved financial benefits for the National Group through operating synergies and the elimination of duplicated products and services, while seeking to maintain and improve rights for investors through product features.

In September 2000, NAFiM approved a high level plan for the implementation of an integration process. This plan followed detailed consideration and analysis of the cost savings of integration and the features of the respective product ranges. Implementation of superannuation integration was subject to, among other things, relevant trustee company approvals.

NAS and MLC Nominees were informed of the integration plan in November-December 2000. The Companies did not disclose that plan to investors at that time. ASIC considers that disclosure of the plan and its likely impact on investors should have been made in December 2000.

The Companies do not agree with ASIC's view because (among other things) the implementation of the integration plan was subject to relevant trustee approvals during 2001 and a number of recommendations in the plan, in particular relating to trade up, have subsequently not been implemented.

Closure to new investors of certain products

In March 2001, as part of the process of integration, NAFiM, in conjunction with NAS, announced to the National Group's financial advisers that it was closing some of its life insurance products to new investors.

From 31 May 2001, NAS closed to new investors the only open superannuation products within the National All in One Superannuation Fund ("NAIOSF"). NAS was, at that time, the trustee of the NAIOSF. Contributions made by investors into the NAIOSF products were invested by NAS into various life insurance products issued by NAFiM.

All existing investors (other than in one product) were told about closure in September 2001 when they received their annual report.

The decision to close the life insurance products to new investors caused, in part, the need for the unit price reductions in October 2001. However, at the time the decision was made, those responsible for the relevant NAFiM products did not foresee the possible implications of closure on the unit prices of those or other affected products. As a result, it was not recognised that closure would (or could) bring about the need for unit price reductions.

Consequently, when the closure of these products was announced to existing investors in September 2001, those investors were not told of the likely implications of closure on the unit prices of those, or other, affected products.

Successor fund transfer

In April 2001, as part of the process of superannuation integration, NAS and MLC Nominees approved a "successor fund transfer" of all members and assets of NAIOSF to The Universal Super Scheme ("TUSS"). MLC Nominees is the trustee of TUSS.

The *Superannuation Industry (Supervision) Act 1993*, and its regulations, permits the transfer of members and assets from one superannuation fund to another without the need to obtain member consent, provided that the members in the new fund receive rights equivalent to the original fund (successor fund transfer). Member consent to the transfer only needs to be obtained where equivalent rights are not available. To enable this to occur, MLC Nominees replicated the products within NAIOSF under TUSS. As such, equivalent rights were provided (until trade-up did or was to occur).

In many cases, NAIOSF members were part of employer-sponsored superannuation schemes. Before the transfer of these schemes occurred, NAS amended the NAIOSF Trust Deed (in accordance with the terms of the NAIOSF Trust Deed) to remove a requirement for employers to consent to the transfer of employer-sponsored members to other superannuation schemes. NAS made the amendment because it believed it would efficiently facilitate the transfer.

Investors were informed of the successor fund transfer, and the associated Trust Deed amendments, after they occurred, in the annual reports delivered to them in September 2001.

ASIC has a number of concerns about disclosure of superannuation integration. ASIC believes that the Companies should have told investors about each step of superannuation integration, comprising closure of the products, the successor fund transfer, the trust deed amendments and the proposed trade-up of some superannuation products in the context of the integration plan before any of these steps occurred.

The Companies do not agree with ASIC because disclosure of each of the steps of superannuation integration was considered and made after each step occurred, and in the case of trade up, in advance of it occurring. In addition, the integration of the businesses of the National and MLC groups was announced in general terms to the public shortly after the acquisition in 2000 and, in the Companies' present view, this created in the minds of investors an awareness of superannuation integration.

The Enforceable Undertaking contains a more detailed account of ASIC's concerns and the Companies' responses to them.

Unit price reductions

On 30 October 2001, NAFiM reduced the unit prices of units within certain investment portfolios into which investors' monies were placed. Across all of the portfolios, the total impact of the unit price reductions was about \$60 million. They affected approximately 235,000 investors and 21 life insurance products. Attached to this booklet is a list of the affected life products.

What caused the unit price reductions?

Investment-linked life insurance products buy and sell assets with investors' money. Costs are incurred when assets are bought and sold. Unitised life insurance products must ensure that transaction costs incurred in the buying and selling of assets are borne equitably. For NAFiM's products, this was usually done by incorporating an allowance for transaction costs into the unit price ("transaction costs factor").

For growing portfolios, some of the money from new investors is used to pay exiting investors, and the balance is used to purchase new assets. However, when a portfolio is contracting, assets must be sold in order to pay exiting investors as there is not enough new investors' money to meet the needs of exiting investors. This purchase or sale of assets incurs transaction costs. In the circumstances of a growing portfolio, the transaction costs factor should generally be set to raise the unit price so that new investors pay their share of transaction costs. Similarly, in the circumstances of a contracting portfolio, the transaction costs factor should generally be set to lower the unit price so that exiting investors receive less money for their investment in order to pay their share of transaction costs.

The October 2001 unit price reductions occurred following the movement of some of the investment portfolios to a net outflow position, which was substantially caused by the product closures referred to earlier.

However, the main reason for the *size* of the reductions (more than 80%) was two underlying historical unit pricing errors, which have only been identified recently. The errors are that:

- the transaction cost factors applied to the investment portfolios were higher than they should have been for most investment portfolios for significant periods between 1993 and 2001. (NAFiM has been unable to locate records that would enable it to determine what the transaction cost factors were or should have been for significant times during that period, and has relied on estimates made by Trowbridge Deloitte for those periods); and
- in relation to five life insurance products, NAFiM applied the wrong unit pricing methodology.

Communication about the unit price reductions

From 1 November 2001, NAFiM made a communication available to advisers informing them about some aspects of the unit price reductions. A more detailed communication was requested by advisers and made available to them from 30 November 2001.

Disclosure of the unit price reductions was intended to be provided, within three months, to approximately 150,000 of the 294,000 investors then considered to be affected by the unit price reductions, on the basis that NAFiM considered those investors to be materially affected by the unit price reductions. The disclosure was to be made by way of a flyer inserted in the "National Perspective" magazine in January / February 2002. Due to a breakdown in communication within NAFiM, only 30,000 investors actually received the flyer. Those investors not considered to be materially affected by the unit price reductions were to be informed of the unit price reductions through the annual reports. Those reports were issued in September 2002.

ASIC has alleged that the communications sent to investors, advisers and employer sponsors in relation to the unit price reductions were misleading in a number of respects.

While the Companies do not agree with ASIC's allegations in relation to those communications, the Companies acknowledge that they did not fully inform all investors about the unit price reductions following 30 October 2001. In particular, the Companies did not inform investors of the overall size of the reductions or the individual impact of the reductions on their investments. The Companies also did not inform investors of all of the causes of the unit price reductions because of a lack of understanding by the Companies at the time.

The Enforceable Undertaking contains a more detailed account of ASIC's concerns and the Companies' responses to them.

Trade-ups

Trade-up was, and is, the proposed final step of the process of superannuation integration. Trade-up involves transferring members from the replicated NAIOSF product within TUSS into an existing TUSS product (with additional features to the replicated NAIOSF product), thereby altering members' terms and conditions. The power to trade-up is provided for in the TUSS Trust Deed.

MLC Nominees' resolved (subject to certain conditions, which were subsequently satisfied) that the two trade-up proposals put to it were in members' best interests and, accordingly, approved them in July-August 2001. As a result:

- approximately 30,000 members of Personal All in One Super and their assets were traded-up to MLC MasterKey Superannuation on 1 December 2001; and
- approximately 90,000 members of FlexiSuper were traded-up to The Employee Retirement Plan on 1 January 2002.

Compensation for affected investors

On 16 August 2002, having received complaints from investors and inquiries from ASIC, MLC Limited, on behalf of NAFiM, announced that affected investors would be compensated a total of \$60 million for the October 2001 unit price reductions. NAFiM made the decision to compensate because of the following concerns:

- following the closure of various products, there had been an outflow of funds which led to the need for unit price reductions;
- certain investors may have been adversely affected by a failure to adjust the unit prices sooner;
- the communication processes around the unit price reductions were not satisfactory.

Since making that announcement, NAFiM has identified the two underlying historical unit pricing errors referred to earlier. NAFiM has also committed to compensate affected investors for the direct impact of these two errors, increasing the total compensation from \$60 million as announced in August 2002 to \$67.2 million.

NAFiM engaged a leading firm of actuaries, Trowbridge Deloitte, to independently assess its approach and confirm the adequacy of the overall compensation commitment.

Trowbridge Deloitte's opinion is that NAFiM's revised compensation commitment will ensure that all affected investors are fully compensated for the direct impact of the unit price reductions and the unit pricing errors.

Enhanced procedures

The Companies have implemented, and are in the process of implementing, a number of enhanced procedures.

These enhanced procedures include:

- clear accountability for, and regular management review of, unit pricing processes and controls;
- annual review of transaction costs by appropriately qualified and independent external experts and reporting to the relevant boards;
- the implementation of a new policy for future product closures; and
- revised staff training and processes to improve communication to all investors.

The Companies are incorporating these enhanced procedures into their ongoing continuous improvement programs.

In addition, as part of resolution of the Federal Court proceedings, the Companies have undertaken to implement a disclosure compliance program that includes regular external reviews of that program which are to be provided to ASIC.

Neither the compensation nor the external reviews will be paid from investors' funds.

Also, under the Enforceable Undertaking, the Companies have agreed to take certain steps to further ensure there are proper and improved processes and procedures in place in relation to:

- the setting and monitoring of unit prices;
- governance within NAS and MLC Nominees; and
- complaint handling.

Further details of the Federal Court action brought by ASIC and the Enforceable Undertaking can be found on ASIC's website www.asic.gov.au.

List of Affected Products

1. National Personal All in One Super
2. National Business All in One Super
3. National FlexiSuper
4. National FlexiSuper Plus (including National Business Super Plans 1, 2 and 3, which were previous versions of National FlexiSuper Plus)
5. National Flexible Pension Plan
6. National Personal Super Bond*
7. National SuperStar 1 and 2
8. National Business Super Bond
9. National Pooled Superannuation Bond
10. National Super Bond
11. National Asset Builder
12. National FlexiBond
13. National Investment Bond*
14. Tax Paid Savings Bond*
15. Deferred Annuity Growth Bond
16. National Rollover Bond (Series 1)
17. National Rollover Bond (Series 2)
18. National Rollover Bond (Series 3)*
19. National Rollover Parking Bond*
20. National Flexible Income Plan
21. National Pooled Superannuation Fund

* An asterisk indicates that NAFiM applied the incorrect unit pricing methodology to at least some of the policies issued in relation to those products.

SCHEDULE 2 TO COURT UNDERTAKINGS

REQUIREMENTS FOR SENDING DISCLOSURE STATEMENT

1. The Defendants must send the disclosure statement by ordinary mail to the most recent address they have recorded in their databases for each relevant person.
2. In the case of those persons whose mail-out is returned, the Defendants must update the addresses they have for such persons by using Australia Post's "Change of Address" database. If Australia Post's "Change of Address" database reveals a different address for those persons, the Defendants will send the disclosure statement by ordinary mail to that different address.
3. Where Australia Post notifies the Defendants that an Affected Investor has changed address, but has not given their consent to Australia Post to the release of their new details, the Defendants will use Australia Post's "Re-Connect Service" to seek to obtain that new address. Australia Post's "Re-Connect Service" is a service whereby Australia Post writes to relevant Affected Investors advising them that the Defendants are trying to contact them, and asking for consent to the release of their new address.
4. If the Australia Post "Change of Address" database or Australia Post's "Re-Connect Service" reveals no different address for those persons whose mail-out is returned, the Defendants will carry out a search of White Pages On-line and if that search reveals a different address for those persons, the Defendants will send the disclosure statement by ordinary mail to that different address.

SCHEDULE 3 TO COURT UNDERTAKINGS

REQUIREMENTS FOR THE DISCLOSURE COMPLIANCE PROGRAM

1. Within 4 months of the provision of this undertaking to the Federal Court of Australia ("**Operational Date**"), the Defendants must:
 - (a) review the manner (including the processes, practices, internal controls, risk management framework, compliance systems, supervision, training, service agreements and resources) (the "**Disclosure Compliance Program**") by which the Defendants seek to comply with sections 12DA of the *Australian Securities and Investments Commission Act 2001* (Cth), section 1041H of the *Corporations Act 2001* (Cth) and the First and Third Defendants comply with Division 2.5 of the *Superannuation Industry (Supervision) Regulations 1994* (Cth) and section 1017B of the *Corporations Act 2001* (Cth) (the "**Disclosure Obligations**"); and
 - (b) document the Disclosure Compliance Program (the "**Disclosure Compliance Documentation**").
2. The Defendants must use their best endeavours to implement the Disclosure Compliance Program.
3. Within 4 months of the Operational Date, the Defendants must engage an external independent compliance expert (the "**Disclosure Compliance Expert**"), on terms to be approved by ASIC to:
 - (a) review the Disclosure Compliance Program and the Disclosure Compliance Documentation to ascertain whether they are appropriate to enable the Defendants to comply with the Disclosure Obligations; and
 - (b) determine whether the Disclosure Compliance Program has been implemented.
4. Within 7 months of the Operational Date, the Disclosure Compliance Expert must provide to the Defendants and ASIC a report on the review conducted by the Disclosure

Compliance Expert pursuant to paragraph 3 (the "Initial Disclosure Expert Report"). The Initial Disclosure Expert Report must either:

(a) confirm that:

(i) the Disclosure Compliance Program and the Disclosure Compliance Documentation are appropriate to enable the Defendants to comply with the Disclosure Obligations; and

(ii) the Disclosure Compliance Program has been implemented; or

(b) if the Disclosure Compliance Expert is unable to provide the confirmation referred to in sub-paragraph 4(a), set out the deficiencies:

(i) in the Disclosure Compliance Program and/or the Disclosure Compliance Documentation identified and recommend changes to the Disclosure Compliance Program and/or the Disclosure Compliance Documentation; and/ or

(ii) in the implementation of the Disclosure Compliance Program and specify the steps to be taken to rectify the deficiencies.

5. If the Initial Disclosure Expert Report identifies deficiencies in the Disclosure Compliance Program and/or the Disclosure Compliance Documentation, within 2 months of receipt of the Initial Disclosure Compliance Report, the Defendants must provide a report to ASIC setting out the action it has taken, or proposes to take, and in what timeframe, to rectify the deficiencies ("Remedial Action").

6. The Defendants must use their best endeavours to implement the Remedial Action.

7. The Defendants must maintain and annually update (for two subsequent anniversaries of the Operational Date) the Disclosure Compliance Program and the Disclosure Compliance Documentation to ensure that they continue to enable the Defendants to comply with the Disclosure Obligations.

8. On or before the date of the two subsequent anniversaries of the Initial Disclosure Compliance Report the Defendants must ensure that the Disclosure Compliance Expert has conducted a review of the implementation of the Disclosure Compliance Program and any Remedial Action (or Subsequent Remedial Action, as defined in paragraph 9 below) (if any) and of the Disclosure Compliance Documentation. The Disclosure Compliance Expert must, after doing so, provide to the Defendants and ASIC a report on the review conducted by the Disclosure Compliance Expert pursuant to this paragraph 8 (the "Subsequent Disclosure Expert Report"). The Subsequent Disclosure Expert Report must either:

(a) confirm that:

(i) the Disclosure Compliance Program and the Remedial Action (or Subsequent Remedial Action as defined in paragraph 9 below) (if any) have been implemented and complied with; and

(ii) the Disclosure Compliance Program and the Disclosure Compliance Documentation remain appropriate to enable the Defendants to comply with the Disclosure Obligations; or

(b) if the Disclosure Compliance Expert is unable to provide the confirmation referred to in sub-paragraph 8(a), set out the deficiencies:

(i) in the Disclosure Compliance Program and/or the Disclosure Compliance Documentation identified and recommend changes to the Disclosure Compliance Program and/or the Disclosure Compliance Documentation; and

(ii) in the implementation of the Disclosure Compliance Program and any Remedial Action (or Subsequent Remedial Action, as defined in paragraph 9 below) (if any), and specify the steps to be taken to rectify the deficiencies.

9. If the Subsequent Disclosure Expert Report identifies deficiencies in accordance with sub-paragraph 8(b), within 2 months of the date of receipt of the Subsequent Disclosure

Expert Report, the Defendants must provide a report to ASIC setting out the actions they have taken, or propose to take, and in what timeframe, to rectify the deficiencies (the "**Subsequent Remedial Action**").

10. The Defendants must use their best endeavours to implement any Subsequent Remedial Action.
11. The Defendants must bear the cost of complying with the obligations in this undertaking including the engagement of the Disclosure Compliance Expert, the Initial Disclosure Expert Report and each Subsequent Disclosure Expert Report and shall not seek reimbursement of the costs from assets of any funds managed for or on behalf of any investor or member of a superannuation fund.

Schedule 2 to Enforceable Undertaking – Disclosure Statement

Compensation for October 2001 Unit Price Reductions to certain NAFiM Superannuation, Pension and Investment Bond Products

Explanatory Booklet for Investors

Introduction

On 16 August 2002, MLC Limited, on behalf of National Australia Financial Management Limited ("NAFiM"), announced that it would compensate investors in a number of NAFiM products who had been affected by reductions in unit prices in October 2001 ("affected investors").

A leading firm of actuaries, Trowbridge Deloitte, has independently assessed NAFiM's commitment to compensate investors and confirmed that as a result of that compensation, no investor will be adversely affected by the unit price reductions of October 2001 and the unit pricing errors referred to below. Compensation is explained later in this booklet.

This booklet has been prepared by NAFiM, National Australia Superannuation Pty Limited ("NAS") and MLC Nominees Pty Limited ("MLC Nominees") in consultation with the Australian Securities and Investments Commission ("ASIC") and following the settlement of Court proceedings commenced by ASIC.

The purpose of this booklet is to provide affected investors with:

- an overview of the circumstances leading to the unit price reductions in October 2001, including the relevant events arising from the integration of NAFiM with the MLC Group (the integration followed National Australia Bank Limited's acquisition of the MLC Group on 30 June 2000);
- detail of the reasons for the unit price reductions in October 2001;
- an overview of the reasons for the compensation announcement in August 2002; and
- a description of the enhanced procedures that are being put in place to address the issues identified in this booklet.

This booklet was foreshadowed to affected investors at the time of the compensation announcement in August 2002 and, relevantly, through the annual reports issued in 2002.

NAFiM, NAS and MLC Nominees are collectively referred to as the "Companies" in this booklet. NAS and MLC Nominees are superannuation trustees.

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ASIC commenced enquiries into the circumstances surrounding the October 2001 unit price reductions in July 2002. In September 2002, ASIC began investigating suspected contraventions of the law by the Companies in relation to:

- the integration of the personal and business superannuation products offered by NAS with those offered by MLC Nominees ("superannuation integration");
- unit pricing by NAFiM; and
- the disclosure of information in relation to these matters.

ASIC's investigation has now concluded. ASIC acknowledges that the Companies co-operated throughout ASIC's investigation and demonstrated their commitment to fully compensate investors.

However, ASIC believes that some of the disclosures made to investors about the unit price reductions and superannuation integration were misleading or deceptive and did not meet the disclosure obligations under the *Superannuation Industry (Supervision) Act 1993*. As a result, ASIC commenced proceedings against the Companies in the Federal Court of Australia. The Companies do not agree with ASIC's view but acknowledge that the investor communication processes around the unit price reductions and the closure of certain products as part of superannuation integration were not satisfactory.

The Companies defended the claims made by ASIC in the proceedings.

The proceedings were settled, without admissions, by the Companies giving undertakings to the Federal Court that:

- this booklet be distributed to affected investors; and
- the Companies take certain remedial action to prevent a recurrence of some of the issues identified in the investigation,

on the basis that:

- the proceedings be dismissed;
- there be no order as to costs.

The Companies have also offered an Enforceable Undertaking to ASIC, which ASIC has accepted, under which they have agreed to take certain steps to ensure there are proper and improved processes and procedures in place in relation to:

- the setting and monitoring of unit prices;
- governance within NAS and MLC Nominees; and
- complaint handling.

Further details of the Federal Court action brought by ASIC and the Enforceable Undertaking can be found on ASIC's website www.asic.gov.au.

Relevant events concerning Integration and the unit price reductions

It has been agreed with ASIC that the following events represent the key matters to be explained to affected investors about the unit price reductions and superannuation integration.

Superannuation integration involved the following steps:

- approval in September 2000 of a plan to integrate the operations of NAS and MLC Nominees, and their various products, including the affected NAFIM products;
- closure of certain NAS products in May and June 2001 to new investors;
- a successor fund transfer, and associated trust deed amendment, in June 2001;
- trade-ups to existing MLC products in December 2001 and January 2002.

An unintended consequence of closure, as part of superannuation integration, was its contribution to the unit price reductions in October 2001.

Each of these events are outlined below.

Integration – September 2000

On 30 June 2000, National Australia Bank Limited acquired the MLC group of companies. At that time, the National Group was essentially operating two distinct wealth management businesses. For example, in relation to superannuation, NAS offered a range of superannuation products, and MLC Nominees offered a range of different superannuation products.

The integration of the businesses of the National and MLC groups was announced in general terms to the public shortly after the acquisition in 2000.

The integration of the superannuation businesses of NAS and MLC Nominees achieved financial benefits for the National Group through operating synergies and the elimination of duplicated products and services, while seeking to maintain and improve rights for investors through product features.

In September 2000, NAFiM approved a high level plan for the implementation of an integration process. This plan followed detailed consideration and analysis of the cost savings of integration and the features of the respective product ranges. Implementation of superannuation integration was subject to, among other things, relevant trustee company approvals.

NAS and MLC Nominees were informed of the integration plan in November-December 2000. The Companies did not disclose that plan to investors at that time. ASIC considers that disclosure of the plan and its likely impact on investors should have been made in December 2000.

The Companies do not agree with ASIC's view because (among other things) the implementation of the integration plan was subject to relevant trustee approvals during 2001 and a number of recommendations in the plan, in particular relating to trade up, have subsequently not been implemented.

Closure to new investors of certain products

In March 2001, as part of the process of integration, NAFiM, in conjunction with NAS, announced to the National Group's financial advisers that it was closing some of its life insurance products to new investors.

From 31 May 2001, NAS closed to new investors the only open superannuation products within the National All in One Superannuation Fund ("NAIOSF"). NAS was, at that time, the trustee of the NAIOSF. Contributions made by investors into the NAIOSF products were invested by NAS into various life insurance products issued by NAFiM.

All existing investors (other than in one product) were told about closure in September 2001 when they received their annual report.

The decision to close the life insurance products to new investors caused, in part, the need for the unit price reductions in October 2001. However, at the time the decision was made, those responsible for the relevant NAFiM products did not foresee the possible implications of closure on the unit prices of those or other affected products. As a result, it was not recognised that closure would (or could) bring about the need for unit price reductions.

Consequently, when the closure of these products was announced to existing investors in September 2001, those investors were not told of the likely implications of closure on the unit prices of those, or other, affected products.

Successor fund transfer

In April 2001, as part of the process of superannuation integration, NAS and MLC Nominees approved a "successor fund transfer" of all members and assets of NAIOSF to The Universal Super Scheme ("TUSS"). MLC Nominees is the trustee of TUSS.

The *Superannuation Industry (Supervision) Act 1993*, and its regulations, permits the transfer of members and assets from one superannuation fund to another without the need to obtain member consent, provided that the members in the new fund receive rights equivalent to the original fund (successor fund transfer). Member consent to the transfer only needs to be obtained where equivalent rights are not available. To enable this to occur, MLC Nominees replicated the products within NAIOSF under TUSS. As such, equivalent rights were provided (until trade-up did or was to occur).

In many cases, NAIOSF members were part of employer-sponsored superannuation schemes. Before the transfer of these schemes occurred, NAS amended the NAIOSF Trust Deed (in accordance with the terms of the NAIOSF Trust Deed) to remove a requirement for employers to consent to the transfer of employer-sponsored members to other superannuation schemes. NAS made the amendment because it believed it would efficiently facilitate the transfer.

Investors were informed of the successor fund transfer, and the associated Trust Deed amendments, after they occurred, in the annual reports delivered to them in September 2001.

ASIC has a number of concerns about disclosure of superannuation integration. ASIC believes that the Companies should have told investors about each step of superannuation integration, comprising closure of the products, the successor fund transfer, the trust deed amendments and the proposed trade-up of some superannuation products in the context of the integration plan before any of these steps occurred.

The Companies do not agree with ASIC because disclosure of each of the steps of superannuation integration was considered and made after each step occurred, and in the case of trade up, in advance of it occurring. In addition, the integration of the businesses of the National and MLC groups was announced in general terms to the public shortly after the acquisition in 2000 and, in the Companies' present view, this created in the minds of investors an awareness of superannuation integration.

The Enforceable Undertaking contains a more detailed account of ASIC's concerns and the Companies' responses to them.

Unit price reductions

On 30 October 2001, NAFiM reduced the unit prices of units within certain investment portfolios into which investors' monies were placed. Across all of the portfolios, the total impact of the unit price reductions was about \$60 million. They affected approximately 235,000 investors and 21 life insurance products. Attached to this booklet is a list of the affected life products.

What caused the unit price reductions?

Investment-linked life insurance products buy and sell assets with investors' money. Costs are incurred when assets are bought and sold. Unitised life insurance products must ensure that transaction costs incurred in the buying and selling of assets are borne equitably. For NAFiM's products, this was usually done by incorporating an allowance for transaction costs into the unit price ("transaction costs factor").

For growing portfolios, some of the money from new investors is used to pay exiting investors, and the balance is used to purchase new assets. However, when a portfolio is contracting, assets must be sold in order to pay exiting investors as there is not enough new investors' money to meet the needs of exiting investors. This purchase or sale of assets incurs transaction costs. In the circumstances of a growing portfolio, the transaction costs factor should generally be set to raise the unit price so that new investors pay their share of transaction costs. Similarly, in the circumstances of a contracting portfolio, the transaction costs factor should generally be set to lower the unit price so that exiting investors receive less money for their investment in order to pay their share of transaction costs.

The October 2001 unit price reductions occurred following the movement of some of the investment portfolios to a net outflow position, which was substantially caused by the product closures referred to earlier.

However, the main reason for the *size* of the reductions (more than 80%) was two underlying historical unit pricing errors, which have only been identified recently. The errors are that:

- the transaction cost factors applied to the investment portfolios were higher than they should have been for most investment portfolios for significant periods between 1993 and 2001. (NAFiM has been unable to locate records that would enable it to determine what the transaction cost factors were or should have been for significant times during that period, and has relied on estimates made by Trowbridge Deloitte for those periods); and
- in relation to five life insurance products, NAFiM applied the wrong unit pricing methodology.

Communication about the unit price reductions

From 1 November 2001, NAFiM made a communication available to advisers informing them about some aspects of the unit price reductions. A more detailed communication was requested by advisers and made available to them from 30 November 2001.

Disclosure of the unit price reductions was intended to be provided, within three months, to approximately 150,000 of the 294,000 investors then considered to be affected by the unit price reductions, on the basis that NAFiM considered those investors to be materially affected by the unit price reductions. The disclosure was to be

made by way of a flyer inserted in the "National Perspective" magazine in January / February 2002. Due to a breakdown in communication within NAFiM, only 30,000 investors actually received the flyer. Those investors not considered to be materially affected by the unit price reductions were to be informed of the unit price reductions through the annual reports. Those reports were issued in September 2002.

ASIC has alleged that the communications sent to investors, advisers and employer sponsors in relation to the unit price reductions were misleading in a number of respects.

While the Companies do not agree with ASIC's allegations in relation to those communications, the Companies acknowledge that they did not fully inform all investors about the unit price reductions following 30 October 2001. In particular, the Companies did not inform investors of the overall size of the reductions or the individual impact of the reductions on their investments. The Companies also did not inform investors of all of the causes of the unit price reductions because of a lack of understanding by the Companies at the time.

The Enforceable Undertaking contains a more detailed account of ASIC's concerns and the Companies' responses to them.

Trade-ups

Trade-up was, and is, the proposed final step of the process of superannuation integration. Trade-up involves transferring members from the replicated NAIOSF product within TUSS into an existing TUSS product (with additional features to the replicated NAIOSF product), thereby altering members' terms and conditions. The power to trade-up is provided for in the TUSS Trust Deed.

MLC Nominees' resolved (subject to certain conditions, which were subsequently satisfied) that the two trade-up proposals put to it were in members' best interests and, accordingly, approved them in July-August 2001. As a result:

- approximately 30,000 members of Personal All in One Super and their assets were traded-up to MLC MasterKey Superannuation on 1 December 2001; and
- approximately 90,000 members of FlexiSuper were traded-up to The Employee Retirement Plan on 1 January 2002.

Compensation for affected investors

On 16 August 2002, having received complaints from investors and inquiries from ASIC, MLC Limited, on behalf of NAFiM, announced that affected investors would be compensated a total of \$60 million for the October 2001 unit price reductions. NAFiM made the decision to compensate because of the following concerns:

- following the closure of various products, there had been an outflow of funds which led to the need for unit price reductions;

- certain investors may have been adversely affected by a failure to adjust the unit prices sooner;
- the communication processes around the unit price reductions were not satisfactory.

Since making that announcement, NAFiM has identified the two underlying historical unit pricing errors referred to earlier. NAFiM has also committed to compensate affected investors for the direct impact of these two errors, increasing the total compensation from \$60 million as announced in August 2002 to \$67.2 million.

NAFiM engaged a leading firm of actuaries, Trowbridge Deloitte, to independently assess its approach and confirm the adequacy of the overall compensation commitment.

Trowbridge Deloitte's opinion is that NAFiM's revised compensation commitment will ensure that all affected investors are fully compensated for the direct impact of the unit price reductions and the unit pricing errors.

Enhanced procedures

The Companies have implemented, and are in the process of implementing, a number of enhanced procedures.

These enhanced procedures include:

- clear accountability for, and regular management review of, unit pricing processes and controls;
- annual review of transaction costs by appropriately qualified and independent external experts and reporting to the relevant boards;
- the implementation of a new policy for future product closures; and
- revised staff training and processes to improve communication to all investors.

The Companies are incorporating these enhanced procedures into their ongoing continuous improvement programs.

In addition, as part of resolution of the Federal Court proceedings, the Companies have undertaken to implement a disclosure compliance program that includes regular external reviews of that program which are to be provided to ASIC.

Neither the compensation nor the external reviews will be paid from investors' funds.

Also, under the Enforceable Undertaking, the Companies have agreed to take certain steps to further ensure there are proper and improved processes and procedures in place in relation to:

- the setting and monitoring of unit prices;
- governance within NAS and MLC Nominees; and
- complaint handling.

Further details of the Federal Court action brought by ASIC and the Enforceable Undertaking can be found on ASIC's website www.asic.gov.au.

List of Affected Products

1. National Personal All in One Super
2. National Business All in One Super
3. National FlexiSuper
4. National FlexiSuper Plus (including National Business Super Plans 1, 2 and 3, which were previous versions of National FlexiSuper Plus)
5. National Flexible Pension Plan
6. National Personal Super Bond*
7. National SuperStar 1 and 2
8. National Business Super Bond
9. National Pooled Superannuation Bond
10. National Super Bond
11. National Asset Builder
12. National FlexiBond
13. National Investment Bond*
14. Tax Paid Savings Bond*
15. Deferred Annuity Growth Bond
16. National Rollover Bond (Series 1)
17. National Rollover Bond (Series 2)
18. National Rollover Bond (Series 3)*
19. National Rollover Parking Bond*
20. National Flexible Income Plan
21. National Pooled Superannuation Fund

* An asterisk indicates that NAFIM applied the incorrect unit pricing methodology to at least some of the policies issued in relation to those products.

Schedule 3 to Enforceable Undertaking

Procedure for locating Affected Investors for the purposes of compensation and the provision of the disclosure statement

1. NAFiM, NAS and MLC Nominees (the "Companies") must send the disclosure statement by ordinary mail to the most recent address they have recorded in their databases for each relevant person.
2. In the case of those persons whose mail-out is returned, the Companies must update the addresses they have for such persons by using Australia Post's "Change of Address" database. If Australia Post's "Change of Address" database reveals a different address for those persons, the Companies will send the disclosure statement by ordinary mail to that different address.
3. Where Australia Post notifies the Companies that an Affected Investor has changed address, but has not given their consent to Australia Post to the release of their new details, the Companies will use Australia Post's "Re-Connect Service" to seek to obtain that new address. Australia Post's "Re-Connect Service" is a service whereby Australia Post writes to relevant Affected Investors advising them that the Companies are trying to contact them, and asking for consent to the release of their new address.
4. If the Australia Post "Change of Address" database or Australia Post's "Re-Connect Service" reveals no different address for those persons whose mail-out is returned, the Companies will carry out a search of White Pages On-line and if that search reveals a different address for those persons, the Companies will send the disclosure statement by ordinary mail to that different address.