

## UNDERTAKING

Insurance Act 1973

Section 126

This Undertaking is given by

**Malcolm Murray Jones** of 4 Jellicoe Street Balgowlah Heights New South Wales (Mr Jones)

and is accepted by

**Australian Prudential Regulation Authority** of level 26, 400 George Street, Sydney, New South Wales (APRA)

under section 126 of the Insurance Act 1973 (the Act). A copy of section 126 is in schedule 1.

### Background

1. This Undertaking arises out of Mr Jones's association with Zurich Financial Services Australia Limited (ZFSA) and its subsidiary, Zurich Australia Insurance Limited (ZAIL), in relation to ZAIL's entry in 2000 into two transactions, being a loss portfolio transfer contract (LPT Contract) in respect of a group of ZAIL insurance policies (ZAIL Liability Portfolio) and a stop loss contract (Stop Loss Contract) (together the Reinsurance Transactions), with companies in the General & Cologne Re Group (GCR).
2. ZAIL and General Cologne Reinsurance Australia (GCRA) entered into an LPT, the risk under which was retroceded to ZIC. ZAIL also entered into a Stop Loss contract with Koelnische Rueckversicherungs Gesellschaft AG (CRAUS) which retroceded the risk to ZIC. Premiums under the Stop Loss Contract were calculated by ZAIL as an amount necessary to cover any loss to ZIC under the LPT.
3. Later, APRA in the course of its normal prudential supervisory activities obtained information which made it concerned about the substantive nature of the Reinsurance Transactions. It then became aware of a series of further transactions which appeared to be related. In the light of this fresh knowledge, the way in which the Reinsurance Transactions were accounted for by ZAIL and reported in the statutory returns provided to APRA by ZAIL under section 44 of the Act (as it then was) and other disclosures to APRA, APRA decided these were issues of prudential concern.
4. On 17 May 2004 APRA appointed an inspector to make (amongst other things) an investigation into the affairs of ZAIL and ZFSA. APRA, formed the view that there were fundamental

misstatements/mistreatments of the Reinsurance Transactions in ZAIL's accounts in 2000. ZAIL and ZFSA, on the basis of advice from its auditors, came to the same view as in response to the matters raised by APRA the Boards of ZFSA and ZAIL met on 29 November 2004 to consider the accounting treatment of the LPT Contract and resolved to:

*DETERMINE, on the basis of the information before the Board concerning the transactions, that the Loss Portfolio Transfer Agreement dated 28 September 2000 (the "LPT") under which ZAIL purportedly reinsured certain insurance liabilities to General & Cologne Reinsurance Australia and related transactions involving Cologne Re Dublin and Zurich Insurance Company did not involve a transfer of risk from ZAIL and so the LPT ought properly to be characterised as financial reinsurance. (Board's determination).*

5. As a result of the above ZAIL formed the view that its accounting misstatement/mistreatment of the Reinsurance Transactions, resulted in ZAIL's profits in 2000 having been overstated by about \$61.3m in its audited accounts as well as in the Annual Financial Position return lodged with APRA for 2000. Moreover, on that basis, ZAIL formed the view that ZAIL would (in the absence of any other corrective action) have failed to meet the statutory solvency requirements under the Act.
6. On 25 May 2005, ZAIL and ZFSA gave undertakings to APRA under section 126 of the Act in which they, amongst other things, stated their view that the accounts of ZAIL for the years 2000 to 2003, on the basis of the Board's determination, contained a fundamental error which was required to be corrected in accordance with the applicable accounting standards.
7. Subsequently, the accounts of ZAIL for the years 2000 to 2003 were amended in accordance with the Board's determination.

#### **Acknowledgements**

8. Mr Jones acknowledges that he has obtained legal advice before executing this Undertaking.
9. Mr Jones acknowledges that:
  - (a) from about 1 July 1998 he was the Chief Executive Officer of ZAIL and (subject to the board's directions) had executive responsibility in that role until 7 March 2002, and from 24 August 1998 he was a director of ZAIL and effectively exercised that role until 7 March 2002;



- (b) on or about 1 November 2000 he was appointed Chief Executive Officer of the Asia Pacific region in relation to the operations, in that region, of companies associated with ZAIL's Swiss parent company Zurich Insurance Company (ZIC) following a restructure of the ZIC group of companies;
- (c) from 24 August 1998 he was a director of ZFSA and effectively exercised that role until about 7 March 2002;
- (d) he approved of ZAIL's proposed entry into the LPT Contract and of ZAIL entering into a stop loss contract which at that time he believed would be with ZIC;
- (e) he signed a representation letter, from ZFSA/ZAIL to their auditors PriceWaterhouseCoopers (PWC) and dated 14 August 2000, which specifically represented, in relation to the LPT Contract entered into in July 2000 between ZAIL and a GCR group company (known as GCRA) (the transaction):
- (i) that ZFSA/ZAIL had not entered into any associated or related contracts to the transaction with GCRA;
  - (ii) that ZFSA/ZAIL would not receive any recharges of other expenses from Zurich Financial Services group companies [the worldwide group of which ZIC, ZFSA and ZAIL were subsidiaries] related to that transaction or any related transaction; and
  - (iii) that PWC had been provided with all documentation pertaining to the proposed transaction with GCRA.
- (f) he accepts that:
- (i) PWC was not provided, at the relevant times, with all the documentation and information relating to the LPT Contract and the Stop Loss Contract and the premium payable under the Stop Loss Contract;
  - (ii) the board of ZAIL was not informed as to the relationship between the LPT Contract, the Stop Loss Contract and the premiums payable under the Stop Loss Contract;
  - (iii) he did not inform himself properly as to all details of the negotiations and transactions with GCR and the related transactions;

- (iv) he did not satisfy himself properly that PWC had been provided with all the documentation and information that it needed to understand the transactions with GCR;
- (v) he did not satisfy himself properly that the board of ZAIL had been provided with all the documentation and information that it needed to understand the transactions with GCR;
- (vi) all the documents and information that APRA needed to understand the transactions with GCR were not disclosed to APRA; and;
- (vii) since leaving ZAIL he has become aware that:
  - i. the transactions with GCR were intended by some ZAIL executives, who participated in the creation of the transactions, to mislead interested parties;
  - ii. APRA and ZAIL both formed the view that there were fundamental misstatements/mistreatments of the Reinsurance Transactions in ZAIL's accounts in 2000;
  - iii. APRA and ZAIL both formed the view that the Reinsurance Transactions were not genuine reinsurance; and
  - iv. as a result the 2000 to 2003 accounts of ZAIL were restated by ZAIL on the basis of advice from its auditors.

### Mr Jones's Undertakings

10. Mr Jones undertakes that:

(a) subject to subparagraph (c) of this paragraph 10, before 1 August 2021 he will not be, or become, or act as::

- (i) a director or senior manager of a general insurer (other than a foreign general insurer);
- (ii) a senior manager, or agent in Australia for the purpose of section 118 of the Act, of a foreign general insurer;
- (iii) a director or senior manager of an authorised NOHC (within the meaning of the Act);

or

(iv) a director or senior manager of the agent in Australia of a foreign general insurer,  
without the written approval of APRA;

(b) he will provide to APRA all reasonable assistance in relation to any matters arising out of this Undertaking and the transactions and events referred to in this Undertaking if requested by APRA for a period from the date of this undertaking until 1 August 2014;

(c) if on or after 1 August 2014, Mr Jones has in his possession written notification from APRA that he has complied with sub-paragraph (b) or it is otherwise determined that he has complied with sub-paragraph (b), sub-paragraph (a) ceases to have effect; and

(d) he irrevocably authorises APRA to obtain such information as may be requested by APRA from time to time about Mr Jones's compliance with this Undertaking where Mr Jones's written consent to release that information to APRA is required before APRA can obtain that information.

#### **APRA's acceptance of Mr Jones's Undertaking**

11. APRA accepts this Undertaking and acknowledges that this Undertaking disposes of all issues between Mr Jones and APRA arising out of, or in any way connected with, the matters referred to in paragraphs 1 to 9 (inclusive) above and, without limiting the generality of the above, APRA agrees that in consideration of Mr Jones execution of this Undertaking it will not take any action against, or with respect to, Mr Jones arising out of, or in relation to, the matters referred to in paragraphs 1 to 9 (inclusive) above except in the event of breach by Mr Jones of subparagraph (a) of paragraph 10 this Undertaking.

#### *Schedule 1*

#### INSURANCE ACT 1973 - SECTION 126

##### Acceptance and enforcement of undertakings

- (1) APRA may accept a written undertaking given by a person in connection with a matter in relation to which APRA has a function or power under this Act.
- (2) The person may withdraw or vary the undertaking at any time, but only with APRA's consent.
- (3) If APRA considers that the person who gave the undertaking has breached any of its terms, APRA may apply to the Federal Court for an order under subsection (4).

(4) If the Federal Court is satisfied that the person has breached a term of the undertaking, the Federal Court may make all or any of the following orders:

- (a) an order directing the person to comply with that term of the undertaking;
- (b) an order directing the person to pay to the Commonwealth an amount up to the amount of any financial benefit that the person has obtained directly or indirectly and that is reasonably attributable to the breach;
- (c) any order that the Federal Court considers appropriate directing the person to compensate any other person who has suffered loss or damage as a result of the breach;
- (d) any other order that the Federal Court considers appropriate.

Executed on 26.2.09  
by **Malcolm Murray Jones**  
in the presence of:



.....  
signature of witness



.....  
Malcolm Murray Jones

Stephen Toomey

.....  
name of witness

Accepted on .....  
by a delegate of the **Australian Prudential Regulation Authority**  
pursuant to section 126 of the Act  
In the presence of:



.....  
signature of witness



.....  
signature of delegate

DAVID SULLIVAN

.....  
name of witness

PATRICK MEANEY, GENERAL MANAGER,

.....  
name and title of delegate LEGAL AND ENFORCEMENT