

LM Investor Victim Centre (LMIVC) submission to the Australian Financial Systems Inquiry August 2014

Introduction

LMIVC represent interests of victims of the Australian registered investment management company LMIM (ABN 68 077 208 461 AFSL 220 281) of which over 570 have registered with LMIVC in support of 'A Fair & Just Resolution for LM Investors'.

LMIVC, we believe, is the only pure investor movement pursuing justice over the LM fiasco.

LMIVC is victim volunteer driven.

The LMIVC web address is <https://sites.google.com/site/lminvestorvictimcentre>

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Objective (of this submission)

To help the Inquiry toward Australian Financial System improvement that will

- A. Enable and speed recovery of [LM] investor positions
- B. Prevent re-occurrence

Submission Structure

1. Background
2. Financial System Inquiry attention is brought to:
 - a. The Magnitude of Private Wealth Destruction
 - b. The Question of Criminality.
 - c. The Fight for Control of Funds
 - d. The Tony Abbot Government Indifference to International Responsibility and Accountability.
 - e. ASIC
 - f. The Absence of Humane Victim Support
3. Closing Comments, Conclusions and Recommendations

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Background

In the first quarter of 2013 the Australian licensed investment management company, LMIM, collapsed owing 12,000 investors across the world a total of AU\$750m. The media has been awash with allegations of mis-management, fraud, breach of trust, and ponzi scheme operation. Advisors worldwide recommended the investment to low risk investors implicating themselves by virtue of their failure to categorise the investment correctly. Advisor commission from LMIM was well above the industry average.

LMIM was an Investment Management Company founded by a New Zealand national named Peter Drake. The Company was registered and operated in Australia. Investors were offered a range of funds that were, allegedly, deploying different investment positions in the Australian residential property market.

During the global financial crisis beginning 2008, growth in funds targeting, principally, Australian and New Zealand resident investors slowed. To counter this LMIM turned to a fund called the Managed Performance Fund or MPF. The MPF was actively promoted across the world through a network of independent financial advisors.

On March 19th 2013 LMIM called in the administrators. What has since unfolded leaves investors in a state of shock, horror and despair.

The Magnitude of Private Wealth Destruction

LMIM operated two prominent funds. The First Mortgage Income Fund (FMIF) and the Managed Performance Fund (MPF). Sat under the FMIF were a number of feeder funds.

The FMIF including feeder funds is believed to have had in the order of AU\$350m under management by LMIM. The FMIF and feeder funds had approximately 7500 investors principally from Australia and New Zealand. An average investment per investor of AU\$46000. David Whyte of BDO, the court appointed receiver, is currently forecasting less than 14 cents in the dollar return to investors.

The MPF is believed to have had in the order of AU\$400m under management by LMIM from approximately 4500 investors. An average investment per investor of AU\$89000. Korda Mentha, the court appointed Responsible Entity, is currently forecasting returns to investors of less than 5 cents in the dollar plus anything recovered from litigation.

Both funds were sold predominantly to mature investors who were approaching or in retirement.

MPF investors were from across the world but with a heavy concentration of Middle East and South East Asian ex-patriates. Lives have been ruined. The reward for aggressively pursued careers, frequently undertaken in challenging environments, robbed in its entirety from professionals at a time in life when it's impossible to recover. The cruelest of sentences.

The magnitude of private wealth destruction and personal hardship inflicted by the LMIM debacle is tragic. One suicide and one attempted suicide has been reported and many are living a basic hand to mouth existence clouded with worry and insecurity during the final decades of lives that have earned so, so much more.

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The Question of Criminality

This entire subject is overarched by the stark, shocking fact that LM Investment Management lost over \$700m of investors money.

The overwhelming sentiment among investors, finance industry players and spectators alike, is that in a developed country with a regulatory structure touted in LM promotional material as a strong reason to invest it must be impossible for this to happen without criminal action.

There is clearly a strong fraudulent element in LMIM marketing of the MPF product.

- I. Peter Drake frequently insists that he used licensed financial advisors. This is a lie. Many were not and therefore held no professional indemnity insurance and had no connection to dispute resolution schemes.
- II. Information regarding the failed FMIF was purposely excluded from all MPF promotional material during the heavy growth period 2009 to 2013. See this [example](#).
- III. Many investors were sold this product as low risk even though the MPF was predicated on 2nd mortgage positions largely against assets already failing to provide the returns described in the FMIF prospectus.
- IV. There is [clear evidence of ponzi operation](#) as far back as 2009.
- V. There is [clear evidence of irrational asset valuation](#) and [resistance to ASIC RG45 guidelines and disclosure](#).
- VI. There is clear evidence of [auditor negligence](#).
- VII. There are very questionable foreign exchange losses.
- VIII. The simple 'where did the money go?' question (that Korda Mentha posed in their [7th report to investors](#)) has, until today, not been properly answered.

Six Enormous, Serious Crime Alerts

LMIVC would like to direct the Financial Services Inquiry to the following simple presentation of data from Korda Mentha's 7th report to MPF investors and the derivation of 6 enormous serious crime alerts.

MPF 2010 - 2012 inc. Au\$m

Year	Income (unit holder receipts)	Investment	Operating Expenses & Fees Paid
2010	60	20	32
2011	90	8	42
2012	82	48	55
Totals	232	76	129

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Alert 1. There is a \$27m discrepancy between Income and Investment + Operating Expenses & Fees Paid.

Alert 2. Operating Expenses & Fees Paid in 7 years to 2009 totaled \$15m, in 3 years to 2012 totaled approx \$130m.

Alert 3. The 'model' is flawed to the point of inevitable doom. How could Investment of 76m reward unit holders input of 232m?

Alert 4. A similar assessment made at the close of 2011 would have produced even more alarming indications.

Alert 5. This fundamental flaw was never highlighted in an auditors report.

Alert 6. A combination of the above must lead to Serious Fraud Office investigations at minimum. Were these years of premeditated white collar crime as the board realized how simply the theft could be perpetrated?

(Figures from Korda Mentha's 7th report to investors)

Administrator, Responsible Entity / Trustee, Liquidator, Receiver Costs

During the three to four month period following the announcement that LMIM were in administration there occurred what has been referred to in some quarters as a 'fight for turf'. Administration began to reveal devastating fund and asset status news. Associated costs turned bad news into an investor nightmare. A nightmare exacerbated by claims pursued through the courts, that the appointed administrators were inappropriate. The already abused funds were further eroded by what investors perceived to be a contest for fees of the work to come. Costs that in some cases were doubled as administrators or trustees were replaced after court action.

FTI billed over AU\$2m for three weeks work and were paid **AU\$1.4m**. Korda Mentha have billed **AU\$2.38m** for work and disbursements from mid April 2013 to 2nd March 2014. Korda Mentha, in their 12th update to investors on the 9th April 2014 report hampered progress toward detailed understanding of MPF operation by LMIM and potential legal recovery actions. Investigations and legal recovery actions funded by MPF resource because ASIC neglected policing of regulation and reactive investigation, one may argue.

Over a year later investors have still received nothing but continued forecasts of declining recovery.

The bleak picture for investors raises questions LMIVC wish the Inquiry to consider very seriously:

1. What incentive is there for Administrator, Responsible Entity, / Trustee groups to close the work and return funds to investors when as long as investigations continue they receive an income?
Whilst investors are encouraged by Responsible Entity statements describing the careful assessment of litigation activity cost versus potential for financial recovery, it is disconcerting to detect some actions may not be pursued due to lack of funds after the above described 'fight for turf'.
2. Should Korda Mentha be billing ASIC for this work?
It is not unreasonable to claim the work currently in hand by Administrator, Responsible Entity / Trustee groups would not be required had ASIC met the expectations set by their mandate described [here](#).
3. For essentially similar reasons (particularly if criminal activities contribute to the FMIF failure) should FTI and BDO be billing ASIC for the work towards resolving investor interests in the FMIF and associated feeder funds?

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**The Tony Abbot Government Indifference to International Responsibility and
Accountability.**

Early appeals from LMIVC to the Australian government were ignored.

At the height of their despair victims had begun to gather under the LM Investor Victim Centre (LMIVC) umbrella.

During December and January 2013/14 the LMIVC:

1. Appealed to the Australian government for recognition and support. That appeal was **ignored**.
2. Wrote to the Attorney General of Australia. That communication was **ignored**.
3. Wrote to the Treasurer of Australia, That communication was **ignored**.
4. Wrote to Senator the Hon John Williams of the ALP. That communication was **acknowledged**.

One may read the communication to these parties from [this page](#).

Amongst increasing public concern for the general performance of ASIC, the LMIVC movement took the decision to lobby for an Independent Inquiry into the affairs and collapse of LMIM and the CEO Peter Drake.

During late April, May and June 2014 approx 150 letters from LMIVC registrants were sent to Tony Abbot politely requesting a full Independent Inquiry be considered. A response was eventually received from Australian assistant treasurer and finance minister Mathias Cormann during mid August 2014. Most of the LMIVC population felt insulted by it's content which, in defence of the process to that point, put forward an IMF assessment of ASIC that was in complete contrast to the damning report to the government from the Senate Inquiry into ASIC's performance. Mathias Cormann's dismissive, uncaring and misguiding response can be accessed from [this page](#).

Arch Cru : LMIM - A Comparison

LMIVC would at this point like to direct the Financial Systems Inquiry to a comparison made between the Arch Cru collapse and the LMIM collapse in illustration of the concern over indifference displayed by the Tony Abbot government. Read it [here](#).

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ASIC

Research by LMIVC into the LMIM / ASIC interaction is presented in a time-line fashion [here](#)

LMIVC hold that there is extensive ASIC neglect amounting to dereliction of duty that must be compensated by the Australian government.

The Absence of Humane Victim Support

There is no other country with more involvement in this debacle than Australia yet Australian authorities and government politicians repeatedly suggest they hold no authority for addressing the plight of thousands of investors in or approaching retirement with little or no chance to recover a financial position that has taken them a lifetime to secure.

Australia make considerable effort to attract foreign investors but when that leads to tragic disaster for the investors the Australian government and authorities under it's control, in this case display an inhumane absence of empathy, concern and compassion.

Closing Comments, Conclusions and Recommendations

In this age of globalisation Australian authorities have performed abysmally in recognising and supporting international investors victims of what is demonstrating itself to be one of Australia's largest ever investment scandals.

Australia could still scoop this up and, with some clever maneuvering, turn this around. Every tragedy comes with an opportunity to learn and improve.

The Madoff scandal, which broke in December 2008, was a beast of greater magnitude (approaching 20 billion USD of principal) however there is one illuminating difference in approach to resolution for investors worth examining. The court appointed trustee for the recovery of investors funds stolen by Madoff, Irving Picard, and his team of lawyers at Barker Hostetler in New York have their bills paid from a trust funded by Wall Street and operated by the Securities Investor Protection Corp. (SIPC). In short investors facing losses due to fraudulent behavior are not penalized a second time by having their already ailing funds subject to unchallenged charges by trustees for the wide range of recovery activities. Five and a half years later the [Madoff Recovery Initiative](#) is reporting recoveries and settlement agreements to be at more than fifty percent of the defrauded amount.

The self regulation model appears successful. Contributions to the fund from the industry reduce as cases decline. Players watch actions and behavior across the patch carefully and observantly. If cases increase then contributions have to increase and players fight harder to identify rogues before they damage the industry further.

Australia's position in the international investments market is in the process of taking a considerable hit as a result of the LMIM debacle. Investors, investor groups and investor institutions around the world are revisiting would be opportunities against the backdrop of revelations about how successful other people, from advisors to administrators are at placing investors money in their own pockets.

The opportunity presents itself to Australia with startling clarity.

Put the investors first, you're in danger of losing many more would be investors if you don't.

Create that 'Recovery Fees Fund'.

Give it some rules and regulations. Establish its ongoing ability to survive with appropriate feeds from the finance industry. Remove the massive obstacle of recovery fees from investors at an already distressed status. Show it off by using the LMIM disaster to demonstrate that investors positions are revered, supporting the best possible chance of recovery and, at the same time,

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turning around the millions of investors, in groups or institutions or as individuals who are
shunning the opportunities in Australia because of the horrors exposed by the LMIM debacle.
