# Proposed acquisition of Suncorp Bank by ANZ

## Expert Witness Report

## Supplementary Report of Mozammel Ali

***Prepared by:*** ***Mozammel Ali***
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***Theorem Consulting Pty Ltd***

***Address:*** [redacted]

***Date:*** ***23 July 2023***

***Signed:*** [redacted]

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# Section 1 – Introduction and scope

## 1.1 Scope

1. I was engaged by Herbert Smith Freehills (**HSF**), to prepare an independent expert report, in connection with the application to the Australian Competition and Consumer Commission (**ACCC**) for authorisation of the proposed acquisition by the Australia and New Zealand Banking Group Limited (**ANZ**) of SGBH Limited, the holding company for Suncorp Bank, from Suncorp Group Limited (**SUN**), (**Proposed Acquisition**).

2. In particular, I was asked to provide my opinion in relation to the availability and cost of funding for Suncorp Bank under alternative counterfactual scenarios of Suncorp Bank remaining under SUN ownership (**Status Quo Counterfactual**) and Suncorp Bank under BEN ownership (**Alternative Buyer Counterfactual**). I was also asked to comment on the submissions by BEN about the relative stability of retail deposits compared with wholesale funding. My comments and opinions in relation to these topics are set out in my initial report dated 17 May 2023 (**Ali Report**).

3. I have since been provided with extracts from the report by Mary Starks dated 16 June 2023 (**Starks Report**) with certain redactions as well as a redacted copy of the supplementary report by Mary Starks dated 7 July 2023 (**Starks Supplementary Report**) and have been asked to comment on certain of the observations by Ms Starks as specified in the commissioning letter provided to me by HSF dated 20 July 2023 (**Supplementary Commissioning Letter**), a copy of which is included in **Appendix A**.

4. I have been provided various additional documents including certain company and other related information (**Information Materials**) which are listed within Attachment 2 of the Supplementary Commissioning Letter, which I have reviewed, considered and relied upon in preparing this Report.

## 1.2 Relevant experience and qualifications

5. My experience and qualifications are set out in Section 1.2 of the Ali Report.

6. In particular, I have over 28 years of experience within the financial services industry, including 18 years across two top tier global investment banks. I am currently Managing Director of Theorem Consulting, an independent consulting firm established in 2018, that provides consulting advice on mergers and acquisitions (**M&A**), acquisition financing, capital raisings and capital structuring.

7. Prior to establishing Theorem Consulting, from 2003 to 2018, I was a senior executive within the Corporate Finance division of Deutsche Bank AG, Sydney Branch, including roles within the Financial Institutions Group, the Capital Markets and Treasury Solutions team and most recently as the Head of Capital Solutions.

8. During my time at Deutsche Bank I was involved in dozens of regulatory capital raisings for Australian financial institutions including advising all four of the Australian major banks, SUN and BEN in connection with capital transactions. In addition to the successfully executed transactions, I have also been involved as an adviser on a vast number of potential transactions which were ultimately not completed for various commercial reasons.

9. I hold a Bachelor of Economics (with First Class Honours) from the Australian National University and qualified as a Fellow of the Actuaries Institute (Australia) in 1999, as a Fellow of the Faculty and Institute of Actuaries (UK) in 2000, and as a Graduate of the Australian Institute of Company Directors in 2017.

10. A copy of my curriculum vitae is included in Appendix B of the Ali Report.

### 1.3 Acknowledgements

11. This Report sets out my independent opinion of the matters herein which is based wholly or substantially on my specialised knowledge arising from my training, study or experience, having regard to the relevant facts relating to the matters and giving due consideration to the prevailing market circumstances.

12. I have been provided with a copy of the Federal Court of Australia Expert Evidence Practice Note (**GPN-EXPT**), including the Harmonised Expert Witness Code of Conduct, which I have read, understood and agree to be bound by. A copy of the Expert Evidence Practice Note (GPN-EXPT), including the Harmonised Expert Witness Code of Conduct, is included in **Appendix B**.

### 1.4 Limitations

13. I declare that, in forming the opinions contained in this Report, I have made all the inquiries and investigations which I believe are desirable, appropriate (other than any limitations or matters explicitly identified within this Report), and that no matters of significance which I regard as relevant or are likely to have a material impact on the opinions contained herein have, to my knowledge, been omitted from this report.

### 1.5 Definitions and capitalised terms

14. Unless otherwise defined in this Report, any defined or capitalised terms within this Report have the same meaning as defined or described in the relevant document within the Commissioning Letter or Information Materials as applicable, where such defined or capitalised terms are used.

### 1.6 Report structure

15. The questions I was asked to address in this report are set out in Section 2.

16. Section 3 contains an executive summary of my opinions.

17. My detailed observations and opinions in relation to the views expressed by Ms Starks on the funding costs and challenges for a merged BEN/Suncorp Bank entity are set out in Section 4.

18. My detailed observations and opinions in relation to the views expressed my Ms Starks on Advanced Internal Ratings Based accreditation issues which would arise for a merged BEN/Suncorp Bank entity are set out in Section 5.

# Section 2 – Questions

19. Please prepare a Supplementary Expert Report giving your opinion on:

a) *the views Ms Starks' expresses in the First Starks Report on the funding costs and challenges for a merged BEN/Suncorp Bank entity (the **alternative buyer counterfactual**) and the implications of achieving Advanced Internal Ratings Based (**IRB**) accreditation, as set out in section 7.2, paragraphs 7.15-7.59; and*

b) *the views Ms Starks' expresses in the Supplementary Starks Report on the credit rating impacts, funding challenges and IRB accreditation which would arise in the alternative buyer counterfactual. These are contained in section 6 at paragraphs 6.1-6.19, 6.30-6.44 and 6.49-6.51 (to the extent paragraphs 6.49-6.51 relate to those matters).*

# Section 3 – Executive Summary

## 3.1 Funding implications

### *3.1.1 Funding costs and challenges under the Alternative Buyer Counterfactual*

20. Ms Starks makes a number of observations in relation to my comments in the Ali Report regarding relative funding costs and the expected funding challenges for Suncorp Bank under the Alternative Buyer Counterfactual, noting in particular:
    i. that, while she agrees that funding costs are likely to be higher for a bank with a lower credit rating (as Suncorp Bank is likely to be under BEN ownership), she considers the magnitude of the funding cost increases to be relatively small compared to the potential capital release from IRB accreditation;
    ii. regarding the likelihood of significant credit market volatility or market dislocation, that the Parties' submissions suggest this is relatively low; and
    iii. in relation to my estimates that (under the Alternative Buyer Counterfactual) Suncorp Bank would likely need to [redacted]

21. Regarding the increased funding costs under the Alternative Buyer Counterfactual, Ms Starks suggests that the net funding cost impact on the merged Suncorp Bank/BEN entity is unclear (and potentially positive *if* it gets an uplift due to sovereign support). I disagree.

22. In my opinion, there would very likely be a net funding dis-synergy under the Alternative Buyer Counterfactual relative to the Proposed Transaction. [redacted]

23. Regarding the comparison between incremental funding costs and the potential benefits of IRB accreditation, I note that there are significant complexities associated with the IRB modelling required and corresponding uncertainty in achieving the potential capital benefits that Ms Starks references. Furthermore, the incremental funding costs are a direct expected consequence of the Alternative Buyer Counterfactual, whereas any potential benefits associated with IRB accreditation for the merged entity under the Alternative Buyer Counterfactual cannot be ascribed as being a consequence of the merger of Suncorp Bank and BEN.

24. Regarding Ms Starks observations about credit market volatility, I consider the likelihood of severe credit market volatility to be distinct from (and substantially greater than) the likelihood of bank failure in Australia. [redacted]

25. [redacted]

26. My detailed observations and opinions regarding the funding costs and challenges under the Alternative Buyer Counterfactual are set out in Section 4.1 below.

### *3.1.2 Funding cost advantages under the Proposed Transaction*

27. Ms Starks states that she has no reason to doubt that Suncorp Bank would face lower funding costs under the Proposed Transaction, but identifies what she considers as being three plausible reasons as to why such reduced funding costs might not represent productive efficiency gains being (i) capital composition, (ii) diversification and (iii) implicit subsidy.

28. [redacted]

29. [redacted]

30. [redacted]

31. My detailed observations and opinions regarding the funding cost advantages under the Proposed Transaction are set out in Section 4.2 below.

## 3.2 IRB accreditation

### *3.2.1 Costs and uncertainty relating to IRB accreditation*

32. Ms Starks notes that achieving IRB accreditation will result in a modest capital benefit that could be used, for example, to support additional home loans.

33. In my opinion, Ms Starks overemphasises the potential benefits of IRB accreditation and overlooks the significant costs and uncertainty associated with obtaining those benefits, which include:

    i. significant management time and effort required to develop the internal capability and to seek and obtain APRA approval for IRB accreditation;

    ii. substantial cost associated with the development of appropriately sophisticated risk management and modelling capability to achieve IRB accreditation; and

    iii. uncertainty regarding whether there would be a capital benefit by moving to IRB accreditation which is dependent on the individual bank's circumstances.

34. I note that Suncorp Bank had elected not to pursue IRB accreditatio [redacted]

### *3.2.2 IRB accreditation not a function of the merger under the Alternative Buyer Counterfactual*

35. Ms Starks inappropriately ascribes any potential benefit to a merger of BEN and Suncorp Bank. However, any potential benefits of IRB accreditation is equally achievable by Suncorp Bank or BEN independently.

36. In my opinion, there is no objective rationale for why the combined BEN/Suncorp Bank:

- would derive any incremental synergistic benefit of IRB accreditation as a merged entity rather than individually;
- would have any increased probability of success in seeking IRB accreditation relative to individually; and
- would derive any material cost saving if it were to seek IRB accreditation as a merged entity relative to individually.

37. Furthermore, given the expected multi-year post merger integration process following a BEN/Suncorp Bank merger, seeking IRB accreditation as a merged BEN/Suncorp Bank entity is likely to be more complex and time consuming than for either Suncorp Bank or BEN independently.

### *3.2.3 IRB accreditation more likely to occur under the Proposed Transaction*

38. Additionally, in my view any potential benefits of IRB accreditation are far more likely to accrue under the Proposed Transaction [redacted]

39. My detailed observations and opinions regarding issues associated with IRB accreditation are set out in Section 5 below.

# Section 4 – Funding implications

## 4.1 Funding costs and challenges under the Alternative Buyer Counterfactual

40. In the Starks Supplementary Report, Ms Starks expresses the view that the funding cost challenges will make a modest difference to BEN/Suncorp Bank's ability to compete and that although Suncorp Bank will likely face higher funding costs under BEN ownership, the net impact on the merged entity is unclear and potentially positive *if* it gets an uplift due to sovereign support.[1]

41. [redacted]

42. [redacted]

- [redacted]
- [redacted]
- [redacted]

43. [redacted]

- [redacted]
- [redacted]
- [redacted]

44. [redacted]

45. [redacted]

[1] Starks Supplementary Report (Paragraph 6.19).
[2] Ali Report (Paragraph 48).
[3] Ali Report (Paragraph 49).
[4] Ali Report (Paragraph 50).
[5] Ali Report (Paragraph 67).

[redacted]

46. [redacted]

47. Ms Starks makes a number of observations in relation to my comments in the Ali Report regarding relative funding costs and the expected funding challenges for Suncorp Bank under the Alternative Buyer Counterfactual, noting in particular:

i. that, while she agrees that funding costs are likely to be higher for a bank with a lower credit rating (as Suncorp Bank is likely to be under BEN ownership), she considers the magnitude of the funding cost increases to be relatively small compared to the potential capital release from IRB accreditation;[6]

ii. regarding the likelihood of significant credit market dislocation, that the Parties' submissions suggest this is relatively low;[7] and

iii. [redacted]

48. I address Ms Starks' observations in Sections 4.1.1 – 4.1.4 below.

### *4.1.1 Increased funding costs*

49. Ms Starks suggests that the net funding cost impact on the merged Suncorp Bank/BEN entity is unclear (and potentially positive *if* it gets an uplift due to sovereign support). In particular, she states that, *"if BEN/Suncorp Bank receives a one or two-notch credit rating uplift relative to BEN's current credit rating, the net result on funding costs for the merged entity as a whole is unclear"*.[8] I disagree.

50. [redacted]

51. [redacted] I also note that BEN had total long-term wholesale funding of approximately $7.9 billion (as at 30 June 2022)[9] which is less than that of Suncorp Bank which had approximately $9.2 billion of long-term wholesale funding (as at 30 June 2022).[10]

52. [redacted]

[6] Starks Supplementary Report (Paragraphs 6.13 and 6.14).
[7] Starks Supplementary Report (Paragraph 6.16).
[8] Starks Supplementary Report (Paragraphs 6.51).
[9] Comprising approximately $3.1 billion of medium-term notes and $4.7 billion of term funding facilities (BEN FY22 Annual Report, Note 15).
[10] Comprising approximately $5.1 billion of long-term borrowings and $4.1 billion of term funding facilities (SUN FY22 Annual Report, Note 14).

53. Furthermore, as Ms Stark acknowledges, even if the merged Suncorp Bank/BEN were to receive a one or two notch rating uplift, the merged entity is still likely to have a lower rating than the existing ratings of SUN (which benefits from a ratings uplift due to group support).

54. [redacted]

### 4.1.2 *Funding costs versus potential capital benefits of IRB accreditation*

55. Although certain parts of the Starks Supplementary Report that I was provided are redacted, I note that Ms Starks appears to compare the detailed estimates of the expected increase in funding costs (as shown in the Ali Report) with the relatively uncertain potential capital benefits of IRB accreditation.[11]

56. However, as described in Section 5.2 below and in the Statement of Clive van Horen dated 14 July 2023, there are significant complexities associated with the IRB modelling required and corresponding uncertainty in achieving the potential capital benefits that Ms Starks references.[12] Indeed, in relation to the potential capital benefits of IRB accreditation for BEN, Ms Starks states that she, *"cannot estimate the precise quantum of this benefit with any degree of confidence"*.[13]

57. Furthermore, the [redacted] (as shown the in the Ali Report) are a direct expected consequence of the Alternative Buyer Counterfactual relative to the proposed transaction. However, as described in Section 5.3 below, IRB accreditation for the merged entity under the Alternative Buyer Counterfactual cannot be ascribed as being a consequence of the merger of Suncorp Bank and BEN, because either of Suncorp Bank or BEN could seek IRB accreditation individually and there is no objective reason for why IRB accreditation is more likely to result from the merger of Suncorp Bank and BEN.

### 4.1.3 *Likelihood of credit market dislocation*

58. [redacted]

59. Ms Starks appears to dismiss the significance of this risk stating that, *"the Parties' submissions suggest this is relatively low in Australia"*,[15] noting comments by Suncorp Bank regarding the strength of Australia's banking system and the potential for bank failures in Australia being relatively low.

60. In making this observation, Ms Starks appears to draw an equivalence between (i) the strength of Australia's banking system and the confidence of investors and depositors have in its resilience, and (ii) the likelihood of severe credit market volatility and potential for market dislocation. Ms Starks seems to imply that, because the Australian banking

[11] Starks Supplementary Report (Paragraphs 6.14).
[12] Statement of Clive van Horen, dated 14 July 2023 (Paragraph 26).
[13] Starks Supplementary Report (Paragraphs 6.38).
[14] Ali Report (Paragraph 48).
[15] Starks Supplementary Report (Paragraphs 6.16).

system is relatively very robust with low potential for bank failures, there is similarly low likelihood of severe credit market volatility in Australia. I disagree.

61. In my opinion, there is far greater potential for severe credit market volatility and market dislocation than the potential for bank failures in Australia.

62. The depth, liquidity and relatively seamless flow of capital across the international debt capital markets in part contributes to a high degree of correlation in credit market conditions across all major credit markets globally. Two patent examples of this are:

- the global financial crisis, during which there were no bank collapses in Australia however credit markets in Australia were severely dislocated consistent with credit market conditions globally; and
- the onset of the COVID-19 pandemic, which resulted in severe volatility in Australian credit markets in early 2020 consistent with global credit market volatility, albeit there were no bank failures.

63. The significance of the likelihood of severe credit market volatility and market dislocation is underscored by regulatory liquidity requirements (such as the LCR and NSFR requirements[16]) which are designed to promote liquidity resilience. These regulatory requirements were introduced under Basel (and by APRA) precisely to address the potential that banks may face liquidity constraints arising from such market volatility.

64. In summary, I consider the likelihood of severe credit market volatility to be distinct from (and substantially greater than) the likelihood of bank failure in Australia. [redacted]

### *4.1.4 Replacement of short-term funding*

65. [redacted]

66. [redacted]

67. [redacted]

68. [redacted]

[16] Refer Ali Report (Paragraphs 206 and 244 – 247).
[17] Ali Report (Paragraph 67).
[18] Ali Report (Paragraph 220).

## 4.2 Funding cost advantages under the Proposed Transaction

69. In the Starks Report, Ms Starks states that she has no reason to doubt that Suncorp Bank would face lower funding costs under the Proposed Transaction, but identifies what she considers as being three plausible reasons as to why such reduced funding costs might not represent productive efficiency gains, namely:[19]

i. **capital composition** – if, for example, ANZ is better capitalised due to facing higher regulatory capital requirements, then it may face a lower cost of debt, but not a lower overall cost of capital;

ii. **diversification** - if ANZ's assets are more diversified, this may mean there is less risk to those providing wholesale debt funding, but not lower overall expected losses; and

iii. **implicit subsidy** – if ANZ is judged to be "too big to fail", then investors might perceive a higher likelihood of government support in the event of significant stress.

70. Ms Starks reiterates these in the Starks Supplementary Report and, having also considered plausible drivers of ANZ's wholesale funding cost advantage that would constitute productive efficiency benefits, concludes that, *"it is likely that some, and potentially a significant proportion, of any wholesale funding cost advantage that ANZ enjoys may be due to factors that do not constitute productive efficiency benefits".*[20]

71. I address each of Ms Starks' three reasons as to why the reduced funding costs might not represent productive efficiency gains in Sections 4.2.1 – 4.2.3 below.

### *4.2.1 Capital composition*

72. Ms Starks notes that, for productive efficiency gains, what matters is overall cost of capital rather than cost of debt. She notes that, if one of the reasons that ANZ has lower funding costs than Suncorp Bank is that it is better capitalised, then benefits from a lower funding cost might not result in a lower overall cost of capital.[21] However, Ms Starks provides no evidence that under the Proposed Transaction Suncorp Bank would have a higher capital composition than it currently does.

73. Under the Proposed Transaction, Suncorp Bank would become part of ANZ and any possibility that it may be required to hold higher levels of capital would be due to the D-SIB regulatory capital requirements applicable to ANZ. However, following integration of Suncorp Bank's asset book into ANZ, Suncorp Bank would likely also have the benefit of IRB accreditation together with ANZ's risk management and modelling capabilities as an Advanced IRB accredited bank.

74. Suncorp Bank's most up-to-date modelling and analysis of the capital impact of IRB accreditation indicated that estimated additional day-1 capital requirement would be [redacted], under the revised APRA capital standards.[22]

75. [redacted]

76. [redacted]

[19] Starks Report (Paragraphs 10.32).
[20] Starks Supplementary Report (Paragraphs 3.14).
[21] Starks Report (Paragraphs 10.32.1).
[22] [redacted]

[redacted]

77. I note that ANZ is subject to an incremental D-SIB capital buffer of 1.0%. [redacted][23]

78. APRA also maintains that there should exist a capital incentive for banks to invest in the advanced modelling capabilities required for IRB accreditation. APRA has estimated that the average pricing differential for residential mortgage loans due to differences in IRB and standardised capital requirements is 0.05 per cent which is a modest benefit.

79. In summary, I consider it more likely that IRB accreditation under Proposed Transaction would potentially yield capital benefits for Suncorp Bank than under the Alternate Buyer Counterfactual, in which case there would be no defrayal of the funding cost benefit enjoyed by Suncorp Bank due to increased capital requirements.

### *4.2.2 Diversification*

80. In the Starks Report, Ms Starks contends that, because ANZ is a larger bank with a more diversified portfolio of assets than Suncorp Bank:[24]

- investors may perceive that there is less correlated risk in ANZ's assets compared to those of Suncorp Bank;
- that this implies greater tail risk with respect to Suncorp Bank's asset book relative to ANZ's;
- this would mean that by merging the asset books the risk of losses with respect to Suncorp Bank's asset portfolio is reduced;
- although overall expected losses on the combined loan book does not change, the risk of losses to senior debt holders does (because the distribution of outcomes is changed), and

therefore, interest paid on senior debt may reduce but this does not necessarily translate to a reduced risk on individual loans or the ability to price those loans at a lower rate.

81. Ms Starks' observations regarding diversification appear to overlook the fact that (under the Proposed Acquisition) Suncorp Bank would become part of ANZ and would be utilising ANZ's IRB approach for determining its regulatory capital requirements.

82. Under the IRB approach, risk weighted assets and the corresponding capital requirements with respect to credit risk is determined using approved IRB models which are based on a specified probability of sufficiency (i.e. a specified confidence level, which is set at 99.9% over a one year horizon).[25]

83. Therefore (under the Proposed Transaction) to the extent that one asset book had a greater tail risk than the other, the corresponding RWA (and capital requirements) in respect of those assets would be set higher such that the probability of sufficiency

[23] [redacted]

[24] Starks Report (Paragraph 10.32.2).

[25] APRA Prudential Standard APS113 Capital Adequacy: Internal Ratings-based Approach to Credit Risk (Attachment A).

remained at the prespecified level of 99.9%. [redacted]

84. More importantly, to the extent that Suncorp Bank's asset book was uncorrelated (or not perfectly correlated) with ANZ's asset book, the combined asset book would benefit from greater diversification. [redacted]

85. [redacted]

### *4.2.3 Implicit subsidy*

86. In the Starks Report Ms Starks makes the observations that:[26]

- because ANZ is a domestic systemically important bank (**D-SIB**), it may benefit from an implicit subsidy in terms of the cost of its debt; and
- if Suncorp Bank does not benefit from such an implicit subsidy, or benefits from a smaller one, then (at least some of) the reduction in its funding costs arising from the merger with ANZ constitute a transfer of risk from the private sector to the tax payer.

87. However, I would note that (i) as a D-SIB, ANZ is subject to additional D-SIB capital buffer requirements under the new APRA capital standards, and (ii) ANZ is also subject to the major bank levy.

88. To the extent that either:

- the additional D-SIB capital requirements offset any systemic risk arising from the implicit subsidy referred to by Ms Stark; or
- some part of the Major Bank Levy contributes towards offsetting the expected cost associated with such implicit subsidy,

the public cost associated with such an implicit subsidy would be correspondingly mitigated.

89. The view that some part of the Major Bank Levy contributes towards offsetting the expected cost of any such implicit subsidy, is consistent with the Australian Government stated policy objectives of the Major Bank Levy which include, *"ensuring that the banking sector makes a fair contribution to the economy given its unique role in Australia's economy and the associated systemic risks that it imposes"*.[27]

90. Furthermore, the view that the additional D-SIB capital requirements contribute towards reducing the incremental risk that D-SIB's pose to the financial system is consistent with APRA's policy intent as noted in its letter to the ACCC (dated 13 July 2023), where it states in relation to the additional D-SIB capital requirements that, *"APRA's intent and*

[26] Starks Report (Paragraph 10.32.3).

[27] https://www.aph.gov.au/About_Parliament/Parliamentary_departments/Parliamentary_Library/FlagPost/2017/June/The_Major_Bank_Levy_explained.

*best judgment is that the new capital framework which commenced January 2023, as well as the LAC requirements, are appropriately calibrated for the risks they are intended to capture".*[28]

91. Under the Proposed Transaction Suncorp Bank would become part of ANZ and accordingly, Suncorp Bank would also be subject to (i) a corresponding D-SIB related additional capital buffer requirement, and (ii) a corresponding Major Bank Levy. [redacted]

92. In my view, Ms Starks over emphasises the public cost of any such implicit subsidy in her observations and I would suggest that any transfer of risk (as referenced by Ms Starks) is substantially mitigated by the increased D-SIB related capital requirements and Major Bank Levy that would apply to Suncorp Bank. [redacted]

[28] APRA letter to the ACCC, 13 July 2023.

# Section 5 – IRB Accreditation

## 5.1 Implications of Advanced IRB accreditation

93. Ms Starks identifies three impacts on the dollar amount of regulatory capital that the combined BEN/Suncorp Bank would be required to hold, in the event that the combined entity were to receive IRB accreditation, being:[29]

    i. change in credit risk RWAs;

    ii. capital requirements for Interest Rate Risk in the Banking Book (**IRRBB**); and

    iii. higher minimum capital requirements for IRB accredited banks.

94. In relation to the change in credit risk RWAs, Ms Starks notes that it would not be possible for her to precisely estimate the credit RWAs for the combined entity, even if she had perfect visibility over its loan book.[30] She also makes the observation that new models may need to be built (either for the standalone Suncorp Bank credit portfolio or the combined loan book) in order for the combined entity to seek IRB accreditation.

95. Notwithstanding the limitations in estimating the impact of credit RWA impacts, Ms Starks uses APRA data and individual bank disclosures to estimate the magnitude of changes in risk weights that the combined BEN/Suncorp Bank entity may face, were it to receive IRB accreditation. Some parts of the Starks Report that I received were redacted, however based on my review of the unredacted parts of the Starks Report that were made available to me, Ms Starks appears to imply that:

    - the combined BEN/Suncorp Bank entity may see a substantial reduction in RWAs for home loans;
    - there is no strong evidence for Ms Starks to conclude that a move from standardised to IRB accreditation would result in substantially different average RWAs for SME lending; and
    - there is insufficient data granularity to make a comparison of RWAs between standardised and IRB banks for agribusiness lending.

96. In relation to IRRBB capital requirements, Ms Starks observes that the precise increase in RWAs in respect of IRRBB for the combined BEN/Suncorp Bank entity is difficult to estimate, however she identifies the midpoint of the range of IRRBB RWA impost for the big four banks as comprising approximately 6 – 7% of credit RWAs.

97. In relation to increased capital requirements, Ms Starks notes that under the revisions to APRA's prudential standards (effective 1 January 2023), IRB accredited banks are subject to a minimum CET1 ratio requirement of 9.25% as opposed to 8.0% for banks under standardised approach (which represents approximately 15.6% increase in the minimum capital requirement).

98. I also note that most banks generally operate with a buffer above the minimum capital requirements and may seek to maintain the same proportional target buffer above minimum capital requirements. In that case, a move from standardised to IRB accredited would result in an approximately 15.6% increase in the target capital ratio (and not just an increase in the minimum capital requirement).

99. Although Ms Starks' conclusions regarding the net impact of IRB accreditation are redacted in the version of the Starks Report that was provided to me, I note Ms Starks' observation that, *"it is difficult to reach a precise estimate of the net change in overall*

[29] Starks Report (Paragraph 7.23).
[30] Starks Report (Paragraph 7.24).

*dollar capital requirements from IRB accreditation for the merged entity".*[31] However, Ms Starks notes that according to BEN's internal preliminary analysis, achieving IRB accreditation will result in a modest capital benefit that could be used, for example, to support additional home loans.[32]

100. Beyond the one-off impact of achieving IRB accreditation status, Ms Starks identifies two further potential benefits of IRB accreditation, being:

i. reduced capital strain in respect of each marginal new home loan;[33] and

ii. the potential for IRB accreditation to enable the merged BEN/Suncorp Bank entity to compete more effectively by aligning incentives for it to price new lending in line with the underlying risk.[34]

## 5.2 Costs and uncertainty relating to IRB accreditation

101. In relation to the potential benefits of IRB accreditation, I would observe that there is substantial management time and cost involved in the process of seeking IRB accreditation and significant uncertainty regarding whether the potential benefits would accrue. In particular, I note that:

i. there is significant management time and effort required to develop the internal capability and to seek and obtain APRA approval for IRB accreditation;

ii. there is substantial cost associated with the development of appropriately sophisticated risk management and modelling capability to achieve IRB accreditation;

iii. the ability to achieve a capital benefit by moving to IRB accreditation is uncertain and dependant on the individual bank's circumstances; and

iv. Suncorp Bank had elected not to pursue IRB accreditation, [redacted]

102. I address each of these aspects in Sections 5.2.1 to 5.2.4 below.

### *5.2.1 Significant time requirement in obtaining IRB accreditation*

103. In the Starks Report, Ms Starks notes her understanding (based on the APRA Service Charter) that if a combined BEN/Suncorp Bank applied for IRB accreditation, it would be conferred within 9 months of APRA receiving a substantially complete application.[35]

104. However, I note that APRA determines an application to be substantially complete only after *"an applicant has demonstrated it has sufficient financial and non-financial resources and has submitted all of the expected supporting material, which is of sufficient quality and detail to allow APRA to complete its assessment".*[36]

105. Ms Starks characterisation of APRA conferral within 9 months doesn't acknowledge the significant management time and effort required to develop the risk management and modelling capability for a bank to be in a position to submit a substantially complete application.

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[31] Starks Report (Paragraph 7.41).
[32] Starks Report (Paragraph 7.41).
[33] Starks Report (Paragraph 7.43).
[34] Starks Report (Paragraph 7.44).
[35] Starks Report (Paragraph 7.15).
[36] APRA Service Charter (https://www.apra.gov.au/apra-service-charter).

106. Suncorp Management estimated (in an internal paper prepared for the Group ALCO, dated 22 November 2021) that preparation for IRB accreditation and APRA approval typically takes [redacted][7].

107. [redacted]

However, the [redacted] preparation time together with a 9 month APRA approval time frame (plus contingency allowance of [redacted] for additional queries from APRA and preparation of corresponding responses) would indicate an aggregate time frame in excess of [redacted] for IRB accreditation.

108. I consider a [redacted] time frame to be more realistic and consistent with my expectations based on my experience and interactions advising APRA regulated clients. However, I would expect this [redacted] IRB development and approval timeframe would be a best case assuming that the IRB model development workstream were commenced immediately following the merger (and therefore excludes any allowance for the anticipated multi-year merger integration workstreams and the associated resourcing constraints and distraction to management attention and focus that would likely arise).

109. Furthermore, there is no certainty that IRB status would indeed be conferred within 9 months of submission of a substantially complete application as APRA may find that the application is not satisfactory for approval.

### *5.2.2 Substantial cost associated with development of IRB capability*

110. There is substantial cost associated with the development of appropriate risk management and modelling capability in order to achieve IRB accreditation, including in respect of:

- resourcing;
- development of systems capability;
- data capture and analysis;
- model development, validation and back testing;
- model refinement and recalibration;
- ongoing data capture and monitoring of output for continuous improvement and recalibration; and
- internal education and management/board approvals processes.

111. Suncorp estimated that it had already invested approximately [redacted] in pursuing IRB accreditation and estimated that a further c. [redacted] additional investment would be required. This estimated total of [redacted] is broadly consistent with my expectation of up to [redacted] investment requirement (depending on the size and complexity of the individual bank's circumstances).

### *5.2.3 Uncertainty of capital benefit*

112. [redacted]

[37] [redacted]

[redacted]

113. [redacted]

114. [redacted]

115. [redacted]

116. Ms Starks acknowledges APRA's recommendation that ADI's should avoid designing models with "excessive procyclicality" and notes that there is no clear requirement on the extent of cyclicality that APRA would deem to be appropriate. Notwithstanding the APRA recommendation to avoid excessive procyclicality, Ms Starks suggests that Suncorp developed its models with insufficient procyclicality, putting it out of line with industry peers.[40]

117. One implication of incorporating greater procyclicality in IRB credit risk models is that it increases volatility of model output under stress conditions (i.e. increased procyclicality increases volatility of capital requirements and results in higher capital requirements during stress periods).

118. I would make the observation that all of the six Australian banks that have IRB accreditation are substantially larger than Suncorp Bank (or a merged BEN/Suncorp Bank entity), when one considers the broader group that each of those banks are part of.

119. For example, ANZ (the smallest of the four major banks) has a market capitalisation of over 7 times the implied value of the merged BEN/Suncorp Bank. Similarly, Macquarie Group (MQG) and ING Group (the Dutch parent company of ING Bank Australia) each have a market capitalisation in excess of 7 times the size of the combined BEN/Suncorp Bank.[41]

120. These existing IRB accredited banks may be in a position to incorporate greater procyclicality in their credit risk models due (in part) to the ability for their respective broader group wide businesses to absorb any increased credit risk volatility (and resulting volatility in capital requirements) under stress conditions, due to their greater scale and business diversification. For example, the four major banks have far greater scale and diversity within their lending books. Macquarie has significant geographical diversity including non-bank components within the group (such as its securities and asset management businesses) that are not necessarily correlated with its banking business. ING Bank Australia is part of major multi-national group with a substantial geographically diverse lending portfolio.

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38 [redacted]

39

40 Starks Supplementary Report (Paragraph 6.35).

41 Assuming implied value of the combined BEN/Suncorp Bank of approximately $10.1 billion, based on BEN market capitalisation of $5.2 billion (as at 19 July 2023) and the announced acquisition price for Suncorp Bank under the Proposed Transaction of $4.9 billion. ANZ market capitalisation of $76.9 billion, MQG market capitalisation of $71.8 billion and ING Group market capitalisation of EUR47.5 billion and EUR/AUD exchange rate of 1.65 (all as at 19 July 2023).

121. [redacted]

122. In summary, the sophisticated risk modelling required for IRB accreditation is complex and inherently dependent on each individual bank's circumstances and it is not possible to conclude from an external desktop review that [redacted]

***5.2.4*** [redacted]

123. Ms Starks identifies one of the key benefits of IRB accreditation as being the ability to compete more effectively by aligning incentives for it to price new lending in line with the underlying risk.

124. [redacted]

125. [redacted]

126. If Ms Starks' observations that:

- there are significant potential benefits to IRB accreditation;
- these benefits considerably outweigh (for example) the funding cost dis-synergies resulting under the Alternative Buyer Counterfactual; and
- [redacted]

[redacted]

## 5.3 IRB accreditation not a function of merger with BEN

127. [redacted] Accordingly, the potential benefits of IRB accreditation would accrue to Suncorp, independent of any such merger.

128. Similarly, BEN could also pursue IRB accreditation and derive the potential benefits thereof independent of any merger with Suncorp Bank. Therefore, any potential benefits of IRB accreditation can be derived independently of the Alternative Buyer Counterfactual and should not be ascribed to the merger of BEN and Suncorp.

129. Relevantly, there is no minimum size requirement for a bank to seek IRB accreditation (so long as the bank can model its risks to an acceptable standard), albeit APRA acknowledges that IRB accreditation may not be cost-effective for some smaller banks

[redacted]

given their lack of scale and diversification. However, APRA has been considering ways to modify its IRB accreditation process with a view to making it easier for ADIs to achieve accreditation without weakening the overall standards that accreditation requires.

130. This is underscored by the fact that in December 2015, following the Financial System Inquiry (**FSI**) recommendations to make the IRB accreditation process less resource intensive, APRA announced changes to the IRB accreditation process to facilitate a staged IRB accreditation process and decouple operational risk modelling from IRB accreditation.[43]

131. In my opinion, there is no objective rationale for why the combined BEN/Suncorp Bank:

- would derive any incremental synergistic benefit of IRB accreditation as a merged entity rather than individually [redacted]
- would have any increased probability of success in seeking IRB accreditation relative to individuall [redacted] and
- would derive any material cost saving if it were to seek IRB accreditation as a merged entity relative to individually [redacted].

132. Indeed, due to the expected multi-year post merger integration following a BEN/Suncorp Bank merger, seeking IRB accreditation as a merged BEN/Suncorp Bank entity is likely to be more complex and time consuming than either:

- Suncorp Bank on its own [redacted] or
- BEN on its own – given the complexity associated with merging the two loan books and systems platforms [redacted].

### 5.4 IRB benefits more likely to accrue under the Proposed Transaction

133. In contrast to the Alternative Buyer Counterfactual, under the Proposed Transaction, Suncorp Bank would effectively inherit ANZ's existing IRB accreditation and benefit from:

- ANZ's existing approved IRB risk management systems and modelling [redacted];
- the diversification benefits of merging the Suncorp Bank loan book with the much larger and [redacted] ANZ loan book; and
- the greater procyclicality inherent in ANZ's risk modelling [redacted]

134. Therefore, the potential benefits of IRB accreditation referenced by Ms Stark, are far more likely to accrue under the Proposed Transaction than under the Status Quo Counterfactual or Alternative Buyer Counterfactual.

[43] APRA Letter to ADIs re Internal Ratings Based (IRB) Approach to Credit Risk: Accreditation Process, 16 December 2015.

# Appendices

# Appendix A – Supplementary Commissioning Letter

HERBERT SMITH FREEHILLS

Mr Moz Ali
Managing Director
Theorem Consulting Pty Ltd
[redacted]

20 July 2023
Matter 82730813
By Email

Dear Mr Ali

**Expert retainer letter - ANZ proposed acquisition of Suncorp Bank (Proposed Acquisition)**

## 1 Introduction

We refer to our letter of instructions dated 16 May 2023.

We previously sought your expert opinion, in the form of a written report, in connection with Suncorp Group Limited's (**Suncorp Group**) response to Bendigo and Adelaide Bank's (**BEN**) submission to the ACCC dated 3 March 2023.

As part of the ACCC's consideration of the Authorisation Application dated 2 December 2022, the ACCC has commissioned expert reports from Mary Starks, Partner at Flint Global. Ms Starks has prepared two reports, dated 16 June 2023 (**First Starks Report**) and 7 July 2023 (**Supplementary Starks Report**).

In the First Starks Report, Ms Starks does not consider the further evidence and submissions by ANZ and Suncorp Group in response to the ACCC's Statement of Preliminary Views dated 4 April 2023.

In the Supplementary Starks Report, Ms Starks considers the further evidence and submissions by ANZ and Suncorp Group in response to the ACCC's Statement of Preliminary Views, as well as material received from third parties. The Supplementary Starks Report references your expert report dated 17 May 2023.

As part of the ACCC's consideration of the Authorisation Application, the ACCC has also requested information from the Australian Prudential Regulation Authority (**APRA**) regarding capital requirements. APRA responded to the ACCC's questions on 13 July 2023 (**APRA Letter**).

The ACCC has published the First Starks Report, Supplementary Starks Report and APRA Letter on the public register.

The purpose of this letter is to confirm your instructions to prepare a supplementary expert report (**Supplementary Expert Report**) in this matter.

## 2 Your instructions

You are asked to prepare a Supplementary Expert Report giving your opinion on:

(a) the views Ms Starks' expresses in the First Starks Report on the funding costs and challenges for a merged BEN/Suncorp Bank entity (**the alternative buyer counterfactual**) and the implications of achieving Advanced Internal Ratings Based (**A-IRB**) accreditation, as set out in section 7.2, paragraphs 7.15-7.59; and

(b) the views Ms Starks' expresses in the Supplementary Starks Report on the credit rating impacts, funding challenges and IRB accreditation which would



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arise in the alternative buyer counterfactual. These are contained in section 6 at paragraphs 6.1-6.19, 6.30-6.44 and 6.49-6.51 (to the extent paragraphs 6.49-6.51 relate to those matters).

## 3 Documents and assumptions provided to you

For the purposes of preparing your Supplementary Expert Report, we have provided you with copies of the documents descr bed in and enclosed with Attachment 2 to this letter. The documents at Tabs 1, 4 and 5 are confidential to Suncorp Group and are marked as such in Attachment 2. The documents at Tabs 2 and 3 contain information which is confidential to Suncorp Group, [redacted] as marked. The information confidential to [redacted] has been provided to you pursuant to confidentiality undertakings you signed on 7 July 2023.

For the purposes of preparing your opinion, you are asked to make the following assumptions:

(a) the market capitalisation of BEN as at 19 July 2023 was $5.24 billion;

(b) the market capitalisation of ANZ as at 19 July 2023 was $76.92 billion

(c) the market capitalisation of Macquarie Group Limited as at 19 July 2023 was $71.8 billion

(d) the market capitalisation of ING Group as at 19 July 2023 was euro 47.49 billion and the EUR/AUD exchange rate as at 19 July 2023 was 1.65.

A short guide for the preparation of your expert report is included at Attachment 2 to our letter of instructions dated 16 May 2023.

## 4 Expert witness code of conduct

Your Expert Supplementary Report may be submitted to the ACCC as part of the Authorisation Application and may be made available to the Australian Competition Tribunal and Federal Court of Australia in any subsequent reviews and appeals of the ACCC's determination.

Your retainer is governed by the Federal Court's Expert Evidence Practice Note (GPN-EXPT) (**Practice Note**). A copy of the Harmonised Expert Witness Code of Conduct (Annexure A to the Practice Note) is attached as Attachment 1 to this letter (**Code**). You should fulfil the duties and responsibilities set out in the Code in undertaking your work and preparing for the presentation of evidence that you may ultimately be required to give.

## 5 Confidentiality

Your independent expert report and any drafts prepared in accordance with your retainer are confidential and are not to be copied or used for any purpose unrelated to the Proposed Acquisition without our permission.

Material supplied to you by Herbert Smith Freehills is confidential and is not to be copied or used for any purpose unrelated to your retainer without our permission. As appropriate, you must:

(a) keep all Suncorp Bank and Suncorp Group documents and information you receive secret and confidential at all times, unless those documents or information are publicly available (**Suncorp Confidential Information**);

(b) only use Suncorp Confidential Information for the purposes of your expert report;

(c) as required, only disclose Suncorp Confidential Information in a form that is aggregated and does not disclose the granular detail;

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(d) ensure that your report is clearly marked confidential;

(e) not disclose, directly or indirectly, any Suncorp Confidential Information to any person other than Herbert Smith Freehills, unless you have prior consent from Herbert Smith Freehills;

(f) not use the Suncorp Confidential Information other than for the purpose of carrying out your engagement in accordance with Herbert Smith Freehills' instructions;

(g) only disclose Suncorp Confidential Information to your employees or contractors who need to know the same for the purposes of your engagement and with the prior written permission of Herbert Smith Freehills, and ensure that each such person makes the same acknowledgement, agrees to comply with, your confidentiality undertaking; and

(h) if required, return all documents, copies and workings at the conclusion or termination of your retainer.

To the extent your Supplementary Expert Report refers to information set out in any of the documents enclosed with Attachment 2 which are marked as confidential, please:

(a) include the words **"RESTRICTION OF PUBLICATION CLAIMED"** in the header of each page of your report; and

(b) highlight any information confidential to Suncorp Group in green and any information confidential to third parties in pink. We may provide you with further instructions as to the specific material in your expert report that should be highlighted confidential, once prepared.

## 6 Communications

All communications, whether verbal or written, should be directed to Linda Evans or Stephanie Panayi.

Yours sincerely

[redacted]

**Linda Evans**
Partner
Herbert Smith Freehills

[redacted]

[redacted]

**Stephanie Panayi**
Partner
Herbert Smith Freehills

[redacted]

HERBERT SMITH FREEHILLS

# Attachment 1

## Harmonised Expert Witness Code of Conduct Federal Court of Australia

**Application of Code**

1 This Code of Conduct applies to any expert witness engaged or appointed:

(a) to provide an expert's report for use as evidence in proceedings or proposed proceedings; or

(b) to give opinion evidence in proceedings or proposed proceedings.

**General Duties to the Court**

2 An expert witness is not an advocate for a party and has a paramount duty, overriding any duty to the party to the proceedings or other person retaining the expert witness, to assist the Court impartially on matters relevant to the area of expertise of the witness.

**Content of Report**

3 Every report prepared by an expert witness for use in Court shall clearly state the opinion or opinions of the expert and shall state, specify or provide:

(a) the name and address of the expert;

(b) an acknowledgement that the expert has read this code and agrees to be bound by it;

(c) the qualifications of the expert to prepare the report;

(d) the assumptions and material facts on which each opinion expressed in the report is based [a letter of instructions may be annexed];

(e) the reasons for and any literature or other materials utilised in support of such opinion;

(f) (if applicable) that a particular question, issue or matter falls outside the expert's field of expertise;

(g) any examinations, tests or other investigations on which the expert has relied, identifying the person who carried them out and that person's qualifications;

(h) the extent to which any opinion which the expert has expressed involves the acceptance of another person's opinion, the identification of that other person and the opinion expressed by that other person;

(i) a declaration that the expert has made all the inquiries which the expert believes are desirable and appropriate (save for any matters identified explicitly in the report), and that no matters of significance which the expert regards as relevant have, to the knowledge of the expert, been withheld from the Court;

(j) any qualifications on an opinion expressed in the report without which the report is or may be incomplete or inaccurate;

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(k) whether any opinion expressed in the report is not a concluded opinion because of insufficient research or insufficient data or for any other reason; and

(l) where the report is lengthy or complex, a brief summary of the report at the beginning of the report.

**Supplementary Report Following Change of Opinion**

4 Where an expert witness has provided to a party (or that party's legal representative) a report for use in Court, and the expert thereafter changes his or her opinion on a material matter, the expert shall forthwith provide to the party (or that party's legal representative) a supplementary report which shall state, specify or provide the information referred to in paragraphs (a), (d), (e), (g), (h), (i), (j), (k) and (l) of clause 3 of this code and, if applicable, paragraph (f) of that clause.

5 In any subsequent report (whether prepared in accordance with clause 4 or not) the expert may refer to material contained in the earlier report without repeating it.

**Duty to Comply with the Court's Directions**

6 If directed to do so by the Court, an expert witness shall:

(a) confer with any other expert witness;

(b) provide the Court with a joint-report specifying (as the case requires) matters agreed and matters not agreed and the reasons for the experts not agreeing; and

(c) abide in a timely way by any direction of the Court.

**Conference of Experts**

7 Each expert witness shall:

(a) exercise his or her independent judgment in relation to every conference in which the expert participates pursuant to a direction of the Court and in relation to each report thereafter provided, and shall not act on any instruction or request to withhold or avoid agreement; and

(b) endeavour to reach agreement with the other expert witness (or witnesses) on any issue in dispute between them, or failing agreement, endeavour to identify and clarify the basis of disagreement on the issues which are in dispute.

HERBERT SMITH FREEHILLS

# Attachment 2

## Index

| Tab | Document | Date |
|---|---|---|
| 1 | Witness statement of Clive van Horen (confidential version), including the documents contained in Confidential Exhibit CVH-5 | 14 July 2023 |
| 2 | Supplementary expert report prepared by M Starks (Supplementary Starks Report) with Suncorp Group's confidential information unredacted | 7 July 2023 |
| 3 | Expert report prepared by Ms Starks (First Starks Report) with Suncorp's confidential information unredacted as well as the following material referred to the First Starks Report: [redacted] | 16 June 2023 |
| 4 | ACCC's request for information dated 11 May 2023 and Suncorp's confidential response, which comprises:<br>• a confidential written response; [redacted] | 11 and 19 May 2023 |
| 5 | S&P ratings report for Macquarie Bank Limited | 14 December 2022 |
| 6 | Confidential screenshots from Bloomberg of the market capitalisa ion of ANZ, Bendigo and Adelaide Bank, Macquarie Group Limited and ING Group | 19 July 2023 |

FEDERAL COURT OF AUSTRALIA

# Appendix B
# Expert Evidence Practice Note (GPN-EXPT)

General Practice Note

## 1. INTRODUCTION

1.1 This practice note, including the *Harmonised Expert Witness Code of Conduct* ("**Code**") (see **Annexure A**) and the *Concurrent Expert Evidence Guidelines* ("**Concurrent Evidence Guidelines**") (see **Annexure B**), applies to any proceeding involving the use of expert evidence and must be read together with:

(a) the Central Practice Note (CPN-1), which sets out the fundamental principles concerning the National Court Framework ("**NCF**") of the Federal Court and key principles of case management procedure;

(b) the Federal Court of Australia Act 1976 (Cth) ("**Federal Court Act**");

(c) the *Evidence Act 1995* (Cth) ("**Evidence Act**"), including Part 3.3 of the Evidence Act;

(d) Part 23 of the *Federal Court Rules 2011* (Cth) ("**Federal Court Rules**"); and

(e) where applicable, the Survey Evidence Practice Note (GPN-SURV).

1.2 This practice note takes effect from the date it is issued and, to the extent practicable, applies to proceedings whether filed before, or after, the date of issuing.

## 2. APPROACH TO EXPERT EVIDENCE

2.1 An expert witness may be retained to give opinion evidence in the proceeding, or, in certain circumstances, to express an opinion that may be relied upon in alternative dispute resolution procedures such as mediation or a conference of experts. In some circumstances an expert may be appointed as an independent adviser to the Court.

2.2 The purpose of the use of expert evidence in proceedings, often in relation to complex subject matter, is for the Court to receive the benefit of the objective and impartial assessment of an issue from a witness with specialised knowledge (based on training, study or experience - see generally s 79 of the Evidence Act).

2.3 However, the use or admissibility of expert evidence remains subject to the overriding requirements that:

(a) to be admissible in a proceeding, any such evidence must be relevant (s 56 of the Evidence Act); and

(b) even if relevant, any such evidence, may be refused to be admitted by the Court if its probative value is outweighed by other considerations such as the evidence being

unfairly prejudicial, misleading or will result in an undue waste of time (s 135 of the Evidence Act).

2.4 An expert witness' opinion evidence may have little or no value unless the assumptions adopted by the expert (ie. the facts or grounds relied upon) and his or her reasoning are expressly stated in any written report or oral evidence given.

2.5 The Court will ensure that, in the interests of justice, parties are given a reasonable opportunity to adduce and test relevant expert opinion evidence. However, the Court expects parties and any legal representatives acting on their behalf, when dealing with expert witnesses and expert evidence, to at all times comply with their duties associated with the overarching purpose in the Federal Court Act (see ss 37M and 37N).

## 3. INTERACTION WITH EXPERT WITNESSES

3.1 Parties and their legal representatives should never view an expert witness retained (or partly retained) by them as that party's advocate or "hired gun". Equally, they should never attempt to pressure or influence an expert into conforming his or her views with the party's interests.

3.2 A party or legal representative should be cautious not to have inappropriate communications when retaining or instructing an independent expert, or assisting an independent expert in the preparation of his or her evidence. However, it is important to note that there is no principle of law or practice and there is nothing in this practice note that obliges a party to embark on the costly task of engaging a "consulting expert" in order to avoid "contamination" of the expert who will give evidence. Indeed the Court would generally discourage such costly duplication.

3.3 Any witness retained by a party for the purpose of preparing a report or giving evidence in a proceeding as to an opinion held by the witness that is wholly or substantially based in the specialised knowledge of the witness[44] should, at the earliest opportunity, be provided with:

(a) a copy of this practice note, including the Code (see Annexure A); and

(b) all relevant information (whether helpful or harmful to that party's case) so as to enable the expert to prepare a report of a truly independent nature.

3.4 Any questions or assumptions provided to an expert should be provided in an unbiased manner and in such a way that the expert is not confined to addressing selective, irrelevant or immaterial issues.

[44] Such a witness includes a "Court expert" as defined in r 23.01 of the Federal Court Rules. For the definition of "expert", "expert evidence" and "expert report" see the Dictionary, in Schedule 1 of the Federal Court Rules.

## 4. ROLE AND DUTIES OF THE EXPERT WITNESS

4.1 The role of the expert witness is to provide relevant and impartial evidence in his or her area of expertise. An expert should never mislead the Court or become an advocate for the cause of the party that has retained the expert.

4.2 It should be emphasised that there is nothing inherently wrong with experts disagreeing or failing to reach the same conclusion. The Court will, with the assistance of the evidence of the experts, reach its own conclusion.

4.3 However, experts should willingly be prepared to change their opinion or make concessions when it is necessary or appropriate to do so, even if doing so would be contrary to any previously held or expressed view of that expert.

***Harmonised Expert Witness Code of Conduct***

4.4 Every expert witness giving evidence in this Court must read the *Harmonised Expert Witness Code of Conduct* (attached in Annexure A) and agree to be bound by it.

4.5 The Code is not intended to address all aspects of an expert witness' duties, but is intended to facilitate the admission of opinion evidence, and to assist experts to understand in general terms what the Court expects of them. Additionally, it is expected that compliance with the Code will assist individual expert witnesses to avoid criticism (rightly or wrongly) that they lack objectivity or are partisan.

## 5. CONTENTS OF AN EXPERT'S REPORT AND RELATED MATERIAL

5.1 The contents of an expert's report must conform with the requirements set out in the Code (including clauses 3 to 5 of the Code).

5.2 In addition, the contents of such a report must also comply with r 23.13 of the Federal Court Rules. Given that the requirements of that rule significantly overlap with the requirements in the Code, an expert, unless otherwise directed by the Court, will be taken to have complied with the requirements of r 23.13 if that expert has complied with the requirements in the Code and has complied with the additional following requirements. The expert shall:

(a) acknowledge in the report that:

(i) the expert has read and complied with this practice note and agrees to be bound by it; and

(ii) the expert's opinions are based wholly or substantially on specialised knowledge arising from the expert's training, study or experience;

(b) identify in the report the questions that the expert was asked to address;

(c) sign the report and attach or exhibit to it copies of:

(i) documents that record any instructions given to the expert; and

(ii) documents and other materials that the expert has been instructed to consider.

5.3 Where an expert's report refers to photographs, plans, calculations, analyses, measurements, survey reports or other extrinsic matter, these must be provided to the other parties at the same time as the expert's report.

## 6. CASE MANAGEMENT CONSIDERATIONS

6.1 Parties intending to rely on expert evidence at trial are expected to consider between them and inform the Court at the earliest opportunity of their views on the following:

(a) whether a party should adduce evidence from more than one expert in any single discipline;

(b) whether a common expert is appropriate for all or any part of the evidence;

(c) the nature and extent of expert reports, including any in reply;

(d) the identity of each expert witness that a party intends to call, their area(s) of expertise and availability during the proposed hearing;

(e) the issues that it is proposed each expert will address;

(f) the arrangements for a conference of experts to prepare a joint-report (see Part 7 of this practice note);

(g) whether the evidence is to be given concurrently and, if so, how (see Part 8 of this practice note); and

(h) whether any of the evidence in chief can be given orally.

6.2 It will often be desirable, before any expert is retained, for the parties to attempt to agree on the question or questions proposed to be the subject of expert evidence as well as the relevant facts and assumptions. The Court may make orders to that effect where it considers it appropriate to do so.

## 7. CONFERENCE OF EXPERTS AND JOINT-REPORT

7.1 Parties, their legal representatives and experts should be familiar with aspects of the Code relating to conferences of experts and joint-reports (see clauses 6 and 7 of the Code attached in Annexure A).

7.2 In order to facilitate the proper understanding of issues arising in expert evidence and to manage expert evidence in accordance with the overarching purpose, the Court may require experts who are to give evidence or who have produced reports to meet for the purpose of identifying and addressing the issues not agreed between them with a view to reaching agreement where this is possible ("**conference of experts**"). In an appropriate case, the Court may appoint a registrar of the Court or some other suitably qualified person ("**Conference Facilitator**") to act as a facilitator at the conference of experts.

7.3 It is expected that where expert evidence may be relied on in any proceeding, at the earliest opportunity, parties will discuss and then inform the Court whether a conference of experts and/or a joint-report by the experts may be desirable to assist with or simplify the giving of expert evidence in the proceeding. The parties should discuss the necessary arrangements for any conference and/or joint-report. The arrangements discussed between the parties should address:

(a) who should prepare any joint-report;

(b) whether a list of issues is needed to assist the experts in the conference and, if so, whether the Court, the parties o r the experts should assist in preparing such a list;

(c) the agenda for the conference of experts; and

(d) arrangements for the provision, to the parties and the Court, of any joint-report or any other report as to the outcomes of the conference ("**conference report**").

***Conference of Experts***

7.4 The purpose of the conference of experts is for the experts to have a comprehensive discussion of issues relating to their field of expertise, with a view to identifying matters and issues in a proceeding about which the experts agree, partly agree or disagree and why. For this reason the conference is attended only by the experts and any Conference Facilitator. Unless the Court orders otherwise, the parties' lawyers will not attend the conference but will be provided with a copy of any conference report.

7.5 The Court may order that a conference of experts occur in a variety of circumstances, depending on the views of the judge and the parties and the needs of the case, including:

(a) while a case is in mediation. When this occurs the Court may also order that the outcome of the conference or any document disclosing or summarising the experts' opinions be confidential to the parties while the mediation is occurring;

(b) before the experts have reached a final opinion on a relevant question or the facts involved in a case. When this occurs the Court may order that the parties exchange draft expert reports and that a conference report be prepared for the use of the experts in finalising their reports;

(c) after the experts' reports have been provided to the Court but before the hearing of the experts' evidence. When this occurs the Court may also order that a conference report be prepared (jointly or otherwise) to ensure the efficient hearing of the experts' evidence.

7.6 Subject to any other order or direction of the Court, the parties and their lawyers must not involve themselves in the conference of experts process. In particular, they must not seek to encourage an expert not to agree with another expert or otherwise seek to influence the outcome of the conference of experts. The experts should raise any queries they may have in relation to the process with the Conference Facilitator (if one has been appointed) or in

accordance with a protocol agreed between the lawyers prior to the conference of experts taking place (if no Conference Facilitator has been appointed).

7.7 Any list of issues prepared for the consideration of the experts as part of the conference of experts process should be prepared using non-tendentious language.

7.8 The timing and location of the conference of experts will be decided by the judge or a registrar who will take into account the location and availability of the experts and the Court's case management timetable. The conference may take place at the Court and will usually be conducted in-person. However, if not considered a hindrance to the process, the conference may also be conducted with the assistance of visual or audio technology (such as via the internet, video link and/or by telephone).

7.9 Experts should prepare for a conference of experts by ensuring that they are familiar with all of the material upon which they base their opinions. Where expert reports in draft or final form have been exchanged prior to the conference, experts should attend the conference familiar with the reports of the other experts. Prior to the conference, experts should also consider where they believe the differences of opinion lie between them and what processes and discussions may assist to identify and refine those areas of difference.

***Joint-report***

7.10 At the conclusion of the conference of experts, unless the Court considers it unnecessary to do so, it is expected that the experts will have narrowed the issues in respect of which they agree, partly agree or disagree in a joint-report. The joint-report should be clear, plain and concise and should summarise the views of the experts on the identified issues, including a succinct explanation for any differences of opinion, and otherwise be structured in the manner requested by the judge or registrar.

7.11 In some cases (and most particularly in some native title cases), depending on the nature, volume and complexity of the expert evidence a judge may direct a registrar to draft part, or all, of a conference report. If so, the registrar will usually provide the draft conference report to the relevant experts and seek their confirmation that the conference report accurately reflects the opinions of the experts expressed at the conference. Once that confirmation has been received the registrar will finalise the conference report and provide it to the intended recipient(s).

## 8. CONCURRENT EXPERT EVIDENCE

8.1 The Court may determine that it is appropriate, depending on the nature of the expert evidence and the proceeding generally, for experts to give some or all of their evidence concurrently at the final (or other) hearing.

8.2 Parties should familiarise themselves with the *Concurrent Expert Evidence Guidelines* (attached in Annexure B). The Concurrent Evidence Guidelines are not intended to be exhaustive but indicate the circumstances when the Court might consider it appropriate for

concurrent expert evidence to take place, outline how that process may be undertaken, and assist experts to understand in general terms what the Court expects of them.

8.3 If an order is made for concurrent expert evidence to be given at a hearing, any expert to give such evidence should be provided with the Concurrent Evidence Guidelines well in advance of the hearing and should be familiar with those guidelines before giving evidence.

## 9. FURTHER PRACTICE INFORMATION AND RESOURCES

9.1 Further information regarding Expert Evidence and Expert Witnesses is available on the Court's website.

9.2 Further information to assist litigants, including a range of helpful guides, is also available on the Court's website. This information may be particularly helpful for litigants who are representing themselves.

J L B ALLSOP
Chief Justice
25 October 2016

Annexure A

# HARMONISED EXPERT WITNESS CODE OF CONDUCT[45]

## APPLICATION OF CODE

1. This Code of Conduct applies to any expert witness engaged or appointed:

   (a) to provide an expert's report for use as evidence in proceedings or proposed proceedings; or

   (b) to give opinion evidence in proceedings or proposed proceedings.

## GENERAL DUTIES TO THE COURT

2. An expert witness is not an advocate for a party and has a paramount duty, overriding any duty to the party to the proceedings or other person retaining the expert witness, to assist the Court impartially on matters relevant to the area of expertise of the witness.

## CONTENT OF REPORT

3. Every report prepared by an expert witness for use in Court shall clearly state the opinion or opinions of the expert and shall state, specify or provide:

   (a) the name and address of the expert;

   (b) an acknowledgment that the expert has read this code and agrees to be bound by it;

   (c) the qualifications of the expert to prepare the report;

   (d) the assumptions and material facts on which each opinion expressed in the report is based [a letter of instructions may be annexed];

   (e) the reasons for and any literature or other materials utilised in support of such opinion;

   (f) (if applicable) that a particular question, issue or matter falls outside the expert's field of expertise;

   (g) any examinations, tests or other investigations on which the expert has relied, identifying the person who carried them out and that person's qualifications;

   (h) the extent to which any opinion which the expert has expressed involves the acceptance of another person's opinion, the identification of that other person and the opinion expressed by that other person;

   (i) a declaration that the expert has made all the inquiries which the expert believes are desirable and appropriate (save for any matters identified explicitly in the report), and that no matters of significance which the expert regards as relevant have, to the knowledge of the expert, been withheld from the Court;

[45] Approved by the Council of Chief Justices' Rules Harmonisation Committee

(j) any qualifications on an opinion expressed in the report without which the report is or may be incomplete or inaccurate;

(k) whether any opinion expressed in the report is not a concluded opinion because of insufficient research or insufficient data or for any other reason; and

(l) where the report is lengthy or complex, a brief summary of the report at the beginning of the report.

## SUPPLEMENTARY REPORT FOLLOWING CHANGE OF OPINION

4. Where an expert witness has provided to a party (or that party's legal representative) a report for use in Court, and the expert thereafter changes his or her opinion on a material matter, the expert shall forthwith provide to the party (or that party's legal representative) a supplementary report which shall state, specify or provide the information referred to in paragraphs (a), (d), (e), (g), (h), (i), (j), (k) and (l) of clause 3 of this code and, if applicable, paragraph (f) of that clause.

5. In any subsequent report (whether prepared in accordance with clause 4 or not) the expert may refer to material contained in the earlier report without repeating it.

## DUTY TO COMPLY WITH THE COURT'S DIRECTIONS

6. If directed to do so by the Court, an expert witness shall:

(a) confer with any other expert witness;

(b) provide the Court with a joint-report specifying (as the case requires) matters agreed and matters not agreed and the reasons for the experts not agreeing; and

(c) abide in a timely way by any direction of the Court.

## CONFERENCE OF EXPERTS

7. Each expert witness shall:

(a) exercise his or her independent judgment in relation to every conference in which the expert participates pursuant to a direction of the Court and in relation to each report thereafter provided, and shall not act on any instruction or request to withhold or avoid agreement; and

(b) endeavour to reach agreement with the other expert witness (or witnesses) on any issue in dispute between them, or failing agreement, endeavour to identify and clarify the basis of disagreement on the issues which are in dispute.

FEDERAL COURT OF AUSTRALIA

ANNEXURE B

# CONCURRENT EXPERT EVIDENCE GUIDELINES

## APPLICATION OF THE COURT'S GUIDELINES

1. The Court's Concurrent Expert Evidence Guidelines ("**Concurrent Evidence Guidelines**") are intended to inform parties, practitioners and experts of the Court's general approach to concurrent expert evidence, the circumstances in which the Court might consider expert witnesses giving evidence concurrently and, if so, the procedures by which their evidence may be taken.

## OBJECTIVES OF CONCURRENT EXPERT EVIDENCE TECHNIQUE

2. The use of concurrent evidence for the giving of expert evidence at hearings as a case management technique[46] will be utilised by the Court in appropriate circumstances (see r 23.15 of the *Federal Court Rules 2011* (Cth)). Not all cases will suit the process. For instance, in some patent cases, where the entire case revolves around conflicts within fields of expertise, concurrent evidence may not assist a judge. However, patent cases should not be excluded from concurrent expert evidence processes.

3. In many cases the use of concurrent expert evidence is a technique that can reduce the partisan or confrontational nature of conventional hearing processes and minimises the risk that experts become "opposing experts" rather than independent experts assisting the Court. It can elicit more precise and accurate expert evidence with greater input and assistance from the experts themselves.

4. When properly and flexibly applied, with efficiency and discipline during the hearing process, the technique may also allow the experts to more effectively focus on the critical points of disagreement between them, identify or resolve those issues more quickly, and narrow the issues in dispute. This can also allow for the key evidence to be given at the same time (rather than being spread across many days of hearing); permit the judge to assess an expert more readily, whilst allowing each party a genuine opportunity to put and test expert evidence. This can reduce the chance of the experts, lawyers and the judge misunderstanding the opinions being expressed by the experts.

5. It is essential that such a process has the full cooperation and support of all of the individuals involved, including the experts and counsel involved in the questioning process. Without that cooperation and support the process may fail in its objectives and even hinder the case management process.

[46] Also known as the "hot tub" or as "expert panels".

## CASE MANAGEMENT

6. Parties should expect that, the Court will give careful consideration to whether concurrent evidence is appropriate in circumstances where there is more than one expert witness having the same expertise who is to give evidence on the same or related topics. Whether experts should give evidence concurrently is a matter for the Court, and will depend on the circumstances of each individual case, including the character of the proceeding, the nature of the expert evidence, and the views of the parties.

7. Although this consideration may take place at any time, including the commencement of the hearing, if not raised earlier, parties should raise the issue of concurrent evidence at the first appropriate case management hearing, and no later than any pre-trial case management hearing, so that orders can be made in advance, if necessary. To that end, prior to the hearing at which expert evidence may be given concurrently, parties and their lawyers should confer and give general consideration as to:

   (a) the agenda;

   (b) the order and manner in which questions will be asked; and

   (c) whether cross-examination will take place within the context of the concurrent evidence or after its conclusion.

8. At the same time, and before any hearing date is fixed, the identity of all experts proposed to be called and their areas of expertise is to be notified to the Court by all parties.

9. The lack of any concurrent evidence orders does not mean that the Court will not consider using concurrent evidence without prior notice to the parties, if appropriate.

## CONFERENCE OF EXPERTS & JOINT-REPORT OR LIST OF ISSUES

10. The process of giving concurrent evidence at hearings may be assisted by the preparation of a joint-report or list of issues prepared as part of a conference of experts.

11. Parties should expect that, where concurrent evidence is appropriate, the Court may make orders requiring a conference of experts to take place or for documents such as a joint-report to be prepared to facilitate the concurrent expert evidence process at a hearing (see Part 7 of the Expert Evidence Practice Note).

## PROCEDURE AT HEARING

12. Concurrent expert evidence may be taken at any convenient time during the hearing, although it will often occur at the conclusion of both parties' lay evidence.

13. At the hearing itself, the way in which concurrent expert evidence is taken must be applied flexibly and having regard to the characteristics of the case and the nature of the evidence to be given.

14. Without intending to be prescriptive of the procedure, parties should expect that, when

evidence is given by experts in concurrent session:

(a) the judge will explain to the experts the procedure that will be followed and that the nature of the process may be different to their previous experiences of giving expert evidence;

(b) the experts will be grouped and called to give evidence together in their respective fields of expertise;

(c) the experts will take the oath or affirmation together, as appropriate;

(d) the experts will sit together with convenient access to their materials for their ease of reference, either in the witness box or in some other location in the courtroom, including (if necessary) at the bar table;

(e) each expert may be given the opportunity to provide a summary overview of their current opinions and explain what they consider to be the principal issues of disagreement between the experts, as they see them, in their own words;

(f) the judge will guide the process by which evidence is given, including, where appropriate:

(i) using any joint-report or list of issues as a guide for all the experts to be asked questions by the judge and counsel, about each issue on an issue-by-issue basis;

(ii) ensuring that each expert is given an adequate opportunity to deal with each issue and the exposition given by other experts including, where considered appropriate, each expert asking questions of other experts or supplementing the evidence given by other experts;

(iii) inviting legal representatives to identify the topics upon which they will cross-examine;

(iv) ensuring that legal representatives have an adequate opportunity to ask all experts questions about each issue. Legal representatives may also seek responses or contributions from one or more experts in response to the evidence given by a different expert; and

(v) allowing the experts an opportunity to summarise their views at the end of the process where opinions may have been changed or clarifications are needed.

15. The fact that the experts may have been provided with a list of issues for consideration does not confine the scope of any cross-examination of any expert. The process of cross-examination remains subject to the overall control of the judge.

16. The concurrent session should allow for a sensible and orderly series of exchanges between expert and expert, and between expert and lawyer. Where appropriate, the judge may allow for more traditional cross-examination to be pursued by a legal representative on a particular issue exclusively with one expert. Where that occurs, other experts may be asked to comment on the evidence given.

17. Where any issue involves only one expert, the party wishing to ask questions about that issue should let the judge know in advance so that consideration can be given to whether arrangements should be made for that issue to be dealt with after the completion of the concurrent session. Otherwise, as far as practicable, questions (including in the form of cross-examination) will usually be dealt with in the concurrent session.

18. Throughout the concurrent evidence process the judge will ensure that the process is fair and effective (for the parties and the experts), balanced (including not permitting one expert to overwhelm or overshadow any other expert), and does not become a protracted or inefficient process.