
National Bank - AUSMAQ Litigation

Briefing Paper: 19 July 2000

1 Introduction

[SLIDE 1, 2]

Good afternoon. My name is Ross Pinney. I am Executive General Manager Specialist and Emerging Businesses.

I would like to tell you something about the AUSMAQ case which is starting next week in Sydney and which we expect will run for between one and two years.

I would first like to say that it is an unusual step for the National to say anything about proceedings which are currently before the Court, and frankly, one which we would rather not have to take. We believe the appropriate forum for disputes to be resolved are the commercial courts, and that this dispute like any other will be resolved in that forum. It also goes without saying that as the proceedings are before the Court we are constrained in what we can and cannot say publicly about the case.

However, in light of the publicity which this case has so far received, we feel that we have a duty to our shareholders, customers and staff to outline, in advance of the case, the National's position, so that you who professionally analyse our business for the investment community are properly informed.

As I say, normally we would not take this step. But this is not an ordinary case. It is a highly unusual case in a number of respects; an exceptional case, with claims of an extraordinary nature and scale, not only for the National, but for any Australian company.

As you would know, the plaintiffs are seeking damages of in excess of \$32 billion.

I should say upfront that obviously the National says that that claim is misconceived and will fail, but it is a very large claim, the largest ever brought in Australia, and the National has, and must continue, to deal with it responsibly.

The case starts next week. We will not have an opportunity to respond in Court until the plaintiffs have finished their opening in weeks one and two. So hopefully you

might remember some of what I have told you today when you hear the plaintiffs' story.

In preparing our case we have completed about 120 witness statements, including 43 from people outside the National.

Only recently, the plaintiffs have served a large amount of new material which we say alters their case very significantly. The plaintiffs of course do not accept that.

We are in the process now of responding to that evidence and obviously cannot comment on it today.

It is unusual to be in the process of gathering evidence at the beginning of a hearing. Normally all of the evidence has been collected and considered by then. However, the judge has said we will be given an opportunity to prepare our response after the hearing starts.

We've tried to anticipate your questions, so this briefing will take a little over an hour. We want to tell you a lot about our side of the story, which is not known, and which we believe is compelling.

Finally, please bear in mind that what I am presenting are our views, only our side of the story. Our case is strongly disputed by Mr Maconochie. Indeed I think it is fair to say that there is almost nothing we agree upon. We will not attempt to present the opposing story, but in thinking about it you should be aware of the other side.

Ultimately of course, it will be up to the Court to decide.

[SLIDE 3]

The key points to take away from today are:

- A clear understanding of what the National says the AUSMAQ service was, and more importantly, was not.
- A clear understanding of what the National says the Consulting Agreement (which is at the heart of this case) does and does not provide.
- An understanding that the National has tried to make a success of this business, so far putting more than \$35 million into it.
- That the National's case will be that Mr Maconochie's business concept was flawed.

- That the National’s case (supported by independent expert evidence) will be that Mr Maconochie’s damages claim is misconceived and will fail.

For simplicity today, I am referring to the plaintiffs (that is the claimants) as “Mr Maconochie”. That is, of course, shorthand. In fact the plaintiffs are two companies in which Mr Maconochie has an interest. Mr Maconochie himself is not a party to this action. He is however a party to the National’s cross-claim.

When I talk about AUSMAQ that is shorthand for the AUSMAQ Service or AUSMAQ System, the company we bought which operated it.

2 National’s acquisition of AUSMAQ

I’d like to now give you some background to the purchase of AUSMAQ.

In June 1996, the National was approached by Mr Maconochie with a proposal to buy a 40% interest in AUSMAQ in return for \$12 million.

2.1 What is the AUSMAQ service?

[SLIDE 4 – What is AUSMAQ?]

It is important to understand at the outset what AUSMAQ did at the time we bought it. This is a basic description of AUSMAQ.

There are two important points:

- AUSMAQ has never been available on the internet.
- The National completely rejects any suggestion that AUSMAQ was to form, or has formed, the basis of its e-commerce strategy.

In late 1996, when we bought it, AUSMAQ, in general terms, assisted users (generally financial advisers) to buy and sell units in unit trusts on behalf of clients. It also assisted with the portfolio management of those units. AUSMAQ was intended to be an improvement on the traditional method of dealing in these units, which involved manually sending a signed application form and cheque to the fund manager.

A financial planner registered with AUSMAQ could buy units for a client by keying the order into the system. AUSMAQ aggregated the orders on the system for each

managed fund product from all clients on the service, and faxed one application to the relevant fund manager for the total number of units. Funds for the purchase were then transferred to the fund manager.

AUSMAQ was able to provide certain reports to advisers and clients on all of the clients' holdings on the system.

Only financial planners who had entered into an agreement with AUSMAQ could use the service. Similarly, only managed funds and debentures which were listed on AUSMAQ could be transacted using the service.

AUSMAQ tried to find a place for itself in the middle of an established relationship between fund managers and financial planners in a market which was and is heavily dominated by fund managers.

[SLIDE 5]

- The service did not:
 - operate as a fully automated service;
 - operate in “real time”;
 - operate over the internet;
 - operate on a Windows based platform;
 - offer the purchase or sale of shares;
 - offer general superannuation products;
 - offer transactions in any products other than managed funds and debentures listed on the service;
 - operate as a master trust;
 - have a multi-currency capability;
 - provide credit or have the capacity to deal with loans.

[SLIDE 6 – History]

2.2 AUSMAQ Limited (Administrator appointed)

AUSMAQ System was wholly owned by AUSMAQ Limited. When Mr Maconochie approached us in 1996, approximately 24% of AUSMAQ Limited was owned by AIDC Limited. AIDC had provided \$5 million in funding to AUSMAQ System.

The AUSMAQ service had been launched in October 1995 following a long period of development by Mr Maconochie and others.

At the time Mr Maconochie approached us, AUSMAQ Limited was in the hands of administrators.

2.3 Consideration of the opportunity by the National

The National considered the AUSMAQ opportunity and, after a due diligence, decided it was worth pursuing.

Our thinking was strongly influenced by an understanding that AUSMAQ was already up and running, had products listed on it and had some advisers using it.

For these reasons AUSMAQ was considered to be different from a lot of other opportunities presented to us, which are conceptually interesting but completely undeveloped.

However, we still recognised the investment as relatively high risk.

This is an extract from a proposal put to our Group Executive Committee:

“An investment in [AUSMAQ] would need to be recognised as receiving a stake in a start up venture and as such, of relatively higher risk than the acquisition of a mature business when the commercial potential is well demonstrated by actual track record.”

[SLIDE 7 with quote]

It also said:

“Our logic is that [AUSMAQ] must first prove its core concept in Australia. Each addition to the core system and expansion into new territories would need to be subject to future business plans where NAB would have the opportunity to assess them separately in light of the circumstances at the time.”

[SLIDE 8, 9]

(a) Mr Maconochie's marketing plan and projections

Mr Maconochie gave us his marketing plan and projections for AUSMAQ.

The marketing plan proposed a "brick-by-brick" sales approach for financial planners, with a sales force going to individual planners and selling the service.

The marketing plan suggested AUSMAQ could increase the number of financial planners using the service simply by increasing AUSMAQ's sales force. Mr Maconochie thought that the weight of money that would flow onto the service from financial planners' clients would compel the reluctant fund managers to list their products on the AUSMAQ service.

Mr Maconochie had secured the dealer group Bleakleys as AUSMAQ's anchor client. However, at the time he approached us, only a small number of Bleakleys planners were actively using AUSMAQ.

One set of Mr Maconochie's projections showed that he expected the business to become cash flow positive by June 1997 even without the ability to transact in shares and in superannuation products. He said these enhancements could be added.

These were Mr Maconochie's projections as at 30 June 1996:

[SLIDE 10, 11 - below]

AUSMAQ PROJECTIONS										
	1996/97					1997/98				
	Qtr 1	Qtr 2	Qtr 3	Qtr 4	Cum 96/97	Qtr 5	Qtr 6	Qtr 7	Qtr 8	Cum 97/98
Revenue	59	132	392	697	1280	1074	1548	2114	2708	7444
Expenses	-534	-545	-536	-540	-2155	-600	-660	-720	-800	-2780
Net Cashflow	-475	-413	-144	157	-875	474	888	1394	1908	4664
Cumulative Net Cashflow	-475	-888	-1032	-875		-401	487	1881	3789	

As you can see, these projections have the business breaking even by June 1997, with a peak funding requirement of just over \$1 million. On the covering note to these projections, he said:

“The revenue forecast excludes revenue that may be derived from the operation of stock markets in shares, and the new client and group superannuation account addition to the Service, both expected in operation within 9 months, but possibly sooner for shares”.

In fact, AUSMAQ has never achieved revenues anything like these projections. It has made significant losses each year.

(b) Negotiations

We entered negotiations with Mr Maconochie. In the negotiations, each party was represented by one of Australia’s largest law firms. Mr Maconochie was represented by Mallesons Stephen Jaques, in Sydney. We were represented by Arthur Robinson & Hedderwicks, in Melbourne.

(c) Control

In the negotiations, we say Mr Maconochie conceded that we would have 100% ownership of AUSMAQ, and 100% control of AUSMAQ.

[SLIDE 12 – 100/100/100 extract]

That, we say, was reflected in Heads of Agreement which were entered into with AUSMAQ Limited.

[SLIDE 13 – Principles from Heads of Agreement]

3 The Consulting Agreement

On 13 September 1996, the National entered into a number of agreements with Mr Maconochie (and many other parties) to buy AUSMAQ. The company AUSMAQ System was acquired by NMG.

[SLIDE 14]

We paid out approximately \$7 million. The acquisition documents provided for how that \$7 million was to be directed, which was mainly to pay back creditors of AUSMAQ, and to pay out AIDC and other investors in AUSMAQ. The acquisition involved a cash payment to Mr Maconochie’s companies of \$4.00.

3.1 Consulting Agreement

A Consulting Agreement with Mr Maconochie was one of the agreements entered into on that day. It is at the heart of the litigation. The National and Mr Maconochie fundamentally disagree as to the meaning and effect of that agreement.

The Consulting Agreement was with Idoport Pty Ltd, or “JMG”, which was Mr Maconochie’s company. “JMG” stood for “John Maconochie Group”.

(a) Services Fee

Under the agreement, JMG was paid in 2 ways.

First, JMG received a “Services Fee” of \$85,000 a month, or \$1.02 million a year. That amount was to be paid to JMG “regardless of whether services are actually required by AUSMAQ for any particular time or in any particular month”.

[SLIDE 15 – Consulting Agreement clause 6.1.]

(b) Performance Bonus

Secondly, JMG received a right to be paid a “Performance Bonus”.

[SLIDE 16 – Consulting Agreement clause 7.]

JMG was entitled to receive a performance bonus of up to 13.5% on a sliding scale, if AUSMAQ’s cost-income ratio fell below 85%.

The Consulting Agreement is still on foot and Mr Maconochie continues to receive the Services Fee.

AUSMAQ’s cost-income ratio for Australian operations has never been close to being below 100%. So no performance bonuses have been payable.

4 November 1996 to August 1997 – Mr Maconochie runs AUSMAQ

[SLIDE 17]

The purchase was completed on 6 November 1996.

4.1 Appointment of Peter Crutchley

After we bought it, we appointed a senior National officer, Mr Peter Crutchley, as Chief Operating Officer of AUSMAQ.

However, Mr Maconochie kept an active role as a consultant, effectively continuing to direct AUSMAQ as he had done before, with the staff that he had before we became involved, subject to AUSMAQ's absolute control.

Mr Maconochie was invited to AUSMAQ's board meetings.

AUSMAQ's first board meeting heard a presentation about the National's objectives and strategy for AUSMAQ. One of the slides said:

“Growth potential in new products & markets BUT MUST BE PROVEN”.

[SLIDE 18 – Slide presentation “NAB Approach to AUSMAQ”].

Another slide said:

“Authority (has) to rest with NAB officers”¹.

[SLIDE 19– Slide presentation “NAB/JMG Balance of interests”].

Mr Maconochie was at the board meeting, and we say he did not object to any of this.

4.2 1997 Business plan

[SLIDE 20]

(a) Two Scenarios

Mr Maconochie produced a draft business plan for AUSMAQ for 1997-1999 under the Consulting Agreement. The Consulting Agreement provides that the Company may amend any such business plan as it "sees fit". He offered two alternative Scenarios, which, with the draft business plan, are also at the heart of this litigation.

Scenario 1 focussed on increasing sales resources and marketing AUSMAQ consistent with Mr Maconochie's earlier plan. It included a budget (about \$200,000) for the analysis and specification of a number of development projects to enhance AUSMAQ's functionality, including a capability to transact in shares and superannuation products.

Scenario 2 encompassed Scenario 1, but also included a full budget (about \$2 million) for the completion of the development projects, including shares and superannuation. Mr Maconochie recommended adopting Scenario 2.

The business plan did not mention commercialising AUSMAQ in the United States or Asia. Mr Maconochie now claims AUSMAQ should have been up and running in those places by 2000.

We say we made it clear to Mr Maconochie (and others), on a number of occasions, that we would not commercialise AUSMAQ outside Australia and New Zealand until it had proven itself locally.

There is also now a dispute as to what the Business Plan meant in terms of the two scenarios.

(b) AUSMAQ's board

At that stage, the AUSMAQ board was made up of two National officers and two external directors, Russell McKimm (currently Deputy Managing Director of D&D Tolhurst Limited) and Kevin Courtney (retired Managing Partner of Ernst & Young in Melbourne).

(c) Board approves Scenario 1

The Board saw no disadvantage with Scenario 1 because it was necessarily the first step in the developments in Scenario 2. The Board encouraged the specification work involved in Scenario 1 to proceed without delay. Our case is that Mr Maconochie and his sub-consultants were responsible for these developments.

The directors also wanted to ensure that AUSMAQ only proceeded with development projects for which there was a convincing business case.

For those reasons, our strategy group recommended, and the board approved, Scenario 1, and adopted that as AUSMAQ's business plan for that financial year. Management told the board that, given all that they had to do, they would be fully occupied with Scenario 1. We say that Mr Maconochie concurred with this course, or at least voiced no objection to it. That too is the subject of dispute between the parties. No objection was recorded in the minutes, nor in any other document from Mr Maconochie to us at the time.

4.3 AUSMAQ's sales experience

(a) Recruitment of sales staff

By March 1997, in accordance with the business plan, AUSMAQ had recruited three new sales staff. Working partly on commissions, the sales force began to market the service to financial planners in earnest.

At that time, Mr Maconochie remained very much involved at AUSMAQ, even though he was a Consultant.

(b) Difficulties in effecting sales

The sales staff found it was very difficult to sell the system to advisers and planners.

Drawbacks included:

- (1) it could not deal in general superannuation products - this impacted on consolidated reporting and administration possibilities;
- (2) few managed funds were listed on AUSMAQ;
- (3) that it contained products that were not competitive when combined with the fees charged by AUSMAQ;
- (4) it did not process partial units;
- (5) it looked old fashioned;
- (6) it was difficult to use;
- (7) it was not Windows-based, so that advisers could not use a mouse to move around the system;
- (8) it did not interface with the software packages that a number of advisers were using, which meant that clients' details and orders had to be keyed in twice in those circumstances.

Those were the kinds of complaints which the National says that AUSMAQ's sales staff encountered when they went out to try to sell the system in the first half of 1997. The lack of superannuation and shares stood out as a particular concern. As a result, despite the efforts of the sales force, very few advisers used AUSMAQ.

(c) Previous sales experience

We say that it is now clear that the problems that the sales staff experienced in selling the service after the National bought AUSMAQ were not new. They were the same problems that were experienced when Mr Maconochie first started selling the service in 1995, long before we were involved.

Certain specific historical experience now forms the basis of a cross claim we have made against Mr Maconochie and others.

5 Redirecting Mr Maconochie's efforts

5.1 Failure of sales efforts

[SLIDES 21 and 22 – Performance figures August 1997]

[SLIDES 23 and 24]

The lack of progress in selling the system was of great concern to AUSMAQ's board.

[SLIDE 25]

The board was also concerned about the lack of progress made on the development projects including the addition of a shares and superannuation capability. At board meetings, the directors urged Mr Maconochie to create the specifications for the development projects for which a budget had been approved under Scenario 1. This did not happen.

There is a dispute about this issue and the reasons why this didn't happen. The National's case is that Mr Maconochie gave a number of different reasons for the lack of progress on the development projects, for example, that he had other priorities, or that he and his consultants were the only people who could brief external people to do the work.

5.2 Breakdown in relationship between Peter Crutchley and Mr Maconochie

Peter Crutchley was concerned about AUSMAQ's lack of progress. He gradually received reports from the sales staff about the reasons that advisers were giving for

not using AUSMAQ, and started to question whether Mr Maconochie was adopting the right approach.

From what the sales staff told him, Peter realised that it was crucial that AUSMAQ develop a superannuation capability as quickly as possible. He raised with Mr Maconochie the need to get on with the development work. Like most of AUSMAQ's staff, the key IT staff had been recruited by Mr Maconochie before the National's involvement.

At the time, Mr Maconochie attributed AUSMAQ's lack of sales to a number of different things, including:

- the alleged incompetence of the sales staff;
- the alleged incompetence of Peter Crutchley; and
- the alleged imposition by Peter Crutchley of a "hiring and expenditure freeze".

Those matters are denied by the National.

AUSMAQ was under budget in its spending, and the board was repeatedly urging AUSMAQ to spend the budget it had and to get on with sales and development work. In May 1997 Mr Maconochie wrote:

"I believe that our May '97 review of the business will show:

...

- a company adequately staffed with sufficient competent and suitably qualified people necessary to contain the business operational continuity risk and carry the company forward; and
- expense and revenue items in line with budget...".

[SLIDE 26 – Extract from memo dated 3 May 1997]

5.3 Redirecting Mr Maconochie

[SLIDE 27]

By July 1997, it was clear to AUSMAQ's directors that changes needed to be made to the management of the AUSMAQ business.

The directors appointed a new Chief Operating Officer of AUSMAQ (Mr Roger Meikle) on Mr Maconochie's recommendation, and directed Mr Maconochie to focus on developing the superannuation and share enhancements. Mr Maconochie has subsequently been critical of Roger Meikle's suitability.

Mr Maconochie was told of the new arrangements on 2 August 1997. He objected strongly.

5.4 Roger Meikle's 1997/98 business plan

The new Chief Operating Officer, Roger Meikle, prepared a new business plan for the 1997/98 financial year (with input from Coopers & Lybrand) which focused on the completion of critical development work and on a closer and more cooperative sales approach.

At that time, and throughout 1998, Roger Meikle and Mr Maconochie continued to be in frequent contact. In addition, another of the JMG Consultants, Mr Brian Martin, continued to work from AUSMAQ's premises.

The AUSMAQ board approved this business plan, and Mr Meikle pursued it.

6 Late 1997 and 1998

6.1 Breakdown in relationship with Mr Maconochie

From that time on, Mr Maconochie's relationship with AUSMAQ and the National deteriorated. Mr Maconochie claims that he was shut out of the AUSMAQ business in August 1997, and that the Consulting Agreement did not entitle AUSMAQ to direct his activities as it has done. Those claims are strongly denied by the National.

6.2 Commencement of proceedings

[SLIDE 28]

Mr Maconochie's companies began proceedings in September 1998.

As well as the National, the plaintiffs sued three National subsidiaries, Glenn Barnes, Frank Cicutto, David Krasnostein and AUSMAQ's two external directors. In March 1999, they added Don Argus to separate (but similar) proceedings. Don Argus was

never a director of AUSMAQ and had very little to do with Mr Maconochie or the AUSMAQ business. In the last couple of weeks Simon Moore and Richard McKinnon, who were involved in the negotiations for the purchase, have also been joined as parties to the Second Cross Claim, filed by Mr Maconochie and his companies. That claim is also strongly disputed.

6.3 The National is currently funding AUSMAQ

The National has provided funding, staff (including secondees) and other support to AUSMAQ since it bought it.

So far, the National has put over \$35 million into AUSMAQ. To date, the business has not been profitable and no performance bonus has been paid.

7 Claim by Mr Maconochie

Mr Maconochie's claim breaks down into four general categories:

- (a) pre-contractual misrepresentations;
- (b) breaches of post-contractual and fiduciary obligations;
- (c) claims in relation to certain National projects; and
- (d) the National's alleged misappropriation of AUSMAQ's intellectual property.

[SLIDE 29 – Categories of claims.]

7.1 Pre-contractual misrepresentations

First, Mr Maconochie alleges that officers of the National made a number of misrepresentations to him before he entered into the agreements to sell AUSMAQ to the National. These misrepresentations relate principally to the role that he would play in the business and in the commercialisation of the business.

He alleges the National represented to him that he would effectively remain the chief executive of AUSMAQ after the acquisition and would be responsible for AUSMAQ's business strategy, technical and market development.

The National denies that the representations were made. We have already referred to the 100/100/100 communication from Mr Maconochie and the Heads of Agreement.

We have strong statements in denial from the two officers involved in the negotiations.

7.2 Post-contractual breaches of obligations

Secondly, Mr Maconochie makes a very large number of claims relating to the conduct of the National and AUSMAQ after the acquisition of the AUSMAQ business. Mr Maconochie claims that the National and AUSMAQ breached their contractual obligations and alleged fiduciary obligations towards Mr Maconochie in numerous respects.

The National denies these alleged breaches. Our position is that AUSMAQ controls its own business. It is also our case that the AUSMAQ board approved Scenario 1 of Mr Maconochie's first business plan and attempted to implement it. It became clear that Mr Maconochie's approach was not working. In particular, it was necessary to add enhancements to the AUSMAQ system before financial planners would contemplate any substantial use of it. Mr Maconochie was therefore directed to focus his attention on development work to progress those enhancements. It is the National's case that he failed to do so.

AUSMAQ's board and Chief Operating Officer continued to pursue what they believed was the best strategic direction for AUSMAQ. That differed from what Mr Maconochie believed to be the best strategic direction for AUSMAQ. Mr Maconochie was not excluded from participating in the business. To the contrary, the Board looked to him for work on the developments.

The National has continued to provide major funding and resources to AUSMAQ.

We have filed statements from AUSMAQ's directors, National executives (both current and former employees), AUSMAQ staff (both current and former staff) and others dealing with the events of the period. In total, 63 statements deal with the post contractual issues.

7.3 Claims relating to National projects

The third category of Mr Maconochie's claims relates to certain projects within the National. Mr Maconochie makes two kinds of allegations about those projects.

First, Mr Maconochie alleges that the Consulting Agreement entitles him to a performance bonus in relation to four projects that have been developed independently of AUSMAQ because, he says, they are services with equivalent or similar functionality to AUSMAQ.

In support of his claim, Mr Maconochie, asserting that he is an expert (which the National will challenge), has filed a report comparing AUSMAQ's functionality to the functionality of those National projects. He concludes that the projects are of "equivalent or similar" functionality. His conclusions are supported by a Professor. Recently, further statements on this part of the case have been received.

The National denies that Mr Maconochie's interpretation of the Consulting Agreement is correct.

In any event, we say that the projects are all quite different to AUSMAQ. The National has also filed an expert statement from a partner at Andersen Consulting (Mr Andrew Macpherson), who is also Managing Partner of Dot.Com Consulting, which concludes that the National projects are not of "equivalent or similar" functionality to AUSMAQ. The report disputes the methodology that Mr Maconochie has used.

One of the projects which Mr Maconochie has made a claim over is the All-In-One Master Trust. Mr Maconochie says it is of "equivalent or similar" functionality to AUSMAQ. However, in a letter dated 7 February 1996, Mr Maconochie said:

"Please understand that the AUSMAQ service is not a master trust."

The second allegation Mr Maconochie makes about the four National projects is that the National misappropriated AUSMAQ's intellectual property in developing and implementing those projects.

We strongly deny that claim. We have filed statements from 18 of the main executives at the National who were responsible for the development of the four National projects. Those executives include both current and former employees of the National. They all strongly deny that there was any use of AUSMAQ's intellectual property in the development of those projects.

A further allegation that Mr Maconochie has made is that the National should have used AUSMAQ to develop each of the National's projects and all of its e-commerce

initiatives. The National contends that such a construction of the Consulting Agreement is without foundation.

8 The National's Cross-Claim

[SLIDE 30]

We have also made a claim against Mr Maconochie. We say:

- At the time the National purchased AUSMAQ System, Mr Maconochie had important market information about the system's commercial viability, namely that dealers would not use the system to the extent necessary to derive the revenues predicted by Mr Maconochie without the addition of a superannuation capability;
- Mr Maconochie did not disclose that information to the National;
- Mr Maconochie had a duty of disclosure (by way of contractual warranty and other obligations) to the National;
- Had he done so the National would not have purchased the business.

This claim is supported by a number of witnesses external to the National. Mr Maconochie disputes these claims. That will be a major issue in the trial.

9 The Second Cross-Claim

[SLIDE 31]

Mr Maconochie has now filed a cross-claim to the National's cross-claim, which is called a "Second Cross-Claim". It is said to supply an answer if the National succeeds on its cross-claim.

There are two main aspects to Mr Maconochie's Second Cross-Claim.

- The first is an allegation that the National represented to Mr Maconochie that it was conducting a due diligence on AUSMAQ prior to acquisition, that the due diligence would be thorough and comprehensive, and that the National would request all relevant and important documents and information.

- The second is that we led Mr Maconochie to believe that we would exploit the AUSMAQ service promptly throughout the world, and would provide the short term capital to develop shares and superannuation capabilities when we had no intention of doing so.

This claim is made, according to Mr Maconochie, in circumstances where it was the fact that there was a need for AUSMAQ to provide shares products and a general superannuation facility if it was to be accepted by dealers and financial planners. We say that was not disclosed to us.

Mr Maconochie alleges, amongst other things, that, by reason of the Second Cross-Claim, the National is prevented from relying on any breaches under the Cross-Claim.

The National has filed a defence to the Second Cross-Claim generally denying it.

A number of these claims were not made by Mr Maconochie originally. This is one of the respects in which we say he has fundamentally changed his case.

10 Damages

[SLIDE 32]

I now wish to turn to the damages claim that Mr Maconochie has made. Mr Maconochie is claiming in excess of \$32 billion in damages.

10.1 History of damages claims

In August 1998, a month before Mr Maconochie's companies commenced this case, he sent a letter to AUSMAQ, stating that he was entitled to damages in the order of \$445 million.

A month later, when Mr Maconochie commenced the proceedings, he was claiming damages in the range of \$190 million to \$8.07 billion. Between that time and April 1999, Mr Maconochie's claim had grown to its present range of US\$271 million to more than US\$21 billion.

The range of values has increased by about 215% (on the lower range) or almost 400% (on the higher range) from when the proceedings commenced, and over 7000% from a month before he started the proceedings.

The National's case is that the damages claim is misconceived and will fail in the face of the very strong defence which the National believes it has on both liability and damages.

Mr Maconochie has told the Court that, with the exception of a few "lay" witnesses to be called early on, he will be calling his damages witnesses first. I understand that this is an unusual approach. Also, Mr Maconochie apparently will himself be the plaintiffs' last witness called.

Whatever order Mr Maconochie may call his witnesses in, the question of damages does not even arise unless and until there is a finding by the Court that the National has been in breach of a legal obligation. As I've said, all alleged breaches are strenuously denied.

10.2 Basis of Mr Maconochie's claim

(a) Gross revenue

Very generally, Mr Maconochie alleges that, if the approach embodied in his 1997 business plan had been implemented, AUSMAQ would have produced gross operating revenue of US\$2.1 billion by the year 2003, being broken down into regions as follows:

Region	Gross operating revenue (US\$ million)	Market capitalisation (at PE multiple of 60) (US\$ billion)	JMG loss (US\$ billion)
North America	\$749 million	\$21.7 billion	\$7.3 billion
Europe	\$665 million	\$19.5 billion	\$6.5 billion
Asia and Oceania	\$712 million	\$20.8 billion	\$7.0 billion
Total	\$2126 million	\$62 billion	\$21 billion

It should be remembered that AUSMAQ has never operated outside Australia and New Zealand.

Therefore, to the extent that Mr Maconochie claims damages in respect of other places, his claim speculates on what might have been the case in the hypothetical situation of a fledgling business with no established brand name or track record of success in Australia opening its doors for business in those sophisticated markets.

As an example of how Mr Maconochie obtains his figures for North America, Mr Maconochie assumes that AUSMAQ had:

- a 25% chance of obtaining a 50% market share (based on obtaining a similar market share to Charles Schwab & Co, the leading US service agent for mutual fund products);
- a 15% chance of obtaining a 15% market share (based on obtaining a similar market share to Fidelity, the second leading US service agent);
and
- a 60% chance of obtaining a 5% market share (based on the market share of TD Waterhouse, the third leading US service agent),

by the year 2003, leading to what he terms a probable market share in 2003 of 17.75%. He multiplies this by his estimate of the size of the US retail market (US\$1.066 to US\$8.3 trillion) and his suggested proposed portfolio fee of 0.30 to 0.10% respectively of assets under management. He then assumes an 80% chance of the lower of these two values being realised and a 20% chance of the upper value to reach the figure of US\$749 million in the table above.

He also assumes a probable market share in Australia of 17.75%. Relying on the reasoning of one of his principal expert witnesses for the UK and European markets, Mr Ian Joslin, Mr Maconochie comes to the conclusion that, by 2003, AUSMAQ would have an expected market share of 8% in Europe. Mr Maconochie chooses a similar figure for Japan, Hong Kong and Taiwan. He then converts these market shares into revenues using slightly different methodologies in each market.

He assumes that, by 2003, AUSMAQ would have a cost-income ratio of 25%. In one of his statements, however, Mr Maconochie says that Schwab in 1999 had a cost to income ratio of 80%. One of the National's independent experts has reviewed cost to income ratio data for 9,335 public companies in the US and found less than 1.5% of all companies had cost to income ratios less than 25% between 1998 and 1999. An analysis of AUSMAQ's target market demonstrated an average cost to income ratio of 88%.

It is interesting to compare Mr Maconochie's damages figures with his own estimates as set out in his business plan for 1997-1999 (extrapolated to the year 2003 by our valuation expert, Professor Lehn, on the basis of a 5% increase in revenue and operating costs for each of the last 3 quarters of the year ending June 2000, and a 20% increase in revenue and operating costs for each of the years 2001 to 2003).

[SLIDE 33 - below]

Year ending	Revenues (A\$ million)	Operating Costs (A\$ million)	Net income before taxes (A\$ million)	JMG Performance Bonus (A\$ million)
Jun 1997	\$0.1 million	\$4.1 million	(\$4.0 million)	-

Jun 1998	\$4.4 million	\$6.1 million	(\$1.7 million)	-
Jun 1999	\$18.3 million	\$6.8 million	\$11.5 million	\$2.5 million
Jun 2000	\$28.4 million	\$7.3 million	\$21.1 million	\$3.8 million
Jun 2001	\$34.1 million	\$8.7 million	\$25.4 million	\$4.6 million
Jun 2002	\$40.9 million	\$10.4 million	\$30.5 million	\$5.5 million
Jun 2003	\$49.1 million	\$12.5 million	\$36.5 million	\$6.6 million

(b) Buy out

Mr Maconochie then alleges that the National would have exercised its right to buy out his company’s right to receive future performance bonuses, first exercisable in the year 2003. On the basis that AUSMAQ would have achieved a price-earnings ratio of between 20 and 100, Mr Maconochie’s final calculations are based on the mid-point between those figures, that is, a P/E ratio of 60.

Mr Maconochie contends the result to be that the National would have paid US\$21 billion, or more, in the year 2003 to buy out his right to performance bonuses under the Consulting Agreement.

The National has no obligation to buy out Mr Maconochie’ company. The buyout procedure is one the National “may” initiate. Whether it does so or not is entirely a matter for the National’s discretion.

In relation to that, in the interlocutory application, Justice Einstein stated the following:

“315. ... These documents make plain that the damages case, insofar as it assumes that the clause 15 rights must lead to a buyout of JMG’s rights by the Bank, or by JMG of NMG and Operating Entities, may well be misconceived”.

10.3 National’s position

[SLIDE 34]

The National strongly disputes Mr Maconochie’s damages assessment.

The National contends that the AUSMAQ service, as envisaged by Mr Maconochie, did not succeed commercially in Australia and would not have done so in foreign markets principally because of problems with its functionality and in the value proposition it offered its key stakeholders: investors, financial intermediaries and financial product providers.

In the case, we have put on statements from independent experts covering a number of jurisdictions refuting Mr Maconochie's claims, including experts from Australia, New Zealand, the USA, the UK and Europe, Japan, Hong Kong and Taiwan. Those experts include leading academics and partners of leading management consultant and accounting firms.

They have come to the following conclusions.

(a) In Australia/New Zealand

Mr Maconochie's approach as embodied in his 1997 business plan, and on which he bases his expert statements, was unsound.

What Mr Maconochie proposed through AUSMAQ also did not offer a sufficiently compelling value proposition to the key stakeholders.

Overall, AUSMAQ increased both costs and complexity for most investors.

For the dealer, from a complexity standpoint, the best AUSMAQ could do was preserve the status quo but at worst it added another layer of complexity to the adviser's dealings with clients.

From the fund manager's perspective, AUSMAQ created a significant revenue disadvantage due to the loss of up front fees and the reduction of ongoing management fees.

AUSMAQ was strategically opposed to the most powerful players in the funds management industry, the funds managers themselves.

As it did not offer significant functional or financial improvement over the existing paradigm it would not, as envisaged, have received support from the funds management industry.

In addition, AUSMAQ had operational deficiencies which meant that it could not support standard industry transactions and practices, amongst other things.

(b) Other Territories

The experts conclude that AUSMAQ would have been unsuccessful if it had been launched in any of the other territories.

That conclusion was reached even though the independent experts were asked to assume that AUSMAQ was capable of doing everything which in our view Mr Maconochie alleges that it might be able to do, rather than what the National says is its capability in real life.

(c) Valuation methodology

We say Mr Maconochie's valuation methodology grossly inflates his damages claim (by a factor of thousands) on top of his inflated market share and revenue projections.

Professor Kenneth Lehn, the National's valuation expert, formerly Chief Economist at the US Securities and Exchange Commission, concludes the methodology used by Mr Maconochie to estimate the terms of the buy out is "inappropriate", for reasons including:

- the use of an inappropriately high P/E multiple of 60;
- an inappropriately low discount rate of 5% (effectively assuming AUSMAQ's rise to market dominance would be risk free);
- the assumption that the National would have exercised the buy out, when it is not certain that the National would have done so.

Mr Maconochie selects Schwab as a comparable company for the purposes of the P/E ratio. Professor Lehn comments on that as follows:

"Mr Maconochie's selection of Charles Schwab as a comparable firm ... is analogous to an amateur golfer who attempts to value his expected prize in the Australian Open by extrapolating from Greg Norman's past scores in the Open. This method would greatly overstate the amateur golfer's expected prize".

11 Rumours of a \$200 - \$300 million settlement

There has been some suggestion that the National would settle these proceedings for \$200 - \$300 million.

I can assure you that those figures have not emanated from us.

While the fact or content of any settlement discussions is of course confidential, I can tell you that no settlement discussions have occurred for about two years.

The nature and extravagance of the claims now made are such that the only realistic avenue for a proper solution appears to be the Courts. The National believes that it has a very strong case and is committed to seeing it through.

We look forward to all the facts and circumstances surrounding the case coming out.

12 The Final Hearing

[SLIDE 35]

The final hearing begins on Monday, 24 July 2000.

You can expect during the plaintiffs' opening that very serious allegations (all of which the National denies) will be made. As we told you recently, we will not have an opportunity to respond in Court to any of those allegations until the Plaintiffs opening has ended.

After that opening, we will then be given an opportunity to open our case.

The Plaintiffs' witnesses will then give their evidence and be cross examined. This will last for at least six months.

Our witnesses will then give evidence and be cross-examined. This will also be a long process.

It is expected that the hearing will continue for at least 12 months and perhaps as long as 24 months. The National is absolutely resolute and confident in its defence of this case.