

HIH Case Study

HIH Insurance was formerly Australia's second largest insurance company. The demise of the HIH Insurance Group is considered to be the largest corporate collapse in Australia's history, with liquidators estimating that HIH's losses totaled up to \$5.3 billion.

In 2001, the board appointed a provisional liquidator to take control of HIH and 17 of its controlled entities. The board hoped this would give HIH time to review its operations and assess its financial position. When McGrath announced his appointment as provisional liquidator he estimated that HIH had lost over \$800 million over the six months to 31 December 2000. He attributed the HIH company failures to rapid expansion, unsupervised delegation of authority, extensive and complex reinsurance arrangements, underpricing, reserve problems, false reports, reckless management, incompetence, fraud, greed, and self-dealing.

Investigations into the cause of the collapse have led to various charges relating to fraud and the conviction and imprisonment of a handful of members of HIH management.

HIH Royal Commission

The HIH Royal Commission was established by the Federal Government on 29 August 2001 to investigate how such a large corporate entity could collapse with so much debt.

In April 2003, the Royal Commission released its report *The Failure of HIH Insurance*. The report provided timely insights into many aspects of **how a company with award winning corporate governance systems and policies, could get it so wrong**. Mr Justice Owen, the Commissioner, identified that the core reasons for the collapse related more to vanity and inflated egos, poor systems and lack of monitoring rather than wide spread fraud.

Justice Owen commented on what is the essence of good corporate governance:

The governance of a public company should be about stewardship. Those in control have a duty to act in the best interests of the company. They must use the company's resources productively. They must understand that those resources are not personal property. The last years of HIH were marked by poor leadership and inept management. Indeed, an attitude of apparent indifference to, or deliberate disregard of, the company's underlying problems pervades the affairs of the group.

Those responsible for the stewardship of HIH ignored the warning signs at their own, the group's and the public's peril. The culture of apparent indifference or deliberate disregard on the part of those responsible for the well-being of the company set in train a series of events that culminated in a calamity of monumental proportions.

The report fundamentally states that the main reasons for the failure of HIH was poor management and greed characterised by a lack of:

- attention to detail and skills
- accountability for performance
- integrity in the company's internal processes and systems

HIH Case Study (continued)

As stated in a 2008 CCH update:

It is interesting to note that one of the key findings of the Royal Commission was that a culture had developed within HIH that leadership decisions were not to be questioned, and that rather than fraud or embezzlement being behind the collapse, the primary reason for the failure was that HIH was mismanaged in the area of its core business activity, being insurance.

It is a timely reminder to all directors that one of their fundamental duties is to question management decisions.

Other weaknesses

HIH also illustrated that senior management and the board had overseen the poor selection of management personnel, and their lack of skills and competencies to manage, what grew to be a multi-national enterprise. In particular, Ray William's personal weaknesses, including a paternalistic vanity and an inability to see his own failings, and the deferring to his judgment by many on the board in an uncritical manner, were significant factors in HIH's downfall .

But equally so, HIH's downfall was hastened by the inability and failure of others, including the auditors, the non-executive and executive directors, and even the regulators (APRA), to curb and check the failures and excesses of Williams and of others, such as Rodney Adler, who took advantage of William's fatal flaws.

As Rodney Adler told a former associate, it was Williams' "complete and utter delusion" that had made him such an easy mark.