

16 November 2015

Committee Secretary

Parliamentary Joint Committee on Corporations and Financial Services
PO Box 6100
Parliament House
Canberra ACT 2600

Inquiry into the Impairment of customer Loans

The Westpac Group thanks the Committee for the opportunity to lodge a submission with the Inquiry. In addition we endorse the submission lodged by the Australian Bankers' Association.

If you require any further information about this submission please do not hesitate to contact me on _____ or _____.

Contents

Section	Subsection	Page
1. Executive Summary		2
2. Westpac approach to business lending	2.1 Commitment to lending responsibly	4
	2.2 Management of credit risk	5
3. Ongoing credit risk assessment	3.1 Covenant monitoring	6
	3.2 Covenant breaches	7
4. Approach to customers in financial distress	4.1 Regulatory requirements associated with impaired loans	9
	4.2 Event of monetary and non-monetary default	9
	4.3 Consequences of an event default	10
5. Recovery action	5.1 Our general approach	13
	5.2 Appointment of third parties	14
	5.3 The sale of real property	15
6. Dispute resolution		16
7. Our support of drought affected communities		16

1. Executive summary

The Westpac Group's vision is 'To be one of the world's great service companies, helping our customers, communities and people to prosper and grow'. This includes a genuine commitment to helping Australian businesses become stronger. Our Commercial and Business Bank currently has over one million business customers and approximately \$80 billion in business lending. The Westpac Institutional Bank has over 3,000 customers and approximately \$180 billion in business lending.

The Westpac Group notes the Inquiry is particularly concerned with business lending and the application of a “constructive default”, defined as “the engineering or the creation of an event of default whereby a financial institution deliberately reduces, through valuation, the value of securities held by that institution, thereby raising the loan-to-value ratio resulting in the loan being impaired”.

The Westpac Group does not engage in practices to artificially engineer a business default, including revaluation of security. It would be rare for the Westpac Group to use a decreased loan to value ratio (LVR) as a sole default trigger to commence enforcement action i.e. when the Westpac Group accelerates the loan and enforces security, which could include the appointment of a Receiver and Manager. Enforcement on the sole basis of an LVR default has not taken place since our merger with St. George in December 2008.

Furthermore, ‘impairment’ is a specific definition under APS220 to reflect a potential loss which requires provisioning. An increase in impaired credit exposures can adversely affect the Westpac Group’s liquidity, capital resources, financial performance and financial condition. Consequently, there is not a commercial incentive for the Bank to increase impairments and suffer such capital imposts.

We also acknowledge the Committee’s request to outline the processes, timelines and relevant legislation that the Westpac Group follows when a customer loan moves to default and enforcement. To address this request our submission outlines the practices and policies that govern our response to distressed customer loans.

The Westpac Group is committed to putting the customer at the centre of everything we do. This is reflected in our “Principles for doing business”. Our support for our customers extends during times when they are experiencing financial difficulty.

There are a variety of factors that may lead a business to experience financial difficulty, including economic downturn, business management capability, change in personal circumstances, fraud, overtrading and specific events such as flood, drought and fire. Our focus is on identifying any difficulties within the business early to ensure a range of options are available to the customer and prevent contractual default. Both Financial and Non-Financial covenants play an important role in facilitating this early identification.

Once we have made that identification, our priority is to work with the customer to find solutions that will, as far as possible, seek to ensure the Customer’s business is sustainable and can be returned to good health. This is in the interests of both the Customer and the Westpac Group. It is industry practice to try and resolve the repayment of debt without relying on the legal rights of loan contracts that enable lenders to enforce mortgage agreements.

It is important to note, that every matter is dealt with on a case-by-case basis to ensure the Westpac Group can respond flexibly to the circumstances of individual customers. We consider

this is industry best practice. Where a matter does proceed to enforcement, and the Westpac Group takes action to recover our debt by exercising its rights under the security document, we consider the existing regulatory regime is appropriate. This includes the strict legal obligations governing the sale of real property.

Nevertheless, the submission by the Australian Bankers' Association outlines some recommendations to further enhance practices associated with specific industry segments, such as the implementation of a nationally consistent farm debt mediation model across Australian agriculture. As a national corporation, the Westpac Group is strongly supportive of a harmonised farm debt mediation model.

Finally, the Westpac Group considers it is imperative to proactively support our business customers to be successful by providing access to advice, information and skills development. For example, providing insights to customers about their cash flow movements or in the agribusiness sector, demonstrating that business reserves and equity remain an essential component of drought and risk mitigation measures. The Westpac Group considers that there are opportunities for partnerships between government and industry to facilitate customers' access to important tools and information that can assist with business management.

2. Westpac approach to business lending

2.1 Commitment to lending responsibly

At the Westpac Group, we are committed to lending to customers in a responsible manner. We acknowledge our obligation to design and market our products responsibly in line with the expectations of customers and the community.

Our "Principles for Doing Business" form the foundation of our commitment to corporate responsibility and sustainable business practice. The extension of both consumer and business credit is also underpinned by the Westpac Group's own "Principles of Responsible Lending", including the principle that we seek to lend only what our customers can afford to repay. It is not in the Westpac Group's interests to extend credit that cannot be repaid. The Westpac Group's interests and the interests of our customers and the broader national economy are ultimately aligned; our success relies on the success and prosperity of our business customers.

In addition to our own credit assessment policies, the Westpac Group complies with all local legislation, relevant codes of practice (including the Australian Bankers' Association Code of Banking Practice adopted by the Commercial and Business Bank and Consumer Bank) and relevant guidelines published by the Financial Ombudsman Service. For example, Clause 27 of

the Code of Banking Practice requires that we “exercise the care and skill of a diligent and prudent banker in ... forming our opinion about your ability to repay the credit facility”¹.

2.2 Management of Credit Risk

All Approved Deposit Taking Institutions (ADIs), including the Westpac Group, are regulated by the Australian Prudential Regulation Authority. APRA Prudential Standard *APS 220: Credit Quality* (APS 220) requires ADIs to control credit risk² by adopting prudent credit risk management policies and procedures.

The Westpac Group’s credit risk framework and policies encompass all stages of the credit cycle – origination, evaluation, approval, documentation, settlement, ongoing administration and problem management. For example, we have established product-based standards for lending to businesses including minimum serviceability standards and maximum loan to security value ratios. We focus on the performance of key financial risk ratios, including interest coverage, debt serviceability and balance sheet structure.

The Westpac Group’s credit risk management framework also incorporates the assignment of risk profile to individual customers and our credit risk appetite (which can vary over time).

For larger customers (usually with an exposure above \$1 million), Westpac evaluates credit requests by undertaking detailed individual customer and transaction risk analysis (the ‘transaction-managed’ approach). Such customers are assigned a customer risk grade representing Westpac’s estimate of their probability of default and loss given default.

When providing finance to smaller business, commercial and corporate borrowers we typically obtain security, including a mortgage over property, a general security agreement over business assets and/or guarantee(s) from the director(s). For larger corporates and institutions we typically also require compliance with selected financial ratios and undertakings and generally hold security.

The effectiveness of our credit risk management framework is demonstrated in our low default and arrears rates and number of distressed customers. Both the Commercial, and Corporate and Institutional Banking portfolios have historically low levels of customers experiencing stress. The Commercial portfolio is at its lowest level of stress since 2010. For example, in our agribusiness segment of 30,600 customers we currently have:

¹ This applies to a small business and sole trader as defined by the Code.

² Credit risk is the risk of financial loss and arises from the possibility that some customers will be unable to honor their financial obligations to us, including the repayment of loan principal and interest.

- 87 'farm gate customers'³ (0.28% of agribusiness customers) under the management of our specialist risk management unit, this includes customers showing early signs of stress and on the 'watch list'; and
- Commenced recovery action against 8 customers and appointed a receiver. 3 of these customers remain in occupancy of the property.

While this is a statistically small segment, we are sensitive to the effect this can have on the welfare of the affected customer and their families. The Westpac Group is engaged in industry initiatives to improve the capability of our staff to support customers in financial distress and associated mental health issues.

3. Ongoing credit risk assessment

3.1 Covenant monitoring

There are many factors which can reduce or increase the risk associated with a customer's capacity to repay their loan throughout the life of the credit facility. As required by regulation, once a credit contract is established, the Westpac Group undertakes ongoing risk assessments to ensure the application of a correct credit risk grade to the customer⁴. This assessment is informed by a number of conditions and reporting obligations that a customer agrees to meet under the terms of the loan contract i.e. 'covenants'.

Covenants are a contractual requirement or restriction placed on a borrower, setting minimum standards for their future conduct and performance. Covenants utilised by the Westpac Group are defined, measurable, anticipatory of deteriorating credit and reasonable in purpose. They provide an early warning of deteriorating risk profiles and form an important part of our broader risk management framework, by highlighting the need for a discussion around stabilising and improving business performance, and therefore risk profile.

There are two broad categories of covenant that may be included in our Loan Facility Agreements:

1. **Financial covenants**, normally expressed as financial ratios that a customer is required to observe.

For example, measures that control financial leverage, minimum profitability, liquidity, serviceability or net worth such as minimum interest coverage ratio, maximum gearing

³ Farm Gate loans are defined as customers designated with ANZIC Code Agriculture Division 01, sub 400 Codes.

⁴ The Westpac credit risk rating system has 20 risk grades for non-defaulted customers and 10 risk grades for defaulted customers.

ratio, minimum shareholder's funds to total assets and maximum Loan to Valuation Ratio (LVR).

These are tested and provided to the Westpac Group on a regular basis and act as an effective early warning mechanism that a customer's financial position or the value of its assets have deteriorated which may adversely impact the customer's ability to repay their loans. It is important to note that not all assets are taken as security in every case.

2. Non-financial covenants, which may be:

- Restrictions that a customer must comply with (for example, not to dispose of or grant security over substantial assets without the Westpac Group's consent); or
- An action that a customer must cause to occur (for example regulatory and legislative compliance and the provision of financial information to the Westpac Group such as annual and half yearly financial statements, interim management accounts, cash flow forecast and a covenant compliance certificate).

Covenants contained within a customer's loan facility agreement are based on an assessment of the customer's credit risk as well as standard and sector-specific guidelines. Therefore, they are individually tailored to each customer, including specific indicators of deterioration in risk grade.

Both financial and non-financial covenants are key in enabling the management and mitigation of the risks associated with extending credit facilities. Non-financial covenants, such as the provision of financial statements and management accounts, provide valuable and transparent information to the lender about how a business is performing on an ongoing basis. This is particularly important where the customer is required to make limited scheduled repayments, for example, asset based finance.

3.2 Covenant breaches

The breach of a financial covenant does not necessarily lead to an immediate acceleration of the loan and commencement of enforcement action to realise security. Rather, a review of the customer's financial position and consideration of other appropriate options would be a common response.

The Westpac Group submits that while financial covenants are often not the sole basis for accelerating a loan and proceeding to enforcement, they are an important and appropriate element of business credit contracts.

Breaches of covenants are a key indicator of financial distress and potential increases in the risks associated with extending facilities to a customer. This enables the Westpac Group to review its position, engage with the customer at an early stage to identify the cause of the

deterioration, assess the impact this may have on the customer's ability to repay its loans and to implement a plan to resolve any issues and restore financial viability. This process can assist the customer to avoid monetary defaults. Such mechanisms are therefore prudent for both the Westpac Group and for the customer.

If covenants could not be applied the risks associated with extending facilities would increase, particularly for unsecured lending. This would impact lending appetite, including a re-assessment of the level of facilities we would be prepared to extend and the terms on which those facilities were extended. For example:

- Appetite to extend unsecured credit to customers would reduce, resulting in smaller facilities;
- Additional security coverage required;
- Increased requirement for facilities to be amortising; and
- Increase in interest expense and associated charges to compensate for the increased risk.

All of the above may adversely impact a customer's ability to successfully pursue its business strategy. We therefore do not consider that restrictions should be placed on the use of covenants in credit contracts. The Westpac Group is therefore particularly concerned about the impact of the enactment of the *Treasury Legislation Amendment (Small Business and Unfair Contract Terms) Bill 2015*. We supported the submission to the Senate Economics Legislation Committee lodged by the Australian Bankers' Association and anticipate a significant risk to lending appetite to Australian businesses given the ABA's recommended technical amendments were not made.

Where the Westpac Group applies covenants we do not consider these are applied in a non-transparent manner. Nevertheless, the Westpac Group is committed to continuous improvement. For example, in 2013 our business lending covenants were reviewed for consistency across the Group and were redrafted in plain English. Our business lending documentation will be revisited again as part of our implementation of the *Treasury Legislation Amendment (Small Business and Unfair Contract Terms) Act 2015*.

We note the Government, in its response to the Financial System Inquiry, has supported the Inquiry's call for industry-led initiatives to improve disclosure of risk and fees. The Westpac Group is also supportive of the industry's move to plain-English documentation.

4. Approach to customers in financial distress

The Westpac Group has processes in place for all our customers in difficulty including SME, Commercial and Institutional businesses. Our approach in these circumstances is case-by-case with a focus on early identification of issues, communication and working with the customer.

For example, the Westpac Group:

- Encourages our customers facing financial difficulty to talk to us directly, treating every case individually.
- Provides specific relief to customers in difficulty due to natural disaster where appropriate for example, deferred payments, loan restructuring, discounted refinancing and interest penalty and fee waivers.
- Finds solutions for customers experiencing financial difficulty that will, to the extent possible, seek to ensure the customer's business is sustainable and can be restored to good health.
- Ensure that where a customer has not met their repayment requirements all discussions are respectful and consider the financial goals of the customer, and that we comply with all relevant legal requirements.

Our priority is to find solutions that will, as far as possible, seek to ensure the customer's business is sustainable and can be returned to good health. We also seek to balance the requirement for ensuring that we protect the financial interest and impact on the Westpac Group with the customer's financial goals.

The Westpac Group's own principles of support for customers facing financial difficulty are further supported by our obligations under the Australian Bankers' Association's *Code of Banking Practice* ("the Code") as a Code Subscriber⁵.

Under Clause 28 of the Code we have an obligation to help our retail and small business customers try to overcome financial difficulties with any credit facility they have with the Westpac Group. This includes:

- Dealing with any authorised financial counsellor or representative of the customer where we will meet to discuss options available; and

⁵ The 2013 Code covers an individual or small business that is an actual or prospective customer involved in retail banking transactions. Any small business that has less than 20 (full time or equivalent) people is covered, as well as a goods manufacturing business that has less than 100 (full time or equivalent) people.

- Making information about our processes for dealing with customers in financial difficulty available on our website or in another form requested by the customer.

It is industry practice to try and resolve the repayment of debt without relying on the legal rights of loan contracts that enable lenders to enforce mortgage agreements. Our preference is always to work with the customer and allow them time to undertake key actions within a mutually agreed strategy. Such a strategy assists the customer to restore its financial position, preserve value and reduce costs.

4.1 Regulatory requirements associated with impaired loans

Compliance with prudential requirements requires the Westpac Group to recognise, measure and report on, and provision for, impaired facilities.

It is important to note that a loan is not automatically considered as 'impaired' if a customer has defaulted under the terms of their contract. Rather, impaired assets are formally defined under APS 220 as those exposures that have deteriorated to the point where full collection of interest and principal is in doubt, based on an assessment of the customer's outlook, cash flow, and the net realisation of value of assets to which recourse is held (i.e. the ability for full collection of interest and principal is in doubt). The decision of an ADI to categorise a loan as impaired does not impact the principal amount the customer owes. Rather, repricing of a loan may occur when the customer's risk grade deteriorates to reflect the higher risk of the lending.

Nor do all events of default result in enforcement action, such as the Westpac Group taking possession of assets. Both loans in default and/or impaired loans can be rehabilitated to a satisfactory position under our credit risk management framework. It is the Westpac Group's preference to work with the customer to restore a customer's financial position. This process is explained further in the sections below.

An increase in impaired credit exposures can adversely affect the Westpac Group's liquidity, capital resources, financial performance and financial condition. In particular, there are implications for the amount of regulatory capital we are required to hold against impaired loans. This reinforces the absence of any commercial justification for the Westpac Group to 'artificially construct' a default or impair a credit exposure.

4.2 Event of monetary and non-monetary default

A customer monetary default is deemed to have occurred when the Westpac Group considers that either or both of the following events have taken place:

- the customer does not pay its credit obligations to its financiers on time in full, without recourse by any of them to actions such as realising security (where held); and

- the customer is past due 90 or more calendar days on any material credit obligation to its financiers (principal, interest and any other fees and charges). Overdrafts will be considered past due once the customer has breached an advised limit, or been advised of a limit smaller than the current outstandings.

Generally, if a customer is meeting their scheduled principal and interest payments, the loan would not be categorised as in monetary default by the Westpac Group. However, as noted above, the Westpac Group's Terms and Conditions include a number of ongoing covenants that can give rise to a loan being in default for other reasons (i.e. non-monetary default) notwithstanding all payments are up to date.

4.3 Consequences of an event of default

The normal consequences from an event of default is the lender's right to terminate its obligation to lend and make the loan repayable on demand.

In considering how to respond to a default the Westpac Group would assess the nature of the default including, among other things:

- Whether the default is capable of being rectified;
- The likelihood of success of the rectification strategy; and
- The customer's overall approach to addressing the event of default.

In the majority of cases for the Westpac Group a non-monetary default, including Loan to Value Ratio (LVR)⁶, is not the sole reason for enforcement action, even where that option is available under the terms of the contract. Currently, the Westpac Group does not have any matters under recovery subject solely to an LVR default in either the farm or non-farm segments.

However, enforcement of security due to a non-monetary default may occur in certain circumstances, such as an Insolvency Event i.e. external administration (the appointment of an Administrator/Liquidator or Receiver and Manager) by a third party or where there is evidence of fraud. Absent these circumstances the Westpac Group's preference is to work with the customer to reach a mutually agreed work out position taking into consideration the customer's business plan, forecasts and cash flow.

⁶ Loan facility agreements include a maximum Loan to Valuation Ratio covenant that includes either the right to revalue the property annually (if more than one property to revalue a portion of the security properties annually), at any time during the term of the loan or if an Event of Default occurs. Valuations are completed during the course of the loan term as part of a standard review process, for example, every three to four years and when customers move into our specialist risk management unit.

The consequences of an event of default are not automatic. Often there will be a substantial period of negotiation where the default may be remedied before it reaches the stage of enforcement. The Westpac Group may determine to waive the breach or acknowledge the breach and reserve its rights and seek additional information such as current financial statements, cash flow forecasts and updated business plan.

It may also be appropriate for the Westpac Group to engage professional firms (generally with the customer's consent and co-operation) such as investigative accountants, particularly where there is a pattern of covenant breaches.

Customer specific strategies are determined and agreed on a case-by-case basis to ensure each matter is dealt with on its individual merits. Therefore, there is no standard time period provided to borrowers to rectify a default event. Nor is there a standard form of assistance offered.

There are a variety of mechanisms the Westpac Group employs to assist a customer resolve its financial difficulties and restore the customer's loan to a satisfactory risk grade position. This may involve renegotiating the customer's loan facilities either through a Forbearance/Standstill Arrangement, whereby the customer acknowledges default and is given 'breathing space' by way of an agreed extended period of time to resolve their financial difficulties, provided performance milestones are met. For example, this may include the extension of loans that have or will expire, waiver of scheduled loan repayments or an agreement on a period of time where no principal repayments are made.

Alternatively, the Facility Agreement may be renegotiated. Terms renegotiated with the customer in the Loan Facility Agreement include:

- the loan term;
- loan pricing;
- repayment arrangement;
- resetting of financial covenants in line with revised forecasts for cash flow and profitability; and
- any undertaking to sell assets, raise additional equity or security or provide security.

Repricing of a loan may occur when the customer's risk grade deteriorates to reflect the higher risk of the lending.

When it is clear that a customer is in default without the possibility of the customer's financial position and risk profile being rectified then the Westpac Group would move to recover the outstanding amount it is owed through enforcement of security.

In circumstances where the Westpac Group decides to exit a customer relationship, reduce the debt or clear the debt, the Westpac Group ensures that the Westpac Group's intentions are clearly communicated to the customer and that the process is done with respect and an empathetic understanding of the dignity and financial needs of the customer.

Furthermore, while the Westpac Group is entitled to charge default interest following a non-monetary default, this is not an automatic response. It is usual, firstly, for a review to be undertaken and, if possible, other arrangements agreed with the customer before an adjustment to the interest rate is made. The Westpac Group does not charge 'penalty' interest. 'Default interest' or 'interest at the higher rate' generally only apply where the customer is late with repayments or has failed to meet their account limit obligations. It would be unusual for the Westpac Group to charge default interest in situations where we are working cooperatively with the customer on an agreed strategy.

5. Recovery Action

5.1 Our general approach to recovery

Recovery occurs when the Westpac Group makes the decision to exit the relationship with the customer in default and we take action to recover our debt by exercising rights under the security document.

As part of our consideration to move a customer to an exit strategy the following types of characteristics are considered:

- Fraudulent or criminal activity by the customer;
- There is no viable workout strategy;
- Staff have received threats of physical violence from the customer;
- Animal welfare considerations;
- Customer is un-cooperative and/or has a history of failing to deliver on Forbearance/ Standstill arrangements;
- Liquidator / Bankruptcy Trustee is appointed;
- Customer is in Voluntary Administration⁷; or
- Customer has commenced legal action against the Westpac Group.

In practice, there is no set time period for refinancing or the sale of assets. As a guide, the time period for refinance or the sale of assets would be 90 to 120 days. However, in practice the

⁷ In relation to a voluntary administrator, these are generally appointed by the directors of the company itself where the directors have resolved by special resolution to voluntarily wind up the company.

actual time period is negotiated directly with the customer and extensions of time are often provided.

A shorter period of time may be necessary where the financial position of the customer is severely stressed or the value of the business assets and the Westpac Group's security are deteriorating rapidly, or where other factors, such as animal welfare are a consideration. As a matter of principle, the Westpac Group considers that customers require sufficient notice of the Westpac Group's intentions and the time period should be aligned to the particular circumstances of the matter.

Flexibility needs to be maintained to ensure the Westpac Group can address the particular circumstances of our customers in financial difficulty and that any assistance provided is balanced against the credit risk to the Westpac Group. Consequently, the Westpac Group considers that the current regulatory regime governing time frames, including statutory notice periods, are appropriate. Additional compulsory time frames should not be imposed on the industry as this would undermine our ability to provide assistance to customers on a case-by-case basis.

5.2 Appointment of third parties

The Westpac Group has a risk assessment process in place, when considering commencing recovery action against a customer, including approval by senior members of the specialist risk management team. Formal recovery action can include the appointment of a Receiver and Manager, Administrator or an Agent for the Mortgagee in Possession.

In most instances the Westpac Group reacts to the appointment of an Administrator or Liquidator by the Directors of the company. To respond to this event of Voluntary Administration the Westpac Group may:

- appoint its own Receiver and Manager;
- become Mortgagee in Possession (for real property); or
- allow the Administrator/Liquidator to realise the assets of the customer.

As noted above, the Westpac Group's preference is to work through the customer's financial difficulties, without taking recovery action and enforcing the rights afforded to it as creditor under the Loan Facility Agreement and *Corporations Act 2001*.

Therefore, if the Westpac Group appoints a Receiver and Manager without the prior appointment of an Administrator/Liquidator it is normally after all other efforts to resolve the situation have been exhausted. In this instance, the Westpac Group acts to protect its position from further deterioration.

5.3 Obligations associated with the sale of real property

There are strict legal obligations governing the sale of real property.

Section 420A of the *Corporations Act 2001* imposes a legal obligation on a creditor or Receivers and Managers appointed by a creditor to take all reasonable care to ensure a property is sold for not less than its market value, or otherwise for the best price reasonably obtainable (if the property has no market value). Relevant legislation (*Corporations Act 2001* and *Bankruptcy Act 1966*) and case law imposes a duty on each insolvency practitioner appointed over an individual (Trustee in Bankruptcy) or corporation (Receiver and Manager/Liquidator) to act in the best interest of all creditors whether it is a secured creditor or unsecured creditor.

The *Corporations Act 2001* imposes additional legal obligations on Receivers and Managers. For example, to act in good faith. It is important to note that Receivers and Managers must comply with their legal obligations under the *Corporations Act 2001*. Nevertheless, the Westpac Group exercises oversight of the conduct of our agents. For example, regular contact with, and reporting by, the Receivers and Managers to track progress against the strategy. We will assess the Receiver's and Manager's strategy and form our own view on whether this represents the best outcome for the business or sale of an asset. While Receivers and Managers do not have to agree with the Westpac Group's views, Bank approval of the Receivers and Managers strategy is required, including any sale of the business or property (as the Westpac Group is required to release its security).

State based legislation regulates the timeframes and requirements for a mortgagee to exercise a power of sale. For example, the *Real Property Act 1900 (NSW)* and *Conveyancing Act 1919 (NSW)*. These acts impose obligations similar to those imposed by Section 420A of the *Corporations Act 2001*.

To ensure the power of sale is being exercised appropriately under relevant legal obligations, the Westpac Group will generally obtain an updated valuation of the property from an independent valuer.

A valuer is selected from the Westpac Group's panel of property valuers who are subject to accreditation by the Westpac Group and regular review to maintain that accreditation. The valuer is required to comply with the Westpac Group's valuation standard which outlines the basis on which the valuation is completed and the standards the valuer is required to adhere in valuing the property. The valuation is vetted for adherence to the Westpac Group's valuation standard and methodology adopted.

The Westpac Group, and the insolvency practitioners it engages, ensure that the market value of an asset sold is achieved by undertaking a transparent and defensible marketing campaign that is appropriate to the asset in question. The courts have generally endorsed this approach.

The Westpac Group considers that the current regulatory regime governing the sale of real property and fair market value is appropriate. We strongly reject any suggestion that the

Westpac Group inappropriately engineers valuations or engineers defaults on the basis of a breach of an LVR covenant. As noted above, the Westpac Group has a strong commercial interest in ensuring that property is sold for fair market value. For example, to ensure that properties in the surrounding areas, over which the Westpac Group may have security, are not negatively impacted.

6. Dispute resolution

As noted above, the Westpac Group has processes and policies in place to govern the provision of support and assistance to our customers in financial distress. Our dedicated customer relations and dispute resolution teams provide an important avenue for our customers to raise any concerns or complaints. These Internal Dispute Resolution (IDR) mechanisms comply with the Australian Securities and Investment Commission's (ASIC) requirements including Regulatory Guide 165 Licencing Internal and External Dispute Resolution.

In addition to IDR, retail and small business customers have access to External Dispute Resolution through the Financial Ombudsman Service (FOS)⁸. The Westpac Group is obligated under the Australian Bankers' Association's Code of Banking Practice to provide customers with access to an independent external dispute resolution service. FOS provides an important forum for customers to have IDR decisions reviewed.

Customers may also make complaints related to compliance with the Australian Bankers' Association Code of Banking Practice with the Code Compliance Monitoring Committee.

7. Ongoing commitment to drought-affected customers

The Westpac Group acknowledges that the drought in parts of Queensland and NSW is particularly challenging and putting farmers, their families and communities under a significant amount of stress. The success of our business relies on the success of our customers. For example, it is not in our interests to take possession of drought-affected properties. While we have very limited exposure to the current problems, the Westpac Group remains committed to assisting our customers in drought-affected regions.

We understand that lending to agricultural businesses requires us to take a long-term view on the position of our customers and work with many customers through the cycle over a number of years. We have a long history of working with farmers through business, weather and seasonal cycles and changes in market conditions. Our experience indicates that it takes commercial customers in difficulty an average of 2 to 3 years to restore their credit standard

⁸ FOS Terms of Reference (current as of 15 January 2015) specifically exclude disputes involving recovery of a debt from a small business involving a credit facility that exceeds \$2 million. However, FOS and the Westpac Group have agreed for FOS to determine a matter outside the FOS Terms of Reference.

back to an acceptable level of financial viability. However, in some circumstances it can take longer for a customer to rectify their financial position and, as mentioned throughout, each remediation is managed on a case-by-case basis.

As part of our approach to agribusiness financial difficulty, we encourage our customers to use Rural Financial Counsellors and use independent mediators to help reach agreement on a debt reduction strategy. The Westpac Group strongly supports the national harmonisation of farm debt mediation as a way to enhance consistency and certainty. For example, in NSW the *Farm Debt Mediation Act 2011* requires formal mediation, where the customer has elected to mediate, before a mortgagee can take possession of a property or other enforcement action under a farm mortgage. In the Westpac Group's experience, the involvement of an independent farm debt mediator has usually resulted in a mutually successful negotiation for both the Westpac Group and customer.

The Westpac Group also has a package of specific measures in place to support drought-affected farmers, which are designed to ensure that viable operators are able to stay on their properties and underpin the long-term sustainability of their farms. These support measures are negotiated on a case-by-case basis with the customer but may include freezing credit card and home loan repayments for a period of time to provide some additional breathing space.

The Westpac Group also has a long history of supporting communities in distress, including the provision of community grants and donations. For example, Westpac Agribusiness has recently donated \$20,000 to GIVIT which will assist in building a platform to enable donations or support to be allocated to those that need it the most in drought affected areas. Westpac is also engaged in the Queensland Drought Appeals to raise awareness of the drought and distribute donated funds and the Queensland Think Tank to discuss long term sustainable solutions to the drought.

8. Conclusion

In summary, the Westpac Group is committed to supporting the success and viability of our business customers. This includes working closely with our customers when they experience financial distress. In these circumstances, our approach is focused on early identification and a case-by-case basis to ensure the individual circumstances of each customer can be appropriately addressed.

Both Financial and Non-Financial covenants play an important role in facilitating early identification of any difficulties in a business. The Westpac Group does not engage in practices to artificially engineer a business default, including revaluation of security.

Where a matter does proceed to enforcement, and the Westpac Group takes action to recover our debt by exercising rights under the security document, we consider the existing regulatory regime is appropriate.

However, the Westpac Group does support two other areas of reform:

- 1) National harmonisation of Farm Debt Mediation (FDM); and
- 2) Continued industry-led initiatives to move to plain-English documentation.