

12 June 2012

The Secretary  
Senate Economics References Committee  
PO Box 6100  
Parliament House  
**CANBERRA ACT 2600**

Dear Sir

## **Banking Sector Inquiry 2012**

### **Introduction**

Bank of Western Australia Ltd (Bankwest) is pleased to provide its Submission to the Senate Economics References Committee on its inquiry and report into "*An examination of recent developments in the banking sector arising out of the impact of the global financial crisis and subsequent events*".

### **Scope of Bankwest's Submission**

Bankwest is a wholly owned subsidiary of the Commonwealth Bank of Australia Group (CBA). CBA is making a submission to the Inquiry, as is the Australian Bankers Association inc (ABA). To avoid duplication Bankwest will not address matters to be dealt with in the CBA and ABA submissions and will primarily focus on matters within the terms of reference of particular relevance to Bankwest.

### **Background**

Bankwest commenced its operations in 1895 as the Agricultural Bank of Western Australia.

Bankwest offers its customers retail and business banking services via its Retail Division and its Business and Private Banking Divisions and has over 1.1 million customers. Bankwest has total assets (loans and acceptances) of \$79 billion and liabilities (including deposits) of \$74 billion as at 31 December 2011. The Bank is active in all banking segments including lending for personal, housing, business and rural purposes and offers a wide range of deposit products. Bankwest's services are offered throughout Australia via 142 stores, 47 Business Banking Centres, access to a network of over 4,000 ATMs, and 24 hour telephone and internet banking.

Many of Bankwest's products are market leading and award winning and Bankwest has introduced a number of innovative and competitive products into the Australian banking market such as online savings accounts for retail and business customers, fee free transaction accounts, and on line personal loans and home loans.

Bankwest employs over 4,000 staff and is actively involved in the community with sponsorships and community support provided to a variety of organisations including Telethon, Redkite, Teen Challenge WA, the West Australian Ballet, CEDA, the Committee for Perth and a number of other sporting, business and community groups.

Since the CBA's acquisition of Bankwest on 19 December 2008, Bankwest has continued to operate under its own ADI licence, management and governance structure. In accordance with APRA guidelines Bankwest is in the process of returning its ADI licence to enable it to operate under CBA's ADI licence.

### **Bankwest's Submission to the Inquiry**

The terms of reference (TOR) that Bankwest wishes to comment on are:

TOR d). "the impact on borrowing and lending practices in the banking sector both during and since the global financial crisis".

#### Lending Practices

As some of the submissions to the Committee have touched upon matters particular to Bankwest and its lending practices during and since the GFC, Bankwest makes the following submissions:

- Lending policies – the Bank's lending policies and procedures require an appropriate assessment of a number of matters. Prior to and since the GFC Bankwest, like many financial institutions, has continually reviewed and adjusted its lending policies.
- CBA acquisition - the CBA sale agreement and purchase price adjustment process did not have any impact on Bankwest's approach to dealing with customers. The acquisition did not cause any change to existing contractual arrangements between Bankwest and its customers.
- Defaults – it is not in Bankwest's interests, and it makes no commercial sense, to "manufacture" defaults or to cause or increase losses.
- Customers in financial difficulty – customers in difficulty have been dealt with appropriately and on an individual basis, not on a global basis.
- Receiverships - Bankwest's level of receivership appointments have not been unreasonable or aggressive and are in line with its market share.
- Valuation process – where Bankwest uses valuers they are independent and have in place proper standards and processes.

#### Bankwest Lending policies

The Bank's lending policies and procedures require an appropriate assessment of a number of matters including: a customer's capacity to repay: the assets and property offered as security: the conditions including loan covenants under which the lending is provided: and the customer's character and conduct. The lending assessment and approval process is managed through the Bank's risk framework and involves a number of levels and stages of review and sign off.

Where lending is approved it is on the basis of customer agreed loan agreements and appropriate covenants which are documented by the Bank. They typically include undertakings to enable the Bank to monitor the customer's capacity to repay and the value and quality of the collateral for the loan. For business lending these covenants can include: operational and financial reporting obligations: maintenance of adequate free cash flow to meet interest (Interest Cover Ratio / ICR) and total debt service obligations (Debt Service Ratio / DSR); and security coverage (Loan to Valuation Ratio / LVR). These obligations, including LVR, are agreed upfront with the customer and are to be met throughout the period of the loan.

The CBA's acquisition of Bankwest on 19 December 2008 did not cause any change to existing contractual arrangements between Bankwest and its customers. The contractual arrangements continued in accordance with their individual terms and conditions.

Prior to and since the advent of the GFC, Bankwest, like many financial institutions in Australia, has continually reviewed and adjusted its lending policies to adapt to the changed economic conditions, and changes to the regulatory environment. The ABA and CBA submissions comment on the economic and regulatory changes in more detail. An example of an adjustment to lending policies Bankwest has implemented as a result of the changing economic and regulatory environment is a reduction in the maximum LVR for certain asset types for new lending. The overriding position of Bankwest is that it is neither in the Bank's nor the customer's best interests to be anything but responsible in its lending practices.

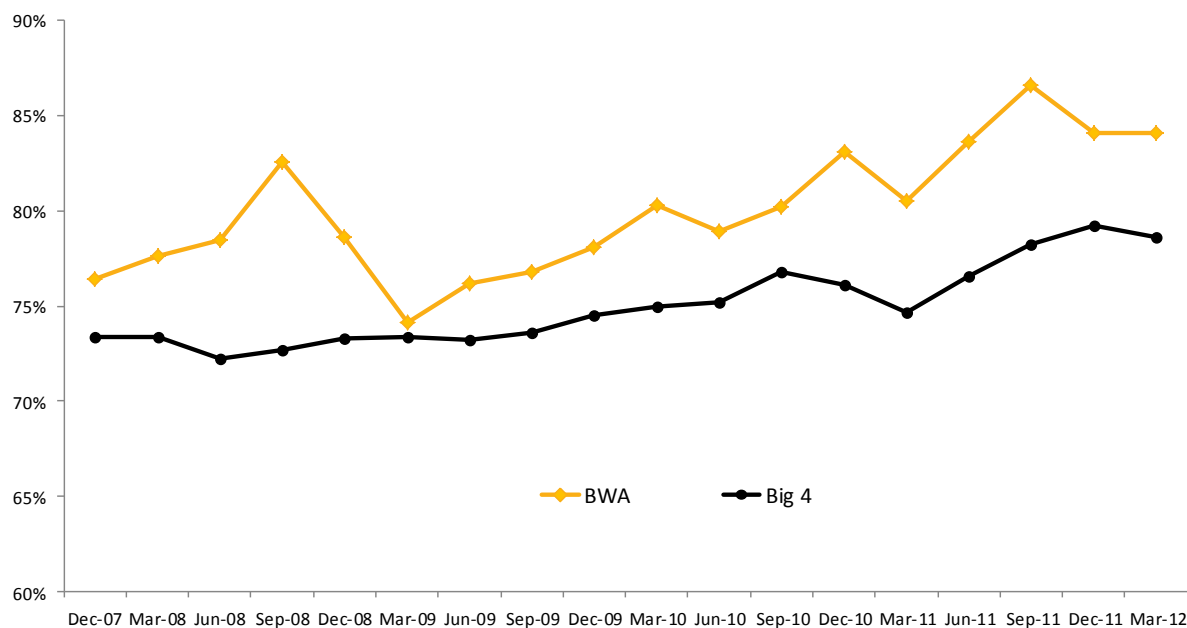
Any amendments to lending policy did not impact existing loan agreements and covenants. However during this period obtaining finance with other financial institutions may have become more difficult for some customers due to the review of lending policies by other financial institutions, weak credit growth and declining property asset values. These factors have impacted on some Bankwest customers seeking to refinance elsewhere, for example when their existing contractual loan period came to an end.

Bankwest did not stop lending at any stage and has continued to responsibly grow its customer base in both retail and business.

Year	Bankwest Retail Customer Base	Bankwest Business Customer Base	Bankwest overall Customer Base
2009	960,500	26,700	987,200
2010	1,036,500	26,800	1,053,300
2011	1,082,400	28,900	1,111,300

During this period Bankwest has also maintained and increased its customer satisfaction levels.

**Bankwest customer satisfaction data since December 2007**  
 (source: Roy Morgan MFI customer satisfaction survey)



***Bankwest’s approach to dealing with customers in difficulty***

Unfortunately due to broader economic factors or their individual circumstances some customers do experience financial difficulties. The Bank strongly prefers to work with customers experiencing financial difficulty to help them resolve their problems as this gives the best outcome both for Bankwest and the customer. Bankwest’s approach is to abide by the standards of good banking practice and deal with customers on a case by case basis and work through a range of options to best manage their situation.

Where a customer fails to meet their loan repayment obligations the Bank also has monetary default reporting guidelines in accordance with APRA and APS guidelines.

The CBA submission sets out the facts relating to the sale agreement the CBA entered into to purchase Bankwest. There is some public conjecture that the sale agreement provided an incentive for the CBA and Bankwest to manufacture defaults and losses on Bankwest customers to achieve a purchase price benefit. This conjecture is incorrect. Any losses that Bankwest incurred in its dealings with customers post acquisition date were borne by Bankwest and could not be “clawed back”. Accordingly it is not in Bankwest’s interests, and it makes no commercial sense, for it to manufacture defaults on customers or to cause or increase losses on lending deals.

Bankwest did not undertake any orchestrated or global approach to customers. In the period following the GFC Bankwest did experience an increased level of loan impairment in its business lending portfolio, primarily in the 2009/2010 period, but this was due to economic

conditions that impacted some of its customers. The impact of the GFC was not widespread across all Bankwest customers but was of most impact to particular sectors and regions of its business loan exposures. During this period the Bankwest retail bank did not suffer any material increase in impairments.

A reasonable proportion of Bankwest's loan impairments were contained in its property lending portfolio and in particular a number of residential, hotel, aged care and land development exposures in regional Queensland and New South Wales. These sectors and regions in general have been suffering difficult financial circumstances since the GFC began such as lower revenues and earnings and a diminution in the value of the underlying assets.

Bankwest was also co-lender in a number of high profile transactions such as ABC Learning Ltd and Great Southern Ltd where large losses were incurred by the joint lenders.

In many cases where customers were impacted the Bank entered into agreed arrangements with the customer to achieve an improvement in their financial position, and the Bank provided extensions of time or other favourable terms to assist them. Unfortunately, in a small number of cases the customer could not deliver an improvement in their financial circumstances and / or failed to comply with the principal terms of their agreements and a decision was taken by the Bank to take enforcement action.

### ***Receiverships***

Any decision by Bankwest to appoint receivers is not taken lightly and is based upon the particular circumstances of the matter. The ability to appoint receivers only arises if the customer is in default of their financing agreements with the Bank. In addition a number of the characteristics below are usually present before Bankwest makes a decision to appoint a receiver:

- The customer breaches their monetary or other contractual obligations
- Interest is not met when due
- The customer's debt levels are increasing and unsustainable
- A third party creditor (e.g. ATO) has initiated recovery action against the customer
- Loss making operations or holdings are deteriorating the customer's equity position
- The underlying project or development has stalled or costs have blown out
- The customer is unable or unwilling to deliver an appropriate strategy to resolve the matter
- Further delay or inaction would only compound the problem

Bankwest's level of receivership appointments have not been unreasonable or aggressive and are in line with the bank's market share. Since 2009 the number of Bankwest Business customers placed in receivership has been small (less than 85 in each year) and, when compared with the overall number of industry wide receivership appointments, are consistent with Bankwest's market share during that period (in the range of 4% to 6%).

Where receivers are appointed they have a number of obligations to act in good faith, including an obligation, when property of a corporation is sold, to sell the property for not less than its market value (Section 420A Corporations Act). Where receivers are appointed to a company they are the agent of the company and their primary obligations are to the company. Receiverships often arise where both the customer and the Bank may incur a loss so it is clearly in the Bank's interests to ensure that property is sold at market value and that receivers and other costs are as reasonable as possible.

## ***Valuation process***

The valuation process generally arises at three stages: the initial funding approval process: during the course of a review of existing facilities: and during the course of the sale of assets. Valuations during the course of a review of existing facilities arise from time to time under the existing terms and conditions in the customer's contractual arrangements. The reviews are conducted to ensure existing obligations such as repayment capacity and/or the security position and agreed LVR's are met and to retest cash flow and asset values. This is standard industry practice and consistent with APRA guidelines.

Unfortunately the GFC saw the market value of a number of asset types reduce, particularly in commercial property. The deterioration of asset values was not isolated to Bankwest customers, as commercial property valuations were generally down across a number of sectors and regions.

Bankwest relies on expert preferred lists (panels) of independent external valuers to undertake mortgage valuations under strict industry standards. This process ensures that valuations are provided by skilled and independent valuers with no coercive influence by the Bank.

The valuer must:

- Be registered or licensed;
- Comply with the regulatory requirements governing licensing or registration;
- Be a member of the Australian Property Institute (API), as a Certified Practising Valuer (CPV);
- Comply with annual compulsory training requirements;
- Comply with the Code of Ethics and Rules of Conduct of the API;
- Be suitably experienced to undertake required valuations;
- Have suitable and current professional indemnity insurance cover.

The process and standards for valuations includes:

- Detailed formal written instructions are issued to Bankwest preferred valuers to undertake valuation reports;
- Valuations are to be based on current unencumbered market value (International Valuation Standards);
- Valuations must be completed in accordance with API Mortgage Security Professional Practice Standards and Bankwest reporting requirements;
- Valuers must not undertake any valuations where a conflict of interest may occur;
- A Director / Head of Valuations of the valuation firm must complete (or countersign) valuations;
- Valuers must maintain strict confidentiality in respect of customer details.

The Bank's standard process is not to provide to valuers the particular circumstances of the proposed lending to be provided to the customer or any loan to valuation ratio hurdles that need to be met. When a customer is in default the Bank typically does not provide the valuation to third parties or to the customer, for appropriate commercial reasons. For example this may adversely influence the sale price if the asset is in the process of being sold.

## ***Complaint handling***

Where customers have grievances or complaints they wish to raise with the Bank they have access to a number of avenues to have their matters addressed. Bankwest adheres to a comprehensive complaints handling process in accordance with the Code of Banking Practice, ASIC legislation and guidelines, the Financial Ombudsman Service (FOS) terms of reference, and the Bank's internal policies and processes. Complaints may be received either directly from customers via phone, letter, fax, email or the public website, or escalated from stores or internal departments. The Bank has a dedicated internal dispute resolution division, Customer Relations, which has a primary focus to provide the Bank's customers with an efficient, fair and accessible mechanism for resolving their complaints.

FOS provides an external dispute resolution service available to all Bank customers free of charge. When a complaint is made to the FOS, the matter is initially referred to the Bank providing an additional opportunity for the Bank to resolve the complaint directly with the customer. If the matter is not resolved, and it is within the terms of reference, the FOS will then deal with the matter.

Finally if customers are not able to resolve the matter through the internal and external dispute resolution procedures in place they can take their matters or claims to appropriate Courts or tribunals.

### **(f) "any other relevant matters"**

Bankwest acknowledges that there has been some recent media coverage, regarding our dealings with particular customers. In assessing this media coverage it is important for the Committee to be aware that, due to privacy and confidentiality obligations, the Bank is often prevented from making full disclosure to the media about a customer's affairs. In addition some of the submissions to the Committee concern individual customer matters that are, or have been, the subject of review and determination by the Courts or the Financial Ombudsman Service.

Thank you again for the opportunity to make a submission to the Committee.

Yours sincerely

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**Bank of Western Australia Ltd**