SENATE ECONOMICS REFERENCES COMMITTEE

Inquiry into the post-GFC banking sector

QUESTIONS ON NOTICE

Bankwest

10 August 2012

Question 1 (Hansard Ref: p. 57)

Senator WILLIAMS: Why has Bankwest registered the websites unhappybanking.com and unhappybanking.com.au?

The domain names in question were registered by Bankwest before the launch of the unhappybanking.net.au site. It is not unusual for an organisation to take steps to protect its brand through registering domain names that may have a likeness to the name or other aspects of the brand.

Question 2 (Hansard Ref: p. 64)

Senator WILLIAMS: You have given us the percentage of your customers who are impaired et cetera—a very good percentage. Do you know what percentage of your customers who were developers on the east coast became impaired?

Mr De Luca: I do not have that statistic.

Senator WILLIAMS: Would you be able to take it on notice? Do you have any idea? That seems to be the sector. East coast development and hoteliers seem to be where the problems arose.

Mr De Luca: Those are industries that were probably the hardest hit as well.

The percentage of East Coast property developer, property operator and pubs customers who became impaired during the period from CBA acquisition (December 2008) to date (30 June 2012) varied over the course of this period and was within the range of 0.85% to 7.23%.

Question 3. Lauderdale GST query

Whilst the committee has not specifically requested information in relation to the Lauderdale matter that was raised during the hearings, Bankwest would like to provide further information:

The question from Senator Williams was as follows:

"Why - when you got that $9.9 million you clearly knew that $900,000 was the GST component. Why would you, as Bankwest, not hand that over to the Tax Office? Why did you have to get the Justice Ron Merkel to hear this case? "

A company's tax liability (including GST) is a matter for the directors of the company to manage in the normal course. The Bank does not manage the day to day affairs of its customers and therefore does not meet any GST payments direct to the ATO on behalf of customers. If Receivers are appointed and GST liabilities arise, such as on the sale of an asset, then the Receivers are responsible for payment of the GST. The Receivers and the Bank are not responsible for payment of GST liabilities that arise prior to appointment.

In respect of the specific Lauderdale query the background is that in February 2010, Lauderdale exchanged contracts for the sale of its property with a purchase price of $9 million plus GST of $900,000. The Bank had not appointed receivers to the Company in question. As the sale proceeds were insufficient to repay the debt due to Bankwest, Lauderdale queried whether it was entitled to keep the GST component of the sale proceeds in the sum of $900,000 and later remit those monies to the ATO. At this time the Bank had concerns that the customer was diverting funds to related parties. Rather than allow this query to hold up settlement, Lauderdale and the Bank agreed to proceed on the basis that the funds would be paid into a solicitor's trust account at settlement and the parties would agree to abide by the views of Ron Merkel. Following Ron Merkel's opinion the $900,000 was released to Lauderdale. The money had never come into Bankwest's control. As the sale was made by Lauderdale prior to the appointment of any receiver, the operation of the GST law is such that any GST obligation is that of Lauderdale and not the Bank who had no obligation to account to the ATO for GST.

Question 4 – Hansard Ref p. 61

CHAIR: Just looking at a couple of general examples. Before you came in we heard—not directly from the person involved, but from a person who was aware of a customer who had been talking with Bankwest—of a particular case where the customer had been asked by Bankwest to refinance. They had found a bank to refinance, being Westpac. Westpac was apparently about to settle the loan and they contacted Bankwest and said it was about to happen. On the Friday, I think, Westpac told Bankwest they were ready to settle on theWednesday, and Bankwest sent the receivers in on the Monday. Does that sound like something that could have happened? [Senator Bushby was referring to Mr Ralph Binks/Allied Hospitality –submission 68]

The full context of the matter is not accurately summarised in the query put forward. The Bank worked with the client over an extended period of time and at no stage was there formal approval for refinance in place from Westpac. In addition at the time of the appointment of receivers the customer had tax debts totalling approx. $1.7m and the funding request to Westpac was not sufficient to pay out the Bank's debt and the tax debts (it was $1.5m short). This matter has also been before the Queensland Supreme Court where the customer challenged the appointment of receivers. At the hearing Westpac produced its file and the documentation produced by Westpac did not disclose any approved unconditional offer by Westpac to the customer. The matter

was heard on 6 September 2010 and after assessing the evidence and hearing argument from counsel for both the customer and the Bank, the Court dismissed the customer's application.

Question 5 – Hansard Ref p. 61.

CHAIR: Similarly, we heard of a number of situations similar to this involving developments being financed by Bankwest. In a number of cases there were pre-sold units. In one case there were something like 14 units and 10 units were pre-sold with contracts signed up and deposits paid. Bankwest stopped the funding two-thirds or three-quarters of the way through the construction despite the fact that there were pre-sold contracts for $8.5 million. A number of things occurred, the receivers came in and it was all sold off at something like $2.5 million.

This despite the fact that there were $8.5 million of pre-sold contracts on the books, which obviously went by the wayside as a result of the receivership. That is not the only case; it was just an example. In those sorts of circumstances it seems it would have been in the interests of Bankwest and the customers to have proceeded with completion of the contracts rather than selling out for something one-third or one-quarter of the value of the pre-sold contracts. Are you aware of circumstances like that having happened? <This refers to Mr Shannon>

There were 7 pre sales for the development in question. One of the pre sales had a $1.00 deposit and one other pre sale had a deposit met by an offset on another development, i.e. no cash deposit was received. Each of the pre sales had a sunset date which meant that the agreement expired on that date. Mr Shannon appointed voluntary administrators to the development company on the project in September 2008. The Bank did not appoint receivers to the development company until 1 July 2009. During the period prior to appointment of receivers Mr Shannon was provided with the opportunity to arrange a sale of the development himself and he made representations that he had a purchaser, but no sale eventuated. When receivers were appointed on 1 July 2009, five of the pre sales had expired and the other two were due to expire in July 2009 and September 2009. The property was later sold after an appropriate sales process.

The building company for this project was a related Geoff Shannon entity, C2C Developments Pty Ltd which was placed into voluntary administration by Mr Shannon in September 2008, with almost $10m in unsecured debts owed to 192 creditors. At the C2C Developments meeting of creditors in December 2008 the administrator noted that the company had been insolvent since at least 2007: "The Chairman explained that he has evidence that the company had traded whilst insolvent for at least 12 months prior to his appointment as Administrator. The Chairman went on to say that while it was possible to commence legal proceedings against the Director (Geoff Shannon), this was a costly option and needed to be funded".

Question 6 -The Committee asked:

Bankwest's submission states: 'it is not in Bankwest's interests, and it makes no commercial sense, to "manufacture" defaults or to cause or increase losses'. If the bank has decided that it does not want to continue with the loan and that a receiver will likely be appointed, is it not in Bankwest's interest to increase the losses (through default interest of 18 per cent) because of the tax benefits through a larger write-off?

It is never in the interest of the bank for losses to be increased. All interest income (including default interest) that the Bank accrues is taxed accordingly as income meaning an increased tax liability. If this interest is subsequently written off the impact is tax neutral, i.e. the tax liability on the interest is offset by the tax written off. Where a property that is held as security is sold for less than the corresponding debt, the bank writes off capital and the negatives of this far outweigh any interest income written off.

When a customer loan is assessed as impaired the outstanding loan is classified as non-accrual. From this point any interest incurred is added to the loan but not recognised as income. Instead of recognising as income the interest is capitalised on the balance sheet (the capitalised interest is known as "interest reserved"). If the loan is subsequently written off, the interest added to the loan after impairment does not increase write-off expense as it is offset with the matching interest reserved account, and this is an offset between two balance sheet accounts. As such, the Bank does not receive any tax benefit from this process.

This Bank's treatment of interest and write offs is consistent with banking industry standards.

Ultimately the Bank is a business and it is always preferable to avoid making losses from our lending, as a loss on a loan means less return to shareholders. Bankwest meets all of its tax obligations and paid $232 million in income tax this past financial year.

Question 7

Bankwest's submission states: 'FOS provides an external dispute resolution service available to all Bank customers free of charge'. Does Bankwest accept that the majority of borrowers that have made submissions to this inquiry would not be able to access FOS as their case would be outside its terms of reference? If this is accepted, how does Bankwest expect customers who have issue with the bank to proceed?

There are a number of avenues open to customers to deal with issues they wish to raise and FOS is one of those avenues. The FOS has jurisdiction to deal with matters in dispute of up to $500,000 with the power to order compensation of up to $280,000. The underlying loans can exceed these limits, for example on a loan of $10m a dispute about $490,000 of interest and fees on the loan can be within jurisdiction. This means that FOS does have wide powers to deal with a number of significant matters in dispute, including business lending customers. The FOS has dealt with Bankwest business lending customers of this nature, including some matters where the debt has been in the millions. It is a matter for FOS to determine if a complaint is within their

jurisdiction. If the customer has a matter beyond the FOS jurisdiction there are other avenues such as the Courts or tribunals where the customer can have their matters dealt with.

Question 8

Bankwest's submission states:

'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'.

A number of submitters have referred to revised facility terms being issued without warning, "congratulating" them that their terms had been revised. One example was given where a number of letters of variation were issued over time, including one which significantly brought forward the expiry date of their facilities:

'On going through my files and finding the paperwork of the variation letter of October 2009 I noted with horror that Bankwest had altered my two loans from 18.5 years and 28.5 years to run, to 6 months indeed expiring in April 2010'. (Ms Fiona Howson, *Submission 39*, p. 5; in July 2010 Ms Howson was informed that the facility would be terminated).

How can Bankwest's statement be reconciled with the evidence received by the committee that contractual arrangements were changed?

The changes to the terms of Ms Howsons's loans came about after she requested additional funding from the Bank to complete construction of her property and the changes to the periods of the loans brought them into line with the anticipated date of completion of the construction. The changes to the amount and period of the loan were the subject of discussions, emails and documentation with the customer and were clearly set out and acknowledged by the customer. The Bank subsequently extended the period of the loans on two occasions and only proceeded to take action after a number of defaults became evident including the non-payment of interest, failing to meet reporting obligations, the customer providing a false asset and liability statement to the Bank (excluding assets that were held by the customer) and the customer allowing their solicitor to take a mortgage over a property held as security by the Bank without obtaining the consent of the Bank.

Question 9

Bankwest's submission states: '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'. What policies/operating procedures do you have in place to ensure that these principles are applied throughout Bankwest's offices?

As mandated by APRA and as part of prudent risk management, the financial position of customers is tracked on a regular basis. Each day customer relationship staff view reports that notify of customers in excess on their accounts/ overdrafts or on monthly arrears reports on lending. Some clients also have quarterly financial covenants that we monitor to ensure the health of their business is sustained with lending subject to a detailed annual review each year. Senior management have line of sight around whether this monitoring is occurring.

The goal of this intensive monitoring is to identify signs of deterioration in the customer's financial profile early and then work with the customer to understand the position and take actions with the customer to rectify the position. If the customer's position continues to deteriorate the customer is then placed on a monthly report that is discussed with senior bank management where appropriate strategies for the client are decided on and monitored, ensuring senior level oversight.

When a customer experiences prolonged or severe financial difficulty, the Bank's approach is that there is a point in time where the client will then be transferred to our Credit Asset Management area for more intensive management by our staff who are most experienced in dealing with customers who are exhibiting a weakened financial position. They will then continue to work through the matter with the customer to attempt the rehabilitate the situation.

Question 10

In total, how much in penalty interest has Bankwest charged its small business customers since Bankwest was acquired by the Commonwealth Bank?

When a customer defaults and the decision is made to apply default interest, the rate is determined on a case by case basis. The requested information is not tracked and we are not in a position to provide it.

Question 11

Senator Eggleston asked:

How do you determine the period in which a foreclosed property must be sold? For example, is it weeks or months, based on market conditions or the like?

Once a business is placed into receivership, the receivers work to obtain the market sale price of the business or asset and this includes using their expert judgement on timelines and other commercial issues needed to achieve this. In some cases a timely sale of an asset is the best outcome; however it is noted in reference to the question that it is extremely unlikely that properties would be sold in a matter of weeks and the process usually takes place over a period of months.

We also wish to refer to a statement of Mr Corfield's during the hearings in relation to sales prices in some sectors and regions during the GFC. "In those cases, especially when the market is continuing to fall, it is very often in the best interests of the customer and the bank to act early rather than late".

Question 12

A recurrent issue in a number of submissions is the quick and undervalued sales of properties that have been foreclosed. How do you undertake valuations of property? Do you use the same valuers for commercial, residential and industrial? What checks and balances are in place? How do you select valuers? Does Bankwest receive any financial benefit (eg. commission) from a valuer?

As covered in the hearings, valuers are formally instructed on individual valuations to ensure the valuation is undertaken on the correct basis. At no stage are customer lending or other details provided. Valuers of each property are selected from a pre-approved panel. As covered in Bankwest's submission, to be on our panel valuers 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.

Some of these valuers have a specific focus such as residential valuations or commercial valuations, so when requesting a valuation the right type of valuer is matched to the right type of property.

Bankwest receives no financial benefit from valuers such as commission.

Question 13

Does Bankwest engage in 'fire sales' of properties that have been foreclosed? Submission nine alleges the Commonwealth Bank insisting on a commercial property being sold within five months when the valuation suggested 12 months would be needed (see p. 3). That submission further alleges "CBA has exerted continuous pressure to sell all our properties at any price".

Submission 9 relates to a CBA customer. Bankwest does not engage in 'fire sales' of properties. Once a business is placed into receivership, the receivers work to obtain the market sale price of the business or asset as required under their statutory obligations and this includes using their expert judgement on

timelines needed to achieve this. It is also important to note that it is in the Bank's interest to obtain the best possible price for an asset being managed by receivers.

Question 14

Can a customer seek an independent valuation for the bank's consideration? Are customers entitled to see valuations? If not, why?

All valuers used by the bank are independent and if the customer wishes to obtain a valuation they are given the choice to select a valuer from a number of valuers on our approved panel. In some instances a customer will come to the bank with a valuation conducted by a valuer outside of our panel and whether the valuation can be relied on by the Bank will depend on if the valuer is a reputable company with requisite professional indemnity cover, if the valuation meets the reporting requirements of the Australian Property Institute, if the valuation is current, and if it can be reissued to the bank.

In relation to customers being entitled to see valuations, where a customer is not provided with a valuation, this is typically when a customer is in default. As referenced in the Hansard Report, Mr Corfield states, in relation to the situation where a customer has defaulted and a receiver is appointed, "when the receiver is in they are absolutely bound to get fair market value for what they have in front of them. And, whilst I am sure that most customers would treat that document confidentially, receivers very often make that call that they are not prepared to take that risk".

Question 15

Did your valuation system or process change once the GFC hit?

The basis for instructions to valuers did not change during the GFC.

Question 16

A number of submission have pointed to a lack of transparency and even "secrecy" (submission 111, p. 4) in the whole lending process. What are Bankwest's/Commonwealth Bank's views on this?

For the bank to enter into any contractual arrangement with a customer, the customer must acknowledge and execute loan agreements including written letters of offer. Customers have the ability to seek advice before acknowledging/executing the letter of offer and other lending agreements. Therefore the customer would have full knowledge of the contractual arrangements they are entering into.

If the question is in relation to confidentiality regarding settlement agreements, we believe Mr Cohen's explanation from the CBA during the hearings best sums up what occurs in commercial arrangements in different sectors (including banking):

“Quite outside the realms of banking, whenever parties enter into a settlement agreement it is standard practice to include a confidentiality clause. The reason is that both parties are generally compromising their legal position to some degree and there commercial position to some degree. It is usually not in either party's interest to have that compromise publicly known”