The Commissioner

The Honourable Kenneth Madison Hayne AC

Royal Commission report into misconduct in the banking, superannuation and financial services industry.

Submission by Shane Reynolds

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1. Introduction

Pursuant to the Royal Commissions Act 1902 I note your appointment on 14 December 2017 by the Governor-General of the Commonwealth of Australia, His Excellency General the Honourable Sir Peter Cosgrove AK MC (Retd) as Commissioner to inquire into and report on misconduct in the banking, superannuation and financial services industry pursuant to the terms of reference for the inquiry found within the Letters Patent and enclose herewith my report to the Commission.

Given the definitions as contained in the Letters Patent, particularly, "(e) A person or entity that acts or holds itself out as acting as an intermediary between borrowers and lenders" it is clear that the Royal Commission's parameters also includes the commercial finance sector which is important because it is in this unregulated sector that the concerning lending practices start and regulators thereafter attempt to curtail or eradicate.

I make my observations based on long term commercial experience.

My submissions will address the conduct of financial services entities as defined by the terms of reference, the effectiveness of mechanisms for redress for consumers of financial services who suffer detriment as a result of misconduct by financial services entities, the adequacy of existing laws and policies of the commonwealth relating to the provision of banking and financial services and recommendations to minimise the likelihood of misconduct by financial services entities in future.

2. Terms of Reference (Published 30th November 2017)

ROYAL COMMISSION INTO MISCONDUCT IN THE BANKING, SUPERANNUATION AND FINANCIAL SERVICES INDUSTRY

DRAFT TERMS OF REFERENCE

Context

Australia has one of the strongest and most stable banking, superannuation and financial services industries in the world, performing a critical role in underpinning the Australian economy. Our banking system is systemically strong with internationally recognised, world's best prudential regulation and oversight.

Most Australians are consumers of banking, superannuation and other financial services. The superannuation system alone in Australia has created more than a $2 trillion retirement savings pool, which continues to grow rapidly, and which compels all working Australians to defer income today for their retirement.

All Australians have the right to be treated honestly and fairly in their dealings with banking, superannuation and financial services providers. The highest standards of conduct are critical to the good governance and corporate culture of those providers.

These standards should continue to be complemented by strong regulatory and supervisory frameworks that ensure that all Australian consumers and businesses have confidence and trust in the financial system.

The Government will appoint a distinguished serving or former judicial officer to lead a Royal Commission into the banking, superannuation and financial services industries.

The Commission's inquiry will not defer, delay or limit, in any way, any proposed and announced policy, legislation or regulation of the Government.

Terms of Reference

1. The Commission must inquire into the following matters;

    a) the nature, extent and effect of misconduct by a financial services entity (including by its directors, officers or employees, or by anyone acting on its behalf);

    b) any conduct, practices, behaviour or business activity by a financial services entity that falls below community standards and expectations;

    c) the use by a financial services entity of superannuation members' retirement savings for any purpose that does not meet community standards and expectations or is otherwise not in the best interest of members;

    d) whether any findings in respect of paragraphs 1(a), (b) and (c):

i. are attributable to the particular culture and governance practices of a financial services entity or broader cultural or governance practices in the industry or relevant subsector; and

ii. result from other practices, including risk management, recruitment and remuneration practices;

e) the effectiveness of mechanisms for redress for consumers of financial services who suffer detriment as a result of misconduct by a financial service entity;

f) the adequacy of:

i. existing laws and policies of the Commonwealth (taking into account law reforms announced by the Government) relating to the provision of financial services;
ii. the internal systems of financial services entities; and
iii. forms of industry self-regulation, including industry codes of conduct;

to identify, regulate and address misconduct in the industry, to meet community standards and expectations and to provide appropriate redress to consumers and businesses;

g) the effectiveness and ability of regulators of a financial services entity to identify and address misconduct by those entities;

h) whether any further changes to:
i. the legal framework;
ii. practices within financial services entities; and
ii. the financial regulators,

are necessary to minimise the likelihood of misconduct by financial services entities in future (taking into account any law reforms announced by the Government); and

i. any matter reasonably incidental to a matter mentioned in the above paragraphs, 1(a) – 1(h).

2. In conducting its inquiry the Commission should give priority to matters which in its opinion, have greater potential for harm if not addressed expeditiously.

3. Inquiring into the matters set out in paragraph (1)(f), the Commission:

a) must have regard to the implications of any changes to laws, that the Commission proposes to recommend, for the economy generally, for access to and the cost of

financial services for consumers, for competition in the financial sector, and for financial system stability; and

b) may have regard to comparable international experience, practices and reforms.

4. However, the Commission is not required to inquire, or to continue to inquire, into a particular matter to the extent that to do so might prejudice, compromise or duplicate:
   a) another inquiry or investigation; or
   b) a criminal or civil proceeding.

   And, the Commission may choose not to inquire into certain matters otherwise within the scope of this Inquiry, but any such decision will be the Commission's, alone.

5. The Commission is not required to inquire into, and may not make recommendations in relation to macro-prudential policy, regulation or oversight.

6. The Commission may submit to the Government an interim report no later than September 2018 and must submit a final report within 12 months. The final report is to contain:

   a) its findings; and
   b) any recommendations relevant to the inquiry that the Commission thinks fit.

Definitions

financial service entity means an entity (other than a Commonwealth entity or company) that is:

a) an ADI (authorised deposit-taking institution) within the meaning of the Banking Act 1959;

b) an entity that carries on the business of undertaking liability, by way of insurance (including reinsurance), in respect of any loss or damage, including liability to pay damages or compensation, contingent upon the happening of a specified event, including:

   i. a general insurer within the meaning of the Insurance Act 1973; and

   ii. an entity undertaking life insurance business within the meaning of the Life Insurance Act 1995.

c) a person or entity required by section 911A of the Corporations Act 2001 to hold an Australian financial services licence or who is exempt from the requirement to hold a licence by virtue of being an authorised representative; or

d) an RSE licensee of a registrable superannuation entity (as that term is defined in the *Superannuation Industry (Supervision) Act 1993*) and any entity that has any connection (other than an incidental connection) to the RSE licensee of a registrable superannuation entity.

Macro-prudential policy and regulation means policy and regulation, including as to the structure, role and purpose of financial regulators, that is concerned with containing systemic risk, which can have widespread implications for the financial system as a whole, beyond simply the banking system.

misconduct includes conduct that:

a) constitutes an offence against a Commonwealth, State or Territory law in relation to the provision of a financial service, as existed at the time of the alleged misconduct; or
b) is misleading and/or deceptive; or
c) indicates a breach of trust or duty or unconscionable conduct; or
d) breaches a professional standard or a recognised and widely adopted (conduct) benchmark.

3. Letters Patent (Published 14th December 2017)

The Terms of Reference for the inquiry can be found within the Letters Patent, a copy of the letters patent can be downloaded from the commission website below:

https://financialservices.royalcommission.gov.au/Documents/Signed-Letters-Patent-Financial-Services-Royal-Commission.pdf

4. Background and Experience

I am a fiduciary specialising in mortgage lending (2001-2018) and bestselling self-help and Financial literacy author. I have been widely involved in the finance industry in Australia for nearly two decades and I've lent money for a living for most of my career. I am a member of Flinders University Law School and member of the Economic Society of Australia, New South Wales.

My family history is detailed in the publication by Bond University, 'Stars under the Southern Cross', a centenary of federation celebration project, containing many Queensland family business stories of families.

In 2017 I published a book titled '*GET A SECOND OPINION BEFORE YOU SIGN'* Lifting the Curtain on Lending Practices & the Australian Financial Services Industry. [1] The publication is endorsed by the President of the Finance Brokers Association and 100% of the profits of the same are directed to Aussie Helpers Charity to help Australian Farmers.

5. Unregulated Finance Sector:

To most borrowers seeking funding, the world of lending beyond the major banks is largely opaque. There is no clear signage or Ikea-like how-to-put-it-together instructions to guide borrowers in the right direction to and the best fit for their needs.

The great Australian dream is a belief that in Australia, home-ownership can lead to a better life and is an expression of success and security. But with that comes the process of obtaining a mortgage.

Funding can be a frightening prospect. Many businesses and consumers in Australia have a distinct lack of financial literacy. Traditionally, borrowers have been supported by a familiar banking system. But recently many Australians are faced with new challenges because of the changing landscape of the Australian lending industry and often decisions are made without the appropriate advice.

Predatory lending is on the rise as a result of a systemic failure of the lending industry. My research in my publication 'Get a Second Opinion Before You Sign' looks at the commercial lending practices of lenders and provides transparency to borrowers in an unregulated industry.

Time and health are two precious assets that we generally don't recognise and appreciate until they have been depleted. What makes us an exceptional country is that Australia is regarded across the globe as a great place to live. However, our financial system is no longer

a case of “She’ll be right” or “whatever is wrong will right itself with time”. Misconduct decays our trust in our financial and legal system.

The establishment of this Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry will ensure that those who have undergone financial hardship due to another’s unlawful misconduct will have access to justice and a platform from which to pursue their rights.

Money can break us or make us, in the past few years it has broken many on wall street and the city of London. The world economy has been on a roller coaster, yet not until it began to veer of the tracks did the passengers realise that they had embarked on a wild ride. Assisted by their thoughtlessness, the amusement park’s management did not set limits on how high they could go or even provide safety equipment. Why didn’t we recognize the warning signs until mortgage funds collapsed, jobs vanished, and millions of mortgages defaulted?

The Global Financial Crisis “GFC” stemmed from our changing levels of confidence. From temptations, envy, resentment, illusions and especially from changing stories about the economy, stories of glorified financial “innovation” and then represented it as Ponzi. People paid small fortunes for property; others financed those purchases; the Australian Stock Exchange “ASX” peaked above 6,800 points and fell, little more than a year later, below 3,120 points. Investment Banks were saved by a US Federal Reserve bailout and Lehman Brothers collapsed.

When bubbles burst, and markets crash, plans paved years into the future can be destroyed. As the impact of the crisis of 2008 subsides, leaving its legacy of unemployment and debt, it is worth asking if the right things are being done to support what is good about finance and remove what is poisonous.

Risk is an inevitable fact of life. People make decisions without perfect foresight of how the future will unfold. However, the only source of knowledge is experience. Our predecessors from previous generations help us evolve. It is with this knowledge that we must identify best policy and implement safeguards for the protection of borrowers and investors. Those who cannot remember the past are condemned to repeat it.

The Global Financial Crisis (GFC) affected the behaviour of businesses and households in several ways, but it particularly adjusted attitudes towards risk, credit and levels of debt.

The GFC decimated trust and left a legacy of singularly non-mutual performance by major banks and large corporations toward clients and investors. The anti-competitive aggregation methods of the major banks implemented over the past 30 years have created behemoth institutions that are the most lucrative in the world. The pursuit of shareholder profit, at the expense of clients and communities, is an unsustainable business model and threatens the very fabric of community. The drastic reduction in capital and finance solutions to regional Australia has greatly impacted the economic health of communities. [2]

The 1:100 event known as the GFC was in fact, a ‘Global Fiduciary Crisis’ [3]. Fiduciaries are people who act or hold themselves out as acting as an intermediary between borrowers and lenders.

I note term ***financial services entity*** *in the Prime Ministers* draft terms of reference excluded item (e) outlined in the Letters Patent which is defined as:

(e) a person or entity that acts or holds itself out as acting as an intermediary between borrowers and lenders.

Under the original terms of reference a financial services entity was defined as an authorised deposit taking institution (or bank), an insurer, holders of Australian Financial Services Licences and registrable superannuation entity licensees.

The decision to include the sector in the terms of reference that is responsible for more than half of every mortgage originated in Australia in my respectful submissions allows the inquiry to investigate non-bank lenders, while it does not mention non-bank lenders, a non-bank lender would fall within the spirit of the inquiry's scope as an entity that acts as an intermediary.

The GFC led to significantly less appetite for credit among households and businesses. Banks generally tightened their lending criteria. On banks' balance sheets, one clear outcome is the heightened level of impairment and non-performance of loans, particularly business loans and those related to commercial property.

Although Australia did not experience a recession, it has still experienced the same difficulties as the rest of the global finance sector, as liquidity left the wholesale financial markets and the confidence levels of investors (of debt and equity) fell.

Over the past few years particularly post GFC, predatory lending practices remain prevalent within the commercial mortgage industry. Since loans are backed by a borrower's real property, a predatory lender can profit from loan terms stacked in their favour and from the sale of a mortgagee in possession security if a borrower defaults.

It is my experience more often than not that a borrower will respond to a situation out of habit, emotion or desperation or in circumstances when they can't cope stick their head in the sand and hope it goes away.

While there is some dispute about what constitutes a predatory lending practice, several actions are often cited as such including a failure to disclose information or disclosing false information, risk-based pricing and inflated charges and fees.

Unfortunately, those who are least able to afford it are most often targeted by predatory lenders. While consumers in poorer areas have the highest rate of predation, those on higher incomes such as professionals do not seem to be targeted.

In some instances, there are second tier lenders who are fully hoping the borrower cannot service their loan. Unfortunately, the reality in the 2nd tier lending industry is that in many instances the lender knows the borrower is going to default, for some lenders who are predatory this is seen as an opportunity to issue a deed of forbearance known as a "setup to fail agreement" or what I call a "legal theft agreement".

It is called this because of the conditions placed on the borrower are so onerous and unachievable that a default is a certainty, thus allowing the lender to take whatever security is offered.

It is in these circumstances that a new breed of predatory lending has arisen where the main focus is not earning interest on money lent but securing the ownership of the securities.

It is known in the industry that no adviser protecting the interests of a borrower would advise their client to entertain these types of deeds that are used in the industry.

In practical terms, predatory lending is lending by any financer, whether tier one or two in circumstances where the lender knows or ought to know that the borrower is not going to be able to comply with the mortgage conditions and thus, the security offered up by the borrower will be taken by the lender.

Predatory lending is the mechanism by which a mortgagor takes peoples security which is now a major multibillion dollar industry in Australia today. Predatory lending happens in the first mortgage market and the same issues borrowers fall foul to in second-tier lending.

Just because the proponents of the second-tier lending industry have been labelled the inauspicious title of predatory lenders simply because they adopted certain practices does not mean that they were the inventors of predatory lending.

What is not regularly publicized is that the tier one banks also indulge in predatory lending. There are many examples of this but no clearer examples than what many of our Australian farmers have experienced in recent years in dealing with the tier one banking system.

For all the coverage about predatory lending where has the coverage been about tier one banks attending upon Australian farmers in circumstances where the farmer is desperate. This is usually as a result of a bad season or a failed crop or something that has occurred outside the farmers control and the tier one lender sits down with the farmer and offers up terms knowing full well that the farmer will not be able to meet those terms.

The tier one lender can subsequently appoint friendly receivers who will charge exorbitant prices for their services to sell that farm from underneath the farmer often to overseas interests. You don’t have to be an economist or experienced business person to understand this is one example of predatory lending.

I have witnessed the banks forcing farmers to sell cattle at ridiculously low prices, actions that decimated their breeding herd thus making it impossible to service and repay their debt without further cutting into breeding stock. Consequently, the borrower no longer has the stock to breed cattle to sell as the bank has cleverly impaired the loan.

Australian farmers are the backbone of our country. For hundreds of years they’ve fed Australia. Prevailing drought conditions in several Queensland regions have exacerbated the financial issues faced by many of the state’s farm businesses.

Debt to equity lending played a significant cant role in financing agricultural business so that, when the GFC came along with reducing asset values, this form of lending became the weakness in financial models built on ever increasing capital values.

The current level of debt in Queensland Agriculture is difficult to determine as financial institutions no longer supply needed information, Queensland agricultural debts totalled $17b in 2011.

On 19 October 2015, the Queensland Treasurer Hon Curtis Pitt MP, announced the establishment of a Rural Debt and Drought Task-force to help identify and recommend solutions to the Queensland Government for addressing rural debt issues in Queensland. [4]

The Taskforce made 15 recommendations to stabilize then revive the state's primary industries and to strengthen our rural communities throughout Queensland. Recommendation #44 of the Taskforce was 'That the Government initiate a Royal Commission to investigate financial conduct within the finance sector'.

The Taskforce was presented with several written and verbal reports alleging serious financial misconduct. It was beyond the scope of the Taskforce to investigate these matters which deserve serious investigation.

Concern was expressed that the current system of valuation used by banks is based on recent sales within that region. An area with a high number of mortgagees in possession can result in valuations which collapse or may vary considerably over the term of loans. This has a particular impact on loan to valuation ratios and credit risk ratings when loans are renegotiated either routinely by banks (every 3-4 years) or loans have to be renegotiated for some other reason, e.g., drought recovery.

Throughout the consultation process and in submissions, numerous issues were raised where producers felt they had been unfairly treated by banks. Conduct was of relevance when businesses were identified as 'at risk'. Receivers and their actions after foreclosure were cited as areas of concern.

There was a view, particularly from those facing debt and drought recovery challenges that they would benefit from further development of skills to accurately assess their situation and develop and negotiate a recovery or exit strategy with financiers.

Problems are now prevalent in major industries and many droughted regions. Other regions live on the edge. Few if any regions rest on a stable economic basis with sound financial prospects on offer.

Traditional banking environments are changing as regulatory controls have grown tougher, as a result farming will need to find different ways to source capital.

Going to the bank manager for a loan will no longer work the way it has in the past and for many borrowers, this is frightening prospect.

During my career, I have been privileged to work with leading legal counsel such as Ian Temby QC, David Pritchard SC of St James' Hall and Niall Coburn former Specialist Adviser to ASIC, who have made significant contributions to their fields.

Ian Temby AO QC was the founding NSW Independent Commission Against Corruption (ICAC). In December 2001, Ian Temby led a Royal Commission into the finance broking industry in Western Australia. [5]

The report dealt with problems that arose in the finance broking industry in Western Australia, chiefly over the period 1995 – 2000.

> *"It can be said with absolute confidence that unlawful and improper practices were rife in parts of that industry over that period. This reflects badly on many individuals. But of course, and more importantly, it means there was a large systemic failure. Many of those guilty of malpractices were licensed by the State. That is true of finance brokers, of valuers and of some others. When they misconducted themselves and got away with it, that encouraged them to continue. Others who found out what they had done followed suit. There has been a shaking out in the industry, in part as a consequence of the close scrutiny to which finance brokers and others have been subjected. A number of firms have collapsed. Lenders often unsophisticated individuals who placed great faith in people such as finance brokers and valuers and the fact that they were licensed lost much money. Many lost all or most of their life savings. Well over $100,000,000 was lost by lenders as a result of malpractices."*

Unlawful or improper activities or practices have continued to occur in many Australian states since the commission in 2001 was required to look for such activities or practices, relating to that industry and since the date in question there has been a series of mortgage fund collapses and evidence of malpractice and poor conduct of various classes of persons, namely private funders and finance intermediaries.

The aggregation of retail banking has been a strong trend in Australia for over 30 years. It reached a compelling conclusion, post GFC, with the substantial decrease in regional banking capacity and finance supply, independent of the major banks arising from the Government's support for our major banks. The loss of St George Bank, Bankwest, Aussie Home Loans, Wizard Home Loans, RAMS home Loans and substantial independent finance has created 4 dangerously powerful and oligopolistic banking system. The G20 describes our banking system as the 'most lucrative in the world' and a 'potential moral hazard'.

Debates over the call for a Royal Commission into the banking industry have brought to the floor the real battle in Australian politics. At stake is whether Australia is committed to being a democracy, ruled by the people as represented by government, or a political system controlled by corporations where government is the political arm of big business.

The scandals over time reflect a culture in banking and finance that runs on greed and is backed up by blatant disregard for any form of responsibility.

In February 2017, the Small Business and Family Enterprise Ombudsman released a report (The Kate Carnell inquiry) reviewing the lending practices by Australia's banks and how their services to small business could be improved. [6]

The report makes 15 recommendations, four of which are for Government and the remaining 11 directed to the banking industry itself. One of the 15 recommendations from the inquiry was for a nationally consistent approach to farm debt mediation.

With Australian farm bank debt levels increasing from around $10 billion to $60 billion over the past 25 years, the relationship between the banks and agriculture has never been more engrained. These findings are damming, and they are concerning for agriculture because farm businesses are capital intensive and they have limited options for alternative sources of finance.

The Inquiry was commissioned by the Government on 31 August 2016 to examine a selection of the most egregious cases that were presented to the Parliamentary Joint Committee on Corporations and Financial Services inquiry into the 'Impairment of Customer Loans'. In total, the Inquiry considered the submissions of 23 affected customers, and conducted a 'deep dive' forensic analysis of six of those.

The cases date from 2008 until more recently and represent various industries. Of the cases considered, the Inquiry found that a third were a result of poor business decisions; another third were a result of both poor business decisions and poor bank practices; and the final third were representative of poor bank practices and possible unconscionable conduct on the part of the banks involved. A key focus of the recommendations for Government include access to an affordable, efficient and binding, out-of-court dispute resolution service for small business lending customers, with access to compensation in appropriate cases.

In February 2017, The Australian Law Reform Commission released a report on the Elder Abuse Inquiry. The Discussion Paper includes 43 proposals for law reform. The report established a 20 per cent increase in reported cases of financial abuse from 2014-15 to 2015-16. [7]

We need Australian's to have confidence in their banks and financial institutions, to sweep away the doubt, to uncover and deal with unethical behaviour that compromises that confidence. I have witnessed this on the frontline around Australia, a system that fails borrowers and guarantors first hand. We should have confidence in our financial system and where there are problems, they should be addressed by the appropriate mechanisms.

Cheap and easily accessible money very often leads to speculative investment choices which, over time, leads to severe losses. Over the years, I have helped many distressed clients with corporate and commercial disputes and financial services/banking litigation, as well as class action lawsuits. Many of the firms have been involved in complex corporate and financial services lawsuits in recent Australian history.

In 2008, Storm Financial collapsed and took the life savings of thousands of Australians with it. Stewart Levitt of Levitt Robinson Solicitors acted for several hundred Storm clients in a class action against three of Australia's major banks. The actions are centred around allegations of unlawful lending practices and alleged participation in an Unregistered Managed Investment Scheme (UMIS) involving equity investment loans and margin loans. Thousands of elderly investors across Australia have lost billions in the past few years in managed investment schemes.

While the Gold Coast has always been known for its entrepreneurial spirit to the envy of many states in Australia and particularly its ability to raise investment funds, Equititrust, City Pacific, MFS and LM Investments all Gold Coast based mortgage funds and many more have all proved to be terrible investments. Investigations have revealed that the investment model of such schemes was in many cases materially flawed, lacking the right risk and compliance strategies.

In some cases, auditors have let investors down by failing to get into the details of the oversight of these schemes and pass concerns on to ASIC. In one scheme, investors on the Gold Coast lost $300 million in what they thought was a safe investment in property, returning 8% per annum.

After the losses, receivers are appointed to the schemes to clean up the mess. This costs investors more money in the hope that some money will be left over for investors to recover. My experience is that once money is lost, it is unlikely that investors will recoup more than 10¢ in the dollar. [8]

This sector employs almost half a million people and is the fastest growing in the Australian economy. If the government and ASIC are going to allow such schemes, they need to ensure that directors are properly qualified and there are independent directors on the board who enforce compliance and risk strategies. Auditors need to be held more accountable for such failures as they are the gatekeepers and the eyes and ears of investors' interests.

Other examples of bank and mortgage fund failure:

2008: GFC takes down Opes Prime, Allco and Babcock and Brown;

2014: Commonwealth Bank financial planning scandal;

2016: ASIC targets ANZ for rigging the bank bill swap rate (BBSW);

2016: CommInsure payments scandal.

The Harvard model of "Now, where, how" is a simple process to follow in order to develop a practical plan. Its core methodologies show the overarching process for resolving any matter big or small starts firstly, where are you now, where will we be in the future and how will we get there?

The Government has determined in the now, where they want to go, but the critical next step in management theory is implementation. Nothing has happened at all; their response has been to have inquiries determine the now and where but where is the implementation?

On 27 March 2017, the Hon Bob Katter introduced to The Parliament of the Commonwealth of Australia the People of Australia's Commission of Inquiry (Banking and Financial Services) Bill 2017. The Bill is for an Act to establish a People of Australia's Commission of Inquiry into banking and financial services in Australia, and for related purposes. [9]

The People of Australia's Commission of Inquiry (Banking and Financial Services) Bill 2017 (the Bill) provides for the establishment of a Commission of Inquiry. The Bill invests the People of Australia's' Commission of Inquiry with the full powers of a Royal Commission as laid out in the Royal Commissions Act 1902. [10][11]

The Commission of Inquiry proposed to inquire into unethical, unlawful and improper conduct in the banking, financial services and related sectors. The purpose of the Bill was to fully expose and shine the light of public scrutiny on the unethical and unlawful conduct/practices in the banking and financial services industries and to put forward recommendations for reform. Particular concern has been raised in relation to the conduct of service providers in the banking, superannuation, insurance and other financial services sectors.

Responding to numerous media reports, whistle-blower disclosures and cases raised with Members of Parliament and Senators, there have been 37 reviews and inquiries into banking and financial services since 2010. However, none of these past reviews/inquiries have had the

level of powers of a Royal Commission. These past reviews/inquiries have often not been independent, have been politicised and have had limited scopes of inquiry.

This has led to little, or no, reform to the sector, nor justice for the victims. Nor has this led to the spotlighting of the malpractices, shortcomings and injustices of current financial practices. The Commission of Inquiry was to have the full powers of the Royal Commissions Act 1902 plus additional powers related to protecting whistle-blowers. The Commission of Inquiry was report to the Parliament, as opposed to this Royal Commission which reports to the Executive arm of Government.

6. Response by Regulators:

In 2009, the federal government enacted changes to the way credit is regulated in Australia. The primary vehicle for the changes is the National Consumer Credit Protection Act 2009, which includes the National Credit Code (NCC) as Schedule 1 of the Act. The Act came into force on July 1, 2010. It provides national uniform regulation for the Australian credit industry and replaced the previous state-based credit licensing legislation systems that existed in the states.

The laws and protections available to borrowers differ depending on the purpose of the loan.

The law provides the highest level of protection to individual consumers borrowing for household and domestic purposes. This also includes loans to consumers to buy residential properties. For these types of consumer and personal loans, the law regulates what lenders need to disclose, how interest can be calculated, how the loan can be enforced and limits on default charges.

Different laws apply to consumers borrowing to make investments e.g. in commercial property, shares or managed funds. Generally, borrowing to make an investment gets a lower level of protection under the law.

The law provides the lowest level of protection to commercial loans, including loans to small businesses. Commercial loans are loans provided to companies and business owners. They are used to fund the running of a business and the purchase of goods or services used in the business. For example, commercial loans may be used to fund purchases of supplies used in manufacturing, new machinery/premises or property development projects.

Commercial loans may have terms of many years and disputes can often arise during the relationship between the borrower and the lender. This is particularly true if the borrower gets into difficulty making repayments on a loan.

Disputes may relate to fees (including fees paid to finance brokers to prepare loan applications), repayment arrangements, valuations, consequences of default, rights under the loan agreement or other terms of the loan agreement. For example, the borrower may have concerns that the lender did not adequately disclose the terms of the agreement or that the conduct of the broker or lender is unfair in some way.

In relation to commercial loans, the courts generally impose a high bar when a borrower alleges that conduct of a broker or lender is unconscionable. Courts interpret these laws considering the business nature of the transaction and on the basis, that generally commercial

parties can look after their own interests. Therefore, although conduct may seem unfair, this may not necessarily amount to unconscionable conduct under the law.

To successfully take action for unconscionable conduct in commercial lending, there must be some evidence that the lender has improperly taken advantage of a power imbalance between the parties and often this exercise can be very costly for the borrower.

As an advocate of responsible lending and I have seen how hard it is to devise legislation that protects the disadvantaged without negatively impacting lending. Non-bank lenders should be required to implement measures to protect borrowers & guarantors.

In my respectful submissions it is my recommendation that lenders should be required to employ a policy that during the assessment of a commercial loan, they require the borrower to demonstrate a proven capacity to exit a loan or show serviceability trends that indicate the borrower will be able refinance or exit a loan facility within a period.

There are of course consequences in adopting bad legalization. For example, here is a basic solution that could clean up the currently unregulated commercial lending industry:

i) Introduction of a licensed responsible credit assessor with responsible lending guidelines; and

ii) Introduction of a lenders register for all lending entities and respective responsible credit assessors.

In this way, ASIC, could, under a simple process and regulatory guide, adopt the application of its own principles of responsibility without the need for borrowers to pursue expensive litigation.

7. Receiver Appointments:

The appointment of an insolvency practitioner can be a great cause of concern for any borrower, events I generally see leading up to a practitioner's appointment including but are not limited to:

7.1 The property securing the loan facility being revalued leading to the borrower being outside the lenders' LVR; (This is particularly inappropriate when a bank or mortgagee triggers defaults solely to rebalance the risk profile of their lending portfolio across segments or industry sectors, including; credit managers who want this ability to cover all risks they have not predicted and/or included in loan price.)

7.2 High rates of default interest being imposed once a default occurred and at a rate that was not clearly disclosed in the loan documentation;

7.3 Disadvantageous changes to facility terms;

7.4. A general unwillingness by the lender to work through issues and unrealistic notices of demand for repayment;

7.5. Deeds of forbearance with confidentiality clauses being required;

7.6. The unnecessary appointments of law firms and receivers in the following circumstances:

i. The borrower breaches their monetary or other contractual obligations;

ii. Interest is not met when due;

iii. The borrower's debt levels are increasing and unsustainable;

iv. A third-party creditor (e.g. ATO) has initiated recovery action against the borrower;

v. Loss making operations or holdings are deteriorating the borrower's

equity position;

vi. The underlying project or development has stalled, or costs have blown out;

vii. The borrower is unable or unwilling to deliver an appropriate strategy to resolve the matter; and

viii. Further delay or inaction on the part of borrowers/guarantors.

7.7. Properties being sold below market value, in some cases at what appears to have been at a significant discount or 'fire sale'.

7.8. Breaches of the Code of Banking Practice 2.2 and 25.2

7.9 Receivers and section 420A

There remains in my respectful submissions a conflict between the receiver and lender while the insolvency industry is made up of almost 650 liquidators and receivers registered in Australia the tier one firms such as BDO, Korda Mentha, PPB and FTI Consulting employ about half the amount, one could see that a monopoly has been adopted. Of great concern is the continued selling of assets by receivers for below market value. Section 420A of the Corporations Act 2001 states:

(1) In exercising a power of sale in respect of property of a corporation, a controller must take all reasonable care to sell the property for:

(a) if, when it is sold, it has a market value--not less than that market value; or

(b) otherwise--the best price that is reasonably obtainable, having regard to the circumstances existing when the property is sold.

(2) Nothing in subsection (1) limits the generality of anything in section 180, 181, 182, 183 or 184

In my respectful submissions it is my recommendation that the Australian Securities and Investments Commission (ASIC) initiate a review into matters raised during the inquiry relating to breaches of the Corporations Act 2001, specifically section 420A and more broadly across the banking and insolvency industry; and

The government introduce higher standards of accountability and transparency for insolvency practitioners regarding the costs they incur while conducting receiverships, namely:

a. Insolvency practitioners be required to disclose their estimate of costs of the receivership prior to being engaged.

b. The Australian Restructuring Insolvency and turnaround Association ensure receivers appointed to agribusiness cases must be appropriately qualified in agribusiness and have a strong background and demonstrated experience in rural management.

c. The Australian Bankers' Association and the Australian Restructuring Insolvency and Turnaround Association ensure that banks and insolvency practitioners must only engage independent valuers to value agribusinesses with appropriate qualifications and demonstrated expertise and experience in the field.

8. Farm Debt Mediation:

On 16 February 2017 the Senate established the Select Committee on Lending to Primary Production Customers to inquire and report on the regulation and practices of financial institutions in relation to primary production industries, including agriculture, fisheries and forestry.

A public hearing into Lending to Primary Production Customers was heard on Friday 11 August 2017 at The Portside Centre in Sydney with opening submissions made by Mr Andrew McLaughlin, (private capacity) (Submission 21). Mr McLaughlin is a national treasure, he has spent 25 years fighting for farmers who face David and Goliath battles against banks. He gave a passionate 43-minute testimony to the Rural Select Senate Committee. The report was completed 6 December 2017. [12]

The report made 27 recommendations, many explicitly directed at the Australian Bankers Association (ABA), the peak body representing Australia's banks and notes that 'The profound emotional toll that bank and receiver behaviour had on many primary production families cannot be disputed' and 'Many farmers who spoke to the committee were often distressed, agitated and spoke of the trauma that their experiences with banks and in particular, receivers, had caused their families'.

A recurring theme of the select committee report was the late repayment of loans as a result of droughts or other natural factors out of the farmers' control.

In case after case, banks were presented as uncompromising and callous towards their customers, insisting that they repay their loans on time regardless of circumstance, and when they didn't, calling in receivers to manage the sale of the farm.

While the final report stressed that some of the claims were contested, the senators said the evidence showed "broader patterns" of "significant problems" in the way banks were behaving towards farmers and other primary producers.

In my respectful submissions it is my recommendation the government establish a nationally consistent compulsory farm debt mediation scheme, based on the NSW model.

9. Unfair Contracts (Contracts Review Act)

The application of the Contracts Review Act 1980 (NSW) (referred to throughout as the "Contracts Review Act") or as commonly known in the industry as the "Unfair contracts act" gives New South Wales courts power to award remedies to consumers that have been affected by procedural or substantive unfairness, in the context of this paper generally an action brought against a mortgagee. The Contracts Review Act allows a court to find a contract (or loan contract) to be "unjust" and rule that the contract is void or make an order to vary the contract.

Under this Act, a contract will not be unjust as against a party unless the contract or one of its provisions is the product of unfair conduct on his part either in the terms which he has imposed or in the means which he has employed to make the contract.

For example, the Contracts Review Act allow remedy to a consumer where the consumer has not had a reasonable opportunity to negotiate the terms of the contract.

While it might be argued that the Australian Consumer Law (ACL) provides sufficient consumer protection in my view it was not intended to replace the Contracts Review Act.

The ACL and the Contracts Review Act work together because of the differing intentions of each Act. The distinction between the ACL and the Contracts Review Act lies in that the ACL focuses more on the contents of the terms of the contract, whereas the Contracts Review Act governs the circumstances that caused the parties to enter into the contract.

The main provision of the Act is section 7 which reads:

1) Where the Court finds a contract or a provision of a contract to have been unjust in the circumstances relating to the contract at the time it was made, the Court may, if it considers it just to do so, and for the purpose of avoiding as far as practicable an unjust consequence or result, do any one or more of the following:

(a) it may decide to refuse to enforce any or all of the provisions of the contract,

(b) it may make an order declaring the contract void, in whole or in part,

(c) it may make an order varying, in whole or in part, any provision of the contract,

(d) it may, in relation to a land instrument, make an order for or with respect to requiring the execution of an instrument that:

(i) varies, or has the effect of varying, the provisions of the land instrument, or

(ii) terminates or otherwise affects, or has the effect of terminating or otherwise affecting, the operation or effect of the land instrument.

Section 9 provides the matters to be considered by the Court when determining whether, for the purpose of section 7, a contract is unjust.

1) In determining whether a contract or a provision of a contract is unjust in the circumstances relating to the contract at the time it was made, the Court shall have regard to

the public interest and to all the circumstances of the case, including such consequences or results as those arising in the event of:

(a) compliance with any or all of the provisions of the contract, or

(b) non-compliance with, or contravention of, any or all of the provisions of the contract.

2) Without in any way affecting the generality of subsection (1), the matters to which the Court shall have regard shall, to the extent that they are relevant to the circumstances, include the following:

(a) whether or not there was any material inequality in bargaining power between the parties to the contract,

(b) whether or not prior to or at the time the contract was made its provisions were the subject of negotiation,

(c) whether or not it was reasonably practicable for the party seeking relief under this Act to negotiate for the alteration of or to reject any of the provisions of the contract,

(d) whether or not any provisions of the contract impose conditions which are unreasonably difficult to comply with or not reasonably necessary for the protection of the legitimate interests of any party to the contract,

(e) whether or not:

(i) any party to the contract (other than a corporation) was not reasonably able to protect his or her interests, or

(ii) any person who represented any of the parties to the contract was not reasonably able to protect the interests of any party whom he or she represented, because of his or her age or the state of his or her physical or mental capacity,

(f) the relative economic circumstances, educational background and literacy

of:

(i) the parties to the contract (other than a corporation), and

(ii) any person who represented any of the parties to the contract,

(g) where the contract is wholly or partly in writing, the physical form of the contract, and the intelligibility of the language in which it is expressed,

(h) whether or not and when independent legal or other expert advice was obtained by the party seeking relief under this Act,

(i) the extent (if any) to which the provisions of the contract and their legal and practical effect were accurately explained by any person to the party seeking relief under this Act, and whether or not that party understood the provisions and their effect,

(j) whether any undue influence, unfair pressure or unfair tactics were exerted on or used against the party seeking relief under this Act:

(i) by any other party to the contract,

(ii) by any person acting or appearing or purporting to act for or on behalf

of any other party to the contract, or

(iii) by any person to the knowledge (at the time the contract was made) of any other party to the contract or of any person acting or appearing or purporting to act for or on behalf of any other party to the contract,

(k) the conduct of the parties to the proceedings in relation to similar contracts or courses of dealing to which any of them has been a party, and

(l) the commercial or other setting, purpose and effect of the contract.

3) For the purposes of subsection (2), a person shall be deemed to have represented a party to a contract if the person represented the party, or assisted the party to a significant degree, in negotiations prior to or at the time the contract was made.

4) In determining whether a contract or a provision of a contract is unjust, the Court shall not have regard to any injustice arising from circumstances that were not reasonably foreseeable at the time the contract was made.

5) In determining whether it is just to grant relief in respect of a contract or a provision of a contract that is found to be unjust, the Court may have regard to the conduct of the parties to the proceedings in relation to the performance of the contract since it was made.

The most quoted judicial commentary on the Act comes from West v AGC (Advances) Limited per McHugh J5:

"The Contracts Review Act 1980 is revolutionary legislation whose evident purpose is to overcome the Common Law's failure to provide a comprehensive doctrinal framework to deal with "unjust" contracts. Very likely its provisions signal the end of much of classical contract theory in New South Wales. Any contract or contractual provision, not excluded from the operation of the Act and which the Court considers is unjust in the circumstances existing at the time when it was made, may be the subject of relief under the Act. Moreover, the provisions of s9(2) do not exhaustively indicate the criteria as to what can be taken into account in determining whether a contract or any of its provisions is unjust… the Court is entitled to have regard to all the circumstances of the case, subject to s9(4) and the public interest …"

Having regard to the above judicial commentary it should be recognised in my respectful submissions the need for the Government to establish a National Contracts Review Act to provide all Australian consumers with the levels of protections afforded under NSW legislation (Contracts Review Act).

10. Conclusion

In conclusion I congratulate the efforts of Andrew McLaughlin, Senator John Williams and Senator Bob Katter and others who have tirelessly pursed solutions in these matters of grave importance to the future of Australia.

I fully support this inquiry into the conduct of banks and lenders with the aim to protect our primary producers. In many cases there is no justified reason for a bank to foreclose or appoint receivers or bankrupt farmers when their asset values are greater than the debts to the bank. No money could ever compensate those who have been so unfairly treated by those banks they borrowed from and the system that let them down. Let us not forget those family members who lost their loved ones to suicide, family breakups, ill health and losses in the millions of dollars in equity.

The calls for a royal commission into Australia's banking sector are growing louder. At the very least a spotlight needs to be shone on tier one and tier two lenders who partake and have embraced in their business model predatory lending practices which has been the basis for many hard-working Australian's to lose their life savings, their dignity and their faith in the system.

Australian lenders and insolvency practitioners have allowed bad behaviour to go on for far too long, the banks are making enough profits to afford and are deserving of footing the bill for the royal commission.

The kinds of malpractices highlighted in this submission can potentially cause financial crises, which are almost always borne by taxpayers.

Most importantly, corporations and professional advisors must respect the importance of trust and the role of the fiduciary.

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