



**SUPPLEMENTARY SUBMISSION TO THE JOINT COMMITTEE ON  
CORPORATIONS AND FINANCIAL SERVICES INQUIRY INTO  
THE IMPAIRMENT OF CUSTOMER LOANS**

**MARCH 2016**

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## **SUMMARY**

1. This supplementary submission addresses evidence given to the inquiry hearing in Sydney on Tuesday 16 February. We have also provided the Committee with a confidential response to customer issues raised in the hearing and in public submissions made by ANZ customers to the inquiry.
2. ANZ did not purchase Landmark for 16 per cent of the value of the Landmark Financial Services (LFS) loan book. ANZ acquired the LFS loan book at net book value after appropriate provisions, that is, approximately \$2.2 billion. The sale price for the Landmark deposit book was also its book value of approximately \$300 million.
3. The LFS business was a large agribusiness portfolio. It was assessed as potentially providing ANZ with significant income and customer growth and was aligned with ANZ's agribusiness strategy. The acquisition included an agreement allowing ANZ to distribute its banking products through Landmark outlets.
4. We reiterate that ANZ aims to work with commercial customers in default to help them get back on track. Less than 0.1 per cent of all commercial customers are subject to ANZ enforced insolvency action.
5. It has been alleged that ANZ enforcement action has been taken at short notice, but we are unaware of any case where this is correct. Details of a number of customer matters have been provided on a confidential basis to the Committee. These show that enforcement action is only taken after negotiations with customers or attempts to negotiate with customers over a period of time.
6. Legal or recovery action by ANZ is costly for all parties and only considered when all other avenues are exhausted. A directly negotiated agreement, or an agreement resulting from mediation, is generally faster, less costly and less distressing for all parties. ANZ undertakes enforcement action as a result of a material monetary default or, in a small number of cases, in response to significant external events (e.g. fraud or animal welfare concerns). Even then, enforcement does not occur before exhaustive attempts are made to resolve matters.
7. There is some confusion between loan impairment and contractual rights of recovery. Loan impairment is a financial accounting process that does not give rise to any rights of recovery against a customer. An account can be in default but not impaired, and vice versa. Impairment without contractual default may occur where an assessment is made, for example, that a business is in decline and although the customer has not defaulted, ANZ has formed a view that a loss will ultimately result.
8. Claims that ANZ truncated long term loans to periods of two to six months are incorrect. Customers in default are given time to sell down assets to get back on track. It would appear that a six month deadline given to sell an asset has been mistakenly construed as a truncated loan period.
9. ANZ rejects suggestions in evidence that the bank has retained the surplus from forced sale of properties after the loan, interest and bank costs have been repaid. We will review any case where it is alleged this is the situation.

## **A. INTRODUCTION**

1. In this supplementary submission, ANZ responds to evidence given to the inquiry hearing in Sydney on Tuesday 16 February. The submission addresses claims made regarding the purchase of Landmark by ANZ (Part B) and ANZ's practices in handling agricultural sector customers and their loans (Part C). It also outlines areas of possible reform we think should be considered by the Committee (Part D).
2. Customer matters are dealt with in a separate confidential attachment to the Committee (Attachment 2). This confidential document responds to customer evidence put to the inquiry at the Sydney hearing and in public submissions provided by ANZ customers to the inquiry.

## **B. PURCHASE OF LANDMARK**

### **ANZ RELATIONSHIP WITH AWB AND LANDMARK PRIOR TO SALE**

3. Landmark is a diversified rural merchandise business which at the time it was acquired by ANZ was a division of the Australian Wheat Board (AWB). Landmark Financial Services (LFS) was a division of Landmark that, at the time of its acquisition by ANZ, provided agribusiness lending of about \$2.4 billion, had debenture (akin to deposit) accounts of about \$300 million and had about 10,000 customers.
4. AWB approached ANZ in late 2008 with an opportunity to purchase LFS's lending and deposit books, take on LFS employees and enter into an exclusive distribution agreement for ANZ banking products to be sold through Landmark outlets. AWB was seeking to sell Landmark to reduce debt and build lower risk income streams.
5. As noted in our earlier response to questions on notice, ANZ was a financier to the Australian Wheat Board (AWB), but did not have a relationship with Landmark prior to the acquisition. ANZ and Rabobank provided wholesale funding for the AWB/Landmark loan book under a securitisation trust structure in which Permanent Custodians Limited (PCL) acted as the trustee. ANZ's component of the wholesale funding was around \$1.1 billion. AWB and Landmark were the administrator/servicer under the trust, which meant they were responsible for the day to day dealings with customers. Whilst customers dealt with Landmark, their loan was legally offered by and owed to PCL.
6. ANZ rejects Peter King's evidence at the 16 February hearing that the decision to purchase LFS was as a result of ANZ's exposure as a securitisation lender to the AWB. ANZ's lending under the securitisation funding was not a factor that influenced the transaction.
7. Further, the acquisition transaction, including its evaluation and management, was the responsibility of a different business unit in a different ANZ division to the business unit responsible for the securitisation.
8. LFS presented an opportunity for ANZ to acquire a significant agribusiness portfolio with an exclusive distribution agreement for ANZ products. The Landmark business was assessed as potentially providing ANZ with significant income and customer growth. The acquisition elevated ANZ to become the number two agribusiness bank, with LFS' portfolio concentrated in States and industries aligned with ANZ's agribusiness strategy.

The purchase also extended ANZ's rural commercial distribution network and brought in Landmark employees with agribusiness expertise.

9. When ANZ bought the Landmark business, Landmark's interest and role in the trust were assumed by ANZ. New mortgages did not need to be written as the lender (from a legal perspective) remained PCL. ANZ contacted customers after the sale to notify them that they would be serviced by ANZ. Over a transitional period customers were re-documented onto ANZ letters of offers and security documents.

### **PURCHASE PRICE OF LANDMARK**

10. At the hearing on 16 February, Mr King inferred that ANZ purchased Landmark for about 16 per cent of the value of its loan book (approximately \$2.4 billion).<sup>1</sup> Consequently, a number of ANZ customers (who were former Landmark customers) have recently contacted the bank with an expectation that ANZ will reduce their debt to 16 per cent of the amount owing.
11. ANZ did not purchase Landmark for 16 per cent of the value of the LFS loan book. ANZ acquired the LFS loan book at net book value after appropriate provisions, that is, approximately \$2.2 billion (details are set out below). (The sale price for the Landmark deposit book was also its book value of approximately \$300 million.) This is confirmed in the Sale and Purchase Deed dated 8 December 2009 entered into between ANZ and Landmark Operations Limited.
12. Between the date of the Sale and Purchase Deed (8 December 2009) and the completion date for the sale (1 March 2010), there were adjustments/movements in the Landmark loan book (e.g. customer repayments), which had the effect of reducing the total value of the loan book to approximately \$2.3 billion. Confirming these adjustments/movements was done by way of a 'completion accounts' process, typical for an M&A transaction to determine the final purchase price.
13. A 'completion accounts' process is generally used to set the final price because, at the time of completion, the parties usually do not have final financial accounts. The price under this type of sale contract is often set by reference to financial accounts. Typically, the buyer will agree to pay an estimated price at the time of completion and the parties will then work to finalise accounts to determine the final price. The final price will generally be different to the estimated price. The completion accounts process usually requires a further payment or refund to be made by the buyer or seller so that the aggregate amount paid by the purchaser and received by the seller reflects the final contract price.
14. ANZ ultimately paid approximately \$2.2 billion for the Landmark loans. This was the adjusted book value as at completion, as determined under the completion accounts process, and represented loans of approximately \$2.3 billion less approximately \$100 million of provisions held against those loans.
15. This is confirmed in a Payments Direction Deed dated 28 February 2010 (the transaction 'completion' date) and a Completion Accounts Payment Directions Deed from 14 October

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<sup>1</sup> He said "ANZ decided to purchase the book debts of the AWB in these various farming arrangements for about 16 per cent of the total value of the capital of farms and securities to which they referred". It is unclear how he could calculate the capital value of these assets.

2010 (when the completion accounts process was finalised). Copies of these can, with the consent of the other parties to the Deeds, be provided to the Committee on a confidential basis.

16. Other than the clawback mechanism, which ANZ has previously detailed in evidence to the Committee, the Landmark transaction agreements did not include any price adjustment mechanisms where the price could be subsequently adjusted based on the performance of the business under ANZ's ownership. For completeness, we note that the warranties regime (detailed in our response to previous questions on notice) provided that any warranty payments would be taken to be a reduction of the purchase price. As previously outlined, no warranty payments were made.

#### ***Clawback mechanism***

17. It has been suggested that the "clawback" in the Sale and Purchase Deed incentivised ANZ to impair or default loans of healthy customers so that ANZ could claim a reduction on the purchase price.
18. The clawback mechanism only had very limited operation and scope. The only loans subject to this mechanism were already identified as being in difficulty by Landmark and were Graded D or E loans by Landmark in accordance with its Credit Manual. The clawback amount was capped at approximately \$14 million against a total loan book of approximately \$2.4 billion.
19. ANZ did not engineer defaults, or impair loans outside its ordinary processes, to trigger the clawback provisions. Any subsequent action taken by ANZ in response to the changing circumstances of former Landmark customers, which had the effect of reducing a customer's risk grading, had no effect on the operation of the clawback provision. That is, if ANZ downgraded a loan from D to E or from a higher grade to D (A being the highest risk grading, E being the lowest), that downgrade did not trigger the clawback provision.
20. The clawback process only resulted in a payment being made to ANZ or Landmark (noting the clawback regime applied for the benefit of each party – it was not a 'one way' process) when the relevant loans were either fully paid out by the customer or written off.
21. There were other restrictions on the conduct of ANZ under the clawback regime. For example, the parties agreed that ANZ could only write off a Grade D or E loan applying usual ANZ policies and practices. Writing off a loan in order to recover under the clawback provision would have been inconsistent with usual ANZ policies and practices.

#### ***LANDMARK TO ANZ TRANSITION***

22. When transitioning Landmark customers to ANZ documentation after the transaction, some customers in financial difficulty were put on 12 month contracts to expedite their access to funding (for example to plant crops). Once access to ongoing funding was secured, a customer review was then undertaken as part of the transition process. Many Landmark customers were subsequently given long term loans. ANZ has acknowledged that there are instances where we think the transition could have been done better.

23. As we said to the Committee on 13 November 2015, a number of former Landmark customers did experience difficulties in operating their accounts during their transition to ANZ in early 2010, but we believe these issues were rectified. Some of these new customers experienced unacceptable delays in our response to both information and funding requests. For many customers, the transfer to ANZ coincided with drought, making a tough situation worse. We are still working with a small number of former Landmark customers to set matters right.
24. There are claims that ANZ truncated long term loans to periods of two to six months. This is incorrect. Customers in default are given time to sell down assets to get back on track. A six month deadline given to sell an asset has been mistakenly construed as a truncated loan period.

## **PROCEEDS FROM SALES**

25. Evidence to the inquiry by Mr King appeared to suggest that ANZ has retained the surplus from forced sale of properties after the loan, interest and bank costs have been repaid. ANZ rejects this suggestion. We would welcome the opportunity to review any case where it is alleged this is the situation.
26. Mr King also refers to PCL as a shell company based in the Caribbean. This is incorrect. As explained above, PCL was the trustee for the Landmark loan book and has no links with the Caribbean. It is an Australian company that is a subsidiary of BNY Mellon, a global financial institution headquartered in New York.

## **C. BANK PRACTICES**

### **CONFIDENTIALITY IN CUSTOMER SETTLEMENTS**

27. Confidentiality promotes effective and more rapid resolution of issues. As the Administrative Appeals Tribunal states:

"Confidentiality is an essential feature of ADR (Alternative Dispute Resolution) processes. Confidentiality is generally maintaining private and secret: all discussions; the contents of documents disclosed that will not be used as evidence; and information provided during the ADR process. Maintaining confidentiality encourages meaningful participation and can promote good outcomes. Respecting confidentiality encourages a full and frank discussion between the parties about the issues in dispute and this can assist in the resolution or narrowing of the issues."<sup>2</sup>
28. Confidentiality clauses give ANZ more scope for flexibility in reaching settlements with customers and allow the parties to settle matters commercially. It reduces the likelihood of a settlement outcome being published and potentially creating unrealistic expectations for customers whose circumstances and banking relationships are different.

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<sup>2</sup> See Administrative Appeals Tribunal at <http://www.aat.gov.au/steps-in-a-review/alternative-dispute-resolution/confidentiality-in-adr-processes>, accessed 23 February 2016. See also "Confidentiality and privilege in mediation", John K Arthur (Dispute Resolution Law Bulletin, November 2015) who states: "Without confidentiality and the without prejudice privilege, the parties would be unwilling to negotiate with the other party for fear that what they said during negotiations may be used against them if the matter went to court. Indeed, confidentiality has been described as the sine qua non of mediation."

29. We are not aware of customers consistently raising concerns with confidentiality clauses, but if there are widespread concerns, ANZ will provide more information to customers about the purpose of confidentiality clauses. ANZ supports FOS updating its guidelines to include a model confidentiality clause for negotiated outcomes.
30. We wish to emphasise our response to questions on notice of 28 January, explaining that ANZ Landmark-related settlement deeds state that customers are free to provide information to this Inquiry.

### **ANZ'S APPROACH TO CUSTOMERS IN DIFFICULTY**

31. A number of comments were made at the 16 February Sydney hearing about ANZ banking practices. As noted in our earlier evidence to the Inquiry, ANZ aims to work with commercial customers in default to help them get back on track. We consider this process generally has worked for the benefit of customers and the bank. The number of commercial customers subject to ANZ enforced insolvency action is very small, less than 0.1 per cent of all commercial customers.<sup>3</sup>
32. Working with a commercial customer experiencing difficulty involves a staged process. Initial concerns are identified through standard monitoring and management of financial covenants, including review of periodic financial and cash flow statements. When issues are identified, oversight is escalated and a detailed review of the customer and the business strategy is conducted. This will identify alternatives which can be put in place. As a last resort, where this is insufficient to turn around a business, enforcement action to take possession of the property may be required.<sup>4</sup>
33. We estimate that on average, the time between ANZ first issuing a default notice and actual enforcement is about 1.5 years for non-Agribusiness customers and over 2.5 years for Agribusiness customers.<sup>5</sup>
34. On 31 August 2015, ANZ announced that we would extend drought relief measures for farmers until 31 December 2016. The measures include a moratorium on farm repossession and expansion of the relief measures to other parts of Australia. The relief measures include a commitment not to increase interest rates on financially distressed farms and interest rate relief in cases of extreme distress, financial assistance to support farmers choosing to relocate off the land and an increase in funding for rural counselling.
35. ANZ offers other forms of support to customers at higher risk where needed. This includes counselling to assist borrowers facing hardship, payment of relocation costs where a borrower needs to vacate a property, and payment of costs to upkeep the property (e.g. cleaning, mowing and general maintenance work).
36. We note allegations that ANZ enforcement action has been taken at short notice but are unaware of any case where this is correct. We have provided details of a number of customer matters on a confidential basis to the Committee. These show that

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<sup>3</sup> ANZ Submission to the Joint Parliamentary Committee on Corporations and Financial Services Inquiry into the Impairment of Customer Loans, August 2015, paragraphs 12 – 13.

<sup>4</sup> ANZ Submission (August 2015), paragraphs 22 to 42.

<sup>5</sup> ANZ Submission (August 2015), paragraph 17.

enforcement action is only taken after negotiations with customers or attempts to negotiate with customers over a long period of time.<sup>6</sup>

37. Final payment notices may be served following the failure of protracted attempts to resolve issues including farm debt mediation and when there are no other alternatives to enforcement action. We endeavour to ensure a 'no surprises' approach so our customers are aware of their position with the Bank and ensure a fair notice period is given before any enforcement. As noted earlier, there is usually a lengthy average time between issuing an initial default notice and enforcement for customers.
38. Final payment notices may trigger insolvency or action by other creditors and affect the position of directors of a company. They are often therefore served at short notice. However, it is important to distinguish between the final payment notices (which typically are served only days before enforcement) and default notices (which are the first warning sign to a borrower and are served many months, sometimes years before enforcement action is taken).
39. It would be misleading to suggest that a final notice period represents the full extent of notice given by ANZ or the process undertaken in a particular matter.
40. ANZ generally charges a higher interest rate for non-performing or impaired facilities because these loans are more costly for the bank to administer, ANZ is required to hold additional capital against the debt, and ANZ often does not recover its costs. Impaired or non-performing loans require intensive management and specialist risk management, legal and accounting treatment.
41. We acknowledge the potential for higher or default interest rates to place additional pressure on customers experiencing financial difficulty. ANZ will assess the consequences of a higher interest rate before deciding on this course of action.

## **BASIS FOR ENFORCEMENT ACTION**

42. ANZ legal or recovery action is costly for all parties and only considered as a last resort, when all other avenues are exhausted. A directly negotiated agreement, or an agreement resulting from mediation, is generally faster, less costly and less distressing for all parties than an enforcement action.
43. ANZ undertakes enforcement action as the result of a material monetary default or, in a small number of cases, in response to significant external events. For example, the appointment of a voluntary administrator by the borrower or another financier. As stated in previous evidence, ANZ examined matters subject to ANZ enforced insolvency administration as at March 2015. Of the 116 commercial customers identified, 113 were in monetary default.
44. It has been alleged that ANZ has relied on technical defaults (such as falling only \$10 behind or missing a payment by a couple of days) as a basis for enforcement action. ANZ has not become aware of any case in which it relied on a minor or technical default as a basis for enforcement action.

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<sup>6</sup> We note that a final payment demand may be served at short notice immediately prior to enforcement (see attachment). A final demand is generally served at short notice because it may trigger insolvency of the enterprise and has implications for all creditors.

45. With the permission of the customer, we would be pleased to provide advice on any matter where it is alleged ANZ has relied on a technical or minor breach as a basis for enforcement action.

## **RELATIONSHIP BETWEEN IMPAIRMENT AND ENFORCEMENT**

46. A bank's rights to recover loans arise through the failure of a customer to meet contractual obligations. Loan impairment is a financial accounting process that does not give rise to any rights of recovery against a customer. An account can be in default but not impaired, and vice versa. Impairment without contractual default may occur where an assessment is made, for example, that a business is in decline and although the customer has not defaulted, ANZ has formed a view that a loss will ultimately result. In this case, there would be no right of enforcement because there has been no default.
47. The main relationship between recovery rights and impairment is that where a customer defaults, the financial institution is more likely to recognise that loan as impaired or non-performing in its accounts.
48. A loan is impaired in the financial accounts of an authorised deposit-taking institution (ADI) to recognise that expected cash flows from the loan are not expected to be received. The timely and effective recognition of non-performing and impaired facilities by an ADI is central to the prudent management of the financial system and the stability of the economy.<sup>7</sup>
49. ANZ and other ADIs must closely monitor non-performing loans and impairments to manage credit risk and meet regulatory and accounting obligations. ADIs are in turn closely supervised by APRA to ensure that regulatory obligations are met.
50. Recognition of impairment does not advantage an ADI, except to the extent that it may increase transparency and market confidence. Impairment of loans results in an expense that must be recognised in the ADI's profit and loss statement, thus reducing profits. All things being equal, it increases requirements to hold capital and reduces shareholder returns.
51. ANZ notes APRA's testimony at the 16 February hearing that "if anything, there is an incentive for banks to not recognise impairment, rather than the other way around ..." (Hansard, page 41). We also note APRA's testimony that "that is not an incentive that is in the system" and that "Banks certainly do not have an incentive to take what are healthy or recoverable facilities and default them." (Hansard, page 40.)
52. In relation to ANZ's acquisition of Landmark, it is clear to us that there are some individual customer matters where the bank should have managed issues differently –

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<sup>7</sup> Reference has been made by the Committee and Mr King to the Tomlinson Report, "Bank's Lending Practices: Treatment of Businesses in distress", an investigation into the practices of the Royal Bank of Scotland's restructuring division by an adviser to the UK former business secretary. We note that another report was prepared by lawyers Clifford Chance on behalf of RBS which found no evidence of RBS systematically defrauding customers. The UK Financial Conduct Authority is conducting its own investigation into whether there were any regulatory breaches with the assistance of consultants Promontory Financial Group, and Mazars, the audit firm. The FCA had intended to announce the conclusions of the review by the end of 2015, but will now report "as soon as possible". See Financial Times, 18 December 2015, 'Report into RBS restructuring held up'.

with more empathy, or responded more quickly and been more transparent. We have sought to address these issues directly with customers.

53. ANZ faced no economic or other incentive for impairing Landmark loans. ANZ made no warranty claim on Landmark based on the information provided to ANZ by Landmark during the transaction. The level of impairment was known to ANZ during the sale process.<sup>8</sup>

### **ABILITY FOR CUSTOMERS TO REFINANCE**

54. ANZ seeks to build and maintain long term customer relationships. However, where a customer in financial difficulty wishes to refinance, it is generally in ANZ's commercial interest for that to occur and for ANZ loans to be repaid.
55. For the 12 months to 30 September 2015, ANZ had a total of 117 Corporate and Commercial customers refinance with limits totalling \$295 million; and in the four months to 31 January, ANZ had 29 customers refinance with limits totalling \$109 million.
56. The only cases we are aware of when ANZ has discouraged or not supported a refinance are:
- a customer in Western Australia who wished to refinance to a third tier financier at an interest rate of 3% per month (36% per annum) which would have crippled the customer's business and any remaining equity. ANZ formed the view that the right thing to do for the customer was for ANZ not to support the refinance; and
  - those cases proposing a partial refinance only and the value of the security ANZ is being asked to release is materially more than the reduction in our facilities. These cases may also lead to the customer having multiple banking relationships, which can be difficult for a small business to manage.
57. In certain circumstances, ANZ will recommend that a customer seek to repay money owed to ANZ by refinancing with another lender. In these instances, ANZ will provide a reasonable period of time for a customer to arrange alternative finance, typically three to six months, and potentially longer for farming customers.
58. It is unsurprising that other financiers are often reluctant to refinance a business that is with a bank's asset management area.
59. When a refinance lender is identified, it is common for that lender to contact ANZ and arrange the refinancing.
60. ANZ customers who wish to refinance should have all necessary information available to them, including details of their current loan facilities in ANZ's letter of offer and the payout figure. The refinancing bank usually contacts ANZ to obtain the final figure the day before settlement.
61. ANZ does not withhold information or documents necessary for refinancing. With the permission of the customer concerned, we would be happy to review any specific examples provided to us where there are suggestions that this is not the case.

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<sup>8</sup> ANZ response to questions on notice, December 29 2015, page 1.

## **VALUATION METHODS**

62. ANZ obtains farm valuations from a valuer selected from a panel of certified practising valuers. Valuations are typically reviewed and counter-signed by a director of the valuation firm and are reviewed internally by an ANZ qualified valuer.
63. ANZ has an obligation to obtain a proper assessment of the value of customer assets. ANZ typically instructs valuers to provide a market value in use for mortgagee purposes (i.e. vacant possession, with a reasonable selling period). We may also seek a valuation for an 'alternate use', depending on location.
64. ANZ does not seek 'distressed sale' valuations or seek to influence the conservative approach taken by valuers. Nevertheless, there are instances where a valuation report may discuss the impact of a rushed sale on value. In cases where an extended sales and marketing period is specified (e.g. 6-12 months), ANZ may seek an opinion as to the value based on a shorter sale period (e.g. 2 – 6 months). 'Quick' sale valuations (i.e. less than 2 months) are not requested by ANZ.
65. It is in ANZ's best interests to obtain an accurate valuation to allow for accurate provisioning. It is also in the best interests of our customers to obtain an accurate valuation so they know how much equity is remaining in their business and options available to them.
66. It is common for customers to overestimate the value of their property. Customers typically value their land based on comparative land sales and a willingness to bid higher for neighbouring properties, rather than what the property can actually produce from a cash flow perspective.

## **SALE PROCESS**

67. Where a loan has been impaired, ANZ does not have an incentive to sell customer assets at a reduced price. This would increase ANZ's loss and therefore reduce ANZ's profit. It may also drive down the value of properties owned by other ANZ customers in the region and reduce the equity these customers have in their property.
68. The appropriate method and timing of a sale will depend on many factors including the property type and geography. ANZ agrees that a "rushed" sale or truncated sale process may result in a lower price. In an enforcement scenario ANZ takes expert advice on the sales process and appropriate time frame and will continue to reassess and if necessary adjust that process as the sales campaign progresses.

## **ANZ'S APPROACH TO FARMS**

69. There is not always a clear distinction between corporate farms and privately owned family farms. Nevertheless, ANZ agrees with Senator Williams' view (expressed in the press) that enforcement on farms owned by individuals needs to be done with appropriate care and in a considerate manner, taking into account individual circumstances. With this in mind, ANZ has made and continues to make a number of changes to our procedures and the way we work with customers. For example, over the past two years, ANZ has set up a dedicated team to work with farming customers in distress. ANZ has recruited agriculture and restructuring specialists to lead this team, many of whom grew up on family-owned farms.

70. ANZ's practice is to provide family-owned farms with sufficient time (over a number of seasons), to restructure their farming business and work with the bank to avoid enforcement. ANZ would support regulatory change to require a minimum period of time between issuing a default notice and the appointment of receivers. Exemptions should allow for cases of fraud, animal welfare issues or acts that jeopardise the quality of the asset.

## D. REFORM

71. The *Treasury Legislation Amendment (Small Business Unfair Contract Terms) Act 2015* will prohibit contract terms that are unfair or cause a significant imbalance in the rights of small business, including farmers, and their financiers. ANZ is currently reviewing its standard terms to meet its obligation.
72. The unfair contract term protections will apply to standard form small business contracts entered into, or renewed, on or after 12 November 2016, where:
- the contract is for the supply of goods or services;
  - at least one of the parties is a 'small business', that is, a business employing less than 20 people; and
  - the upfront price payable under the contract does not exceed \$300,000, or \$1 million if the contract is for more than 12 months.
73. ANZ supports amending the Code of Banking Practice to require banks to provide customers with a copy of any valuation paid for by the customer. There is a case for industry-wide bank guidelines on the role and use of valuations, particularly to make sure the valuations process is transparent and easily understood by our customers. For example, how we appoint valuers and when customers should receive copies of valuations.
74. ANZ supports amending the Code of Banking Practice to require a minimum period of notice for customers to repay arrears before demanding full repayment of the loan.
75. We also support further consideration of how the industry uses non-monetary default as a trigger for restructuring, assisting customers in financial difficulty and, in rare instances (e.g. cases of fraud or animal welfare concerns), for use in enforcement.
76. ANZ supports the introduction of a national approach to farm debt mediation. While formal schemes are not currently available in all States and Territories, ANZ's approach is to offer farm debt mediation in all cases, even if it is not mandatory. The existing process could also be strengthened through the introduction of an advisory committee to represent farmers at farm debt mediation. All Australian farmers should have access to a high quality, independent mediation process operating under nationally consistent principles.
77. The Committee might also consider whether a formal, ASIC-approved external dispute resolution process could be established in relation to insolvency practitioners.
78. In ANZ's view, the banking industry should do more to provide clear and easy to understand information upfront to customers about what constitutes a 'default event'.

Customers should be made more aware of what defaults are and that there are non-monetary defaults.

## **ATTACHMENT 1 – DEFINITION OF TERMS**

79. A number of technical terms have been used in evidence to the Inquiry. ANZ believes it is helpful to distinguish these to assist the Committee:
80. Default (contractual): Default arises in a contract where the customer fails to repay agreed moneys or breaches other contractual terms. Such contractual terms commonly include requirements to provide ANZ with financial statements or a current financial statement within 30 days on request, provision of taxation returns, or a loan to security value. ANZ will treat breaches of a non-monetary covenant or initial failure to make repayments as a trigger for discussions with the customer and development of corrective actions. They not used as a basis for ANZ enforced insolvency action.
81. Default notice: A default notice is issued when a customer fails to comply with the terms of the loan documentation. It can be sent in respect of both monetary and non-monetary defaults. A default notice will specifically identify the default and set out the action that ANZ requires the customer to take to remedy the default (if it is capable of being remedied) including any timeframe in which that action must be taken. Where ANZ is working with the customer to agree on a turnaround strategy and if a default occurs, ANZ's default notice may simply reserve ANZ's rights (rather than set out specific action to be taken). This will then give ANZ and the customer time to finalise the turnaround strategy and document any new arrangements.
82. Default (prudential): Banks use the definition of default outlined in APRA standard APS 113 to calculate risk weighted assets (that is asset valuation adjusted for risk) for regulatory capital adequacy purposes. The relevant definition is not the same as a default under contract.<sup>9</sup>
83. Payment demand: A payment demand will typically only be issued when all alternatives are exhausted, likely after a long period of customer negotiation, and immediately before enforced insolvency administration. It is generally issued at short notice (e.g. 48 hours) because it may render a borrower insolvent and creditors of the enterprise will seek to protect their assets. The borrower can pause the banks enforcement action through lodging a complaint with FOS or seeking a court injunction.
84. Impaired loan: Impairment is an accounting and prudential regulatory requirement. A loan must be classified as impaired if there is doubt over the collection of the cash flows to be received by the bank. The purpose of this is to ensure that the bank's financial position can be properly assessed. Impairment is not a ground for enforcement (although a loan subject to enforcement must be impaired since it is not expected to be repaid). APRA standards APS 220 and APS 113 set out the most relevant regulatory standards.<sup>10</sup>

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<sup>9</sup> ANZ Submission, paragraph 105 to 106.

<sup>10</sup> ANZ Submission, paragraphs 92 to 104.