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Unethical' banks under scrutiny as royal commission returns

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Senior conservative figures have criticised the big banks for their aggressive treatment of some small businesses, with the royal commission expected to reveal more examples of irresponsible lending and harsh loan enforcement this week.



Dario Pappalardo is a former property developer who was declared bankrupt.

Photo: Jason South

Business lending and the policing of loans will be the focus of the next round of the financial services [royal commission](#) in Melbourne. Senior counsel assisting the commission Rowena Orr and Michael Hodge are likely to focus on the impact of overzealous lending and enforcement when customers provided guarantees involving their property and other assets.

Liberal senator David Fawcett said a parliamentary inquiry he chaired in 2016 into the "impairment" of small business borrowers left him thinking some small businesses that borrowed from banks were set up to fail.

"Yes, I was surprised that there was such a disregard of the human costs of their decisions and the fact that they allowed their systems to develop to the point where small businesses were essentially set up by the way the banks operated," Senator Fawcett said.

He said the inquiry had found some small business owners were overly optimistic, but added loan contracts were "completely asymmetric" by placing too much power in the hands of the banks. While bank staff selling loans offered optimistic valuations for customers, the contracts allowed banks' credit departments to foreclose on the loans by applying "dramatically" different valuations.

Senator Fawcett said: "Was that illegal? No. But was the way that they then subsequently dealt with those people unethical? Absolutely."

After the global financial crisis in 2008, banks tightened their loan books, leading many small businesses to complain their rights had been overridden by unfair provisions in their contracts.

One issue that is likely to be scrutinised closely at this round of hearings is the allegation the Commonwealth Bank deliberately defaulted customers who were lent money by Bankwest, which CBA acquired at the peak of the global financial crisis. The bank has denied any wrongdoing.

Former attorney-general Philip Ruddock, a member of Senator Fawcett's inquiry, said he believed CBA acted inappropriately and he would not be surprised if the royal commission came to a similar conclusion.

"I was of the view that the Commonwealth Bank, having acquired Bankwest under instructions from the government, was unhappy about their loan book and wanted to change fundamentally those arrangements and did so inappropriately," Mr Ruddock said.

ANZ Bank, Commonwealth Bank, Westpac, National Australia Bank, Suncorp and Bank of Queensland will all face the hearing over the next two weeks. On Monday, the commission will hear from Philip Khoury, who reviewed the code of banking practice for the Australian Banking Association, Dana Beiglari from Legal Aid and Alastair Welsh, head of commercial banking at Westpac.



Senator David Fawcett

Carolyn Flanagan, a former Westpac customer, is listed as a witness in Monday's hearing. She told Fairfax Media she had acted as a guarantor for her daughter and her partner when they applied for a loan from Westpac to buy a Poolwerx franchise.

However, the business did not succeed and Ms Flanagan lost ownership of her home. Ms Flanagan claimed she had been misled by the bank, and brought her case before the Financial Services Ombudsman. She was unsuccessful and Westpac has granted her a lifetime tenancy.

"Never trust them, otherwise you will lose your home," Ms Flanagan said.

Non-monetary defaults

Australian Small Business and Family Enterprise Ombudsman Kate Carnell claims the alleged power imbalance between banks and small businesses continues.

"I am very hopeful that the royal commission will look at the [Commonwealth Bank and Bankwest takeover](#), ANZ Landmark and a range of the fairly systemic approaches the big four banks particularly, but others as well, took in terms of defaulting small business, but particularly those that continued to pay what they owed," she said.



Kate Carnell is concerned about the use of non-monetary default.

Photo: Jessica Hromas

Ms Carnell said a key issue was the banks focus on their own risk and profitability rather than working with small businesses to help them through difficult times.

Unequal relationship

Former senior National Australia Bank executive Joseph Healy said small business customers could find themselves exposed to "hugely unfair" arrangements.

Mr Healy, a former head of business banking at NAB and co-founder of challenger bank Judo Capital, says the problems with banking stem from the big four banks having close to 85 per cent of all small and medium-sized business lending.

"It is quite an unequal relationship and the apparent strength of the banks places them at a huge advantage," he said. "Most small businesses don't negotiate but have to accept the terms and conditions offered to them."



Joseph Healy is the former head of NAB business banking.

Photo: Elke Meitzel

Mr Healy also highlighted non-financial default as an issue for small business.

"A small business can be performing exactly in line with a contract, but if the bank takes a particular view on an industry, let's say, for example, retail pharmaceuticals, suddenly all facilities, regardless of how well they have performed, come under scrutiny with the risk of them being withdrawn," he said.

Scarred

Dario Pappalardo, who was a property developer in Melbourne, says he is still wearing the scars after a dispute with NAB during the global financial crisis. His case is not expected to appear before the royal commission.

Mr Pappalardo, 56, said funding for an off-the-plan apartment project he was pursuing was frozen in mid-2008, and he never received a complete answer on why the bank had done so.

Construction stopped, and he was transferred to the bank's restructuring division. Family members helped financially, including by borrowing against property, but he was ultimately declared bankrupt in mid-2009 by a creditor. Family members ended up with the debt, which Mr Pappalardo is still paying back. He lost his building licence as a result.

He said that in mid-2007, the bank failed to obtain a document that it should have sought from a former business partner, and this later prevented him from selling a property when things became financially difficult.

He said was unable to refinance and described being stuck in the bank's "default mechanism" as being like a "sand trap".

A spokesperson for NAB said that when customers had difficulty repaying their debts, the bank worked closely with them to preserve their businesses so they could keep trading and ultimately repay their debts or sell assets to maximise their return.

"While we can't comment on specifics of this case, NAB continued to work with the customer to look for solutions after the customer and other directors appointed voluntary administrators to one of their companies," the spokesperson said.

NAB is set to appear before the commission's case studies on enforcement and management of loans, which may take place next week.

Commentary Footnote:

It has been six years and three Federal elections since the Royal Commissioner Hayne handed its final report the Josh Frydenberg and nothing meaningful has changed.