Consumer Protection against Pro-active Repricing

Introduction

My submission relates to the Financial System Inquiry's (FSI) recommendation 34 – to ratify The Treasury's review of the proposal to extend unfair contract term protections to apply to financial contracts between Small and Medium-sized Enterprise's (SME) and banks.

Unfair contract term provisions

Support Government's process to extend unfair contract term protections to small businesses.

Encourage industry to develop standards on the use of non-monetary default covenants

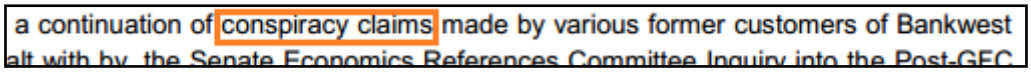
The key example highlighting the current imbalance of power between banks and SME's is the 2008 CBA takeover of Bankwest and CBA/Bankwest's use of manufactured non-monetary covenant defaults to foreclose on otherwise productive Bankwest customers in order for CBA to improve its financial position by way of a clawback clause embedded in the Bankwest purchase contract.

I make this submission as a private citizen of Australia and include attached my original submission to The Treasury's review into Unfair Contract Terms.

CBA/Bankwest allegations – abuse of non-monetary covenants

For several years the Bankwest victims have been writing to Senators and Members of Parliament alleging that they were aggressively forced into foreclosure during the 2008-2012 period. The 2012 Senate Inquiry into the post-GFC Banking Sector heard that during this period Bankwest had its own internal funding withdrawn by its parent company HBOS (UK). CBA bought Bankwest on 19th Dec 2008 and immediately proceeded to foreclose on otherwise performing loans by manufacturing various non-monetary defaults on these Bankwest customers (Reference : Appendix A – Senator Eggleston's speech 25th March 2014).

The bank's position has always been that of obfuscation and denial. CBA General Counsel Mr David Cohen wrote to the Senate Committee on 4th July 2013 saying that these allegations are "conspiracy claims made by various former customers of Bankwest" and that "those former customers find the truth as provided by CBA to the (2012 post-GFC Banking Sector) Inquiry inconvenient because it does not fit their myopic belief that somebody other than themselves must be responsible for how events unfolded."


a continuation of conspiracy claims made by various former customers of Bankwest
alt with by the Senate Economics References Committee Inquiry into the Post-GFC

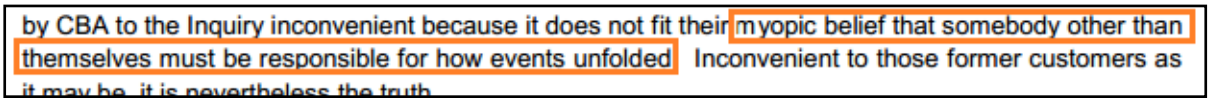

by CBA to the Inquiry inconvenient because it does not fit their myopic belief that somebody other than themselves must be responsible for how events unfolded. Inconvenient to those former customers as
it may be, it is nevertheless the truth

Figure 1 - Excerpts from CBA General Counsel's Letter to the Senate, 4th July 2013

CBA Financial Planner Scandal

Unbeknownst to many Australians, while Mr Cohen was denying the Bankwest "conspiracy" another CBA conspiracy was being exposed in the media in 2014. Allegations aired at the Senate Inquiry into the Performance of ASIC in its handling of the CBA Financial Planner scandal showed Australians that CBA are capable and willing to engage in systemic misconduct and subsequently mislead Parliament and in turn the public in order to cover it up (Reference: Appendix B – CBA mislead Senate with "sketchy" information). The Bankwest scandal will soon play itself out in the media and Parliament just as the Financial Planner scandal did.

Moral Hazard

Despite a Senate recommendation that a Royal Commission be called to investigate the CBA Financial Planner misconduct and cover-up there has been no punitive action for any of the executives involved in the initial misconduct or subsequent cover-up. In fact CBA does not even need to pay damages to the aggrieved customers. This means the bank can unlawfully take customer's money, deny it for up to 10 years and then in the unlikely event that they get caught, simply pay it back at their convenience. The bank gets the benefits of keeping this ill-gotten money for 10 years - effectively a form of forced vendor financing via the customer.

The unwillingness of ASIC to prosecute those involved in the scandal and cover-up coupled with the financial benefits of such a fraud-based banking model has effectively created a moral hazard in that all financial institution can now see that there is no punitive action taken against anyone by the regulators for systemic misconduct.

As if to highlight their ineptitude, ASIC management has attempted to brag about their recent achievement of gaining a record fine against a company that is already in administration (Appendix E - Appendix E – ASIC's record fine on company in liquidation). Fining a company in administration is akin to fining a death-row inmate - it serves no purpose. This is the best that the Australian Financial Regulator can achieve and highlights the need to give SME's legislative protection from misconduct from banks. Any new legislative protection or recourse needs to be such that SME's do not need to rely on ASIC to take action.

Capital Constraints and Prudential Reserves

In an attempt to reduce the chances of a re-occurrence of the 2008 financial crisis Government Regulators have been imposing stricter prudential reserve "buffers" on banks. There have been several articles on how this effects the Australian banks (Reference: Appendix C- APRA imposes increased prudential reserve rules). I have previously put forward the theory that CBA foreclosed on performing Bankwest loans in order to maintain its higher capital reserve requirements in 2008.

The bank has refuted this putting forward the argument that banks are forced to hold extra capital against defaulted customers. I believe that the extra capital holding cost is far outweighed by the benefit in penalty interest and exorbitant penalty fees and asset stripping that occurs when a performing loan customer is forced into default by the bank alleging a non-monetary covenant breach.

Other banks follow CBA's lead

In recent times we have now seen other banks follow CBA's lead. ANZ have recently come under scrutiny by the media for foreclosing on a farmer using non-monetary covenant default. Similar to the Bankwest allegations, this farmer never missed any mortgage payments and was evicted by the bank. The customer has no legal recourse or protection. Many end up with serious mental and physical illness and some resort to suicide. (Reference: Appendix D – ANZ foreclose on farmer by invoking non-monetary covenant default). There are many other examples like this.

Banks use non-monetary covenant defaults to circumvent the original contract once the bank unilaterally decides to change risk profiling when the economy and credit market changes. The customer has no protection from banks who decide that a certain sector of the economy is no longer profitable in relation to credit risk or, in the case of the Bankwest purchase, when an acquired bank's risk profile across business sectors needs to be brought into line with the acquiring bank (CBA). Currently it does not matter if the customer is up to date on their repayments. The bank will simply engage receivers to asset strip the customer knowing that the customer's cash flow and assets are sufficient enough to repay the extra penalty fees.

Standard Form Contracts vs Non-Standard Form Contracts

Currently the proposed extension of Unfair Contract Protections only applies to Standard Form Contacts also known as "Take it or leave it Contracts". The FSI Report notes that any protection extended to bank contracts will not apply to non-standard contracts. I am not aware of any legal definition or precedence's that distinguish between the two types of contracts.

In my experience with bank's I believe that if given the opportunity banks will simply circumvent proposed changes by manipulating their credit contracts to fit within the legal definition of a non-standard contract by making minor grammar or format changes and issuing various contract templates across different lending sectors or locations and claim their contracts to be non-standard form. It will then be up to the customer to spend hundreds of thousands of dollars to firstly have a court declare the contract to the "standard form" for the purposes of the Unfair Contract protection which then adds to the cost of having to run the court action pursuant to the Unfair Contract legislation. **If banks are allowed to circumvent the Treasury's attempt at bank reform legislation then this makes this whole exercise of legislative reform futile**. I propose that the extension of unfair contract term protections be applied to both standard form contracts and non-standard form contracts.

> The Inquiry supports Government's public consultation and policy development process for extending the coverage of UCT protections under standard form contracts to small businesses. Although such protections would not prevent unfair terms in non-standard contracts, the Inquiry believes this approach may improve broader contracting practices and the fair exercise of rights pursuant to non-monetary default covenants. The Australian Securities and Investments Commission (ASIC) could also make protections more effective by clarifying its intent to enforce UCT provisions.

Figure 2 - FSI Report, Page 264

Unfair Contract Term enforcement

When looking at legislative reform to rectify the imbalance of power between banks and SME's it is important that the financial regulator is prepared to enforce these laws. Given the recent Commonwealth Bank scandals it is common knowledge that ASIC have systemic issues of competence within senior management. I have made a submission (#73) to the current Senate Economics References Committee's Inquiry (Scrutiny of Financial Advice – SoFA) that the oversight of the portfolio of ASIC be better suited to the Office of the Attorney General rather than Treasury as the Attorney General will have the appropriate legal background in which to hold ASIC management accountable for complicity and when required invoke the Ministerial Direction provision of the ASIC Act (section 14). The FSI Report has made note of the importance of the issue of ASIC (Figure 2) and I believe that this current review by Treasury coupled with the forthcoming SoFA Senate Inquiry is an opportune time to transfer oversight of ASIC to the Attorney General.

Wealth Creation doctrine vs Wealth Transfer doctrine

The traditional banking doctrine is that of *wealth creation*. The bank engages with a customer. The customer's business grows and the customer in turn repays the bank for their assistance. The bank profits along with the customer whose business in turn creates more jobs. All parties benefit.

The current banking doctrine is not of *wealth creation* but rather *wealth transfer*. The bank engages with a customer. The bank uses non-monetary covenant clauses to default the customer in order to charge exorbitant penalty fees and charges. The customer goes bankrupt or worse still takes money from their super or from family to pay the banks demands. The customer is no longer a productive, employment creating entrepreneur. **The bank benefits at the expense of the customer**.

The banks will no doubt argue that they must appoint receivers and "go in early" to protect their security however with the *wealth transfer* model the banks protect their security by destroying the business which then has negative effects through the economy. The bank has no vested interest in the customers or their business – only its security. In fact it is in the bank's interest to take whatever equity is left in the business through fees and charges through the banks' Receiver network.

Alternatively the customer has every reason to protect the bank's security as it forms part of their business and personal life, especially as most SME's mortgage the family home. A more beneficial option is to provide the customer with legislative protection and recourse to stop the banks from "going in early" unnecessarily or unlawfully. When next we have a situation when the customer is not in financial difficulty and the banks are, then the customer will be able to take steps to either move to another bank or sell-up or "tip in" extra funds to satisfy the bank. The bank's security is protected and the economy does not suffer as the customer's business continues.

In its 2008 Annual Report, Bankwest refer to this wealth transfer process using the colourful euphemism "proactive repricing".

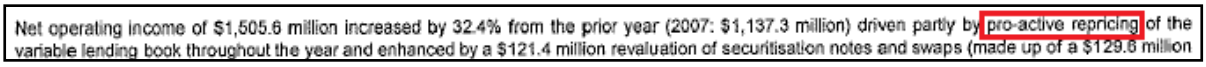

Net operating income of $1,505.6 million increased by 32.4% from the prior year (2007: $1,137.3 million) driven partly by pro-active repricing of the variable lending book throughout the year and enhanced by a $121.4 million revaluation of securitisation notes and swaps (made up of a $129.8 million

Figure 3 - 2008 Bankwest Annual Report, page 3

Currently customers have no protection for when the next GFC occurs and banks decide to once again engage in "proactive repricing" using non-monetary covenant defaults. It is for this reason that adopting FSI Recommendation 34 is so important for the economy and the community. It is important to note that the adoption of FSI Recommendation 34 will not affect the bank's ability to

take mortgagee-in-possession of its security if the customer has missed mortgage repayments (i.e. monetary default).

Conclusion

I am aware that many Bankwest victims have either met with Mr David Murray or spoken to the FSI Panel at the public forums about their experience with CBA/Bankwest's abuse of non-monetary covenant defaults. I commend the FSI Panel's ratification of Minister for Small Business Mr Billson's proposal to extend unfair contract protections to apply to financial contracts. The inclusion of any contract term that can be unilaterally invoked by a bank with no warning or recourse by customers is by its very nature unfair. I would assume that the banks will lobby the government to maintain this unfairness and hope that the Government recognise that given the current climate of a struggling business sector and booming bank profits this position is indefensible.

Appendix A – Senator Eggleston's Bankwest Speech 25th March 2014

http://www.smh.com.au/business/banking-and-finance/cba-accused-of-defaulting-customers-to-fix-bankwest-books-20140326-35htg.html

CBA accused of defaulting customers to fix BankWest books

March 26, 2014

James Eyers

Bankwest has been accused of improperly defaulting clients.

In an extraordinary late night speech to parliament, Liberal Party Senator Alan Eggleston has accused the Commonwealth Bank of Australia of improperly defaulting various business customers of Bankwest - which CBA bought during the financial crisis - to claw back the acquisition price and prevent its funding costs from rising due to global banking rules.

Senator Eggleston said he was in possession of information provided by a victim of a CBA forced sale that may lead a court to "conclude that CBA had a predetermined outcome it needed to achieve, and it opportunistically capitalised on Bankwest's dire financial situation by manufacturing defaults on certain customers to engineer the result that it wanted".

Allegations of aggressive conduct by CBA and Bankwest during the financial crisis are long-running and the Senate investigated the claims in 2012. Several customers told the economics committee they had never missed interest repayments and CBA and Bankwest took possession of their businesses in 2009 without proper due process.

CBA and Bankwest have consistently and strenuously denied any misconduct. The CBA takeover of Bankwest was led by CBA's then-head of strategy Ian Narev, who is now chief executive, and was supported by Australia's financial regulators and federal government. The banks told the 2012 inquiry foreclosure typically incurred substantial costs.

However, Senator Eggleston said a victim of a forced sale had recently suggested to him that the capital provisions of the global banking rules known as the Basel Accords could provide an explanation for the behaviour of CBA and Bankwest, and he called for a new inquiry to establish the facts.

"It was very much in CBA's interests to impair otherwise viable loans," Senator Eggleston told the Senate late on Tuesday night. "The implications of this conduct are profoundly serious, and it has been suggested the matter can only be resolved by establishing a public inquiry to establish the facts as to whether or not the foreclosures on Bankwest clients were driven by Basel Accord requirements and whether [borrowers] need greater legislative protection."

Senator Alan Eggleston. *Photo: Andrew Taylor JAT*

'Continuation of conspiracy claims'

The Basel Accords are global banking rules which have been implemented nationally by the Australia Prudential Regulation Authority. Rules regarding capital adequacy require banks to hold capital relative to their risk weighted assets. The ratio feeds through to a bank's credit rating and the price they pay for funds. The Senator suggested CBA had an incentive to remove certain Bankwest assets from its books to improve the ratio. He said at the time, CBA had progressed to Basel II advanced accreditation and was applying for US Federal Reserve holding status, which both required higher levels of capital.

"If the incorporation of Bankwest's capital and risk weighted assets put downward pressure on Commonwealth Bank's Basel ratio, then it was put to me that it would be in the Commonwealth Bank's commercial interest to remove certain customers from the balance sheet rather than risk a drop in the Basel ratio," Senator Eggleston said.

"Such a drop would decrease Commonwealth Bank's profitability across all products through an increase in capital costs, among other things."

A response to the Senator's speech was being sought from CBA.

Senator Eggleston also said CBA was motivated to default customers to "claw back" the amount paid to Bankwest's former owner, HBOS of the UK. He said the clawback price reduction mechanism allowed CBA to offset $302 million of the original $2.428 billion purchase price.

Claims of clawback have been made previously but never been proved.

CBA general counsel David Cohen told the Senate last year that allegations about clawback were a "continuation of conspiracy claims made by various former customers of Bankwest".

"CBA categorically denies that any form of separate or collateral financial benefit was advanced to CBA prior to acquisition that would compensate it for any post acquisition impairments."

Appendix B – CBA mislead Senate with 'sketchy' information

http://www.smh.com.au/business/banking-and-finance/cba-asic-slammed-over-sketchy-senate-inquiry-submissions-20140528-3942s.html

CBA, ASIC slammed over 'sketchy' Senate inquiry submissions

May 28, 2014

Adele Ferguson and Ben Butler

The Commonwealth Bank has revised key details about the measures it took in compensating victims of misconduct by several of its financial planning businesses *Photo: Jessica Shapiro*

- CBA told to reopen compensation for advice victims
- Insider's view to CBA financial planning scandal
- Rollo Sherriff and Meridien Wealth: How a rock-solid institution backed impenitent maverick

The senate inquiry into ASIC has slammed the Commonwealth Bank for providing "sketchy" information and failing to keep it and the corporate regulator fully informed about compensation for victims of its financial planning scandal.

Chairman Senator Mark Bishop said new information received from ASIC and CBA was "sketchy" and left many key questions about the scandal unanswered.

This included the number of clients affected by poor financial advice from some of the bank's planners who had not been told of their loss or offered financial help to assess their claim.

In a tweet, Senator Bishop said "I am alarmed ASIC says over 4000 clients affected by inconsistent approach CBA applied to compensation measures Maybe tens of thousands."

Senator Bishop also tabled a letter from the bank that corrects earlier evidence to the senate inquiry.

Contrary to its earlier submissions and public statements, the bank admitted it had not offered all victims of its Commonwealth Financial Planning and Financial Wisdom arms $5000 to pay for an independent adviser to help assess offers of compensation.

It also admitted that not written to all victims of CFP with offers of compensation as previously claimed.

Financial Wisdom customers also did not receive letters and there was no independent oversight of compensation offers made to those customers.

The bank also admitted that earlier statements that it had paid out compensation of more than $50 million to Commonwealth Financial Planning victims was incorrect.

The bank also admitted that earlier statements that it had paid out compensation of more than $50 million to Commonwealth Financial Planning victims was incorrect.

This number in fact included Financial Wisdom.

It said its earlier claim in a senate submission, that over 7000 file reviews were carried out, overstated how many customers it had actually reviewed.

This is because some cases involved multiple customers such as husbands and wives.

ASIC also made a supplementary submission to correct the record. It blamed the bank for providing it with the wrong information.

Appendix C – APRA imposes increased prudential reserve rules

http://www.abc.net.au/news/2013-12-23/apra-imposes-new-capital-rules-on-big-four-banks/5172614

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APRA imposes new capital reserve rules on big four banks to limit economic impact of financial crises

By business reporter Pat McGrath

Updated 24 Dec 2013, 7:36am

Australia's banking regulator is introducing higher financial stability hurdles for the four major lenders, as part of a global effort to ensure big banks can withstand economic shocks.

The Australian Prudential Regulation Authority has announced it will force the banks to increase the amount of cash they hold in reserve as a buffer against financial crises.

It says the changes come amid the growing belief among Governments that tax payers should not be required to bailout banks in the event of another global financial crisis.

APRA will increase the capital reserve requirement by 1 per cent, potentially forcing the banks to hold billions of dollars more in financial assets deemed safe by global financial regulators.

PHOTO: APRA has deemed Australia's big four lenders to be "domestic systemically important banks". (AAP)

RELATED STORY: Customers take ANZ to court in class action over bank fees

RELATED STORY: NAB warns against financial new regulation

MAP: Australia

The rules will be introduced in January 2016, and apply to the Commonwealth Bank, ANZ, Westpac, and the National Australia Bank.

APRA has identified the four lenders as "domestic systemically important banks" that carry potential risk for the economy, as part of its implementation of an international protocol established by Basel Committee on Banking Supervision.

"The Basel Committee's framework responds to the strongly held view of the G20 Leaders, including Australia, that no financial firm should be "too-big-to-fail" and that taxpayers should not bear the cost of resolution," APRA said in a statement.

"The framework also emphasises that other policy tools, such as more intensive supervision, can play an important role in dealing with domestic systemically important banks."

Australia's biggest domestic investment bank, Macquarie Bank, will not be subject to the requirements.

Banks respond to new rules

In a statement to the share market, ANZ says its capital reserves are already in excess of APRA's requirements.

"Over time and through organic capital generation, ANZ may modestly increase its capital buffers from current levels," it said.

Westpac says it well placed to meet the requirements.

"Following these announced changes Westpac will review its preferred capital levels noting that there is potential for the additional capital conservation buffer to substitute, in part, for existing management buffers," it said in a statement.

"This review will take place over 2014."

The Commonwealth bank also says its current capital position is above APRA's requirements.

NAB says it has a strong capital position and expects to able to meet the new requirements.

Shares in all the major banks lifted after the announcement.

At 2:30pm (AEDT), shares in the Commonwealth Bank and Westpac shares were up by 0.7 per, NAB was 0.5 per cent higher, and ANZ was flat.

Appendix D – ANZ foreclose on farmer by invoking non-monetary default

http://www.theaustralian.com.au/business/financial-services/thousands-rally-for-grapes-of-wrath-farmers/story-fn91wd6x-1227150433006

Thousands rally for Grapes of Wrath farmers

THE AUSTRALIAN | DECEMBER 10, 2014 12:00AM

Sue Neales
Reporter - Rural/Regional Affairs

Follow @BushReporter

Grazier Charlie Phillott, 80, standing at Jumpup Country, just north of Winton, Queensland. Picture: John Elliott
Source: TheAustralian

THOUSANDS of ordinary Australians yesterday rallied to help farming families being evicted from their drought-hit stations by the big banks, as pressure grew on the federal government to intervene in the mounting crisis.

Joe Hockey promised to "do what he could" to call the banks to account, but stopped short of committing to an immediate moratorium on forced farm foreclosures that happen in the current drought.

More than 46 farm families have been driven from their homes and properties in the past six months in the bone-dry Longreach-Muttaburra district.

In northwest Queensland and the Gulf Country, now in its third year of record drought, federal MP Bob Katter yesterday said there were now nine farm foreclosures or receiverships and two suicides a week.

Winton grazier Charlie Phillott, 80, yesterday became the face of the farm debt crisis after his treatment by the ANZ bank — featured in *The Weekend Australian* on Saturday — was highlighted in a letter written by Toowoomba vet David Pascoe on social media.

Mr Phillott, his wife, Anne, and their adult family were this year thrown off remote Carisbrooke station without having missed a mortgage repayment when the ANZ began legal possession proceedings, after it had been their home for 54 years.

The octogenarian said yesterday from Winton he hoped the spotlight on his eviction would speed government action on a moratorium. "Mine's an all too common story; you make your payments, even when the banks raise the interest rate to 12 per cent, then they engineer a default and all of a sudden you find you have no rights and are off your land," Mr Phillott said.

Dr Pascoe's Facebook post compared Mr Phillott's plight with that of dispossessed American Grapes of Wrath farmers in the 1930s Great Depression.

He wrote of hundreds of "shocked, humiliated and penniless farmers" now living like "hunted-down refugees" because of banks allowed to act as "corporate terrorists."

"There is a terrible, gaping wound that has been carved across the heartland of this nation; our people — dignified, decent and honourable old men like Charlie Phillott — have been deliberately terrorised, brutalised and sold out," Dr Pascoe's letter said. "All over the inland of both Queensland and NSW, there is social and financial carnage on a scale never before been witnessed in this nation; our own Australian people are being bullied, threatened and abused by both banks and mining companies until they are forced off their land."

By last night, 1.2 million people had read and supported the letter.

Federal Agriculture Minister Barnaby Joyce told the Winton rally last Friday that there was no support in cabinet to set up the bank they demanded, in a bid to reduce the national $66 billion rural debt burden.

Dr Pascoe said it was clear Australians were enraged and had "had a gutful" of politicians allowing banks to sell farms and evict families — with foreign buyers often the beneficiaries.

"City people are only just discovering what has been going on, and are appalled this is happening in our country; that farmers are being treated like second-class citizens and politicians have no interest in doing anything about it," he told *The Australian* last night.

Sydney radio's Alan Jones yesterday read Dr Pascoe's plea to his two million listeners. He asked the Treasurer to rein in the banks and stop foreclosures while the drought continued.

Mr Hockey told Jones that he had heard the Phillott story and promised he would follow up the case with the ANZ Bank.

Appendix E – ASIC's record fine on company in liquidation

http://www.smh.com.au/business/banking-and-finance/payday-lender-slapped-with-record-fine-of-19m-20150219-13joto.html

The Sydney Morning Herald
BusinessDay

Payday lender slapped with record fine of $19m

February 19, 2015 - 7:26PM

Clancy Yeates
Banking reporter
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The Cash Store has been slapped with a huge fine.

The Federal Court has handed out a record-breaking fine of $18.975 million against a failed payday lender and its loan funder, after the two businesses flouted consumer protection laws.

On Thursday the Court unveiled the penalties against The Cash Store, which is in liquidation, and its funder, Assistive Finance Australia (AFA), after a judgement found the vast majority of contracts arranged by the firms breached consumer laws.

The Court has previously found that The Cash Store sold "useless" consumer credit insurance to customers, who were mostly on lower incomes or were receiving benefits from Centrelink.

The fine is the biggest ever civil penalty obtained by the Australian Securities and Investments Commission.

However, the judgement said neither of the two companies attended the penalty hearing, as The Cash Store was in liquidation, and AFA could not be served with legal documents because it no longer had a registered office, directors, or solicitors acting for it.

The Cash Store, which had about 80 stores and wrote up to 10,000 short-term loans of up to $2,200 a month, was a payday lender owned by a company listed in Canada. Now in liquidation, it operated until September 2013.

A judgement by Justice Jennifer Davies published yesterday cited an examination of 281 randomly-selected consumer credit insurance contracts arranged by The Cash Store (TCS) between July 2010 and September 2012.

"Out of the 281 contracts, only four contracts were found not to have involved some contravention," Justice Davies wrote.

"I found systemic and gross failures by TCS and AFA to comply with legislative requirements and a wholesale failure in process."

ASIC had argued it was "very likely" that 300,000 of the total 325,726 contracts arranged by The Cash Store had breached responsible lending rules.

ASIC's deputy chairman, Peter Kell, said the regulator had brought the case to send a signal about how seriously it took responsible lending laws.

"This is a landmark case for the consumer credit regime and is essential reading for all credit licensees. The significant size of the penalty imposed shows ASIC and the Court take these obligations very seriously, as must all lenders, no matter how small the loan is," Mr Kell said in a statement.

"ASIC is all about making sure people taking out loans have trust and confidence in the consumer credit sector and that those offering credit obey the law. And those laws have responsible lending provisions that aim to protect consumers of credit services from taking out loans they can't afford and to stop businesses from taking unfair advantage of vulnerable people."

Preface

I make this submission as a private citizen of Australia. I have previously made submissions to the Senate Economics Reference Committee's inquiry into the Performance of ASIC, submission number 422 and 281. The content of my submission 281 was later used as a source of reference for the speech made by Senator Alan Eggleston in Federal Parliament on 25th March 2014 with regards to the unilateral termination of credit contracts by CBA during and after the purchase of Bankwest.

I hereby make this submission to the Treasury as part of The Hon. Bruce Billson's review as Minister for Small Business to extend unfair contract term protections to small business.

Introduction

The CBA takeover of Bankwest generated allegations from hundreds of Bankwest customers that they were unfairly and aggressively foreclosed on for no apparent reason. Most Small to Medium sized Enterprise (SME) customers who were either not in any financial difficulty or had minor difficulties that in any other situation could have been easily mitigated by a bank found themselves forced into receivership and bankruptcy. The abruptness of the bank's actions subsequently created mental and physical health issues for the Bankwest customers which led to the break-up of many families. The financial ramifications of the conduct flowed on to losses to creditors and suppliers such as builders, labourers etc.

The traditional banking process for customers in difficulty involves placing the customer into a specialised "turnaround" team. The specialised nature of this team warrants the charging of higher interest to cover the cost. After the customer is turned around the customer is then returned to local area management to continue business as usual. The CBA/Bankwest conduct exposed serious flaws in access to regulator assistance and protection legislation for SME's and shows that there are circumstances where it is in a bank's commercial interest to act in contravention to the customer's commercial interests and aggressively foreclose on the customer.

The three situations arising from the Bankwest takeover are:

1) If, such as Bankwest did in 2008, a bank becomes insolvent due to the withdrawal of its funding base by its parent company;
2) If, such as CBA did in 2008/9, a bank is engaged in a Basel strategy that requires a higher Basel Capital Adequacy ratio; and
3) If, such as CBA did in 2010/11, a bank wishes to adjust its risk portfolio and exposure to certain sectors.

Non-monetary covenant defaults

The solution used to address all of the above situations was to manufacture 'non-monetary' covenant defaults on the Bankwest SME customers. By 'non-monetary' covenant default I refer to any default not related to a regular monetary payment pursuant to the terms of the agreed credit contract.

The list of the most prevalent non-monetary defaults used by CBA/Bankwest are:

1) LVR defaults – The bank unilaterally decides that a customer's security has decreased in value and hence breaches the prescribed minimum loan to value ratios. N.B. There is no legal requirement for the bank to engage a registered valuer.
2) Documentation defaults – Provisions within commercial credit contracts allow for banks to request financial reports from SME's. I met with one Bankwest customer who was placed into administration simply because he had not prepared financial reports in time. He was subsequently bankrupted and lost all his assets and savings.
3) Earnings Before Income Tax (EBIT) default – I met with one Bankwest customer who was sent an EBIT default letter indicating that his pub takings had dropped below the prescribed minimum levels of the credit contract terms. After being told to ignore the letter because "everybody gets these" he was then placed into receivership and lost his business.
4) Anniversary date expiration – Many customers were never told of any problems with their loans and after the expiration of their contract continued with their business and made repayments relying on the law of conduct by estoppel to continue only to be abruptly terminated without notice.

Banks have a myriad of non-monetary methods to terminate a customer when needed but they all have one thing in common. They are done unilaterally without the customer having any chance to make any changes to their business finance.

All businesses require a short, medium and longer term plans so that businesses can plan their cash flow. If an SME owner is aware that they may struggle to make a mortgage payment in a few months then they can make the necessary changes to sell down assets or cut expenses to make sure they have the money for the repayments to avoid a monetary default.

However, an SME owner has no warning about whether a non-monetary default may arise as these are unilaterally determined by the bank. This is fundamentally unfair.

Proposed changes to Unfair Contract Terms

My submission focusses on the abuse of non-monetary covenants by banks as a tool for removing customers from their balance sheets as economic and risk profiles change. For this reason I base my suggestions on the use of standard form contracts for financial products.

Focus questions

1. How widespread is the use of standard form contracts for agreements with small business and in what circumstances are they used?
2. What types of transactions are they commonly used for, that is for which goods and services, in which industries and over what range of transaction values?
3. What are some of the benefits and disadvantages of standard form contracts?

Almost all contracts provided by banks are a standard form 'take-it-or-leave-it' contracts. Banks use standard form contracts for all services provided whether they are credit facilities, investment products or savings accounts. Standard form contracts provide economies of scale savings and have an important part in small businesses however, it is clear from the many banking related scandals,

whether it be the CBA unilateral termination of Storm margin loans, or, CBA CFPL financial planner scandal or CBA's unilateral termination of Bankwest commercial customer loans it is clear that the over use of these contracts by banks has created a significant imbalance of negotiation power between banks and small businesses.

Focus question

4. To what extent are businesses reviewing standard form contracts or engaging legal services prior to signing them? Does this depend on the value or perceived exclusivity of the transaction?

From my experience whilst small businesses will engage legal services before signing a contract with suppliers most find that it is a waste of money getting legal services to review a bank credit contract because there is nothing that can be done to change it anyway. Nearly all bank credit contracts are non-negotiable and it is for this reason that the government, through legislation, needs to increase the bargaining power of small business to improve how businesses interact with their bank.

Whilst this may create an increase in costs for the businesses it is outweighed by the protection the business gets from unconscionable conduct and enforcement by the banks of unfair contract terms.

Focus question

5. To what degree do small businesses try to negotiate contracts that are presented on a 'take it or leave it' basis? Are there types of goods and services where small businesses are more likely to try to negotiate contracts?

There is currently very little room for a business to negotiate for financial services for banks. This goes to the imbalance of power between banks and small businesses which is why banks can rely on draconian clauses embedded in credit contracts to call in loans.

Focus questions

6. What considerations influence the design of terms and conditions in standard form contracts?
7. What terms are businesses encountering that might be considered 'unfair'?
8. Do these terms relate to the operation of the contract or to remedies available under the contract?
9. What detriment have businesses suffered from UCTs and are there examples of business sectors where detriment is particularly prevalent?

The most publicised example is the recent **NSW Supreme Court case O'Brien vs Bankwest (NSWCA 71)** where on appeal it was found that clauses known as suspension clauses are incapable of defeating a claim of misleading, unconscionable or deceptive conduct. That is, **the clause embedded in all credit contracts – a clause which still exists to this day – which attempts to suspend the customer's right to sue the bank until all monies are repaid, is unlawful if there is a claim of misleading, unconscionable or deceptive conduct**. This new precedent protects the customer from any attempt by the bank to get summary judgement over them.

Interestingly the Unfair Contracts Review Consultation Paper released by Treasury contains a list of examples of what are considered to be unfair terms in standard form consumer contracts. It is worth

noting that nearly all of these are standard for commercial credit contracts. Is there any wonder why banks are running riot over small businesses?

30. Below are some common examples of terms that may be regarded as unfair if they are included in standard form consumer contracts:

Terms that may be regarded as unfair in consumer standard form contracts include terms that:

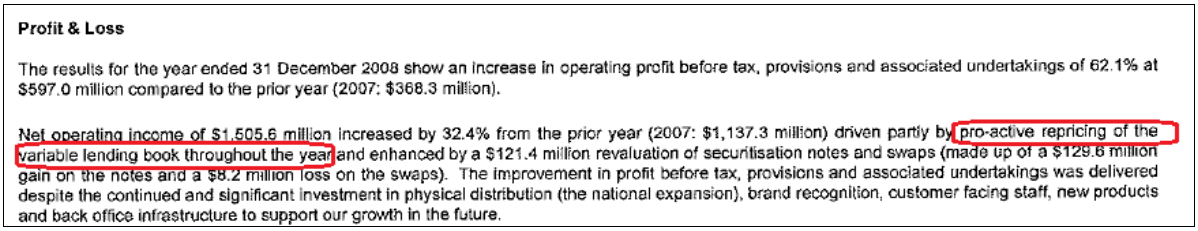
- Permit the supplier but not the customer to avoid or limit the performance of the contract, terminate it, vary its terms or renew or not to renew the contract.
- Permit the supplier to:
  - change prices without the customer's right to terminate the contract (lock in terms);
  - unilaterally determine when the contract has been breached;
  - unilaterally vary the characteristics of the goods or services to be supplied; and
  - assign the contract to the customer's detriment without the customer's consent.
- Penalise the customer but not the supplier, for breach or termination of contract.
- Limit the customer's right to sue the supplier.
- Limit the supplier's explicit liability for its agents.
- Limit the evidence the consumer can lead in proceedings on the contract.
- Impose the evidentiary burden on the customer in proceedings on the contract.

Bullet Point 1 – I have previously discussed above how banks can manufacture non-monetary covenant defaults within credit contracts. The CBA's conduct in the takeover of Bankwest shows that, in practise, a bank can unilaterally terminate or vary or chose not to renew a credit contract without having any obligation to inform the customer. There is a myriad of non-monetary covenants that can be invoked as a 'get out clause' for the bank. The most prevalent being the unilateral revaluing of the security, at the customer's expense and without the customer's knowledge which in turn creates a LVR breach. Whilst most Australians believe a bank has a duty to give the customer time to 'tip-in' extra funds to bring the LVR back down to agreed levels, we now know that it is far more profitable for the bank to immediately foreclose and then use cross-default provisions in the credit contract to seize the customer's cash. After all, why wait 30 years for a customer to pay back a loan when the bank can induce a default and seize all cash and assets immediately?

Bullet Point 2 – The Bankwest 2008 Annual Report uses the phrase "proactive repricing" as a euphemism for drastically changing the price of a credit contract (i.e. increasing the interest rate) after the start date.

Using the current state of the law, let's assume that a bank sells a credit contract to a business for a term of, say four years, for 8% and then half way through the term of the contract the bank is affected by a global crisis. The bank finds itself in a position where it should have sold this four year credit contract for 13% rather than 8%. The bank has a simple way of retrospectively repricing that contract. The bank need only manufacture a non-monetary covenant default and then charge 18% penalty interest for the second half of the contract, thereby raising the average price of the contract to 13%. (i.e. The average of 8%+8%+18%+18%). This is what has made CBA so profitable since the

takeover, by transferring the wealth of Bankwest customers to the CBA. This is the process referred to by Bankwest as "proactive repricing". Hence, non-monetary covenant defaults can be (and are) used by banks to unilaterally reprice credit contracts.



Profit & Loss

The results for the year ended 31 December 2008 show an increase in operating profit before tax, provisions and associated undertakings of 62.1% at $597.0 million compared to the prior year (2007: $368.3 million).

Net operating income of $1,505.6 million increased by 32.4% from the prior year (2007: $1,137.3 million) driven partly by pro-active repricing of the variable lending book throughout the year and enhanced by a $121.4 million revaluation of securitisation notes and swaps (made up of a $129.6 million gain on the notes and a $8.2 million loss on the swaps). The improvement in profit before tax, provisions and associated undertakings was delivered despite the continued and significant investment in physical distribution (the national expansion), brand recognition, customer facing staff, new products and back office infrastructure to support our growth in the future.

Figure 1 - Bankwest Annual Report 2008, page 5

Bullet Point 3 – It is now common knowledge that in early 2008 Bankwest was trading in insolvency and could not fulfil its lending obligations to its contracted commercial loan customers. With the current laws not only is there no penalty placed on the bank, but the bank can manufacture a non-monetary covenant defaults on the customer and charge penalty interest to extract more funds from the customer. Bankwest passed the parent company's (HBOS) default onto the customers in the form of penalty interest and receivership asset fire-sales. The Bankwest takeover has shown there is no legislative protection for SME customers in this situation.

Bullet Point 4 – See discussion above on suspension clauses, (O'Brien vs Bankwest).

Bullet Point 6 & 7- The current financial services and credit contracts are written with such favour for the banks that consumers have a raft of 'challenges' trying to even get to trial, let alone actually win at trial. I will leave this to more experienced legal minds to list.

Focus questions

10. How do unfair terms in standard form small business contracts impact on confidence and trust in the market?
11. Who is including 'unfair' terms in contracts to small businesses? Is it larger business and/or a third party (such as a lawyer) drawing up the contract?
12. Is it the terms or the process by which some contracts are negotiated between small business and business to be the primary issue for small businesses?

Bank credit contracts have been drawn up for many years by highly paid bank lawyers. They are then thrust upon SME's to take-it-or-leave-it with no room for negotiation. If we add to this, the banking oligopoly that exists in Australia then SME's and in turn the Australian economy, are effectively held hostage to these contracts with no protection against any unfair terms.

Furthermore the Australian public, media and politicians are only now starting to understand through the various inquiries, be it, CBA Storm Senate Inquiry, CBA post-GFC Senate Inquiry (2012) and CBA/CFPL (performance of ASIC) Senate Inquiry 2014 that there is no effective regulatory protection – FOS,COSL, and ASIC are toothless tigers. This does not bode well for market confidence and will discourage foreign investment.

Focus question

15. How are small businesses currently addressing issues with respect to UCTs? Are they resolving complaints informally or addressing complaints through more formal channels such as regulators?

The current process of complaint handling for contractual breaches by banks is beyond farcical. The customer must first complain via the banks Internal Dispute Resolution (IDR) process. If this fails then the customer may progress the complaint to COSL/FOS, which in the case of CBA may include the same person. The most publicised example of this is that of Dr Brendan French who was concurrently a FOS Board member and CBA General Manager of Customer Service until this alleged conflict of interest was highlighted in a social media campaign.

If the FOS/COSL process fails then the customer may progress the complaint to ASIC. ASIC have shown that they are reluctant to prosecute high level systemic misconduct by the banks. From my experience this is related to career progression by ASIC senior management. After all, once ASIC senior management complete their tenure at ASIC they will most likely be using their financial services skills at a private financial institution. It can then be safely argued that prosecuting one's potential future employer does not bode well for career progression.

Whilst I cannot provide a solution on what the government can do to fix this, I can however suggest what the government should not do. It should not reward repeated failures by ASIC management but rather remove those who repeatedly fail to act, and final accountability lies with the Chairman and Deputy Chairman.

Focus question

18. To what extent are businesses relying on/enforcing unfair contract terms?

In terms of financial services, nearly all recent banking scandals are based on banks unilaterally enforcing unfair terms of financial services contracts. (i.e. CBA unilaterally called in Storm financial margin loans without issuing a margin call. CBA unilaterally called in Bankwest commercial loans using non-monetary covenant default).

Focus questions

32. Would the benefits of a targeted legislative response (such as only deeming specific unfair terms offered to small business as void) outweigh the costs of such an approach?
33. How would such an approach interact with existing regulatory protections?
34. Are particular types of terms in standard form contracts (such as unilateral contract variation, or termination rights) more likely to be considered 'unfair' by small businesses?

I would applaud any government moves to specifically target non-monetary defaults to deem them as unfair for use in financial credit contracts. Such a move would be a swift and decisive solution to the many bank scandals and improve business productivity and confidence through enabling long term business planning without the inherent fear of the bank acting unilaterally on such unfair contract terms to terminate the SME's credit contract.

It is safe to assume that banks will lobby against such changes by arguing that deeming non-monetary clauses as unfair will mean the increase of risk in the bank's portfolio so the banks will need to reprice this risk in the form of higher interest rates passed onto customers. The reality is that banks currently already have a risk premium priced into the interest rates charged, but the legislation is such that they currently have little or no risk in their portfolio, hence this argument is mute.

Furthermore, any threat to increase in interest rate risk premium by such changes can be mitigated by an accompanied government policy to increase competition in the banking sector. The idea has been floated of the divesting of Bankwest and St George Bank, however, the topic of competition is beyond the scope of this submission.

Summary

Issue A	To extend the provisions to small business, an amendment will be required to repeal the term 'consumer contract' so that small business standard form contracts, where goods and services are not purchased for personal consumption, are also captured by the provisions.
Option A.1	Define on the basis of whether a business is publicly listed.

For the purposes of this submission I nominate option A.1.

Focus questions

41. What are the benefits and disadvantages of each definition option?
42. What option is the most appropriate definition for extending the UCT laws? Should it be defined by business or transaction size?

It is my opinion that UCT laws should extend to any financial service or credit contract entered into by a small business with another business defined as a credit provider pursuant to the National Consumer Credit Protection Act 2009.

Issue B	Currently, the UCT provisions only apply where a consumer acquires goods or services. Small businesses play a dual role in the consumer policy space — they acquire goods and services from businesses for the purpose of using them or transforming them in the process of production or manufacture, and they supply goods and services to businesses.
Option B.1	The amendments could capture small business contracts involving supply or acquisition of goods or services with another business.
Option B.2	The amendments could capture small business contracts only involving the acquisition of goods or services from another business.

For the purposes of this submission I nominate option B.1.

Focus question

43. Should the extension of the UCT provisions provide protection for small business when they acquire and supply goods or services?

Yes.

Issue C	There is a question whether the UCT extension should cover contracts between two small businesses (however defined).
Option C.1	The extension could allow for a contract between two small businesses to be captured by the laws.
Option C.2	The UCT provisions could be restricted to where there is one small business (however defined) to the transaction.

For the purposes of this submission I nominate option C.1.

Focus question

44. Should any extension void unfair terms in a small business to small business contract?

Yes. The extensions should also cover situations where small businesses enter into financial contracts with smaller credit wholesalers or brokers. Essentially, the extensions should cover any credit provider who must apply for a credit license pursuant to the National Consumer Credit Protection Act 2009.

Issue D	The UCT provisions in the ACL are substantially replicated in the Australian Securities and Investments Commission Act 2001 (ASIC Act), as they apply to financial services and credit. In the context of the ASIC Act, a consumer contract is defined as a standard form contract that is a financial product or a contract for the supply, or possible supply, of services that are financial services.
Option D.1	The extension of the UCT provisions could also cover financial products and services provided to small business so that the ASIC Act provisions remain consistent with equivalent ACL provisions.

For the purposes of this submission I nominate option D.1.

Focus question

45. Do you consider that the UCT laws within the ASIC Act should be extended to apply to small business contracts?

Yes! Most Definitely! This would be a good start to addressing the imbalance of power between banks and SME's. Of course, getting ASIC to act on breaches of this nature by banks is another issue altogether. As it is now clear from the many senate inquiries into CBA misconduct that ASIC are unwilling to pursue cases of high level banking misconduct it would be of further benefit for SME's if the government were to extend these protections such that SME's could seek remedy themselves rather than rely on ASIC.

A colleague of mine who is a lawyer with a financial services enforcement background has suggested that the consumer protections within the Corporations Act could be extended to financial products with the simple changes in Appendix A below.

<u>Conclusion</u>

CBA used the imbalance of legislative power to unfairly manufacture non-monetary defaults on Bankwest SME customers. It did so to make the Bankwest loan book fit within the constraints of CBA's more stringent Basel strategy. Basel 3 will be implemented in 2015.

For the reasons detailed above I suggest that the government take legislative steps to either directly target the deeming of non-monetary defaults in credit contracts as unfair contract terms and/or the changes highlighted in option(3), option (A.1) , option (B.1), option (C.1) and option (D.1). These options provided in the consultation would be a good start to the process of increasing protections to stop banks from using unconscionable methods for foreclosing on otherwise viable SME's.

Appendix A

Issue:

Legislative changes to ensure bank customers have the same rights as clients of other financial services providers.

The Problem:

Section 1041 of the Corporations is intended to establish fair standards of practice by providers of financial services and financial products by prohibiting certain conduct, the relevant provisions being:

1041E False or misleading statements

1041F Inducing persons to deal

1041G Dishonest conduct

1041H Misleading or deceptive conduct (civil liability only)

(See Sections Attachment -1)

A person who suffers loss or damage as a consequence of such conduct is entitled to take civil action to recover such loss or damage, in accordance with Section 1041I.

However, bank loans are excluded from the definition of financial products despite the fact that bank loans are probably the most common financial product, especially for small businesses.

(See Sections Attachment-2)

A Solution:

Amend the Corporations Act to remove common financial products issued by banks from S765A (Specific things defined not to be financial products for the purposes of the Act) and add these products into S764A (Specific things that are financial products for the purposes of the Corporations Act) and similarly amend Regulation 7.1.06

Prepared by

{Name withheld}, {Firm withheld} *[1]

[1] Contact details of author of suggested Corporations Act changes can be provided on request

Attachment -1

Sections 1041E to 1041G and S1041I Corporations Act

CORPORATIONS ACT 2001 - SECT 1041E

False or misleading statements

(1) A person must not (whether in this jurisdiction or elsewhere) make a statement, or disseminate information, if:

(a) the statement or information is false in a material particular or is materially misleading; and

(b) the statement or information is likely:

(i) to induce persons in this jurisdiction to apply for financial products; or

(ii) to induce persons in this jurisdiction to dispose of or acquire financial products; or

(iii) to have the effect of increasing, reducing, maintaining or stabilising the price for trading in financial products on a financial market operated in this jurisdiction; and

(c) when the person makes the statement, or disseminates the information:

(i) the person does not care whether the statement or information is true or false; or

(ii) the person knows, or ought reasonably to have known, that the statement or information is false in a material particular or is materially misleading.

Note 1: Failure to comply with this subsection is an offence (see subsection 1311(1)). For defences to a prosecution based on this subsection, see Division 4.

Note 2: Failure to comply with this subsection may also lead to civil liability under section 1041I. For relief from liability under that section, see Division 4.

CORPORATIONS ACT 2001 - SECT 1041F

Inducing persons to deal

(1) A person must not, in this jurisdiction, induce another person to deal in financial products:

(a) by making or publishing a statement, promise or forecast if the person knows, or is reckless as to whether, the statement is misleading, false or deceptive; or

(b) by a dishonest concealment of material facts; or

(c) by recording or storing information that the person knows to be false or misleading in a material particular or materially misleading if:

(i) the information is recorded or stored in, or by means of, a mechanical, electronic or other device; and

(ii) when the information was so recorded or stored, the person had reasonable grounds for expecting that it would be available to the other person, or a class of persons that includes the other person.

Note 1: Failure to comply with this subsection is an offence (see subsection 1311(1)). For defences to a prosecution based on this subsection, see Division 4.

Note 2: Failure to comply with this subsection may also lead to civil liability under section 1041I. For relief from liability under that section, see Division 4.

(2) In this section:

"dishonest" means:

(a) dishonest according to the standards of ordinary people; and

(b) known by the person to be dishonest according to the standards of ordinary people.

(3) This section applies in relation to the following conduct as if that conduct were dealing in financial products:

(a) applying to become a standard employer-sponsor (within the meaning of the *Superannuation Industry (Supervision) Act 1993*) of a superannuation entity (within the meaning of that Act);

(b) permitting a person to become a standard employer-sponsor (within the meaning of the *Superannuation Industry (Supervision) Act 1993*) of a superannuation entity (within the meaning of that Act);

(c) applying, on behalf of an employee (within the meaning of the *Retirement Savings Accounts Act 1997*), for the employee to become the holder of an RSA product.

CORPORATIONS ACT 2001 - SECT 1041G

Dishonest conduct

(1) A person must not, in the course of carrying on a financial services business in this jurisdiction, engage in dishonest conduct in relation to a financial product or financial service.

Note 1: Failure to comply with this subsection is an offence (see subsection 1311(1)).

Note 2: Failure to comply with this subsection may also lead to civil liability under section 1041I.

(2) In this section:

"dishonest" means:

(a) dishonest according to the standards of ordinary people; and

(b) known by the person to be dishonest according to the standards of ordinary people.

CORPORATIONS ACT 2001 - SECT 1041H

Misleading or deceptive conduct (civil liability only)

(1) A person must not, in this jurisdiction, engage in conduct, in relation to a financial product or a financial service, that is misleading or deceptive or is likely to mislead or deceive.

Note 1: Failure to comply with this subsection is not an offence.

Note 2: Failure to comply with this subsection may lead to civil liability under section 1041I. For limits on, and relief from, liability under that section, see Division 4.

(2) The reference in subsection (1) to engaging in conduct in relation to a financial product includes (but is not limited to) any of the following:

(a) dealing in a financial product;

(b) without limiting paragraph (a):

(i) issuing a financial product;

(ii) publishing a notice in relation to a financial product;

(iii) making, or making an evaluation of, an offer under a takeover bid or a recommendation relating to such an offer;

(iv) applying to become a standard employer-sponsor (within the meaning of the *Superannuation Industry (Supervision) Act 1993*) of a superannuation entity (within the meaning of that Act);

(v) permitting a person to become a standard employer-sponsor (within the meaning of the *Superannuation Industry (Supervision) Act 1993*) of a superannuation entity (within the meaning of that Act);

(vi) a trustee of a superannuation entity (within the meaning of the *Superannuation Industry (Supervision) Act 1993*) dealing with a beneficiary of that entity as such a beneficiary;

(vii) a trustee of a superannuation entity (within the meaning of the *Superannuation Industry (Supervision) Act 1993*) dealing with an employer-sponsor (within the meaning of that Act), or an associate (within the meaning of that Act) of an employer-sponsor, of that entity as such an employer-sponsor or associate;

(viii) applying, on behalf of an employee (within the meaning of the *Retirement Savings Accounts Act 1997*), for the employee to become the holder of an RSA product;

(ix) an RSA provider (within the meaning of the *Retirement Savings Accounts Act 1997*) dealing with an employer (within the meaning of that Act), or an associate (within the meaning of that Act) of an employer, who makes an application, on behalf of an employee (within the meaning of that Act) of the employer, for the employee to become the holder of an RSA product, as such an employer;

(x) carrying on negotiations, or making arrangements, or doing any other act, preparatory to, or in any way related to, an activity covered by any of subparagraphs (i) to (ix).

(3) Conduct:

(a) that contravenes:

(i) section 670A (misleading or deceptive takeover document); or

(ii) section 728 (misleading or deceptive fundraising document); or

(iii) section 1021NA, 1021NB or 1021NC; or

(b) in relation to a disclosure document or statement within the meaning of section 953A; or

(c) in relation to a disclosure document or statement within the meaning of section 1022A;

does not contravene subsection (1). For this purpose, conduct contravenes the provision even if the conduct does not constitute an offence, or does not lead to any liability, because of the availability of a defence.

CORPORATIONS ACT 2001 - SECT 1041I

Civil action for loss or damage for contravention of sections 1041E to 1041H

(1) A person who suffers loss or damage by conduct of another person that was engaged in in contravention of section 1041E, 1041F, 1041G or 1041H may recover the amount of the loss or damage by action against that other person or against any person involved in the contravention, whether or not that other person or any person involved in the contravention has been convicted of an offence in respect of the contravention.

(1A) Subsection (1) has effect subject to section 1044B.

Note: Section 1044B may limit the amount that the person may recover for a contravention of section 1041H (Misleading or deceptive conduct) from the other person or from another person involved in the contravention.

(1B) Despite subsection (1), if:

(a) a person (the ***claimant***) makes a claim under subsection (1) in relation to:

(i) economic loss; or

(ii) damage to property;

caused by conduct of another person (the ***defendant***) that was done in contravention of section 1041H; and

(b) the claimant suffered the loss or damage:

(i) as a result partly of the claimant's failure to take reasonable care; and

(ii) as a result partly of the conduct referred to in paragraph (a); and

(c) the defendant:

(i) did not intend to cause the loss or damage; and

(ii) did not fraudulently cause the loss or damage;

the damages that the claimant may recover in relation to the loss or damage are to be reduced to the extent to which the court thinks just and equitable having regard to the claimant's share in the responsibility for the loss or damage.

Note: Division 2A also applies proportionate liability to a claim for damages under this section for a contravention of section 1041H.

(2) An action under subsection (1) may be begun at any time within 6 years after the day on which the cause of action arose.

(3) This section does not affect any liability that a person has under any other law.

(4) Section 1317S (which provides for relief from liability) applies in relation to liability under subsection (1) as if:

(a) the sections referred to in subsection (1) were civil penalty provisions; and

(b) proceedings under subsection (1) were eligible proceedings.

Note: Relief from liability under this section may also be available (depending on the circumstances) under Division 4.

Attachment 2 - Corporations Act and Regulations that exclude Bank loans from Definition of Financial products and thereby excludes bank loans from this prohibited conduct.

CORPORATIONS ACT 2001 - SECT 765A

Specific things that are not financial products

(1) Despite anything in Subdivision B or Subdivision C, the following are not ***financial products*** for the purposes of this Chapter:

(a) an excluded security;

(b) an undertaking by a body corporate to pay money to a related body corporate;

(c) health insurance provided as part of a health insurance business (as defined in Division 121 of the *Private Health Insurance Act 2007*);

(ca) insurance provided as part of a health-related business (as defined by section 131-15 of that Act) that is conducted through a health benefits fund (as defined by section 131-10 of that Act);

(d) insurance provided by the Commonwealth;

(e) State insurance or Northern Territory insurance, including insurance entered into by:

(i) a State or the Northern Territory; and

(ii) some other insurer;

as joint insurers;

(f) insurance entered into by the Export Finance and Insurance Corporation, other than a short-term insurance contract within the meaning of the *Export Finance and Insurance Corporation Act 1991* ;

(g) reinsurance;

(h) any of the following:

(i) a credit facility within the meaning of the regulations (other than a margin lending facility);

(ii) a facility for making non-cash payments (see section 763D), if payments made using the facility will all be debited to a credit facility covered by subparagraph (i);

(i) a facility:

(i) that is an approved RTGS system within the meaning of the *Payment Systems and Netting Act 1998* ; or

(ii) for the transmission and reconciliation of non-cash payments (see section 763D), and the establishment of final positions, for settlement through an approved RTGS system within the meaning of the *Payment Systems and Netting Act 1998* ;

(j) a facility that is a designated payment system for the purposes of the *Payment Systems (Regulation) Act 1998* ;

(k) a facility for the exchange and settlement of non-cash payments (see section 763D) between providers of non-cash payment facilities;

(l) a facility that is:

(i) a financial market; or

(ii) a clearing and settlement facility; or

(iii) a payment system operated as part of a clearing and settlement facility; or

(iv) a derivative trade repository;

(m) a contract to exchange one currency (whether Australian or not) for another that is to be settled immediately;

(n) so much of an arrangement as is not a derivative because of paragraph 761D(3)(a);

(p) an arrangement that is not a derivative because of subsection 761D(4);

(q) an interest in a superannuation fund of a kind prescribed by regulations made for the purposes of this paragraph;

(r) any of the following:

(i) an interest in something that is not a managed investment scheme because of paragraph (c), (e), (f), (k), (l) or (m) of the definition of ***managed investment scheme*** in section 9;

(ii) a legal or equitable right or interest in an interest covered by subparagraph (i);

(iii) an option to acquire, by way of issue, an interest or right covered by subparagraph (i) or (ii);

(s) any of the following in relation to a managed investment scheme (whether or not operated in this jurisdiction) in relation to which none of paragraphs 601ED(1)(a), (b) and (c) are satisfied and that is not a registered scheme:

(i) an interest in the scheme;

(ii) a legal or equitable right or interest in an interest covered by subparagraph (i);

(iii) an option to acquire, by way of issue, an interest or right covered by subparagraph (i) or (ii);

(t) a deposit-taking facility that is, or is used for, State banking;

(u) a benefit provided by an association of employees that is registered as an organisation, or recognised, under the *Fair Work (Registered Organisations) Act 2009* for a member of the association or a dependant of a member;

(v) either of the following:

(i) a contract of insurance; or

(ii) a life policy or a sinking fund policy, within the meaning of the *Life Insurance Act 1995* , that is not a contract of insurance;

issued by an employer to an employee of the employer;

(w) a funeral benefit;

(x) physical equipment or physical infrastructure by which something else that is a financial product is provided;

(y) a facility, interest or other thing declared by regulations made for the purposes of this subsection not to be a financial product;

(z) a facility, interest or other thing declared by ASIC under subsection (2) not to be a financial product.

(2) ASIC may declare that a specified facility, interest or other thing is not a financial product for the purposes of this Chapter. The declaration must be in writing and ASIC must publish notice of it in the *Gazette* .

CORPORATIONS REGULATIONS 2001 - REG 7.1.06

Specific things that are not financial products: credit facility

(1) For subparagraph 765A(1)(h)(i) of the Act, each of the following is a ***credit facility*** :

(a) the provision of credit:

(i) for any period; and

(ii) with or without prior agreement between the credit provider and the debtor; and

(iii) whether or not both credit and debit facilities are available; and

(iv) that is not a financial product mentioned in paragraph 763A(1)(a) of the Act; and

(v) that is not a financial product mentioned in paragraph 764A(1)(a), (b), (ba), (f), (g), (h) or (j) of the Act; and

(vi) that is not a financial product mentioned in paragraph 764A(1)(i) of the Act, other than a product the whole or predominant purpose of which is, or is intended to be, the provision of credit;

(b) a facility:

(i) known as a bill facility; and

(ii) under which a credit provider provides credit by accepting, drawing, discounting or indorsing a bill of exchange or promissory note;

(c) the provision of credit by a pawnbroker in the ordinary course of a pawnbroker's business (being a business which is being lawfully conducted by the pawnbroker);

(d) the provision of credit by the trustee of the estate of a deceased person by way of an advance to a beneficiary or prospective beneficiary of the estate;

(e) the provision of credit by an employer, or a related body corporate of an employer, to an employee or former employee (whether or not it is provided to the employee or former employee with another person);

(f) a mortgage:

(i) that secures obligations under a credit contract (other than a lien or charge arising by operation of any law or by custom); and

(ii) that is not a financial product mentioned in paragraph 763A(1)(a) of the Act; and

(iii) that is not a financial product mentioned in paragraph 764A(1)(a), (b), (ba), (f), (g), (h) or (j) of the Act; and

(iv) that is not a financial product mentioned in paragraph 764A(1)(i) of the Act, other than a product the whole or predominant purpose of which is, or is intended to be, the provision of credit;

(g) a guarantee related to a mortgage mentioned in paragraph (f);

(h) a guarantee of obligations under a credit contract.

(2) The provision of consumer credit insurance that includes a contract of general insurance for the *Insurance Contracts Act 1984* is not a credit facility.

(2A) A litigation funding scheme mentioned in regulation 5C.11.01 is not a credit facility.

(2B) A litigation funding arrangement mentioned in regulation 5C.11.01 is not a credit facility .

(3) In this regulation:

credit means a contract, arrangement or understanding:

(a) under which:

(i) payment of a debt owed by one person (a ***debtor***) to another person (a ***credit provider***) is deferred; or

(ii) one person (a ***debtor***) incurs a deferred debt to another person (a ***credit provider***); and

(b) including any of the following:

(i) any form of financial accommodation;

(ii) a hire purchase agreement;

(iii) credit provided for the purchase of goods or services;

(iv) a contract, arrangement or understanding for the hire, lease or rental of goods or services, other than a contract, arrangement or understanding under which:

(A) full payment is made before or when the goods or services are provided; and

(B) for the hire, lease or rental of goods--an amount at least equal to the value of the goods is paid as a deposit in relation to the return of the goods;

(v) an article known as a credit card or charge card;

(vi) an article, other than a credit card or a charge card, intended to be used to obtain cash, goods or services;

(vii) an article, other than a credit card or a charge card, commonly issued to customers or prospective customers by persons who carry on business for the purpose of obtaining goods or services from those persons by way of a loan;

(viii) a liability in respect of redeemable preference shares;

(ix) a financial benefit arising from or as a result of a loan;

(x) assistance in obtaining a financial benefit arising from or as a result of a loan;

(xi) issuing, indorsing or otherwise dealing in a promissory note;

(xii) drawing, accepting, indorsing or otherwise dealing in a negotiable instrument (including a bill of exchange);

(xiii) granting or taking a lease over real or personal property;

(xiv) a letter of credit.