

**Royal Commission into Misconduct in the Banking,
Superannuation and Financial Services Industry**

HEARING ROUND 3: LOANS TO SMALL AND MEDIUM ENTERPRISES

ANZ'S SUBMISSION ON FINDINGS ARISING FROM THE CASE STUDY INVOLVING ANZ

A. ANZ RESPONSIBLE LENDING TO SMALL BUSINESSES (RUBRIC 3-7)

A.1 Gelato case study: summary of facts

- 1.1 On 8 August 2014, ANZ received a credit application from a small business seeking to establish a gelato franchise kiosk at the Miranda Westfield Shopping Centre in Sydney (the **Gelato Business**).¹ The application was supported by a wife and husband (**Mrs G** and **Mr G**; collectively, the **Gs**)², and was submitted by an ANZ accredited broker.³ Mrs G was originally the sole director and shareholder of the Gelato Business,⁴ with Mr G subsequently appointed as a second director.⁵
- 1.2 The purchase price for the franchise store was approximately \$340,000, plus a bond of \$38,092⁶ (for the lease of premises at the Miranda Westfield Shopping Centre).⁷ The Gs, by their application, proposed to finance 50% of the total cost through ANZ,⁸ while contributing the remaining 50% from their own funds (comprising \$110,000 in savings, plus proceeds from the sale of a property).⁹
- 1.3 Mrs G had previously worked in the food industry, including as a store manager at a well-known restaurant franchise.¹⁰ During the financial year 2013-2014, she ran an online jewellery business from her home in Sydney,¹¹ and also undertook online business management courses.¹² By August 2014, Mrs G was looking to start her own business, and to apply her skills and knowledge in pursuit of that goal.¹³

¹ As to the application, see exhibit KGG-29 to the witness statement of Kate Gibson (exhibit 3.15) (ANZ.999.009.0065) (the **Gibson Statement**): ANZ.800.534.0112. As to the location, see exhibit KGG-29 to the Gibson Statement: ANZ.800.534.0125 and ANZ.800.534.0128 at .0134. The name of the business is subject to a non-publication direction (No. DIR-136) made on 22 May 2018.

² The names of the Gs are subject to a non-publication direction (No. DIR-136) made on 22 May 2018.

³ As to the broker, see exhibit KGG-29 to the Gibson Statement: ANZ.800.534.0112; Gibson Statement: ANZ.999.009.0065 at .0096 [105]. The names of the broker, and the broking business, are subject to a non-publication direction (No. DIR-136) made on 22 May 2018.

⁴ Exhibit KGG-32 to the Gibson Statement: ANZ.800.474.0001 at .0002.

⁵ Exhibit KGG-33 to the Gibson Statement: ANZ.800.470.0611 at .0612; exhibit KGG-35 to the Gibson Statement: ANZ.800.470.0103; Gibson Statement: ANZ.999.009.0065 at .0099 [120].

⁶ The bond was ultimately \$24,161.64. See exhibit KGG-46 to the Gibson Statement: ANZ.800.546.0044; exhibit KGG-50 to the Gibson Statement: ANZ.800.474.0255 at .0257.

⁷ Exhibit KGG-29 to the Gibson Statement: ANZ.800.534.0112; Gibson Statement: ANZ.999.009.0065 at .0097 [107] and .0106 [164]. The ultimate purchase price was \$340,388 plus GST (as the "Franchise Fee") plus \$3,000 as a "Document Fee". See exhibit KGG-48 to the Gibson Statement: ANZ.800.470.0733 at .0780.

⁸ Exhibit KGG-29 to the Gibson Statement: ANZ.800.534.0112; Gibson Statement: ANZ.999.009.0065 at .0097 [107].

⁹ Exhibit KGG-33 to the Gibson Statement: ANZ.800.470.0611 at .0613.

¹⁰ Exhibit KGG-31 to the Gibson Statement: ANZ.800.539.0015 at .0047.

¹¹ T2169.06-07; exhibit KGG-29 to the Gibson Statement: ANZ.800.542.0003 at .0010.

¹² Exhibit KGG-31 to the Gibson Statement: ANZ.800.539.0015 at .0047.

¹³ Exhibit KGG-31 to the Gibson Statement: ANZ.800.539.0015 at .0047.

- 1.4 Mr G was a business analyst with another major bank. By August 2014, he had held that position for about three years.¹⁴ Mr G's gross annual income was about \$120,000.¹⁵ Mr G also owned an investment property in Griffin (Queensland), having previously owned another property in Campbelltown (Sydney).¹⁶ The Griffin property generated rental income of about \$1,600 per fortnight.¹⁷
- 1.5 It was proposed that Mrs G would work in the Gelato Business, with Mr G assisting during weekends and at nights.¹⁸ It was also contemplated that Mrs G would be assisted by another employee, and casual staff as well.¹⁹
- 1.6 Before applying for the loan with ANZ in August 2014, Mrs G, on behalf of the Gelato Business, had already entered into an "agreement to proceed" with a gelato franchisor (in June 2014). That agreement required the payment of an initial \$3,000 deposit.²⁰
- 1.7 The Gelato Business' credit application submitted to ANZ was supported by a number of documents, including a business plan. In broad terms, the proposed Gelato Business involved a lease of centrally located premises in the Miranda Westfield Shopping Centre; the construction and fit-out of a kiosk (with signage) and provision of gelato making and storage machinery and equipment at the shopping centre; and access to an existing product range, as well as training, marketing and accounting support.²¹ While the franchise was new to Australia (and was not an ANZ accredited franchise),²² it had been successfully established in New Zealand,²³ receiving a number of industry awards.²⁴ As at August 2014, there was no direct competitor to the Gs' proposed Gelato Business in, or near, the Miranda Westfield Shopping Centre.²⁵ The shopping centre itself was a multi-level centre near Cronulla, and at that time was one of the largest shopping centres in Australia, with high-level foot traffic.²⁶
- 1.8 The Gelato Business' credit application was handled by an ANZ banker who serviced an area of Sydney where the Gs lived (the **Banker**).²⁷ The Banker's activities with respect to the credit application included communicating with the Gs' broker;²⁸ speaking and meeting

¹⁴ Exhibit KGG-31 to the Gibson Statement: ANZ.800.539.0015 at .0047.

¹⁵ Exhibit KGG-29 to the Gibson Statement: ANZ.800.542.0003 at .0015 and ANZ.800.542.0025.

¹⁶ The Campbelltown property was sold in about March 2014. See exhibit KGG-29 to the Gibson Statement: ANZ.800.542.0013 at .0019-.0023; and exhibit KGG-33 at ANZ.800.470.0611 at .0614.

¹⁷ Exhibit KGG-29 to the Gibson Statement: ANZ.800.542.0002. This figure does not include expenses incurred, as identified in the rental statement.

¹⁸ Exhibit KGG-35 to the Gibson Statement: ANZ.800.470.0103.

¹⁹ Exhibit KGG-35 to the Gibson Statement: ANZ.800.470.0103. See also the business plan at exhibit KGG-30 to the Gibson Statement: ANZ.800.534.0008 at .0033.

²⁰ Exhibit KGG-29 to the Gibson Statement: ANZ.800.534.0122 and ANZ.800.534.0123.

²¹ See the business plan at exhibit KGG-30 to the Gibson Statement: ANZ.800.534.0008, and the franchise agreement at exhibit KGG-48 to the Gibson Statement: ANZ.800.470.0733.

²² T2153.43-44.

²³ See page 3 of the business plan at exhibit KGG-30 to the Gibson Statement: ANZ.800.534.0008 at .0010.

²⁴ See pages 7 and 8 of the business plan at exhibit KGG-30 to the Gibson Statement: ANZ.800.534.0008 at .0014-.0015.

²⁵ See pages 3, 5, 21 and 33 of the business plan at exhibit KGG-30 to the Gibson Statement: ANZ.800.534.0008 at .0010, .0012, .0028 and .0040.

²⁶ See pages 3 and 5 of the business plan at exhibit KGG-30 to the Gibson Statement: ANZ.800.534.0008 at .0010 and .0012.

²⁷ Gibson Statement: ANZ.999.009.0065 at .0096 [105].

²⁸ Gibson Statement: ANZ.999.009.0065 at .0098 [111]. See, for example, exhibit KGG-29 to the Gibson Statement: ANZ.800.534.0112.

with the Gs;²⁹ compiling, reviewing and submitting for assessment materials provided in support of the application;³⁰ and responding to questions from the ANZ credit assessor.

- 1.9 In speaking with the Gs, the Banker informed them that they should obtain independent legal and financial advice.³¹ Documents on ANZ's file indicate that the Gs told the Banker that they had already obtained legal advice in relation to the lease and franchise agreements and the risks associated with purchasing the Gelato Business.³² With respect to financial advice, the Banker arranged for the Gs to speak to a financial planner, but the Gs decided not to proceed with the meetings.³³
- 1.10 The Gelato Business' credit application was reviewed and manually assessed by an ANZ assessor (the **Assessor**). The assessment process took place between about 29 August and 8 October 2014. Over that period, the Assessor considered the information about the Gs, the Gelato Business, and their loan application, that was uploaded onto ANZ's small business loans system. The Assessor also sought answers to questions, and explanations for or confirmation of various matters, from the Banker.³⁴ The Assessor examined the cash flow forecast in the business plan,³⁵ and conducted a break-even analysis (involving a serviceability assessment if projected profits of the business were decreased to zero and Mrs G's salary was reduced).³⁶ The Assessor concluded, after looking first at the business and its projections, and then the circumstances of the directors (including Mr G's income), that the Gelato Business could be expected to service the ANZ debt.³⁷
- 1.11 An indicative letter of offer dated 8 October 2014 was provided by ANZ to the Gs (subject to the fulfilment of various conditions).³⁸ The letter of offer was then signed on 10 October 2014.³⁹

²⁹ Gibson Statement: ANZ.999.009.0065 at .0098 [111]; T2207.10-11.

³⁰ Gibson Statement: ANZ.999.009.0065 at .0098 [115]. The Banker first submitted the application into ANZ's SBL (small business loans) system on 27 August 2014: exhibit KGG-31 to the Gibson Statement: ANZ.800.539.0015, including at .0047-.0048. The Banker did not speak to the franchisor during the assessment process: T2170.29-30; Gibson Statement: ANZ.999.009.0065 at .0098 [111].

³¹ Gibson Statement: ANZ.999.009.0065 at .0103 [141].

³² Although the exhibits to the Gibson Statement do not explicitly refer to the Gs having received legal advice on the franchise agreement (as opposed to the lease agreement), so much should be inferred from the Banker's account that the Gs had told him that they had received advice regarding the risks of purchasing the business: Gibson Statement: ANZ.999.009.0065 at .0103 [141]; exhibit KGG-42 to the Gibson Statement: ANZ.800.470.0107; exhibit KGG-56 to the Gibson Statement: ANZ.800.470.3162 at .3167. See also exhibit KGG-58 to the Gibson Statement: ANZ.800.470.2444.

³³ Two meetings were set up, which the Gs cancelled. Exhibit KGG-56 to the Gibson Statement: ANZ.800.470.3162 at .3167. See also exhibit KGG-58: ANZ.800.470.2444.

³⁴ See, for example, the email exchange and notes of the Assessor at exhibits KGG-33: ANZ.800.470.0611), KGG-35: ANZ.800.470.0103, and KGG-42: ANZ.800.470.0107 to the Gibson Statement.

³⁵ T2161.39-44; exhibit KGG-35 to the Gibson Statement: ANZ.800.470.0103.

³⁶ T2161.39-47-2162.05; Gibson Statement: ANZ.999.009.0065 at .0101 [132]; exhibit KGG-41 to the Gibson Statement: ANZ.800.539.0217 at .0263-.0264.

³⁷ T2161.39-2162.23.

³⁸ Exhibit KGG-43 to the Gibson Statement: ANZ.800.470.0855.

³⁹ Exhibit KGG-44 to the Gibson Statement: ANZ.800.470.2947.

- 1.12 ANZ provided three facilities (totalling \$221,100) to the Gelato Business:⁴⁰ (1) a business loan (variable rate) of up to \$150,000; (2) a temporary business overdraft facility of up to \$34,000; and (3) an indemnity guarantee facility (for the rental bond at the Miranda Westfield Shopping Centre) in the amount of \$38,100.⁴¹
- 1.13 The Gelato Business and the Gs provided the following security in support of the facilities:⁴² (1) a second registered mortgage over Mr G's investment property in Griffith; (2) a general security agreement over all of the present and future acquired property of the Gelato Business; (3) an individual guarantee and indemnity from Mrs G (limited to \$222,100); and (4) an individual guarantee and indemnity from Mr G (limited to \$222,100).
- 1.14 ANZ established a bank account and business overdraft facility for the Gelato Business and, on 10 October 2014, deposited \$150,000 as proceeds of the loan draw down into the account, and made available the \$34,000 line of credit.⁴³ On 13 October 2014, \$145,000 was withdrawn from the Gelato Business' bank account and, two days later, a further \$34,000 was withdrawn.⁴⁴ On 13 October 2014, ANZ also provided a bank guarantee with respect to the bond for the Gelato Business' premises at the Miranda Westfield Shopping Centre.⁴⁵
- 1.15 Although the Gelato Business franchise agreement, sub-lease agreement and cash flow forecast in the business plan contemplated that the business would start trading in November 2014,⁴⁶ it appears that trading did not, in fact, commence until late April 2015.⁴⁷ In consequence, the Gelato Business was not able to take advantage of potential sales during the summer period. The Gelato Business ultimately commenced trading after the well-known brand, "Gelato Messina", had opened a new outlet connected to the Miranda Westfield Shopping Centre.⁴⁸
- 1.16 The Gelato Business continued to trade during 2015. However, it appears that difficulties were experienced and, in about December 2015, a decision was made to close down the business.⁴⁹
- 1.17 Mr G made a complaint to ANZ on about 30 March 2016.⁵⁰ The complaint was referred to ANZ's internal credit control governance team. Following a review of the complaint, a

⁴⁰ Exhibit KGG-44 to the Gibson Statement: ANZ.800.470.2947; T2154.15-27.

⁴¹ The bond was ultimately \$24,161.64. See exhibit KGG-46 to the Gibson Statement: ANZ.800.546.0044 and exhibit KGG-50 to the Gibson Statement: ANZ.800.474.0255 at .0257.

⁴² T2154.32-47; exhibit KGG-44 to the Gibson Statement: ANZ.800.470.2947 at .2952, ANZ.800.470.2428, ANZ.800.470.2436, and ANZ.800.546.0046.

⁴³ Exhibit KGG-45 to the Gibson Statement: ANZ.800.528.0865.

⁴⁴ Exhibit KGG-45 to the Gibson Statement: ANZ.800.528.0865.

⁴⁵ Exhibit KGG-46 to the Gibson Statement: ANZ.800.546.0044. The bond, by that time, was in the amount of \$24,161.64.

⁴⁶ Exhibit KGG-48 to the Gibson Statement: ANZ.800.470.0733 at .0780 (Sch. 1, item 1); exhibit KGG-50 to the Gibson Statement: ANZ.800.474.0321 at .0341 (Sch. 1, item 2); exhibit KGG-30 to the Gibson Statement: ANZ.800.534.0008 at .0035.

⁴⁷ Exhibit KGG-53 to the Gibson Statement: ANZ.800.470.1901 at .1902; exhibit KGG-51 to the Gibson Statement: ANZ.800.546.0001 at .0011.

⁴⁸ Exhibit KGG-65 to the Gibson Statement: ANZ.800.546.0048.

⁴⁹ Gibson Statement: ANZ.999.009.0065 at .0104 [152]; exhibit KGG-53 to the Gibson Statement: ANZ.800.470.1901 at .1902; exhibit KGG-51 to the Gibson Statement: ANZ.800.546.0001 at .0040.

⁵⁰ Gibson Statement: ANZ.999.009.0065 at .0105 [155].

credit review report was prepared (dated 6 April 2016) which upheld the Assessor's decision to approve the facilities.⁵¹ Mr G was informed of the result of the review.⁵²

- 1.18 Mr G then made a complaint to the Financial Ombudsman Service (**FOS**).⁵³ The dispute was unable to be resolved consensually, and the complaint was progressed for consideration and determination by FOS.⁵⁴ On 21 December 2016, FOS made a recommendation which it described as "substantially in favour of the Applicants".⁵⁵ The recommendation concluded, among other things, that: (1) ANZ did not act responsibly when it approved the loan; (2) the Gs were not responsible for the guarantees they provided because ANZ did not exercise the care and skill of a diligent and prudent banker when it assessed the Gelato Business' capacity to afford the loan; (3) ANZ was liable for payments made by Mr G towards the overdraft account; and (4) the Gelato Business remained responsible for the principal amount borrowed under the loan and the principal amount funded under the overdraft facility, but not for the interest and fees which had accrued.
- 1.19 ANZ disagreed with FOS's recommendation and, on about 20 January 2017, wrote to FOS setting out its position.⁵⁶ FOS made a final determination on 24 March 2017.⁵⁷ It concluded that the findings in the recommendation were substantially correct, and adopted them in its determination. It departed from the recommendation in one respect, deciding that ANZ should not be liable for payments (totalling \$67,500) that Mr G personally made towards the business. The reasons for the determination relied on the reasons contained in the recommendation, together with some further reasons in response to ANZ's submission. The correctness of those reasons, and the conclusion reached, are addressed further below.
- 1.20 Although ANZ did not agree with the FOS determination,⁵⁸ it complied with the determination by:⁵⁹
- (a) reducing the balance of the business loan and overdraft facilities to \$105,575 and \$21,505 respectively (as at 10 November 2016);
 - (b) releasing the guarantees provided by the Gs; and
 - (c) discharging its mortgage over Mr G's investment property to the extent it secured Mr G's guarantee.

A.2 Evidence of Kate Gibson

- 1.21 Ms Kate Gibson, General Manager, Home Lending, at ANZ, made a witness statement and gave evidence to the Commission in relation to the Gelato Business case study.

⁵¹ Exhibit KGG-57 to the Gibson Statement: ANZ.800.470.3142.

⁵² Exhibit KGG-58 to the Gibson Statement: ANZ.800.470.2444.

⁵³ Exhibit KGG-59 to the Gibson Statement: ANZ.800.470.1637. The precise terms of the original complaint to FOS are set out in this exhibit at .1638. Although Counsel Assisting stated in closing address that "one of the bases for [the] complaint was that the borrowers could not afford to repay the loan" (T3029.07-08), that is not apparent on the face of the dispute information provided by FOS.

⁵⁴ Gibson Statement: ANZ.999.009.0065 at .0105 [159]-[160].

⁵⁵ Exhibit KGG-62 to the Gibson Statement: ANZ.800.470.1644 at .1646.

⁵⁶ Exhibit KGG-63 to the Gibson Statement: ANZ.800.470.2419.

⁵⁷ Exhibit KGG-64 to the Gibson Statement: ANZ.800.470.2019.

⁵⁸ T2156.35-36, T2157.40-45.

⁵⁹ Gibson Statement: ANZ.999.009.0065 at .0107-0108 [174]-[175].

Ms Gibson's witness statement (with exhibits) – which responded to a request from the Commission for answers to 17 questions – was tendered in evidence.⁶⁰

- 1.22 The original request from the Commission (titled "Rubric 3-7") included a statement of the proposed evidence of Mr G with respect to the Gelato Franchise. Ultimately, Mr G was not called to give evidence, and no witness statement was provided to ANZ or sought to be tendered by Counsel Assisting.
- 1.23 Ms Gibson gave evidence before the Commission over two days: 22 and 23 May 2018. She gave honest, considered and responsive answers to questions from Counsel Assisting and the Commissioner.
- 1.24 Ms Gibson's expertise, detailed understanding of the relevant subject matter, and very careful and competent approach, was evident during the course of her evidence.⁶¹ Ms Gibson made appropriate concessions, including identifying errors with respect to ANZ's processes in considering the Gelato Business' credit application.⁶²
- 1.25 Having regard to these considerations, including Ms Gibson's rigorous and frank assessment of the loan process and the credit decision made with respect to the Gelato Business, the Commission should give weight to her evidence, including the opinions she expressed.

A.3 Findings

- 1.26 In closing address, Counsel Assisting referred to the FOS determination, summarised briefly parts of the factual background to the Gelato Business case study, and referred to Ms Gibson's evidence. Counsel Assisting then submitted that it was open to the Commissioner to find that, in assessing and approving the loan application, ANZ may have failed to exercise the care and skill of a diligent and prudent banker as required by clause 27 of the Code of Banking Practice (the **Code**).⁶³
- 1.27 ANZ submits, for the reasons set out below, that the bases for the FOS determination, and the evidence referred to by Counsel Assisting in closing address, do not support a finding that ANZ breached clause 27 of the Code. Ms Gibson's careful and reasoned evidence to that effect should be accepted.
- 1.28 ANZ acknowledges, however, that in the process of receiving and recording information with respect to the Gelato Business loan application, an unacceptable number of data and related errors occurred. ANZ accepts that, in this limited respect, there may have been a failure to meet the standards expected of a diligent and prudent banker exercising the care and skill required by clause 27 of the Code.

FOS determination

- 1.29 In relation to the FOS determination, as explained by Ms Gibson in her evidence, a diligent and prudent banker exercising care and skill in this case would not have been compelled to:
- (a) conclude that the Gelato Business' sales forecasts were overly optimistic;
 - (b) adopt industry benchmarks published by the ATO in assessing the Gelato Business' cash flow forecasts; or

⁶⁰ T2148.26.

⁶¹ T2196.30-34; T2202.40; T2216.22-23; T3030.06-07.

⁶² Gibson Statement: ANZ.999.009.0065 at .0108 [177]; T2160.05-2161.32, T2221.42-2222.41.

⁶³ T3030.01-04.

- (c) refrain from accepting guarantees from the Gs on the basis that Mr G's PAYG income was insufficient to service the business loan and the family's personal liabilities without incurring substantial hardship.

Each of these points is addressed in turn.

- 1.30 **Sales forecasts.** ANZ submits that it was open for the Assessor to form an opinion, in the exercise of her judgment, that the Gelato Business' sales projections were not overly optimistic. In support of this conclusion, Ms Gibson gave evidence that:⁶⁴ (1) the business plan contained many aspects that she would have expected to see; (2) because the Gelato Business was going to have \$15,000 of initial stock it would be in a position to commence operations and generate income immediately; (3) the store was going to be located in a large shopping centre in southern Sydney and had, or could reasonably be expected to have had, significant foot traffic; (4) there was, at the time of the application, no competitor in the shopping centre or nearby; and (5) the business plan included assumptions that were relevant to the detailed cash flow forecast.⁶⁵
- 1.31 As Ms Gibson further stated, any over-optimism in the sales projections was addressed by the break-even analysis conducted by the Assessor,⁶⁶ as further verified by the independent assessment conducted by Ms Gibson herself. That further assessment showed that, even if one were to increase the cost of goods sold to 30% (from 20%) and decrease Mrs G's salary to \$25,000 (from \$50,000), the projected sales could have been reduced to 70% before the business reached the break-even point.⁶⁷
- 1.32 Even if the cash flow forecast was overly optimistic, it does not follow that in deciding to extend credit to the Gelato Business on the terms it did, ANZ failed to meet the standard of a diligent and prudent banker exercising care and skill. Clause 27 of the Code is concerned with a lender's process in forming an opinion about whether a borrower has the ability to repay the loan applied for. It is not directed to the content of that opinion or to the ultimate decision to approve a credit application, which may take into account other matters.⁶⁸ ANZ has at all times maintained, and continues to maintain, that the approval of facilities to the Gelato Business was within the judgmental discretion of the Assessor, properly exercised.
- 1.33 **Industry benchmarks.** ANZ submits that while a bank may consider industry benchmarks when assessing a cash flow forecast, there is (and should be) no requirement to do so. A decision not to consult industry benchmarks or, having done so, not to reset cash flows to accord with industry benchmarks, does not establish a failure to exercise the care and skill of a diligent and prudent banker.
- 1.34 The fact that, in this case, a decision to lend was made in circumstances where the cost of goods sold as a percentage of turnover was lower than the applicable ATO benchmark, does not support a conclusion that ANZ failed to exercise the care and skill of a diligent and prudent banker. While it might be reasonable to expect that a customer should have an understanding of why the figures in their cash flow forecast are outside industry benchmarks, it is not incumbent on a bank to adjust such projections in forming its opinion about a customer's ability to repay its loan.

⁶⁴ T2168.44; T2210.05-06; T2220.27-2221.35; Gibson Statement: ANZ.999.009.0065 at .0106-.0107 [166]-[169].

⁶⁵ See page 26 of the business plan at exhibit KGG-30 to the Gibson Statement: ANZ.800.534.0008 at .0033.

⁶⁶ Gibson Statement: ANZ.999.009.0065 at .0107 [168], .0101 [132(b)].

⁶⁷ T2222.39-41.

⁶⁸ See *Doggett v Commonwealth Bank of Australia* (2015) 47 VR 302 at 342 [163]; *Westpac Banking Corporation v Haynes* [2017] SASC 23 at [63] (Nicholson J).

- 1.35 In any event, for the reasons expressed in [1.31] above, even if the cost of goods sold for the Gelato Business were increased to 30% (in line with the applicable ATO benchmark), there is no basis for concluding that that would have affected ANZ's decision to lend. The business would, even in that event, have remained cash flow positive – even if the business only achieved sales lower than the sales projections in the cash flow forecast.
- 1.36 **Guarantees.** ANZ was entitled to obtain personal guarantees and indemnities from the Gs. In this case, the guarantees and indemnities were obtained from the Gs in their capacity as directors of the borrowing entities. In taking this step, ANZ did not fail to exercise the care and skill of a diligent and prudent banker. As Ms Gibson explained in her evidence, ANZ took a conservative approach to assessing serviceability, first by assessing the business projections based on the cash flow forecast, and then by performing a break-even analysis that took into account Mr G's PAYG income and 50% of Mrs G's projected income.
- 1.37 Although a primary consideration in assessing serviceability is the projected performance of the business, banks are entitled to consider other potential funding sources in this assessment. As McLeish JA stated in *Doggett v Commonwealth Bank of Australia*:⁶⁹
- In my opinion, as the trial judge [Hargrave J] held, it is natural that a bank may take account of the financial position of a guarantor or other third parties as part of its credit assessment of a borrower and in forming its opinion as to the borrower's ability to repay. A person's ability to repay a loan may depend in part on the financial resources of a person or persons who 'stand behind' that person and upon whom the borrower may call to supply the funds to enable repayment.
- 1.38 In looking at those who 'stood behind' the Gelato Business in this case, ANZ was entitled to consider Mr G's PAYG income (as well as rental income from his investment property), and his capacity to supply funds to enable the Gelato Business to service interest payments on the business loan and overdraft facility. The fact that Mr G contributed \$67,500 to the business after November 2014 (and during 2015), indicates that this was a reasonable assumption for ANZ to make. Mr G stood to gain directly and personally from the success of the business.
- 1.39 Further, the fact that the Gs may have experienced financial hardship if Mr G gave a guarantee and the Gelato Business was not producing any cash to service the loan does not support a conclusion that ANZ failed to act responsibly.⁷⁰ As Ms Gibson explained in her evidence, if small business loan applications were required to be assessed on this basis (that is, that each individual guarantor must have the capacity to service both business and personal liabilities in the event of default by the business), this would have the potential to materially limit the ability of a start-up business to obtain finance.⁷¹ It would particularly limit the availability of credit to start-up businesses by persons who do not have tangible security, or a partner with sufficient income to cover both personal expenses and the servicing of a business loan.⁷²

Evidence referred to by Counsel Assisting in closing address

- 1.40 In Counsel Assisting's closing address, brief reference was made to some of the evidence in the Gelato Business case study. Counsel Assisting concluded that, "on the evidence" (and "having regard to Ms Gibson's acknowledgement"), it was open for the Commissioner

⁶⁹ (2015) 47 VR 302 at 332 [120]. See also the comments of Whelan JA at 306 [8]. The Court in that case considered cl 25.1 of the 2004 version of the Code, which was expressed in substantially the same terms as cl 27 of the current (2013) version of the Code.

⁷⁰ *Contra*: FOS determination at exhibit KGG-63 to the Gibson Statement: ANZ.800.470.2019 at .2024.

⁷¹ Gibson Statement: ANZ.999.009.0065 at .0107 [173]; T2199.17-2200.03; T2201.24-39.

⁷² T2200.01-03; T2201.33-37.

to find that ANZ may have failed to meet its obligations under clause 27 of the Code. In submitting that such a conclusion was open "on the evidence", Counsel Assisting did not specify which evidence informed this conclusion, nor how such evidence supported that result.

- 1.41 Having regard to the focus and content of the cross examination of Ms Gibson by Counsel Assisting, and the matters referred to in Counsel Assisting's closing address, ANZ infers that "the evidence" which is said to support a possible conclusion that ANZ failed to comply with clause 27 of the Code is:
- (a) ANZ's reliance on cash flow forecasts which were overly optimistic;⁷³
 - (b) the business plan, which was said by Counsel Assisting to be "very generic in nature", with "inconsistencies between the various cash flow forecasts", and no evidence about whether the Banker had spoken to the Gs "to make sure that the borrower understood the business";⁷⁴ and
 - (c) there being a culture of sales pressure underpinned by an incentive scheme focused on financial targets and a key message to small business bankers to relentlessly acquire new-to-bank customers.⁷⁵
- 1.42 If ANZ is wrong about whether these matters of "evidence" are what Counsel Assisting was referring to in closing address, then ANZ requests an opportunity to put on a further short written submission concerning any other evidence that may be relied on by the Commission.
- 1.43 The first of the evidentiary matters identified above – regarding the cash flow forecasts – has already been addressed in this submission, in paragraphs [1.30]-[1.32].
- 1.44 As to the second matter – the business plan, cash flow forecasts, and conversations with the borrowers – the following points can be made:
- (a) *First*, while aspects of the business plan were generic in nature, most of the detail that one would expect to see in a business plan was, in Ms Gibson's opinion, contained in the document.⁷⁶
 - (b) *Secondly*, as Ms Gibson also said, in her experience, business plans "are many and varied, and there are very different levels of detail in them",⁷⁷ and "business plans serve multiple purposes" including an element of marketing.⁷⁸
 - (c) *Thirdly*, while the business plan included various marketing features (such as photos and colourful descriptions of the business),⁷⁹ it also included specific information about the store location, its forecast cash flows, an indicative roster, the sources and extent of potential competition, industry research and growth projections, the target market (including demographics) and associated marketing strategy, the nature and quality of the gelato product, and store systems and ongoing franchise support. The cash flow forecast also included seasonally adjusted

⁷³ T3029.09-19.

⁷⁴ T3029.20-29.

⁷⁵ T3029.30-45.

⁷⁶ T2210.02-05.

⁷⁷ T2206.14-16.

⁷⁸ T2206.39-41.

⁷⁹ T2206.32-33.

revenue projections, and an assessment of the nature and extent of likely expenses to be incurred by the business.

- (d) *Fourthly*, the allegation that there were inconsistencies in the cash flow forecasts in the business plan is not made out on the evidence, and no such suggestion was put to Ms Gibson in her evidence. If, instead, Counsel Assisting was intending to refer to the difference between the cash flow projections and the company's hypothetical budget in the business plan, then that was a difference without particular significance. ANZ relied on the net profit stated in the cash flow forecast, not the higher figure in the budget.⁸⁰
- (e) *Fifthly*, although Ms Gibson considered that the Banker should have spoken to the Gs about their understanding of the business:
- (i) she also stated that where applicants such as the Gs are putting a very significant amount of their own money into a business, "it's not unreasonable for a banker to expect that they have thought hard about that investment";⁸¹
 - (ii) in addition, having regard to Mr G's role as a business analyst at a major bank, it was not unreasonable to assume that he was in a position to review and assess the business plan;
 - (iii) the evidence was that the Banker had in fact met with and spoken to the Gs;⁸²
 - (iv) further, the Banker told the Gs that they should obtain independent legal and financial advice;⁸³
 - (v) documents on the file indicate that the Banker was then told by the Gs that they had already obtained legal advice in relation to the franchise agreement and the risks associated with purchasing the Gelato Business, and that they did not wish to take up the Banker's offer to meet with a financial planner;⁸⁴ and
 - (vi) there was no evidence about whether the Banker spoke to the Gs about their "understanding of the business" and, if so, what was discussed. Neither Mrs G nor Mr G were called to give evidence about what was said in any conversation with the Banker, and no reason was provided by Counsel Assisting why the Gs were not called or could not have given evidence. In these circumstances, it is not reasonably open to the Commission to conclude that the Banker did not satisfy himself, based on his conversations with the Gs, that "they understood the business", including the salient elements of the business plan and cash flow forecast.

1.45 Having regard to these matters, it is submitted that the Commission ought not conclude that there was a failure, in any of these respects, by ANZ to exercise the care and skill of a diligent and prudent banker.

⁸⁰ T2172.16-18.

⁸¹ T2207.14-16.

⁸² T2168.42-44.

⁸³ See the references in footnote [32] above.

⁸⁴ See the references and observations in footnotes [32]-[34] above.

- 1.46 Finally, the reference by Counsel Assisting in closing address to a “culture of sales pressure” at ANZ, does not support a conclusion that ANZ breached clause 27 of the Code in this case. The evidence does not establish that, in this case, the Banker’s conduct was influenced by a culture of sales pressure, or that any alleged failings by ANZ resulted from this alleged culture.
- 1.47 Ms Gibson was asked about these matters during her cross-examination, and she did not accept the propositions put to her. She stated that it was very clear to bankers at the time that they needed to meet their compliance requirements, and that it did not follow that bankers who focused on building a circle of influence and finding opportunities to bring customers to ANZ led to poor practices.⁸⁵ Ms Gibson also stated that while there was a culture in the Small Business Banking team of wanting to perform, she did not accept that staff were under sales pressure.⁸⁶ While, in the first half of 2014, the Banker in this case had not met his new-to-bank lending targets, he was noted as having had a great first half and meeting the majority of his targets.⁸⁷ It is not open to conclude that there was a connection between the Banker’s performance (on new-to-bank lending) in the first half of 2014, and the loan that was made in this case in the first half of 2015.⁸⁸
- 1.48 Counsel Assisting also stated in closing address that, during the period in which the loan was made to the Gelato Business, “the key message given by ANZ to its small business bankers was to relentlessly acquire new to bank customers.”⁸⁹ That statement, when read in context and having regard to the whole of the document, does not support a conclusion that this was “the” key message given by ANZ to its small business bankers.⁹⁰ Moreover, the statement was concerned with the need to “review” and “change” the way new-to-bank customers were attracted by ANZ.
- 1.49 Counsel Assisting in closing address did not identify or explain any connection between the alleged culture referred to, and the finding, said to be open in this case, that ANZ failed to exercise the care and skill of a diligent and prudent banker. No such connection was established on the evidence. The errors cannot be explained as having been caused by an inappropriate sales culture.

A.4 Conclusion

- 1.50 The evidence in this case study distinguished between ANZ’s decision to approve the loan application for the Gelato Business, and the data errors that were made by ANZ in processing the application.
- 1.51 As to the former, the evidence does not support a finding that ANZ failed to meet its obligations under clause 27 of the Code. Ms Gibson’s evidence to that effect was compelling and should be accepted.
- 1.52 As to the latter, ANZ accepts that there were errors, as identified by Ms Gibson, and that these aspects of the loan process may have involved a failure by ANZ to exercise the care and skill of a diligent and prudent banker.
- 1.53 Had the errors not occurred, it would have remained open to a diligent and prudent banker in this case, in the exercise of a judgmental credit assessment, to approve the

⁸⁵ T2214.40-44.

⁸⁶ T2215.24-26. Ms Gibson acknowledged that this is what the Banker said in 2017 in connection with a disciplinary process relating to two loans made in 2015.

⁸⁷ T2213.16-20.

⁸⁸ T2213.13-14.

⁸⁹ T3029.35-36.

⁹⁰ Exhibit 24 to the Gibson Statement: ANZ.800.528.0345 at .0346.

loan application for the Gelato Business. The Commission ought not conclude that any different result would have occurred in this case but for the errors acknowledged by ANZ.

Date: 8 June 2018

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