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

Submissions of Michael Doherty and Doherty Hotels Group (DHG) with respect to Conduct of Bankwest in relation to its funding of Hadleys Hotel in Hobart, Tasmania and an adjacent mixed-use development known as Inner Collins, in 2011 and 2012

The Question

1. The single question for Mr Doherty is whether specific conduct of Bankwest in 2011 and 2012 was unconscionable within that meaning in the ASIC Act 2001 and the general law.

2. The specific alleged conduct of Bankwest is the aggregate of the following facts (the **Conduct**):

   (a) Deciding during about 2010 and 2011 that the bank wanted to be free of its exposure to the loans to DHG which represented a high risk, non-core exposure in the form of an east-coast hospitality property[1]; and

   (b) In pursuit of that decision, deciding between March and July 2011:

      (a) To ignore the recommendation in February 2011 of 333 Real Estate regarding how to value the property[2]. That recommendation was to expand the draft "update" valuation report of the property (valuing the property at $75.317 million using a range of valuation approaches appropriate for the various components of the property on an "as if complete" basis) issued by Knight Frank to DHG on 28 November 2010, into a full report with detailed analysis and valuation rationale. That valuation method would have been consistent with the approach the bank instructed CBRE to value the property with in August 2008, which the bank relied on in August 2009 when it funded the project; and

      (b) To not instruct CBRE to prepare a new valuation report in 2011. CBRE could have updated its August 2008 report using its same method of valuation the bank relied on to underwrite the transaction in 2009. It could have explained any assumptions the bank had concerns about and could have included relevant market assumptions and actual and projected revenue forecasts including Accor's revenues as manager of Hadleys Hotel and Mantra's revenue forecasts for Inner Collins, to create a like-for-like comparison between the CBRE valuation in 2008 and in 2011; and

---

[1] Paragraph [88] of Witness Statement of Michael Doherty dated 24 May 2018

[2] Page 37, Report of 333 Real Estate dated February 2011, PNC-18 to Witness Statement of Peter Clark of 27 May 2018

(c) To instruct Jones Lang LaSalle (JLL) to value the property solely as if it operated as one consolidated going concern “in one line”, subject to the Accor management agreement for Hadleys Hotel and assuming vacant possession[3]. That valuation approach ignored the range of valuation approaches that Knight Frank adopted in May 2010[4] and December 2010[5] and that CBRE adopted in August 2008[6]. Those approaches were more appropriate for the various components of the property than the approach the bank asked JLL to take, which also ignored the borrower’s agreement with Mantra for it to manage Inner Collins separately from Hadleys Hotel; and

(d) To ignore the multiple pleas of DHG in emails between 8 March 2011 (MED-13 and 14) to July 2011 (MED-16, 17, 18) asking the bank to ask CBRE to re-value the property and or to ask JLL to incorporate into its valuation, methods and assumptions that were more appropriate to the components of the property than the method JLL was instructed to use; and

(e) To ignore the valuation Knight Frank performed for the possible refinance by Bendigo Bank in late 2011 of Hadleys Hotel of $32.5 million, $12.5 million or 60% higher than the JLL valuation for the same part of the property (see para [15] below); and

(f) To ignore the CBRE valuation prepared for refinance of the property by Tasmanian Perpetual Trustees in November 2011, which valued the Inner Collins part using the same or substantially similar basis as the CBRE valuation in August 2008 that the bank relied on. That November 2011 valuation was given to Bankwest by Michael Doherty in 2011 and valued Inner Collins itself at $48.725 million (MED-24 to Witness Statement of Michael Doherty), substantially above (c.40%) the JLL valuation for the same part of $35 million; and

(g) To not perform a critical comparison and SWOT analysis between the valuation methods used by JLL in July 2011 and Knight Frank in May 2010, December 2010 and late 2011 and by CBRE in August 2008 and November

---

3 JLL Valuation dated July 2011, PNC-22 to Witness Statement of Peter Clark
4 MED-09 to Witness Statement of Michael Doherty
5 MED-11 to Witness Statement of Michael Doherty
6 MED-03 to Witness Statement of Michael Doherty

2011 to fully consider the differences between the figures and methods used to understand the potential inherent value of the property. That analysis would have been prudent to understand the potential to roll the construction tranche of the debt into a term facility until the expiry of the existing term loan due to expire in June 2013. That approach would have been consistent with a cautious clever risk managing bank intent on protecting the value of the asset in its balance sheet and minimizing any losses from unnecessary knee-jerk decisions resulting from the JLL valuation figure (that was substantially below other available valuation evidence for the same property);

(c) To use the foreseeable lower JLL valuation result ($55 million) to drive the borrower to have to re-finance the whole exposure instead of supporting it with a term loan for the construction debt secured by the higher valuations until June 2013, when the 1st tranche was due to expire. That approach was contrary to the expectation of the borrower which it adopted when it and the bank entered into the loans in August 2009. In August 2009, the expectation was that the construction debt would roll into a term facility when the project was complete, implied by Item 10 of Schedule 1 to the August 2009 Facility Agreement: PNC-7 to Witness Statement of Peter Clark. That expectation was further created by the joint decision of the bank and borrower at about the same time to enter into a fixed rate swap for the 1st and 2nd tranches of the debt until the maturity date of the 1st tranche (Jun-13), two years after the expiry of the 2nd tranche;

(d) To then apply the LVR breach to justify the appointment of receivers and managers in January 2012, when the borrower had to appoint a voluntary administrator and had to pay c.$900,000 to cancel the fixed interest swap over the 1st and 2nd tranches of the debt, in place until June 2013.

The Complaints

3. Mr Doherty's complaint is that from about 2010, the Commonwealth Bank through Bankwest (together the **bank**), decided to exit certain classes of higher-risk exposures. His property was within one of those classes. He says that internal decision led to his loans falling within Project Magellan and being transferred to the bank's asset management division for troubled loans. He says that new strategy caused a tunnel vision within the bank, causing its officers to pursue the outcome of excising the exposure from its portfolio, indifferent to the cost to the borrower.

4. He also says the loss the bank suffered from the mortgagee sale of the security properties was the price the bank was willing to pay to be free of the loans. It was not evidence of the bank being a victim of the borrower's defaults and failing property markets for risky assets caused by the GFC, which it would have this Royal Commission believe.

5. Mr Doherty also says that the unnecessary decision to transfer the loans to the bank's asset management division and appoint 333 Real Estate was the primary reason it had to appoint a voluntary administrator in 2012. The reason is the transfer accompanied a worsening in the bank's risk grade for the project which increased the margin payable on the two loans. That adversely affected the borrower's cash-flow and capitalized interest allowance within the construction facility. The appointment of 333 Real Estate cost the borrower c.$217,000 of cash in that firm's fees plus c.$450,000 in additional accounting fees of its own to respond to the bank's continued requests for further information.

6. These adverse events occurred as a result of the internal findings of the bank's executives in a Magellan File Review in May 2010 (see PNC-10) which gave the loans a "Double Red" internal classification, over-exaggerating the comments of bank officers in Credit Deterioration Reports dated 31 March 2010 and 22 April 2010 (see PNC-8).

7. Comments in the 22 April 2010 Credit Deterioration Report included "a diminished level of earnings that will have a direct bearing on existing valuations relied on" and "the bank could not reconcile how CBRE arrived at current valuations" (see p.4). However, the loans were transferred to asset management as a result of the Magellan Report of 10 May without investigating either of those two issues. In contrast, ten months later in February 2011, 333 Real Estate reported (PNC-18) at page 5 that:

   (a) To date performance covenants have been satisfied largely as a result of agreed adjustments but even after backing out the effects of accounting policies, minimum EBITDA requirements have been satisfied;

   (b) Report Interest Cover Ratio (ICR) has been satisfying the minimum covenant and reflects satisfactory debt servicing capacity;

   (c) A miss-match in timing between project completion and step-up in EBITDA required under the Facility Agreement means the EBITDA covenant may be breached for the 12 months ended 30 June 2011;

   (d) The LVR is within the covenant and is expected to be breached only as the construction debt peaks;

(e) There had actually been a net advance of funds in to the central trading entity (CTE) from the wider Doherty Group within the prior 3 years to 30 June 2010.

8. The 333 Real Estate Report also referred to a Knight Frank valuation performed in December 2010 as an update of its May 2010 report for the borrower. The 333 Real Estate recommendation was to ask Knight Frank to update the valuation using the appropriate methods for the various components of the property (at pages 36-37). The bank later completely ignored that recommendation and instead adopted a valuation method that was certain to cause an LVR breach and enable it to justify forcing the borrower out. The bank must be inferred to have known that outcome would arise from the valuation method it required JLL to use because of the objections of DHG to the use of that approach.

9. The 333 Real Estate Report at "Recommendations" (page 25) says "*We recommend that Bankwest continue to support the borrower until 30 June 2010, or completion of construction, in order to maximize the security value of the Hobart asset."*

10. The reference to 30 June 2010 is clearly intended to be 30 June 2011. However, implied in the recommendation is an awareness in the authors of the report of instructions by the bank to identify how and when the bank can create the outcome that the loans cease to exist on its books.

11. The bank's strategy paper of 18 February 2011 (PNC-19) reported on the findings of 333 Real Estate's report and recommended an improved risk grade and provisioning for the loans. It also says the level of debt continues to be serviceable and the security acceptable and improving (p.4). It refers at [6.1] to the Knight Frank valuation and the lack of supporting analysis and independent verification but omits that 333 Real Estate recommended that it be updated. It omits that the instructions the bank has given or will give to JLL will not follow the recommendation of 333 Real Estate and will instead confine the instructions to methods other than those used by Knight Frank and CBRE, that it previously relied on.

12. The strategy paper also recommends (p.4) that the bank continue to support the development to completion in order to maximize security. One cannot infer from that statement any consideration of the borrower, any consideration of extending the construction facility to align with the underlying term facility that was to expire in June 2013 nor any other consideration except becoming free of the exposure when it will be possible to achieve maximum security value from it. One can however infer from the statement an

intention to compel the borrower out of the bank by selling the assets, if necessary, because maximizing security value is not relevant in that particular sentence to re-finance risk.

13. The bank produced a strategy paper on 24 May 2011 before the new valuation was issued (PNC-23). At [2.7], it noted that delayed completion of the project does not constitute a breach of the facility. At [5.1] it recommends continuing funding to enable completion of the development. Implicit within that is the embedded prior decision to free the bank of the exposure at the most opportune time. At [5.4] the paper says on receipt of the fresh valuation it will consider recommending continued support to DHG or a short extension to permit refinance. Meanwhile the bank was accepting second mortgages offered on other security properties by the borrower to support the increased exposure [7.2.1]. The price of the bank's approach for the borrower was an increase in the margin from 3.25% (see PNC-8, p.5) to 4.25% for an extension of term from 30 June 2011 to 31 July 2011.

14. At June 2011, there had not been any defaults by the borrower of any critical loan covenants that the bank complained about. The extent of any complaint by the bank about covenants was limited to earlier financial reporting covenants which the February 2011 333 Real Estate Report resolved for the bank. There were occasional excesses in the overdraft that 333 Real Estate report had also commented on but evidence on discovery is likely to prove the borrower's contention that the excesses could not have occurred without the bank giving express permission for them: they paid for overseas imports for the development pending drawdowns against the construction facility. The payments could not be made without the bank releasing the funds.

15. The JLL valuation was issued in July 2011. It was substantially below the valuation contended by Knight Frank in its December 2010 report. It was lower than the lowest valuation for the bank by Knight Frank three and a half years earlier, before construction commenced, in December 2007 ($60 million). It did not take account of any of the various components of the property and valuation methods applicable to them that 333 Real Estate acknowledged the Knight Frank update report for. It was a simple "in one line" valuation intended to take the most limited, pessimistic view of value and was destined to cause an LVR breach.

16. The valuation was commented on in 333 Real Estate's September 2011 Report (PNC-26). On page 5 it states the borrower's accountant's financial model reflects a significant write-up in trading for Hadleys based on forward bookings at 20% higher room rates and

constant occupancy. It reports a higher EBITDA for Hadleys and said despite a drop in EBITDA for Ballarat it posted a 39% improvement in EBITDA for the June 2011 quarter compared to the same period in the prior year. On page 6, the report comments on the Knight Frank valuation having a higher value for “several of the Inner Collings Lots” which JLL was not comfortable valuing on a stand-alone basis. The next paragraph affirms that Knight Frank (for Bendigo Bank) had placed a value on Hadley’s of $32.5 million compared to JLL’s value of $20 million and that CBRE was also performing a valuation (MED-24).

17. On page 8, 333 Real Estate restated the recommendation to support the borrowing until the Inner Collins component is trading. Despite the potential for higher valuations (Knight Frank and or CBRE) and improved LVR’s adopting those valuations, implicit in the statement is complete acceptance of the bank having no appetite to continue to support the borrower except for the sole benefit of maximizing its security value.

18. The next paragraph talks about the use of “enforcement action” and when best to exercise it. Again, there is no consideration of rolling the completed building into a term facility until the other tranche matures in June 2013 is present, which was the intention of the parties when the bank first underwrote the transaction in 2009. The LVR based on the only valuation the bank was interested in would not permit that: the only way forward for the loans was “out”.

19. In the bank’s Strategy Paper of 12 September 2011 (PNC-27), the officer says at [5.2] that 333 Real Estate is supportive of the JLL valuation methodology. That was not at all evident from the 333 Report. Mr Clark did not include in his evidence any email between the bank and 333 Real Estate to make good that proposition. It would not be a ready inference to draw from the report itself.

20. The bank’s decision in its 12 September 2011 Strategy Paper to sign-off on the JLL valuation methodology was the point of no return for the bank and borrower. That position was the turn that the bank took at the fork in the road that meant the end for DHG.

21. That is so because after it declined to consider any other possible valuation methodology or valuation process or valuation outcome, it deleted from consideration any other possible range of values to inform itself about the true potential value of the property, which would have helped it to understand its security position for itself, the borrower and future funding options.

22. This was despite the aggregate of the Knight Frank value of Hadleys for Bendigo Bank ($32.5 million), the CBRE value of Inner Collins for Tasmanian Perpetual Trustees ($48.75 million) ($81.25 million (JLL's combined value was $55 million using the "one line" method")), the $16.5 million for Ballarat (JLL valuation), the $0.9 million valuation for Man O'Ross Hotel and the $1.59 million of additional security provided to the bank by the borrower in second mortgages (see PNC-38, page 6) giving the bank total security value of $100.24 million. That value secured debt of $60.439 million on 9 January 2012 (PNC-38, page 5), representing an LVR of 60%, well within the 65% LVR covenant.

23. With the $55 million valuation the bank controlled the option to exercise the ultimate power over the borrower and call a breach of the LVR as a reason for declining to support it further. With that valuation it could knowingly and unconscionably force the borrower into a position of special disadvantage: *information asymmetry*. It could compound that position by refusing despite the borrower's reasonable requests to provide it with a copy of the valuation: removing angles the borrower could use to argue the valuation method and outcome was inappropriate and being used for an undisclosed purpose.

24. With the $55 million valuation, when the borrower had to appoint a voluntary administrator in January 2012, it had the perfect excuse to remove any further support from DHG and appoint Korda Mentha. The catch-22 for the borrower however was:

    (a) It had to appoint a VA because it owed the ATO $1.2 million which had accumulated largely due to its impaired cash-flow from funding the higher margin imposed by the bank on the loans and because of the c.$750,000 of cash it had to pay for 333 Real Estate and its accountants' responses to 333 Real Estate's requests; and

    (b) Construction was complete and Mantra was ready to occupy the property and the $3 million Mantra was to pay could be used to pay the ATO debts and reduce debt but the bank refused to agree any terms with Mantra for the management of Inner Collins because it wanted to be free to deal with the property without the burden of the Mantra contract: so, the borrower could not benefit from the Mantra deal in any way and collapsed.

25. With the $55 million valuation, the bank created the perfect opportunity to excise the loans from its books, a course it first chose for itself in 2010 when it assigned the loans to its asset management division in its May-10 Magellan Report. That course was to rid itself of high risk east coast hospitality exposures: Witness Statement of Michael Doherty at [87].

26. The facts outlined above demonstrate an unstoppable plan by the bank to excise this exposure (and presumably others) at any cost to itself and willfully blind to the cost to the borrower. That must be so because the facts outlined are not consistent with a cautious clever bank intent on preserving value in its balance sheet.

27. At best, the bank's conduct in choosing not to assess value options and understand how its security position could justify continued support of the borrower, and benefit from the known years of experience of Mr Doherty with assets of this type, was at the extreme end of incompetence. The standard of care applied to its own balance sheet preservation was so low it is inconceivable a bank with its track record of property lending could inadvertently fall to that level.

28. The banks approach to seeking the "in one line" valuation from JLL was an intended standard of conduct. It was willfully blind to the potential for higher value in the properties using appropriate valuation methods and assumptions adopted by Knight Frank and CBRE and pleaded for by Mr Doherty. It was evidence of a bank that was recklessly indifferent to the outcome for the borrower and possessed only of its own strategy of supporting the borrower until completion of construction to maximize its security value.

29. The conduct leads to the conclusion that the bank by adopting the valuation approach in the JLL valuation knew or believed it was continuing to engage in a strategy of excising the DHG portfolio from the bank's loan book, without expressly disclosing that plan to DHG, and that by doing so it was likely to or would cause DHG loss.

30. The question is whether that conduct was in all the circumstances unconscionable within the meaning of the ASIC Act 2001 and the general law.

Unconscionable Conduct

ASIC Act 2001

31. The conduct of dictating the approach to be adopted in the JLL valuation occurred between March and July 2011. The failure to analyze the range of valuation outcomes occurred between July 2011 and January 2012. The appointment of the receiver and manager occurred on or about 9 January 2012 (PNC-38).

32. The bank's loans to DHG were a credit facility within that meaning of financial product in s.12BAA(7) of the ASIC Act 2001. The provision of those loans was a dealing in a financial product within that meaning in s.12BAB(1)(d) and s.12BAB(7)(b) of the ASIC Act 2001.

33. The borrower was a private company so the relevant restraint on unconscionable conduct provision before 1 January 2012 was s.12CC of the ASIC Act 2001 and after 1 January 2012 was s.12CB of the ASIC Act 2001. In both editions of the Act, s.12CC included a non-exhaustive list of matters the court may have regard to “in connection” with the supply of financial services for the purpose of trade and commerce. The scope of the provision is broad enough to include conduct of the bank after the facility formally expired on 31 July 2011.

34. The conduct complained of by Mr Doherty offended various sub-paragraphs of s.12CC(2) (pre Jan-12) or s.12CC(1) (post Jan-12) of the ASIC Act 2001.

35. The unilaterally decision to direct JLL to only value the properties on an “in one line” basis and ignore the more appropriate methods for the various components of the property in the Knight Frank and CBRE valuations, and not seek an update or either or compare them all, was an unfair tactic used against the borrower (sub-para (d)). It was destined to cause an LVR breach to enable the bank to secure its intended exit of the borrower at the borrower’s expense. The refusal to provide the borrower with a copy of the valuation report (preventing the borrower from arguing its position or challenging the assumptions) was consistent with the bank knowing and believing the advantage it was giving itself: completely indifferent to the effect on the borrower of pursuing that course. It was an exploitation of its superior bargaining position for a specific undisclosed purpose.

36. The bank’s decision not to provide a copy of the valuation or the valuation outcome was inconsistent with its own instructions in Appendix A to the JLL valuation in which it says “*please provide one original report and one copy for release to the client*”. The client is clearly intended to mean DHG. This is clearly a standard form of instruction letter and it would be the normal practice of the bank to release the valuation to the client (who pays for the valuation). On this occasion, the bank withheld the valuation and created an information asymmetry that the borrower despite any endeavor or reasonable enquiry could not overcome. The conduct was not consistent with the bank’s usual means of dealing with similar customers (sub-para (f)). It was unfair, underhanded and unconscionable. It was also overwhelmingly below community expectations.

37. The bank did unreasonably fail to disclose to DHG its intention within the decision not to update the Knight Frank valuation, not to use CBRE to update its August 2008 valuation, not to apply appropriate valuation techniques for the various components of the property

and to use JLL valuation to value the property adopting the "in one line" approach only. It also did not disclose the risk to the borrower of that intended approach (sub-para (i)).

38. The extent to which the bank extended the term of the loan after its expiry on 31 July 2011 was limited to its own commercial needs of maximizing security. The idea of permitting the borrower to convert the construction loan to a term loan at the end of the project until June 2013 (to line up with the 1st tranche), contemplated when the loan was first advanced, was displaced in 2010 and 2011 by the decision to excise the loans from the bank's portfolio.

39. When the borrower had to appoint a voluntary administrator in January 2012, the steps taken by the bank excluded any negotiation of terms that supported the borrower to trade through that period by negotiating alternative arrangements with Mantra, securing a cash payment from Mantra to partially reduce the borrower's debts to the bank and the ATO and renegotiating the terms of the loan into a term facility because construction was complete.

40. Such steps would have been commercial commonsense considering the property was complete, Mantra was preparing to manage it, Hadleys' Hotel performance was improving and DHG was a superior manager of the asset in normalized trading conditions than any receiver would be. That approach would have assisted the bank to preserve the value within the loans and significantly improve the prospects of the borrower refinancing the whole exposure in June 2013. That approach was not taken because the bank wanted to be free of the exposure, indifferent to any effects of that decision on the borrower: (sub-para (j)(i)).

41. The bank did not act in good faith towards the borrower but the borrower did act in good faith towards the bank: sub-para (l).

42. The concept of good faith (as referred to in s.12CC ASIC Act 2001) was said by the Full Federal Court to include "*an obligation…not to act to undermine the bargain entered or the substance of the contractual benefit bargained for" and "an obligation to act reasonably in and with fair dealing having regard to the interests of the parties…and to the provisions, aims and purposes of the contract, objectively ascertained.*"[7]

43. The bank's conduct in appointing receivers in January 2012 will easily be dismissed by some critics of the arguments within, as the bank acting within its rights after the facility

---

[7] ASIC v Westpac (No 2) [2018] FCA 751 at [2194]

expired with covenants breached, administrators to be appointed and the only available and obvious option. That is an over-simplistic view and ignores the undercurrent of the bank's conduct that caused that outcome.

44. That position was a consequence of the decision in 2010 to excise this risky asset, to shovel it into asset management on the whim of an internal officer adopting assumptions later proven to be untrue in the 333 Real Estate Report.

45. It was a consequence of the higher risk grade that resulted from that decision and the resulting higher margin, adversely impacting the borrower's cash-flow and capitalized interest facility.

46. It was a consequence of the appointment of 333 Real Estate which cost the borrower an estimated additional $750,000 in their fees and the borrower's own accountant's fees for modelling requirements demanded by 333 Real Estate. That caused the borrower's cash-flow to suffer and meant it became indebted to the ATO because of a reduced ability to pay GST on imports for the development.

47. It was a consequence of the bank ignoring 333 Real Estate's recommendation to ask Knight Frank to update its valuation report and fully explain its conclusions in its December 2010 report and of the bank driving a valuation that was as certain to cause an LVR breach as night follows day.

48. It was a consequence of the focus of the bank being solely on supporting the borrower for as long as necessary to maximize its security value, blinded by that. The bank was thereafter unable to reflect on the position of the borrower and its need for continued support that would in turn help the bank to maximize the true value in the completed property.

49. That approach caused the bank not to negotiate any terms with Mantra which was already on site in September 2011, preparing to operate the completed Inner Collins Hotel and ready to pay DHG $3 million in cash to start operating the hotel.

50. That approach caused the bank to appoint a receiver, which spent a further c.$4 million on the property and sold it as mortgagee in possession at a huge unnecessary loss.

51. There was a complete lack of good faith in the bank towards the borrower. The most basic criticism is the bank was highly incompetent to cause itself to lose so much money. That is not the complete answer.

52. Such incompetence would not be accepted within any commercial organization as experienced as the Commonwealth Bank at managing commercial loans.

53. The Commonwealth Bank could not be that accidentally incompetent. The outcome it created was contrived from an intention created in 2010 that was completely against the borrower's interests from that point.

54. The bank's actions set out to undermine the bargain entered and the substance of the contractual benefit DHG bargained for in August 2009.

55. The bank acted unreasonably and unfairly having regard to the provisions, aims and purposes of the loan contract, objectively ascertained.

56. The bank admitted in its own report that completion not being on time was not a breach.

57. The development took until September to achieve completion. Thereafter it was perfectly poised to be used for the purpose intended. The bank and borrower were perfectly poised to convert the construction facility to a term facility until 30 June 2013, when the 1st tranche expired, the swap expired and DHG would have established a trading record with Mantra's efforts. The valuation decision taken by the bank shut that potential out from consideration when it was most needed.

58. Objectively ascertained, the bank failed to act in good faith.

59. In all of the circumstances of this case, the bank's conduct was unconscionable within that meaning in s.12CC of the ASIC Act 2001.

General Law

60. At the core of the general law of unconscionable conduct is the need to demonstrate a special disadvantage: *Commercial Bank of Australia Limited v Amadio (1983) 151 CLR 447* at 462. The categories of special disadvantage are not closed and one may arise from the specific or situational features of the relationship between the parties to a transaction: *ASIC v Westpac (No.2) [2018] FCA 751* at [2220].

61. Justice Beach in *ASIC v Westpac* at [2223] recently stated that "*ignorance of an important matter may be sufficient to establish a special disadvantage where it seriously affects a person's ability to make a judgment as to his best interests and where the knowledge in question was not readily available through reasonable diligence in a practical sense*."

62. It is also a requirement that the party engaging in the conduct must have some awareness of the other person's special disadvantage and the special disadvantage must be sufficiently evident to make the conduct exploitative or unfair: *ASIC v Westpac* at [2225].

63. That formula can be seen to apply to the bank's treatment of the borrower in this case.

64. Albeit that Mr Doherty gives evidence at [87] of his Witness Statement that Mr Hogan explained to him that he bank no longer had the appetite for the type of exposure in Tasmania, that was not something Mr Doherty was aware of during 2010 or early 2011, especially during the phase of the bank deciding how to instruct JLL to value the property.

65. During the period from May 2010 when the Magellan Report assigned the loans to the asset management division and at all times subsequently until October 2011, Mr Doherty did not know the underlying motivation of the bank. He could not understand how the bank would choose to only instruct JLL to value the property on an "in one line" basis and would not take account of the various components of the property. He could not understand how the bank would choose to ask for a valuation approach from JLL that was not appropriate for the property and bound to cause an LVR breach.

66. Mr Doherty could not understand how the bank would choose not to use Knight Frank which had prepared three prior valuations of the property (May 2010, December 2010 and one for the bank in December 2007: see MED-2 to the Witness Statement of Mr Doherty) and Knight Frank was a panel valuer for the bank.

67. Mr Doherty could not understand how the bank would not use CBRE to update its August 2008 valuation with up to date and relevant market assumptions and would not consider the November 2011 valuation performed for Tasmanian Perpetual Trustees, which was $13.75 million higher (40%) for Inner Collins than the JLL valuation. CBRE was a panel valuer for the bank.

68. Mr Doherty could not understand how the bank would not instruct JLL to take into account the revenue forecasts for Inner Collins that the CEO of Mantra would personally convey through discussions with the valuer if the two were permitted to meet.

69. Mr Doherty could not understand how the bank would require JLL to perform a valuation "in one line" when the valuer did not value strata units[8] and a high value component of Inner Collins that needed valuing was a series of larger sized hotel suites designed as

---

[8] Email from Michael Doherty to Nicole Tartaglia dated 30 March 2011, MED-13

penthouse apartments that could be sold to investors at significantly higher rates per square metre than traditional hotel rooms. The value increment inherent in a proper valuation approach for those strata units was significant: see MEDF-24, p.80).

70. Mr Doherty could not understand how the bank would not release the valuation to him and would not discuss the assumptions or outcomes in any specific sense.

71. None of the information Mr Doherty wanted from the bank was readily available to him through his reasonable diligence in a practical sense. The reason is the bank would not give it to him. The bank was aware that possessed of the information, especially the actual JLL valuation report, Mr Doherty was in a stronger position to negotiate with it, or complain to it, which it did not want.

72. The bank was clearly aware then of the "special disadvantage" or "disability" Mr Doherty would labour if it did not provide him with the JLL valuation or knowledge of its intention of only supporting the borrower until its own security position was maximized. Alternatively, the bank was too embarrassed to disclose its own behavior by providing a copy of the valuation and so refused to do so.

73. The bank exploited that position by simply not providing Mr Doherty with the valuation and not entertaining discussions with Mr Doherty about alternate methods of valuation. Any prudent bank would seek the input of a person more experienced in projects of this kind than themselves, in this case Mr Doherty. Mr Doherty was very well positioned to provide insight into the underlying strategy for each component of the property that would inform possible valuation approaches that could be taken to understand true value. He was able to introduce Simon McGrath, the CEO of Mantra to the valuer to also discuss future performance expectations which would inform underlying revenues that would be capitalized in the valuer's model to arrive at a final figure.

74. "Management" is a risk the bank placed great weight on when it advanced the loans. In its submission to credit in December 2008 (PNC-6, page 17) it described Mr Doherty and his employee Harry Kelly to be "well experienced and knowledgeable in the hospitality industry and hotel development with proven experience in managing large, complex development projects due to strong relationships with a number of professional services companies such as builders and fitting suppliers (China), effective cost controls and strong management of meeting key milestone dates."

75. Further comments included: "The success of the group's projects may be attributed to the strong management skills and good business acumen of the Borrower, who has an extensive industry background. Regarded as a highly experienced hotelier, Michael pursues a growth strategy via capex initiatives for the maintenance and improvement of hotels…..Michael undertakes fortnightly inspections of all the properties. While Michael maintains a very active role in the various business enterprises of the entire group, management of daily operations is principally handled by very experienced staff of Accor management."

76. Objectively understood, on its own evidence, the bank could not have had a better person to listen to about cash-flows, projections, strategies and trading through tricky conditions than Michael Doherty. When they wanted to give him the loans they could not speak highly enough of him. When they no longer wanted the loans, they completely ignored him. The bank was willing to sacrifice the borrower to be free of the loans. Any loss to the bank was an acceptable price for rationalizing the exposure and cleaning up its balance sheet.

77. It was the bank's own conduct that created the multiplier effect that caused the loans to eventually become impaired when there was otherwise no reason for them to become so.

78. The bank's conduct was not operational incompetence. It was a course of action chosen in 2010 and pursued persistently and patiently until the appointment of the receiver. That conduct was willfully blind and or recklessly indifferent to the outcome for the borrower. It was unconscionable in every material respect.

79. As Justice Beach said in ASIC v Westpac at [2225], "*Willful ignorance is equated with knowledge*".

Conclusion

80. The bank's decision in 2010 (and continuing) to reduce its over-exposure to east coast high-risk hospitality assets at any cost to the borrower was completely against the understanding struck with the borrower in August 2009 that the construction facility would roll into a term facility and expire at the same time as the 1st tranche of debt, in June 2013.

81. The use of the inappropriate valuation methodology to contribute to the success of that decision was a cynical exploitation of a commercial advantage in a position of control that despite Mr Doherty's reasonable inquiries he could not overcome.

82. The conduct that Mr Doherty complains of caused him, his wife and his parents to lose the wealth they had built up from successfully developing and managing hospitality assets over 40 years. In contrast, the bank went from quarter to quarter proudly announcing to its shareholders how it was managing the difficult property portfolio inherited from Bankwest.

83. The conduct almost destroyed Mr Doherty's life. The bank caused Mr Doherty and his DHG to lose $60 million. The bank itself didn't blink. There were other clients it treated similarly and left behind as it forged ahead.

84. The conduct is actionable as unconscionable conduct within that meaning in the ASIC Act 2001 and the general law. The time for making a successful claim may now be at risk.

85. Finally, Mr Doherty requests that the Royal Commission refer his claim to be determined by an Arbitrator, whose decision is to be binding on both parties. Alternatively, he asks the Royal Commission to recommend that a statutory compensation fund for victims of misconduct by the banks is established, against which he may claim.

Giles Stapleton

Nine Selborne Chambers, Sydney **19 June 2018**