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TRANSCRIPT OF PROCEEDINGS

O/N H-911840

THE HONOURABLE K. HAYNE AC QC, Commissioner

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

DARWIN

10.01 AM, MONDAY, 2 JULY 2018

Continued from 29.6.18

DAY 35

MS R. ORR QC appears with MR M. COSTELLO as Counsel Assisting with MR M. HOSKING and MS S. ZELEZNIKOW
MR D.J. BATT QC appears with DR C.O.H. PARKINSON for Rural Bank

THE COMMISSIONER: Ms Orr.

MS ORR: Commissioner, we commence this second week of the fourth round of hearings with a final case study in relation to agricultural finance involving Rural Bank. For that case study, our witness will be Alexandra Gartmann.

<ALEXANDRA ESME MARIA GARTMANN [10.02 am]

<EXAMINATION-IN-CHIEF BY MR BATT

THE COMMISSIONER: Thank you very much, Ms Gartmann. Do sit down. Yes, Mr Batt.

MR BATT: Thank you, Commissioner. Ms Gartmann, your full name is Alexandra Esme Maria Gartmann?---Yes.

And your business address is the Bendigo Centre, 22 to 42 Bath Lane, Bendigo, Victoria?---Yes.

And your position is that you are the chief executive officer and the managing director of Rural Bank Limited?---Yes.

Also executive agribusiness, Bendigo and Adelaide Bank Limited?---Yes.

You received, did you Ms Gartmann, a summons to give evidence before the Commission?---I have.

And do you have the original summons with you?---I do.

I tender that, Commissioner.

THE COMMISSIONER: Exhibit 4.120 will be the summons to Ms Gartmann.

EXHIBIT #4.120 SUMMONS TO MS GARTMANN

MR BATT: Ms Gartmann, you prepared and signed a witness statement in response to the Commission's Rubric 4-36?---I did.

Do you have with you the original statement and its exhibits?---I do.

And are those – are the contents of that statement true and correct?---They are.

I tender the statement and exhibits, Commissioner.

THE COMMISSIONER: Exhibit 4.121, the statement and exhibits to the statement of Ms Gartmann.

EXHIBIT #4.121 STATEMENT AND EXHIBITS TO THE STATEMENT OF MS GARTMANN IN RESPONSE TO RUBRIC 4.36

MR BATT: Ms Gartmann, for completeness, one formal matter not addressed in your witness statement. You have a Bachelor of Science degree with honours from the ANU?---I do.

And you are a member of the Australian Institute of Company Directors?---I am.

Nothing further, if the Commissioner pleases.

THE COMMISSIONER: Thank you. Ms Orr.

<CROSS-EXAMINATION BY MS ORR [10.03 am]

MS ORR: Ms Gartmann, Rural Bank is a wholly owned subsidiary of Bendigo and Adelaide Bank?---It is now.

And you have been CEO and managing director of Rural Bank since late 2015?---I have.

And from September 2014 to October 2015 you were a non-executive director of Rural Bank?---Correct.

Now, since October 2015 you've also been a member of the executive committee of Bendigo and Adelaide Bank?---Yes.

And Bendigo and Adelaide Bank first became involved with Rural Bank in December 1998; is that right?---That's correct.

And at that time, Bendigo Bank established Rural Bank as a fifty-fifty joint venture with Elders?---Correct. It was called Elders Rural Bank.

And Elders began trading as an authorised deposit taking institution, Elders Rural Bank, in June 2000?---Correct.

And in May 2009 Bendigo Bank acquired a controlling interest in Rural Bank?---That's correct.

And in late 2010 Rural Bank became a wholly owned subsidiary of Bendigo Bank?---Yes, that's correct.

All right. Now, Bendigo Bank's engagement with rural and agricultural clients is now, you tell us, substantially achieved through Rural Bank?---Yes.

But Bendigo Bank still has its own small direct agribusiness portfolio?---Correct.

And Rural Bank products and services are currently available through Bendigo branches?---They are.

And also through Elders rural services outlets; is that right?---They are.

And that's under a distribution agreement between Rural Bank and Elders?---It is.

Now, putting to one side the Rural Bank offices referred to in paragraph 18 of your statement, Rural Bank doesn't have its own branded branches?---Correct. We are essentially mobile, because we work with our customers largely on farm, or we utilise the offices of some of our partners.

You describe Rural Bank in your statement as a dedicated agribusiness bank?---Yes. So we only do lending in the agricultural sphere, and that is largely within the farm gate. There's a small amount of lending post farm gate.

And what do you see as the main differences between a dedicated agribusiness bank and a bank that deals with agribusiness customers as well as other customers?---There's a range of products that are different. So we have a farm management deposit offset facility. The only one that's available through a bank in Australia, post the legislation passing in Federal Parliament. We also lend against stock and crops, as opposed to just lending against land, and the understanding and knowledge of the agricultural cycles and the impact of commodity prices and other externality, such as droughts and disasters, has a different impact on agricultural production, and therefore the businesses that are reliant on that production.

And do Rural Bank employees have particular training or experience in dealing with agribusiness customers?---We largely get our staff having come from farm, or have undertaken some form of agricultural training, as well as then training in the finance and banking sector.

And what sort of training or experience do loan origination staff at Rural Bank have in dealing with agribusiness customers?---Are we talking about this particular point in time now?

No, I am talking about now?---Yes.

Presently?---So we will look for formal qualifications in agriculture or finance, and we will – now when we bring on a new staff member, part of our corporate induction, regardless if you are a frontline staff member or within the back office, you actually spend some time on farm understanding farm issues and talking to our customers. We undertake training in credit assessment, we undertake training in hardship – understanding the hardship policy. We certainly have people attending a number of industry conferences and events, and connecting with specialist agricultural knowledge expertise, such as the Australian Farm Institute and various research and development corporations so we are staying abreast in the latest in both production trends and production practices, but also the technologies and some of the emerging opportunities for the industry.

And when did that start to be the case, that your loan origination staff moved towards having these sorts of levels of training and experience?---Well, certainly, a quite – having staff with a background in agriculture and finance has been, I think, the history of the organisation. So we pull people from the agricultural sector and train them up in banking, or have brought them in from banking and train them up in agriculture. So that's been part of the history of the organisation. And more specifically, I mean, I can only talk about my time. We've had some very targeted training around credit assessment, also around valuations, around the hardship policy in the last two and a half years, and I am very aware of those ones, but when I look back at – for the purposes of this exercise, had a look at the historical training, there was substantial amount of training developed from 2011 onwards, and rolled out nationally through both pilot programs and then broader programs.

And - - -?---So we made sure we did that at a national scale.

What training or experience do your asset management staff have in dealing with agribusiness customers?---So they undertake the same training and credit assessment. So our sales staff as well as our credit staff and our asset management staff all undertake our credit training and we have a number of different tiers of credit training, credit 101 and then for more experienced people we developed further training modules. We also have undertaken training with our team with the national centre for farmer health around identifying signs of distress and hardship and working with people that are under a great deal of pressure, because our asset management team, because of the customers that they work with, need to be cognisant of the emotional state and how they can appropriately work with those individuals.

Do you think that there are particular skills or qualities that are more important for bank staff who deal with agribusiness customers than staff who deal with other customers?---Well, look, I am a passionate supporter and advocate for agriculture and, therefore, I would always say yes, that I think agriculture is an industry that does require specialist expertise, and an understanding of the industry, and an understanding of the cyclical nature of the industry and how those external events that are beyond the control of the farm manager can impact production and returns. So I think then looking at any of the actions to respond to those production challenges and external challenges requires quite a long workout time, and in consumer banking you can rely on a POHE and knowing someone will have more regular income. However in agriculture, particularly in annual production systems, if it hasn't rained this year we are in a challenging situation for 365 days. So how we then manage things like 90 days out of order, and how we look at strategies to get back into a better performing state, does require a longer term lens, and therefore I think, if we have someone coming in without a deep understanding of agriculture, they will be thinking about strategies that are not appropriate for the industry that we are operating in.

Do you think the skills or qualities that your staff need in dealing with agribusiness clients differ in the loan origination area to the asset management area?---Fundamentally, no, because the frontline staff are dealing with the customer on a day-to-day basis, and their understanding of credit needs to be strong in order to have the appropriate conversations, and their understanding of hardship and working with people in – under stress situations also needs to be appropriate. Our asset management team are more likely to be dealing with people in distress, and suffering from hardship, but that doesn't reduce their requirement to truly understand credit and – and how they interact with individuals on a day-to-day basis.

Do you have KPIs at Rural Bank for your loan origination staff?---We do, yes.

And what are they?---So we have them – there's 50 per cent on key result areas and 50 per cent on behaviours, and our key result areas include retention. So retention of customers, customer acquisition, compliance, also includes values and leadership, and then we have a range of behaviours that they have to meet and they – and that's equally weighted across all of those categories.

So – sorry, I just want to be clear about how many KPIs there are in the key results half of the - - -?---Yes.

- - - KPIs. How many are there? Did you say there was - - -?---So we have acquisition, we have retention, we have compliance, and account conduct.

Account conduct?---So that's in terms of annual – annual reviews.

What's expected by way of account conduct in connection with annual reviews?---Annual reviews need to be less than 2 per cent of the portfolio of that individual banker, outside of the annual reviews that have not been undertaken.

So that's four KPIs in the key results portion; is that right?---Correct.

And you said they were - - -?---I may have missed one. My memory may slightly fail me.

Yes. So four or five?---Correct.

Potentially?---Yes.

Equally weighted?---Yes. And that makes up 50 per cent, and the other 50 per cent are around values, demonstrating our values, leadership and people elements. Their engagement with the branch network through Bendigo, and there may be – there may be another one in there as well.

And coming back to the key results KPIs, the first of those that you mentioned was acquisition. Can you explain what that's referable to?---Yes. So that's usually about a 10 per cent portfolio increase sought, which might be about four customers.

So on an annual basis the expectation is that loan originators will increase their portfolio by 10 per cent?---Correct.

And retention - - -

THE COMMISSIONER: Sorry, 10 per cent in number, 10 per cent in value, 10 per cent in a combination?---It's – well, I couldn't tell you the 10 per cent, but it's usually about four customers. So – and it – well, also that depends a little bit on where they are located. So some industries will have larger values, whereas if we have somebody working in horticulture, there's a slightly different scale. So it really depends on the region they're operating in.

MS ORR: Retention is what I was moving to ask you about, Ms Gartmann. What does that require?---Well, I don't like to see any customer leaving us, so I have a very low appetite for lost customers.

And does that mean there's a target that needs to be met in relation to retention?---It's not a prescribed target, but if there are retention issues then that will raise a conversation.

So that's approximately a 10 per cent share as well, is that right, of the KPIs?---I actually couldn't tell you the specific percentage, but I'm happy to come back to you on that.

On retention?---Yes.

Yes. Okay. And then the other two that you mentioned were compliance and account conduct. And you've explained the account conduct is being referable to annual reviews; is that right?---Correct.

And are there incentive programs for your staff connected with satisfying the KPIs?---No. Since 2002, the Bendigo Bank Group have had no performance or volume-based incentives, so that applies to the Rural Bank channel as well. If – if the business performs well collectively, then there is a all staff share in a bonus pool, and that – for our sales staff is a maximum of 10 per cent of their salary – which largely doesn't go anywhere over $10,000.

So there's an incentive for your staff to contribute to the pool from which bonuses - - -?---Correct.

- - - of up to 10 per cent of their fixed remuneration can be applied?---That's correct.

Is that right?---Yes.

But no individual performance target?---No.

And you said that had been the case since 2002?---For the Bendigo Bank and then, since full acquisition, for Rural Bank.

Yes. Now, what about in your asset management branch. Are there KPIs there?---We do now have some KPI that have been introduced since I've been in place, and they relate to the number of post-decision overviews that are undertaken and – and their engagement with customers and also with the banking officers. But otherwise, no, there are not strong KPI for asset management, because these things take a long time.

THE COMMISSIONER: You will need to explain better to me what you mean by post decision overviews undertaken?---Yes. So we have had a post-decision overview process in place where any decision for – it's both for origination as well as annual reviews, temporary limits, will then get reviewed by a higher delegated authority. And so those decisions within asset management will also be overviewed by a higher delegated authority to ensure everything was undertaken well, and if not then there is some coaching undertaken.

MS ORR: So the KPIs are connected to the results of those post-decision overviews; is that right?---No, they need to undertake a certain number of PDOs.

All right. And then the results of those PDOs, post-decision overviews, dictate whether there's some form of action taken with the employee; is that right?---Correct. Yes.

And is there any incentive structure - - -?---No.

- - - connected with asset management?---There's not.

You've exhibited Rural Bank's asset management policy to your statement. Could I ask you to turn to that. It's exhibit 2 of your statement, BAB.5014.0001.0168. We have that on the screen now. Could you explain to the Commission when this policy was introduced, Ms Gartmann?---This policy was introduced in 2014, I believe.

We see a reference, I think in your statement, to October 2017?---That could be the – so we regularly review this.

Yes?---Almost on an annual cycle.

So you have had an asset management policy since 2014, and the one you've exhibited has been in place - - -?---Is the latest.

- - - since October 2017?---Correct.

And is still in place?---Yes.

Thank you. Could I ask you to turn to 169 in that document, the second page, and we see at the top of the page that it contains Rural Bank's asset management mission statement which is to:

> *Actively engage our customers experiencing financial difficulty with the intention of identifying an acceptable solution and strengthening our long-term relationship, yet being prepared to act decisively where necessary to safeguard customer and shareholder interests.*

And what I want to ask you about is how Rural Bank balances the two parts of that mission statement being working to identify "an acceptable solution and strengthening the long term relationship with the customer", which seem to sit together, and being prepared to act decisively where necessary, particularly to safeguard shareholder interests." Could you explain how Rural Bank balances those competing objectives?---It is – as – an art as much as it is a science, particularly in agriculture, given the long-term cycles and the cyclical nature of the agricultural industry. So we will work with customers and I try and identify, once they are – I will go back a step. Once they are identified as coming into asset management unit, which has been established since 2014, that we will then work with the customer to identify a strategy that will help to address some of the financial challenges that they are facing. We, on average, are working with – with people in asset management for about three years. So it's not a – there is no quick solution, and often they've come into asset management because of external events, and it could be they've suffered health issues or there could have been a death or divorce, and if we had an ability to pre-empt death and divorce there would be a lot less challenges with asset management. When we look at industries that have had large external impacts, like the shutdown of a market, or long-term drought, you know that the solution is not going to be particularly quick because there actually needs to be that annual cycle of rain or commodity production or a change in the market for there to be a work-out option. And our customers and ourselves will always look to try and trade out of challenges. And the challenge – the balancing act comes into place where when someone is in asset management and they are what we would call impaired, which is a requirement from APRA, we are also carrying 150 per cent of our capital against that loan. So it's costing us more to work through, and we're also putting a lot more resources and time from a staffing perspective into working with those customers. So we do need to try and balance knowing the agricultural cycle, knowing it takes a number of years to work out, particularly in – in longer term drought cycles, with making sure that we're not misusing depositors' and shareholders' funds and also making sure that we're not eroding the equity for the individual customer that we can find a solution so that there is an ability to continue to operate.

So what I'm particularly interested in, Ms Gartmann, is how you do that. So you've explained articulately the challenges that are faced in these situations on both sides of this ledger, but how do you encourage your staff to balance those challenges in any particular situation?---So there are a number of things that we would put in place. So extending terms, changing loan arrangements to extend and make those repayments more manageable. We will restructure, noting that restructured facilities under APRA guidelines also mean that you have to carry 150 per cent capital against those. There is an allowance in agriculture that if you restructure for less than 12 months that you don't have to carry that extra capital but really, in an agricultural sector, less than 12 months just doesn't work because you're actually trying to get through to the next season. So we're balancing the needs from a regulator perspective in terms of the capital that we hold. We will look at, as I said, changing terms, restructuring, there will be some discussion around – you know, debt reduction. Often – particularly because we lend against perishable product, so that's cattle and crops, sheep, livestock, we will look to try and realise some of those to reduce debt, but always cognisant that you actually need to leave sufficient stock available so people can continue to operate a herd. So, again, that's a balancing act as to what assets you can realise to help to reduce debt to put people in a better position that when the season does turn – and you always hope it's going to turn the next year – that they're better positioned to then continue to trade out.

So what guidance do you give your staff about when the balance has shifted towards the need to act decisively? How do you tell them to identify that point when that decisive action is required?---So that will often come down to how cooperative the customer is in working with us, and we will often discuss strategies and agree strategies but they may not actually be actioned. So if we find that the customer is not actually wanting to work with us to address the – the financial scenario, then we will need to think about acting more decisively to take firmer action.

And what about the situation where a customer is prepared to work with you, to the best of their abilities, but they're being defeated by the matters that you've referred to a number of times in your evidence so far. What happens in that situation?---So if we – if we get to the situation where, despite everybody's best endeavours, there is not a viable operating entity that can continue to trade out, then we will discuss enforcement action, and that will incorporate, if they're willing, a mortgagee in possession where they continue to have control of the asset until sale, and if the customer is really not particularly happy to collaborate and cooperate in that instance, then we will appoint a receiver manager.

And are there guidelines to your staff about when that extreme remedy is used, of appointing a receiver?---It's something that we discuss on a regular basis. So we have management credit committees where the asset management team report regularly on – on customers and discuss what the strategy is, what the situation is, and there will be discussion and some direction at those monthly meetings.

And your policy here on the screen is said to be informed by two particular priorities. Under the mission statement we see the priority of:

Providing the customers with every reasonable opportunity to preserve their debt and any underlying loan security.

And the priority of:

Minimising and mitigating both customer and shareholder loss.

Now, is there anything you would like to add to the answers you've given already to elaborate on how Rural Bank minimises and mitigates both customer and shareholder loss?---I think one thing I will add is that we – because we work with customers for a particularly long time, and if I use the Queensland cattle example, the longest period of time we worked with a customer was seven and a half years. And, to some extent, you could say that we are working with customers for too long at – without giving adequate consideration to our shareholder, and also our deposit base. My response to that is that I think we need to give as much opportunity to trade out as possible, and to find that positive season in order to truly be an agricultural specialist.

Ms Gartmann, are you familiar with the Code of Banking Practice?---I am.

And is Rural Bank a subscriber to the Code of Banking Practice?---Since December last year we are a subscriber.

Since December last year. And how long has the Code of Banking Practice been in operation?---I believe that the one that we have subscribed to is the version from 2013. However, there are prior iterations to that.

There have been prior iterations since 1993?---That's new to me, but I know that there are prior iterations.

How long has Bendigo and Adelaide Bank been a subscriber to the Code of Banking Practice?---I – for a substantial period of time, I think they may have – actually, I would just be hypothesising as to the date.

Perhaps if I could show you a document to assist with that, which is RCD.0006.0006.0001. What will be brought up in a minute, Ms Gartmann, is a list from the ABA website of subscribing banks to the Code of Banking Practice. So we see there an alphabetical list of subscribing banks and the dates of adoption of the Code of Banking Practice. And you see there the reference to the Code of Banking Practice 1993 in the far right column?---Yes.

And then it was revised in 2003, in 2004 and in 2013. Do you see that?---I can see that.

Now, Bendigo and Adelaide Bank, a division of Adelaide Bank Limited as of 1 December 2008, is listed in this table as having been a subscriber – it appears since the start?---Yes.

And Rural Bank, we see towards the bottom of the page, did not subscribe to any of the earlier iterations, and subscribed to the current 2013 iteration on 11 December last year?---Yes, it states that.

Yes. Which you will see from this document shows that Rural Bank is the last of the subscribing banks to subscribe to the code?---It states that there, yes.

So why did Rural Bank take so long to subscribe to the Code of Banking Practice?---Prior to my appointment, I honestly cannot say why. Since my appointment, we committed to signing up to the code, and it required some substantial technology investment, which was a project that was initiated when I commenced, and that project took place on 27 September – no, sorry, 27 November 2017, at which time we could enable and we adopted the Code of Banking Practice. That was a decision that I took to ensure that there weren't too many changes taking place for staff across the business, and so I looked to align the large change programs.

So the necessary technological investment was made in November 2017?---No, it actually commenced in 2015, but the – the project was a multi-year project that was then finalised, and the big technology completed over the weekend of 27 November 2017.

And what was the nature of the technological investment that you needed to make to be able to subscribe to the code?---So we were actually undertaking some migration of banking platforms, and we decided that because there would be a number of policy changes across – across our sales force, and in fact the entire bank, that the policy changes to align with the Code of Banking Practice, which was predominantly guarantees – so moving from unlimited guarantees to limited guarantee as part of the code, was all aligned at the same time. Since my appointment we also signed up, in advance of the code, to the voluntary Queensland farm mediation scheme. So that was also undertaken in the last couple of years, prior to it becoming a compulsory scheme.

So when did you make the decision that Rural Bank should subscribe to the code?---Shortly after I came on board.

In 2015?---It was probably early 2016 by the time I got my head around the business.

And you then embarked on this technological project, which related to the move from unlimited to limited guarantees or to other matters?---No, to other matters.

Matters connected with compliance with the code?---No, it wasn't related to the compliance with code. It was largely an integration of technology systems post the acquisition of the rural finance portfolio in Victoria.

So if it wasn't related to compliance with the code, why not subscribe to the code from early 2016 when you had made that decision?---Because there were a number of changes taking place in the business and, in my view, aligning the policy changes to one point in time allowed us to roll out a supportive change program and training across the business, rather than doing it iteratively and potentially achieving change fatigue.

So that resulted in a period of almost two years, after your decision that it was appropriate for the bank to subscribe, before the bank did subscribe?---Correct.

And do you think that's acceptable, Ms Gartmann?---We were operating in the intent of the code, so I do think it's acceptable.

And if you were operating within the intent of the code, then I will ask you again why you didn't subscribe to the code in early 2016?---Because of the changes that were required to some of the policies.

So is there a tension there between operating within the intent of the code but still needing to change your policies in order to comply with the code?---Sorry, could you ask that again?

I'm struggling to understand those two concepts. On the one hand you say that you were operating within the intent of the code, but on the other hand you say that it was necessary to make policy changes to ensure compliance with the code?---So it did require all of our loan contracts, that had guarantees associated, all needed to then be changed, which impacted customers, and so we decided to do those changes in alignment with a number of other changes that were taking place as a result of the technology and platform migration.

All right. I - - -?---But we still – we were operating with the intent apart from the guarantee.

You had loan contracts that still provided for unlimited guarantees?---Up until we signed.

Yes. In December last year?---Correct.

So in that sense, you weren't operating within the intent of the code which is restricted to limited guarantees?---In that one element, but in every other element I believe that we were operating within – with the intent and faith in the code.

Would you have changed those loan contracts at some point earlier within that two year window, Ms Gartmann?---Factoring in the substantial number of initiatives that I was driving through the business, I think if we had incorporated those we may have compromised on some other areas of work. So it was a – a decision to sign up and ensure that people understood that, but still apply the principles in every way that we operated.

I tender the web page from the ABA website, Commissioner.

THE COMMISSIONER: List of bankers adopting Code of Banking Practice, RCD.0006.0006.0001 exhibit 4.122.

EXHIBIT #4.122 LIST OF BANKERS ADOPTING CODE OF BANKING PRACTICE

MS ORR: One of the obligations in the Code of Banking Practice, Ms Gartmann, is that a bank must act fairly and reasonably towards its customers in a consistent and ethical manner. You're familiar with that obligation?---I am.

And in your view, how should a bank go about ensuring that it complies with that obligation?---I think it's appropriate to act in a fair and ethical manner with your customers, disclose information, have the right discussions, and consider the customers' interests for every decision.

So it's about having the right discussions, and considering – did you say the customers' interests in every decision?---Yes.

Now last week, in the hearings that were conducted in Brisbane, you may have heard the Commissioner suggest that one way to test whether a bank is complying with that obligation in the Code of Banking Practice is to ask the question: what is the right thing to do? Do you agree with that?---Yes, I do. And actually doing the right thing is one of the core values of Rural Bank.

And do you think that the obligation to act fairly and reasonably in a consistent and ethical manner requires a bank to do something more or something different in relation to agribusiness customers than other customers?---No, I think every customer should be treated the same in that respect. The knowledge that you draw upon as to interacting with the customer is different.

Your evidence so far has made clear that lending to agribusiness customers can present complexities that lending to other customers might not, and these customers often have a particular connection to the land upon which they are farming. Do you agree with that?---There is often a very deep association and multiple generations connected to a particular piece of – of country.

And – and there are the external events that you've referred to, climatic events, droughts, floods. There are also regulatory changes?---And - - -

You agree with that?---I do agree with those, and I would also add political decisions.

And do you think that those matters, the complexities of lending, the long connection to the land, the external events – do you think that those features of lending to agribusiness customers can make it harder to figure out what fairness and reasonableness require for agribusiness customers?---No, I – I believe that the – that under – being fair and reasonable, that is fairly clear regardless of what industry or business or individual customer you are dealing with. I believe that the agricultural context means that the knowledge base that you're drawing upon – and you have to contextualise it in that if someone doesn't have an income this year, that it could be 365 days before they have income next year, whereas, someone – your average consumer is likely to – they will have cash flow every fortnight or on their – on their pay cycles, and there is more – there is easier access to regular welfare support as well to underpin individuals' – individual consumers in distress.

So do I take it from that answer that you think that the features of agribusiness lending that we've discussed don't make it harder to assess what's fair and reasonable as long as you have the knowledge base, as you refer to it?---Yes, that is an appropriate summary of my attempt.

And I just want to finally on this topic understand, Ms Gartmann, what Rural Bank does to ensure that it acts fairly and reasonably towards its customers in a consistent and ethical manner?---So firstly, having the right staff and having them appropriately trained and skilled, and appropriately monitoring and oversight their performance, and how they do their role, is an – a first priority for us in ensuring that our customers are dealing with people that know the industry and that are acting appropriately. So I see that as a highest priority.

Are there other priorities – are there other things you would like to add that are part of ensuring you treat your customers fairly and reasonably?---I think that that largely – and that's not just – our front line staff as well as every staff member within our lending value chain should be considering the customer and their interests, and balancing that up with those of shareholders as well, in making appropriate considerations and decisions. So it's not just our front line staff that need to do that, it's everybody within the business. And, therefore, having people within the business – even if they're not directly interacting with agricultural customers – need to have an understanding of the agricultural industry.

All right. I want to turn to asking you some questions about a number of loans taken out with Rural Bank by customers in the Queensland cattle industry, which you've dealt with in your statement. Now, Bendigo and Adelaide Bank made a submission to the Commission on 15 December 2017. Are you familiar with that submission?---I am, yes.

And that submission was made in response to a request from the Commissioner that the bank identify any instances where it had engaged in misconduct or conduct that fell below community standards and expectations over the last 10 years?---Correct.

Now, if I could take you to that submission, which is RCD.0001.0024.0002. Now, before we turn to that document, you explain in your statement, Ms Gartmann, that in this submission Bendigo Bank told the Commissioner that it had identified instances during that 10 year period where the bank's lending practices may have fallen below community standards on the basis that appropriate inquiries and verifications were not made prior to the approval of the loans; is that right?---Which statement was that, please?

That's your statement and it's paragraph 76 of your statement?---Yes, that's correct.

Now within this submission, if we turn to 0021, we see at paragraph 80 there that Bendigo Bank gave two examples of this, and one related to a number of loans taken out by customers in the Queensland cattle industry that became non-performing?---Yes, I can see that written there.

And Bendigo said in this submission that:

> *Contributing factors to the non-performance of those loans included weak underwriting, an over reliance on security values, compounded by the live cattle export ban, falling cattle prices, a prolonged and severe drought and a fall in property values.*

?---Yes, that's what's written there.

And that's the position?---It is.

Thank you. And Bendigo Bank also told the Commissioner in paragraph 93 on page 0023 – you see in 93 there that Bendigo Bank told the Commissioner that the conduct in relation to those non-performing loans – these are the cattle industry loans – could be attributed at least in part to aspects of industry credit practices that prioritised asset growth?---Yes, that is written there.

And what's that Bendigo Bank told the Commissioner?---Yes.

And we see that Bendigo Bank recognised that that conduct might reflect elements of industry credit practices that fell short of community standards and expectations?---Yes. That's written there.

I tender that document, Commissioner.

THE COMMISSIONER: Submission Bendigo Bank 29 January '18 – is it? Is that the date of the submission, I would have thought?

MS ORR: Yes, 29 January 2018, Commissioner.

THE COMMISSIONER: RCD.0001.0024.0002, exhibit 4.123.

EXHIBIT #4.123 SUBMISSION BENDIGO BANK DATED 29/01/2018 (RCD.0001.0024.0002)

MR BATT: Commissioner, I do apologise for interrupting our learned friend. I should just record on the transcript, of course it was erroneous, but a couple of minutes ago at transcript 3624, line 31, it was put to the witness it was paragraph 76 of her statement that recited a certain matter. I think in fact it was paragraph 76 of the Bendigo letter that has just been tendered.

THE COMMISSIONER: Thank you.

MS ORR: I apologise. That's correct. The reference to paragraph 76 was a reference to this document.

THE COMMISSIONER: Thank you.

MS ORR: Thank you for that correction.

Now - - -

THE COMMISSIONER: Save me hunting later, Mr Batt.

MS ORR: Bendigo Bank provided some more information about this conduct, that was covered in these paragraphs, in a further submission that was provided to the Commission on 18 May 2018; is that right?---That's correct.

And that information again was produced in response to a request for information from the Commission, this time a request for information about the bank's agricultural lending practices, in particular?---Yes.

Now, if we could turn to that letter from the managing director of Bendigo and Adelaide Bank, dated 18 May 2018, RCD.0014.0021.0001. This is the letter from the managing director to the Commission on 18 May 2018?---Yes, it is.

And we see in paragraph 2 of that letter that Mr Hirst, the managing director, acknowledged that a number of agribusiness customers had made submissions to the select committee on lending to primary production – sorry, you now won't be able to see that paragraph. Paragraph 2 is lower down on the page?---Yes, we do believe that a small number of customers have made submissions – or made submissions last year to that Senate select committee.

Yes, and Mr Hirst accepted that in some of those cases there was conduct on the part of the bank that fell below community standards and expectations?---Yes, that is written there.

And that included the expectation of the community that the bank would assist customers when they were in difficulty, and take account of individual circumstances, including unforeseen hardship when collecting on money loaned out. That was accepted by Mr Hirst?---I believe so in his statement, yes, in his letter.

And Rural Bank didn't have a hardship policy until 2014?---That is correct.

And why not, Ms Gartmann?---I don't know.

Should it have?---There are always policies that can be in place. My understanding from the investigations I've undertaken is that those that were working in the asset management portfolio prior to 2014 were aware of hardship considerations, so were acting in good faith. However, there was no policy in place prior to 2014.

And I want to understand whether you think there should have been, because the current hardship policy appears to be something that you're quite proud of. It's the first exhibit to your statement. And you've referred to it more than once in your evidence so far. Do you accept that the bank ought to have had a hardship policy before that time?---Yes, I do accept that.

Thank you. Now, Mr Hirst, in this submission to the Commissioner told the Commissioner that Rural Bank's customers are primarily family-owned businesses; is that right?---They are, yes.

And Mr Hirst also told the Commission that in his view the industry as a whole needed to increase its awareness of the impact that mental health, relationship breakdowns, and death have on family farming businesses, because the presence of those factors was over-represented in farming businesses that were in financial stress?---That is correct. I will just add to the fact that about 98 per cent of farm businesses in Australia are family owned. So it is the vast majority of farm businesses.

And do you agree with Mr Hirst's views about the need for the industry as a whole to increase its awareness of the impact of mental health, relationship breakdowns, and death on family farming businesses?---Yes, I do believe that is so. There are a number of contributing factors to that, being geographic isolation, lack of services, and support across rural, regional and remote Australia. So working on farm, particularly when you have external challenges that are outside of your control, does have quite a large impact on mental health. One of the reasons why we now work with the National Centre for Farmer Health – and have had training with them for each and every one of our relationship managers. So it is a substantial issue.

What is Rural Bank doing to increase the awareness amongst your staff of those matters? You referred to one initiative already?---Yes. So certainly training with all of our frontline staff with the National Centre for Farmer Health around mental health awareness and being able to identify signs, early warning signs, understanding where to refer people, how to access rural financial counsellors. We also have supported the National Centre for Farmer Health to join us at agricultural days across the country to undertake health assessments and try and get as many customers as possible to be thinking about the frequency that they do an annual health check, both physical and mental, just like they would with servicing their tractors on an annual basis or getting the vet to have a look at their livestock. So the largest and most important asset on farm is actually the health and wellbeing of the individual customer. So, therefore, we are really prioritising and have a long-term partnership with a national provider that focuses on supporting our customers with their awareness, but also our own staff.

Now, in this submission to the Commissioner, Mr Hirst gave more information about the conduct in relation to the loans to the Queensland cattle farmers. You are familiar with that?---I am.

And - - -

THE COMMISSIONER: Just before we go on with that, Ms Orr.

Can I go back a moment, Ms Gartmann, and the evident issues about health and wellbeing. What role, if any, does continuity of contact with the bank – I am talking not frequency, but continuity of contact with the bank – what part does that play in these issues?---Particularly when you're going through tough periods as a producer, I think it's absolutely vital that the person you have built up a relationship with is the person that you remain working with, because if you change – if the relationship manager were to change, you have to rebuild trust and the individual needs to have a better understanding or get up to speed on the historical performance and your management capability and, therefore, that puts extra stress and pressure on the customer. During my time working with the Birchip Cropping Group through the Millennium Drought in southwest – south-western Australia, we actually hosted a number of events with multiple banks to support farmers, knowing that changing banks during a drought or during challenging financial times is not a good outcome for the customer, nor the bank, because you're actually rebuilding what should be a trusted relationship. You know, the word trust has been overused a lot lately in terms of banks and their customers, but there is a relationship and that level of understanding and knowledge of the farm, the performance, and particularly the management capability of the individuals. So in my view that continuity of relationship, regardless of how frequently you engage, is of the utmost importance, and the stronger that relationship – it's almost less important about the frequency because the – there's a greater level of understanding, and ease of which to interact, and you know that you can – particularly in remote locations getting on to farm on a regular basis can be challenging. And yet, when people are in distress, face-to-face is always ideal, is always the preferred method of engagement with customers. However, if you're wanting to stay in touch more regularly, phone and support via other mediums is required, and if the trust and the longer term relationship is there, that is much easier to undertake. So I do place a great deal of emphasis on the long-term relationship between the banker and the customer.

Thank you.

MS ORR: Now, I was taking you, Ms Gartmann, to the part of this document where Mr Hirst gave more information about the conduct in relation to the loans to the Queensland cattle farmers. If I could ask you to turn to 0008 at paragraph 49. I'm sorry, I will get my reference to the document. We understand that it is 0008 within the document.

THE COMMISSIONER: So 0014.0021.0001 at 0008; is that it?

MS ORR: Not 0001. 0008, 0001 being the first page of the document.

THE COMMISSIONER: Yes.

MS ORR: Yes, I'm sorry.

THE COMMISSIONER: Yes.

MS ORR: What I want to put to you, which you might be able to answer before the document comes up on the screen Ms Gartmann, is that Mr Hirst said that in addition to over reliance by the bank on security values, and not appropriately assessing loan serviceability, the bank had identified that the loans were inadequately managed, that there had been a lack of follow-up on excesses, arrears, and out of order accounts, there had been a failure to conduct timely reviews and collect updated farm performance information, and there had also been failures in relation to enforcement processes?---Yes.

Yes?---Yes, I see that.

And Mr Hirst said in paragraph 50 that there were also failures in relation to valuations. The bank had not ensured valuations were accurate and independent. It had failed to physically visit and inspect livestock and properties. And in some instances, the security provided included assets where the value was not indicative of the economic returns achievable?---Yes, I have read those paragraphs a couple of times now, and I've also investigated the 62 loans in the Queensland cattle industry, and I think Mr Hirst has actually been quite harsh with his assessment, having now looked at the 62. A number of these were originated between 2003 and 2007 – or 2008, and a number of those that were – had valuations and origination in the '07 – '06, '07 years were on a dramatically rising property market and in 2008, coinciding with the lack of capital as a result of GFC, the global financial crisis, that property prices fell on average 30 per cent in Queensland, in far north Queensland up to 46 per cent. There's a Herron Todd White report from 2014 that highlights that data. So at that time any loan that was originated as a bridging loan, in order to buy a new property and you plan to sell your prior property or one of your prior properties, the valuations were dramatically out in 2008 and '09 as a result of that substantial rise in property prices, and then that – and then that decline. So, therefore, the valuations, they were not contemporary, and they – the dramatic changes in the property market impacted the appropriateness of those valuations. One issue with valuations in the agricultural sector – you mentioned the economic return achievable. Valuations are largely undertaken by comparable sales. So the market – what the market is willing to pay for. And that doesn't always translate to the production and the return that you can get per beast or per acre in a cropping enterprise. There has been a substantial amount of debate in the valuations field about comparable sales versus productive capacity, and valuers are reluctant to look at the productive capacity because a lot of that actually comes down to management capability. You might have a great property, but if your management capability is not high quality, then you will not get the same returns as someone with stronger management capability. So the comment about the economic returns not being achievable based on the market value, I think is a symptom of valuations being based on comparable sales as opposed to the productive capacity of the land. So that was certainly a key external contributor to that – those valuations that were original – or the loans originated pre-2008 and then their valuation and therefore security held against them post-2008. I do point out that we did not action any non-monetary defaults as a result of those changed land values, instead understanding the cycle and looking to work long-term, because we anticipated that prices would return. Now, they haven't returned to the same peak of early 2008, but they certainly have recovered somewhat in far north Queensland. There are also a series of events that impacted Queensland cattle operators, in that cattle prices also declined in 2010. I think they got down to about 300 cents, or below actually, now sitting at about 500. We then had '10, '11, Cyclone Yasi and substantial impact of flooding impacting a lot of our customers, and a number of the 62. And in 2011 on 8 June, an impact that was not natural, and that was a closure of the live export market. We had 15 customers 100 per cent reliant on that market.

THE COMMISSIONER: Sorry, you had?---We had 15 customers that were 100 per cent on the live export market, and 281 customers largely reliant on the live export market. And cattle mustering takes place mid-year, and so there was no market to sell into in 2011. Therefore, people held on to their cattle and sales were not achieved. Cash flow did not come in to service debt. We were aware of that, and therefore allowed – you know, made changes to payment terms. What we didn't anticipate, and in hindsight what would have been good for us to do as an agricultural specialist, is then further stress tested our book to say, "We've had property price changes, we've had political interference in a global market. And what else could go wrong to further challenge our customers that are already quite challenged?" We did not anticipate a five year drought commencing in 2012, which continues now into its sixth year. So there are extreme external events that impacted the Queensland cattle producers. I've looked at the 62 loans that became non-performing during that time, and they became – categorised them as non-performing because they either were downgraded by three or more grades in our credit risk rating or they were unable to meet repayments. And I've looked at those 62 to see whether or not we actually should have made different decisions under the previous policies, and there are very few that I don't believe would not be written now. There were nine bridging loans in those 62, and the strategy was to acquire a larger or better property and to sell other assets to address the debt. And that was impossible in the 2009 through to 2011, and then into the drought. So property sales, the property market became quite depressed, and our customers would have been selling attach lower values than what they had anticipated, so we agreed to continue to work through. There were probably six of those nine where, under our current risk appetite, I think we would say they were high risk strategies and probably could have had more robust discussions with our customers about what-if scenarios, “What if this strategy does not work out?” There are another three of those 62 where the serviceability was reliant on off-farm income. One of those does include a customer that did not disclose they were in asset management with another financial provider, and we became aware of that post origination. So there are a couple there that we would have thought more critically about, and thought about the mitigating strategies to support those customers in executing their strategy.

I want to come back to a number of themes of what you’ve just said there, Ms Gartmann, but before we move away from this submission from Bendigo Bank, I understood a large part of your answer then – particularly the first part – to be directed to the final sentence of paragraph 50:

> *In some instances the security provided included assets where the value was not indicative of the economic returns achievable, further impacting loan serviceability issues.*

Is that right?---That’s right.

But do you take issue with Mr Hirst’s assessment in the first part of that paragraph that in addition to that, there was:

> *A failure to make appropriate inquiries and verifications of valuations and appraisals, including failures to ensure valuation accuracy, independence and integrity, and failures to physically visit and inspect livestock and properties.*

?---So certainly the verifications of valuations and appraisals, I have looked back at the policy from that period of time, and believe everything was undertaken as per policy. The area that I do agree is with physically visiting and inspecting livestock. At that time, the Elders district banking managers – there were not as many on the ground as should have been. There was less investment in the district banking manager employee numbers, and so those staff that were on the ground were really challenged to get to some remote locations and to physically inspect stock numbers on pastoral properties. Now, there are a number of ways that this take place and often you will go to a watering point and do an estimated head count. If it’s a new to bank, you really do need to do that physical assessment. If it’s an existing customer, you can have a look at their stock records and get a greater understanding of their trading history and, therefore, the likely stock numbers on hand, but I do believe that the physical visits and inspection of livestock wasn’t always carried out with enough diligence.

And you’ve said in relation to the rest of that sentence, as I understood your answer, that what went on was as per policy. That was the phrase you used. But do you accept that whether it was within or outside of policy there were failures to make appropriate inquiries and verification of valuations and appraisals, including failures to ensure the accuracy, independence and integrity of the valuations?---Between our credit team and the frontline district banking managers, there was insufficient challenge of those.

Of the valuations?---Of the value – the appraisals as opposed to the valuations.

Yes. Internal appraisals. Is that what you were referring to?---That's correct. Yes.

So the credit team didn't interrogate those - - -?---Insufficient focus.

- - - appraisals in the way they should have?---Yes.

Okay. And what about what Mr Hirst says in paragraph 49:

> *Inadequate loan management, evidence of a lack of follow-up of excesses, arrears and out of order accounts, failures to conduct timely reviews or collect updated farm performance information, and failures to otherwise detect signs of financial distress at an earlier point in time, as well as failures in relation to enforcement processes.*

Do you take issue with that characterisation?---I do, in some respects. There certainly was poor loan management and follow-up with individual customers. Largely, those customers were in distress situations post the closure of the live export market and also during the drought period in recent times, and following those up and putting pressure on our customers doesn't necessarily add to positive mental health. So part of the – part of the poor performance in that area was failure for our district banking managers to inform our credit team of the performance of individual farm businesses and their loans. So I do accept that the failure in relation - - -

Just before you move on, because I just want to ask something about that answer. A failure to follow-up those matters, excesses, arrears, and out of order accounts, is not just relevant to whether or not you put pressure on the customer, is it? These are warning signs of farmers in distress, and they're important for that reason, aren't they? And they need to be followed up so that there's a conversation with the farmer about that distress and the way to manage it?---You are correct. I think what we have to add here is that these industry-wide issues were very well known.

Yes?---So we were aware of the impact of those on – on our customers, and having a conversation that we were – we knew of the externalities and the customer knew of the externalities, for the sake of having the conversation, was something that I think individuals applied their judgment to, sometimes incorrectly. What it did do was challenge our overall loan portfolio management so that we were appropriately provisioning and impairing as per APRA requirements.

I interrupted you. You were about to move to another part of this paragraph?---So the final sentence in – or line in 49 and the failure in relation to our enforcement process - - -

Just pausing there, do you mean the final – this is all one sentence. Are you referring to the last two parts of that sentence, the failures to detect signs of financial distress at an earlier point of time, and failures in relation to the enforcement process?---I am, yes.

Thank you?---And I do believe that we are much better at identifying signs of financial distress now through our specific portfolio stress testing that we do. And if I can give you an example, in the dairy industry we had stress tested our dairy book in late 2015, and identified a number of customers that, were there to be a change in climatic conditions or a change in milk price, would come under financial duress. And we then went and spoke to those individual customers about what they could do to better mitigate that risk were it to happen to them. And then in May 2016, with the milk prices crashing, we already knew which customers would be impacted. So that sort of approach is a more recent introduction to the business, and allows us to pre-empt potential externalities on the industry, which we did not do back in the 2000s, or 10 years ago. The – that earlier identification can allow some action to take place and – and as I – we discussed earlier, the sorts of activities that would take place in extending terms, changing loan arrangements to suit, to mitigate that risk. And in relation to the enforcement process, sometimes I think we – we will try and work with a customer for too long, and that's my deep focus on trading out, and working through the long-term cycle, and I believe that Mr Hirst highlighted here that, perhaps, the quick and timely decisions around enforcement are sometimes the ones that we are less likely to take.

That's what you interpret him as referring to when he refers to failures in your – in relation to your enforcement processes?---It is, yes.

Okay. Now, you've made clear that the failures that Mr Hirst is referring to here, subject to the qualifications that you've given, affected 62 loans in total made by Rural Bank to Queensland cattle producers, and the majority of those loans were originated between 2003 and 2007; is that right?---The original origination, yes.

Yes. And the loans became non-performing at a later time. They became non-performing from the start of 2008 through to 31 December 2017?---Yes, correct.

And how did you, or Mr Hirst, or whoever before you identified the 62 loans, how were they identified?---So we looked at our Queensland cattle customers, and then we looked at those that had been downgraded at a credit risk rating of three or more.

Yes?---We looked at those that had become a credit risk rating of eight or nine. And I think there was one other element that was used in that determination.

You referred to them being unable to meet their financial obligations before. I'm not sure if that was a separate element, or reflective of the others?---I think that's often reflective in the downgrade, if they've been unable to make a repayment.

So you identified 62 loans on that basis?---Yes.

And before I – I want to spend just a little bit of time dealing with these different categories of failures in relation to those 62 loans. But before I do that, I want to do two things. Firstly, I want to tender this document, the 18 May 2018 letter from Mr Hirst.

THE COMMISSIONER: Bendigo Adelaide Bank letter to Royal Commission, 18 May '18, RCD.0014.0021.0001, exhibit 4.124.

EXHIBIT #4.124 BENDIGO ADELAIDE BANK LETTER TO ROYAL COMMISSION DATED 18/05/2018 (RCD.0014.0021.0001)

MS ORR: And the second thing is I just want to come back to those external events that you've referred to that affected Queensland cattle producers in this period. You identify in your statement four major categories of events that affected those producers, and if I deal with them chronologically the first was that in about 2008 there was a major decline in property prices for Queensland cattle properties; is that right?---That's correct.

And then that was accompanied by a significant drop in cattle prices?---Yes.

And in 2008 to 2009, there was a severe drought across much of Queensland?---Yes.

And in the summer of 2010 to '11, there was widespread Cyclone Yasi related flooding - - -?---Yes.

- - - across parts of Queensland. And then in June 2011 there was the live export ban that we've heard about multiple times in the hearings already?---Yes.

Yes. And you tell us in your statement that at that time Indonesia represented the largest market for Australian live cattle trade?---Correct.

And this particularly affected the northern Queensland farming properties because numerous properties in that part of Queensland relied either exclusively or heavily on that market?---That's correct.

And in many cases, you tell us that affected Queensland cattle producers had no other viable market for their cattle?---Correct. I'm not sure how familiar you are with the cattle market, but certainly - - -

Becoming more and more familiar, Ms Gartmann?---Certainly the cattle from far North Queensland are not appropriate for the domestic market. So there are major challenges in being able to transport them and then have them meet the market requirements.

And then, during 2013 to 2017 and ongoing, there were severe droughts across most of Queensland?---Yes.

And in your statement you describe the cumulative effect of all of those events as almost the perform storm scenario for Queensland cattle farmers?---Correct.

And you say that these events – these events occurred in rapid succession, and in some cases almost simultaneously?---That's correct.

And you also explain and you've, I think, given this evidence today, that these – this chain of events was almost impossible to predict?---Correct.

And you accept that the scale of financial impact was extreme for a very high number of Queensland cattle producers?---Correct. Yes.

Now, whilst those external factors contributed to the 62 loans becoming non-performing, you accept that the conduct of Rural Bank, which I now want to come to in a bit of detail, also contributed to those loans becoming non-performing?---It certainly made them more vulnerable to those externalities.

Thank you. All right. Now, you categorise the various failings that were referred to in Mr Hirst's communications with the Commission. You categorise them in your statement as involving three interrelated issues. Do you recall that?---Yes, I do.

And the first set of issues that you identify are associated with the serviceability of the loans?---Yes.

And in some cases we know that loan serviceability wasn't properly established for those loans?---It was not appropriately challenged by our credit team.

You're referring to the credit team interrogating the information provided by the loan originator?---Correct.

And that resulted in loan serviceability, from the bank's perspective, not being properly established?---It meant that there was insufficient financial resilience within the business. So we had assessed serviceability, but in many instances it was quite tight.

Now, the second set of issues that you refer to are associated with security and valuations. And do you accept that in some cases Rural Bank over-relied on the security values?---I do, yes.

And in some cases, there was a failure to make appropriate inquiries by your credit department before offering a loan?---Correct. Along with the challenge of physically inspecting livestock - - -

Yes?--- - - - to determine actual numbers, yes.

Thank you. So two separate problems there?---Yes.

Challenging – not challenging the lack of a physical inspection, and not verifying the valuation – the credit department down to the internal appraiser?---Correct.

Okay. And the third set of issues that you use to categorise these failures is management of the loans?---Yes.

And in some cases, there was inadequate loan management which exacerbated the loan performance?---It did not exacerbate the loan performance. It meant that at times we were late in identifying when that loan may have become non-performing.

Well, the language I used was Mr Hirst's language. He talked about inadequate loan management that exacerbated loan performance. You would not describe it that way?---It's challenge to connect the loan management with the loan performance, apart from the context of a performing versus non-performing loan. So it's the language I'm challenged with, sorry.

You would put that differently?---I would, yes.

And when you refer to issues with the management of the loans, you're referring to the bank being late in identifying – what did you say?---The – so that when the – if a loan became non-performing, were we timely with that in identifying when that took place, because of the cycle of being – undertaking annual reviews, or considering the requests for temporary limits and increases.

So a lack of timeliness in terms of identifying the non-performing - - -?---Correct.

- - - nature of the loan?---Yes.

And that's a loan management problem?---It is, yes.

All right. Now, you also tell us in your statement that in your view there were a number of causes for these issues, and you deal with this in paragraph 69 of your statement, and the causes that you've identified are poor judgments by Rural Bank staff in the exercise of their discretions?---So that was – judgment was largely by our agents, as opposed to direct Rural Bank staff.

Yes. On behalf of the bank, though?---Yes.

So poor judgment in the exercise of their discretions. What discretions did they have that you're referring to there?---So when we're assessing a credit, obviously an agricultural credit – I'm sure you're rapidly learning – is not a black and white – it doesn't fit into a particular box and it will depend on what is the business strategy, where are they in their cycle, is it a younger farmer stepping up, are they in a rapid expansion phase, are they in a consolidation phase or a wind-down phase. So therefore we have – within the policy there are opportunities to utilise discretion to consider the different and unique factors for each and every loan. And that will often be, if I use the example of off-farm income, so the credit assessment largely does not factor in off-farm income when we're looking at our debt service ratios, however a number of farms do have off-farm income from either one member of the farm family having a job in the local community, or that business utilising their expertise, their helicopter, their seeding equipment, to do contract work for other farmers. And so when you exercise your discretion you are taking account of those other revenue sources to consider in serviceability. The judgment piece is also in respect to management capability. It's not an easy – you don't actually do a formal qualification and have a tick box for management, so understanding the management capability and expertise of the individual, and the farm family, is an important judgment within our credit assessment.

So the poor judgments in the exercise of those discretions, do I understand from that that the individuals were exempting some of the customers from the bank's requirements because of the uniqueness of their situation?---No, no, it was still within policy.

Yes?---And their judgment as to how likely that income was, it wasn't always highly accurate, and particularly when we think about off-farm income in the contracting sense, if you're in a drought then many of your – the farmers' customers that are other farmers are less likely to have the cash to spend on – on that off-farm income service.

So the poor judgments – I just want to understand - - -?---Yes.

- - - exactly what it is that you say was poor about them. They failed to give sufficient weight to factors that they should have given weight to, they got it wrong?---Well, they – they were certainly operating within policy.

Yes?---To understand the unique nature for each loan.

Yes?---They were often very supportive of what the customer identified as some of the mitigating factors, and I believe that from a judgment perspective they weren't adequately pushing back - - -

I see?--- - - - and taking account of the variability that might be inherent in the off-farm income or the management capability.

I see. So that's the first cause that you refer to, those poor judgments in the exercise of discretion. The second is inadequate management oversight of the exercise of those discretions, which I think is self-explanatory. People weren't supervising the exercise of those discretions as they ought to have been?---That's correct, yes.

And the third is inadequacies in staff training. What are you referring to there?---Well, I don't believe that – on my investigations, it's very hard to identify what training and development was in place pre-2008. I understand that from 2011 there was a substantial increase and execution of training which, to me, indicates that there was insufficient training delivered. And training and development does aid in an individual's judgment and understanding of agriculture and – and particular business performance. So, hence, I have identified staff training as a key factor.

And you've also identified insufficient performance management of some individuals?---Correct.

So some individuals were not being taken to task about the way they were conducting themselves and ought to have been?---Yes. Particularly if there is inadequate oversight, then you're not aware of the – if it was judgment or, you know, poor practice, and therefore addressing that with the individual staff member.

And then you refer to, as another cause, matters of sales and credit culture. What are you referring to there?---So at the – this refers to a number of the issues highlighted in the Willis Report.

Yes?---And certainly, having an understanding of the credit risks and the risk appetite for the business, there were cultural challenges between the district banking managers and the credit team, and as a relative newcomer into the industry, I am regularly told that there is always a degree of tension between sales and credit, and that you need to have that. But when there is misalignment of understanding of the credit appetite and the credit risk between sales and credit, that that actually does influence the appropriate engagement and the operation as a team.

So if I attempt to put that in simpler terms - - -?---You will do it much better than I will.

No, no, no. I just want to make sure I understand your answer. There was too much emphasis given to sales rather than the credit risk appetite of the bank. So individuals were selling loans that were too risky?---There was – no, that's not quite right. I don't believe that – the credit and the sales force were not aligned around the appropriate credit appetite, and also the required information to inform a credit assessment.

So that's what I'm just trying to understand, what it – what it actually means to have the sales people and the credit team not appropriately aligned?---Mmm.

On these matters?---Yes.

What do you mean by that?---Well, if I talk about the situation now, we're very clear around what is the maximum exposure we are comfortable with, what are the target industries, what are the common characteristics of a customer that we are – would like to have as part of our customer base. And that needs to be shared across both the frontline and the credit teams, and that strategic alignment was not present.

Okay. Okay. And was the consequence of that that loans were made to customers that ought not to have been made? That's what I'm trying to understand?---No, I don't believe - - -

What was the consequence?---I don't believe so. Particularly having reviewed the 62, there were very few that I – that we would not still write. But it did create challenges in the relationships internally between sales and credit, so that actually meant there was not – I am just trying to find the right words – the respect between each team was poor and the engagement between each team was poor, but having a look at the loans, particularly the 62, that did not directly impact on the writing of inappropriate credit.

I understand. And you say in your statement that these problems that you've identified didn't necessarily of themselves have an impact on customers?---Correct.

But you do say in your statement – and you've said here in your evidence today – that they made the loans more susceptible to the cumulative effect of the external stresses that we've discussed?---That's correct.

Is that right?---Yes.

And when did Rural Bank identify the conduct of its staff that affected these 62 loans and made them more vulnerable?---The conduct of the individual staff – sorry, you might need to - - -

When did Rural Bank appreciate that this was a problem for these 62 loans?---So – well, the 62 – if I go back to two – from 2009 we identified, from – and I have had a look at minutes and reports from 2009 onwards – and it was identified and being discussed within the board credit committee meetings and they initiated a number of reports to investigate the challenged Queensland portfolio. And the 62 loans was really only following January this year that we did the analysis to identify the specific loans that may have been impacted in the Queensland cattle industry.

So the broader issues were detected from 2009 onwards?---Correct.

But the 62 loans were identified in January of this year, or around January - - -?---I think around May, actually.

Around May of this year. Do you mean at the time that Mr Hirst was putting together his response - - -?---Yes, correct.

- - - to the Commission's request for information about the bank's agricultural lending - - -?---Yes.

- - - practices?---Yes.

So in response to that letter asking for that information, investigations were conducted that led to the identification of the 62 loans?---That's correct.

Now, I just want to understand if that's correct, because my memory was that the 62 loans may have been referred to in the December 2017 response, but I will check that?---So we did – because we were aware of the portfolio challenges for Queensland cattle, and we had had – there were a number of management reports presented to various board committees, we were aware of a number of challenged files, and that was included in the January letter.

Yes. I'm sorry, I referred to December, which was the date of the letter. The response to that letter was January 2018. And now that I look at that, I can see that no figure was placed on the number of loans in the January 2018 letter. The first time that figure of 62 loans was identified was in the May 2018 response to the request for further information - - -?---That's correct.

- - - from the Commission?---Yes.

All right. So it was at that time that investigations were done that allowed those particular 62 loans to be identified?---That's correct.

Now, I do want to ask you some questions about each of these categories of issues, and I think it might be appropriate for you to have a short break before I move to doing that, but could I just deal with one other topic first, which is: do you accept that from 2003 onwards, Rural Bank was attempting, quite aggressively, to expand its Queensland loan portfolio?---No, I don't accept that.

So when we come to look at some documents in relation to the particular issues, I might draw some particular matters to your attention, but perhaps that is an appropriate point to have a brief break, before I move on to some of those topics in more detail.

THE COMMISSIONER: If I come back at, what, Ms Orr, quarter to midday or - - -

MS ORR: Yet. Thank you, Commissioner.

THE COMMISSIONER: Quarter to midday. Very well.

ADJOURNED **[11.39 am]**

RESUMED **[11.46 am]**

THE COMMISSIONER: Yes, Ms Orr.

MS ORR: Just before we move on, Ms Gartmann, I just want to come back to when the 62 loans were identified. I think your evidence was that they were identified in investigations conducted in response to the letter from the Commission that was responded to in May 2018?---Correct.

And that May 2018 response did not give a number of loans affected. Would you like to see that document to answer that question?---The May 2018?

Yes. So, the May 2018 letter - - -?---You may be right, actually.

Yes. In both the January and the May 2018 letter, the references were to "a number" of loans - - -?---Yes.

- - - affected by this. Now, the Commission sent a Rubric to Rural Bank asking a series of questions about the loans identified in both of those documents, and that led to you producing a statement?---Yes.

In that statement, which was finalised on 20 June, you identified for the Commission that there were 62 loans affected by these issues?---That's correct.

Do you accept that?---Yes.

Okay. Thank you?---Over the long weekend, yes.

Yes. But the discovery of the 62 loans was in May 2018, at the time you were preparing the May 2018 response, but the 62 loans was not identified in that document?---No, correct. So - - -

Well before the long weekend?---Allow me to – sorry, so the portfolio performance and the issues in the Queensland cattle industry were identified from 2009 onwards, through a number of reports and portfolio analysis.

Yes?---And we were aware of a number of Queensland cattle loans - - -

Yes?--- - - - that in my time within the bank have continued to be managed.

Yes?---And then when the Commission asked for some specific numbers, then we did the analysis as to specifically which ones.

Yes. And I understood that you said that that analysis was done in the time that you were preparing the letter to the Commission from 18 May 2018?---And I was incorrect. It was in response to the rubric.

Right?---Yes.

So when do you now say that you identified the 62 loans?---In response to the rubric, which required a specific number.

Okay. So around June - - -?---Yes.

- - - 2018. Thank you. Now, I said I wanted to ask you some questions about your three categories of issues that affected these loans. And the first category of issues was serviceability. And, now, I want to ask you about when the first wake-up call, if I can call it that, for the bank was about problems with the serviceability of these loans?---I believe that some of the reports that were commissioned from majority ownership onwards were highlighting concerns with the Queensland portfolio, and the credit quality and the credit deterioration in the Queensland portfolio. And there was a report in – in September 2009, I believe, in May – actually, I'm trying to – I might – there were three reports.

Yes. I think the first report – unless there's a report that is not referred to in your statement – the first you refer to in your statement was a report from KPMG - - -?---That's correct.

In March 2010?---'10. Okay.

And that report was commissioned as a result of an action item from a board credit committee meeting on 22 December 2009; is that right?---I believe so.

Yes. And – so firstly, I want to understand why did Rural Bank engage KPMG?---KPMG were undertaking our internal audit function.

And what did you ask them to do in response to this action item from the board credit committee meeting in December 2009?---I believe it was to investigate and have a look at what information was being collected by the Elders district banking managers in informing the bank of loan applications and what information they were providing for loan management.

All right. Could I ask you to look at BAB.5022.0001.0001. This is the engagement letter to KPMG?---Yes.

I'm sorry, I misled you before. The engagement of KPMG was in March 2010, and the report produced?---September.

- - - in response was September 2010?---Yes.

So 18 March 2010, Rural Bank engages KPMG. And we see there on the first page that Rural Bank asked KPMG to undertake a sample testing of existing credit files for a number of district banking managers?---That's correct.

Now, you've mentioned district banking managers a number of times, but could you just explain what the work of a district banking manager is?---Yes. So the role of a district banking manager in today's terms is essentially a relationship manager, and they interact directly with the customer, collect information from the customer, and enter that into the agribusiness banking system in order for the credit assessment to take place.

And how many district bank managers did Rural Bank ask KPMG to look into?---I don't believe that was specifically outlined in the engagement letter, so I – I can't answer that question.

We understand from the documents provided by Rural Bank that Rural Bank asked KPMG to look into the conduct of five particular district bank managers. Does that sound right to you?---Could you point me to where the engagement letter highlights the number, please?

It is dealt with in one of the exhibits to your statement, rather than the engagement letter, Ms Gartmann. I think the best place to see it is probably the KPMG report - - -?---I am familiar with the report.

- - - that was put - - -?---I wasn't clear what – I don't believe the instruction letters articulated how many district bank managers had .....

No. But, putting the instruction letter to one side, do you know how many district bank managers Rural Bank asked KPMG to look into?---I know that the report – so I don't know what was requested, but I know the report that came back looked at four – four locations and five district banking managers.

Four locations across the country. Four different states; is that right?---I believe - - -

Three different states?---Three different states.

Victoria, Queensland and South Australia?---Correct.

And the conduct of five different district bank managers across those states?---Correct.

Okay. Now, do you know how those five district banking managers were chosen?---No, I do not.

Were there known issues with their conduct?---I can't answer that. I'm unaware.

All right. Have you seen the action item that I referred you to earlier from the December 2009 board credit committee meeting, which I'm happy to show you, which referred to a need to investigate personnel issues and report if the issue is systemic or isolated?---I do remember that.

And does that suggest to you that these were individuals for whom there were personnel issues and there was a need to work out if the issues connected to these individuals were isolated or systemic?---I couldn't answer that without speculation, I'm sorry.

So you're unable to tell the Commission how those five district banking managers were chosen?---That's correct.

Okay. Now KPMG, we see from the engagement letter, was asked to consider a number of matters. And these spread across the first and the second page. So if we could have both of those pages on the screen. You see that there was to be sample testing. Do you see that on the left-hand side:

> *Sample testing of existing credit files specific to individual district banking managers to consider –*

a number of matters. And they included:

> *The adequacy and quality of information provided –*

by those district banking managers –

> *to the credit and lending team, the extent of non-provision of any material information from the initial credit submission; the extent to which the district banking managers were monitoring credit approvals and conditions imposed by the credit and lending team; more broadly, the adequacy of the district banking managers loan monitoring, any instances of negligence –*

presumably by the district banking managers –

> *and any instance of or evidence of omissions, dishonesty, in the provision of services to Rural Bank.*

?---Yes, I can read those points. Yes.

So those were all things KPMG were asked to look into in connection with the individual banking managers. And you've read the KPMG report?---I have, yes.

And you know that on each of those fronts the KPMG report returned a number of very concerning findings?---It did return a number of findings, yes.

And do you accept that they were very concerning findings, Ms Gartmann?---They are.

Yes. Now, you've annexed the KPMG report to your statement as exhibit 8, BAB.5022.0001.0254.

THE COMMISSIONER: Are we tendering the engagement letter?

MS ORR: I will tender the engagement letter.

THE COMMISSIONER: KPMG engagement letter, 18 March 2010, BAB.5022.0001.0001, exhibit 4.125.

EXHIBIT #4.125 KPMG ENGAGEMENT LETTER DATED 18/03/2010 (BAB.5022.0001.0001)

MS ORR: Now, the KPMG report which is exhibit 9 to your statement, we see – I'm sorry, exhibit 8 to your statement, we see it's dated 27 September 2010. And we see from 0255, the second page, under the heading Approach:

> *Our engagement work was conducted through observation, inquiry and discussions with personnel.*

And we see that:

> *The engagement was undertaken in a way that included consideration of 10 credit files, including both financial and non-financial information.*

?---Yes, correct.

If we bring 0256 on to the screen next to this page, so that you have the two pages side-by-side, you will see that those files, the 10 loan files at the top of the page, had combined peak debts of $20.2 million?---Yes.

And you also see underneath that that KPMG compiled a standard of 16 behaviour checks focusing on the lending standards code of conduct consistent with the banking industry practice of code of conduct for bankers?---Yes, I can see that.

Now, the observations of KPMG are summarised on this page, and we see that in respect of those 10 credit files KPMG found major themes arising which were, firstly, misrepresentation of data in Rural Bank's system which went beyond window dressing of credit submission; reasons for excesses providing by district banking managers in the seasonal/overdraft accounts did not reflect the actual cause of excesses of customer's accounts; there were instances of livestock appraisal values appearing to have been inflated to improve the security position of the exposures; there was suppression of information pertinent to the credit; deteriorating features were not reported to Rural Bank in a timely manner; there was noncompliance with conditions precedent, including confirmation that all tax liabilities were up to date and in order with no arrears or repayment arrangements; there were failures to comply with loan conditions prior to loan drawdown; failures to follow up on loan conditions, and inadequate financial and cash flow analysis was evident. Major material financial movements should have been probed and documented?---Yes.

You see these were the findings that KPMG made?---Yes, they were.

And over the page at 0256 – I'm sorry, I've taken you to 256. I just want to draw your attention to the part on the page before, 0255, under the heading Key Findings, because we see similar issues in relation to both of those sections: a greater number of issues identified on the right-hand side incorporating the issues under the heading Key Findings on the left-hand page. Now, if we turn to 0257, we see a table prepared by KPMG, which summarised the breaches of lending standards that were identified by KPMG. You have that there, Ms Gartmann?---I do.

And we see there the three states at the top of the page where the district banking managers were from, and you will know – although it's redacted in this version – that there are five district bank managers referred to under those redactions, one from Victoria, next to that one from Queensland, another from Queensland, and two from South Australia?---Correct.

All right. Now, I want to turn to the key breaches of the lending standards that KPMG identified, firstly in relation to serviceability?---I just point out, the behaviour checks – I've tried and undertaken a number of inquiries to understand where those 16 came from, so what particular lending standard and code, and we've been unable to identify which document they actually pertain to.

Okay. So you're referring to the 16 behaviour checks compiled by KPMG?---Correct.

Which KPMG tells us focused on the lending standards code of conduct?---Correct.

Thank you. Now, if we come back to this table and focus, firstly, on lending standards/breaches in relation to serviceability, we see from this table that all five of the district banking managers have suppressed information pertinent to the credit, which I understand to mean that they had not provided relevant information to the credit and lending branch of Rural Bank?---That is correct.

That's a concerning finding, Ms Gartmann?---It was a very concerning finding.

And all five had misrepresented data into the Rural Bank systems, including data in relation to appraisals and cash flow forecasts?---That's correct.

Another concerning finding?---Yes.

And two had failed to verify information provided by the customer?---Yes.

Also a serious matter?---Yes.

All right. Now, in an appendix to this KPMG report, KPMG provided some information about its analysis of the particular 10 files that it had conducted. Are you familiar with that appendix?---I am, yes.

All right. Could I ask you to turn, firstly, to 0259. I want to ask you some questions about these file reviews conducted by KPMG in which serviceability issues were identified. So this file that we see at 0259 involved an agribusiness client from Queensland?---Yes.

And this client had been a customer of Rural Bank since December 2003?---Yes.

And the client had started with a loan of 145,500. Do you see that at the top, exposure at origination?---Yes.

And ended up with a peak debt of 2.155 million?---Yes.

This client had submitted an application in November 2007 to purchase an additional property?---Yes.

And the application for finance was for 2.7 million?---Yes.

And we see at this page, and the following page – it's probably a little difficult to have the two pages on the screen at once, but you have both pages there, Ms Gartmann, I see?---Yes.

That the application was initially denied by Rural Bank on the basis that the request was for a speculative purpose, that there was no intended equity contribution from the borrowers, and there was significant questions about whether the borrowers would be able to service the debt?---Yes, I believe that's written here.

Thank you. This was the findings of KPMG about this file?---Yes.

Yes. All right. And then after that application was denied the application was resubmitted, and we see at 260 that that happened following support from two Elders senior managers?---Yes, I can see that.

And when the application was resubmitted, the amount of finance sought had been reduced by $1 million?---Yes.

And that was because that $1 million was to be provided by the borrower's aunt?---Yes.

And the loan application was then approved by head office, with the approving officer noting that the previous decline comments remained pertinent but that there had been strong support from the two Elders senior managers and the loan had been approved as a special matter in light of the above?---Yes.

The district banking manager had, in fact, been made aware before the application was resubmitted that the source of the $1 million contribution was a margin loan, hadn't he?---I can see that it was a – it was not disclosed at the time of the transaction being approved.

Yes. And can you see that the district banking manager was aware of that?---I can see that, yes.

Thank you. And that the district banking manager didn't disclose that at the time the transaction was approved?---Yes.

And we see at 0261, in KPMGs observations about this file, that KPMG found that the district banking manager had failed to disclose that the $1 million sourced from the customer's aunt was from a margin loan provided by Macquarie, and that the loan from the aunt, which was presented as a capital contribution, actually gave rise to liabilities in excess of 1 million by virtue of the margin calls?---Yes, I can see that.

And KPMG also found that the district banking manager had misrepresented the bank's position to the borrower by advising the borrower that Rural Bank required him to source $1 million from another source as a condition of approval? You see that in the second paragraph there?---I can see that's written there, yes.

And I know you keep saying these things were written there, Ms Gartmann. I just want to understand: you accept that these were the findings of KPMG who Rural Bank engaged to examine these files?---Yes, correct.

Thank you. Now, as KPMG put it, the fact that Rural Bank had declined the earlier application for finance and had not approved a lesser amount which would not in turn – I'm sorry, which would in turn require the borrower to fund the shortfall, that was the fact – sorry, I put that question very awkwardly. I want to ask you if you accept that the fact was that Rural Bank had declined the earlier application and had not approved a lesser amount which would in turn require the borrower to fund the shortfall?---Sorry, I'm – I - - -

Do you see the final sentence in the second paragraph there:

> *The fact was that RBL had declined the deal and had not approved a lesser amount which would, in turn, require the borrower to fund the shortfall.*

?---Yes. Thank you, I can see that sentence now.

And the district manager – the district banking manager responsible for this file had manipulated and suppressed information from the bank that was relevant to the assessment of serviceability?---Yes.

So he had misrepresented the bank's position to the customer?---Yes.

And in doing that he had acted dishonestly, both towards the bank and towards the customer involved?---Having not looked at this particular one in a great deal of detail, I am accepting what KPMG have written, yes.

And you accept that the findings of KPMG showed that the district banking manager acted dishonestly both towards the bank and towards the customer?---Yes.

So even assuming the bank had, at this time, robust serviceability policies, this led to a loan being originated in circumstances where Rural Bank lacked material information about whether the debt could be repaid?---That's correct.

All right. Now, the Code of Banking Practice, as it existed at this time – which we know Rural Bank was not a subscriber to – but the Code of Banking Practice required subscribing banks to exercise the care and skill of a diligent and prudent banker in selecting and applying credit assessment methods, and in forming an opinion about the customer's ability to repay it. Are you familiar with that clause?---I am familiar with that clause, yes.

Now, had Rural Bank been a subscriber to the Code of Banking Practice, do you accept that the conduct of this district banking manager would have breached that obligation?---Had we been a signatory, then yes.

And what action did Rural Bank take in response to this district banking manager's conduct?---He is no – he was no longer with the business.

Following the receipt of these findings from KPMG, did Rural Bank communicate to the client that their loan was affected by these breaches of the lending standards?---I'm unaware of that. I believe that these customers did have engagement with our asset management team to work through their situation.

They had engagement with who, did you say - - -?---Asset management team.

Your asset management team. But were they told that their loan was affected by these breaches of the lending standards?---I'm unable to answer that, but happy to respond later. I haven't – have not inquired of that.

Well, I understood you to be dealing with this in paragraphs 93 to 95 of your statement, which are BAB.9000.0002.0019 and 0020. The question that you were asked to address in that part of your statement was whether the bank communicated with any customers in connection with or as a result of the failings, identify when the bank did so, and what was communicated. And you were also asked – sorry – you were also asked to identify whether the bank undertook any remediation program in connection with or as a result of the failing?---So those questions were asked - - -

MR BATT: I'm sorry to interrupt. I did want to rise because, as I would understand the question, there is an unstated or assumed premise that the loan file the subject of these questions is – is within the 62 Queensland loans which are the subject of Ms Gartmann's statement. The loan file that Senior Counsel Assisting is dealing with is established in the papers to be from Queensland, but it has not been exposed that it is one of the files dealt with in Ms Gartmann's statement.

THE WITNESS: That's correct. It's not one of the 62 loans that became non-performing.

MS ORR: I had understood Ms Gartmann, from your evidence earlier, that you said these issues were detected in 2009 and 2010 as a result of investigations, and that you had referred to a series of reports - - -?---Yes.

- - - as part of that investigation and the KPMG report was the first of those?---It was, for identifying portfolio issues in Queensland, and then investigations into loans for Queensland cattle investigations became non-performing over the last 10 years, but that did not include this particular customer. So this particular customer, we obviously continued to work with, and that loan did not become non-performing.

So this file is not one of the 62 files that you've referred to in your statement?---No, it's not.

And therefore you are unable to tell the Commission whether you communicated with this client about whether their loan was affected by breaches of the lending standards?---Well, we would not have communicated in relation to breaches of the lending standards, because we were not a signatory to it at the time.

But the lending standards didn't rely entirely for their existence on the Code of Banking Practice, did they? Do you say Rural Bank was exempt from lending standards because it was not a subscriber to the code?---Lending – I am unclear as to what lending standards you are referring to?

I am referring to the lending standards identified by KPMG in the annexure to your statement that is exhibit 8. So if we go back to that and we go to BAB.5022.0001.0256. We see that the standard of 16 behaviour checks was compiled - - -?---Yes.

- - - focusing on the lending standards code of conduct, consistent with the banking industry practice of code of conduct for bankers?---And I have been unable to find what those documents were.

Yes?---Or to draw - - -

I understand that?--- - - - upon what industry code, because I don't even know if they're Australian.

Well, can I ask you this: accepting that you don't know where they came from, do you accept that the 16 behaviour checks are appropriate checks for the behaviour of staff of Rural Bank?---Yes, I do.

All right. And you accept then that they were breached by this district banking manager in relation to this customer?---The fact that this particular customer did not become non-performing indicates to me that the work that we did with this customer subsequent to identification of the KPMG findings meant that this customer had no negative impact.

Yes?---Or no non-performing.

I understand that?---And actually, the misrepresentation was between our agent and Rural Bank, I accept that that is inappropriate.

I understand that too, but I would be grateful if you could address my question, which is whether you accept that the conducts of this district banking manager breached those lending standards? Let's not worry about - - -?---According to the 16 behaviour checks, yes.

It did. And you accept that they're appropriate behaviour checks?---Yes.

And that they were breached?---They were.

And so then I come back to my question about whether the customer was informed about the breach of those lending standards?---And I cannot answer that question at this point in time.

All right. Now, I asked you to assume, when answering an earlier question about this customer's file, that Rural Bank had robust serviceability policies in place - - -?---Yes.

- - - at the time?---Yes.

And that this occurred despite robust serviceability policies. Did Rural Bank in fact have robust serviceability policies at this time?---I've had a look at the credit policy from 2005 onwards, and I do believe that it had robust policies in place.

Well, by the time Rural Bank had commissioned this KPMG report it already knew that there might be systemic issues with its serviceability policies and practices, didn't it?---I disagree with that statement.

All right. Well, do you accept in 2006 APRA had made a recommendation that should put have put Rural Bank on notice of serviceability issues?---There was an APRA prudential review in 2006 that highlighted credit risk assessments.

And do you accept that that 2006 review should have put Rural Bank on notice of serviceability issues within Rural Bank?---It did highlight some areas to strengthen in terms of serviceability, yes.

All right. And APRA made further recommendations in 2009 that, again, should have put Rural Bank on notice of issues with its approach to assessing serviceability?---It did highlight those in 2009, and our response to that APRA prudential review also highlighted the work that we had done, and the appropriateness of our systems and policies.

But APRA highlighted for you that there were problems with your approach to serviceability?---Yes, they did, and I imagine in 2009 they made that recommendation to a number of financial institutions.

Well, that might be the case, but I'm only concerned for now with yours, Ms Gartmann. Could I show you BAB.5034.0001.0026. This is a letter from APRA to Rural Bank in July 2009?---Yes.

And do we see there at 0027 that at this point – just wait until it comes up on the screen for you, under the heading Policy Exceptions Observation:

> *APRA identified that a high proportion of loan proposals were approved, notwithstanding the failure of one or more policy tests.*

?---This is where APRA looked at the initial hurdles, and not the ability to take into account the unique circumstances of each individual farm business through the exercising of delegations.

But you accept that they were telling Rural Bank at this time that a high proportion of your loan proposals were being approved notwithstanding the failure of your own policy tests?---Correct.

And we see that APRA required Rural Bank, lower down on this page, amongst other things:

> *…to review the extent of deviation from key credit policy standards such as LVR, minimum equity and interest cover.*

?---That's correct, yes, and we did do that in the follow-up response to APRA.

And APRA also required that Rural Bank review its:

> *…system in respect of Delegated Lending Authorities, and incorporate the extent to which various delegated lending authority levels or positions can override or deviate from minimum key credit policy standards.*

?---That's correct.

And at 0028, we see that APRA also raised some serious concerns about the appropriateness of Rural Bank's credit risk grading system?---Yes, I can see that on the screen, and I accept that APRA made that recommendation.

Yes. Thank you. I tender that letter, Commissioner.

THE COMMISSIONER: Letter APRA to Elders Rural Bank, 1 July - - -

THE WITNESS: That – that letter came to us, or that prudential review, was undertaken pre - - -

MS ORR: If you wouldn't mind waiting a moment I think the Commissioner is marking that exhibit.

THE COMMISSIONER: Letter APRA to Elders Rural Bank, 1 July 2009 BAB.5034.0001.0026, exhibit 4.126.

EXHIBIT #4.126 LETTER APRA TO ELDERS RURAL BANK DATED 01/07/2009 (BAB.5034.0001.0026)

MS ORR: Yes, Ms Gartmann?---So at this time Rural Bank – or, sorry, Bendigo Bank had only just acquired majority share in the joint venture with Elders, and so there was a period of time from May 2009 through to the end of 2010 where there were a number of actions that had a stronger banking focus.

Yes. And, having received that letter in July 2009, we see that by February 2010 Rural Bank had marked its response to APRAs requirements and recommendations as complete, with some additional comments being provided in some areas?---That's correct.

But, as later became apparent, APRA didn't consider that Rural Bank had effectively actioned all of its recommendations. Do you accept that?---I believe – is that in the 2011 prudential review?

Yes?---Yes.

So from the recommendations that were being made by APRA, Rural Bank should have been on notice from at least 2009, if not 2006, of potential systemic issues with its loan serviceability policies and practices?---I would disagree with the comment of "systemic". I certainly believe that there were areas to strengthen and improve.

Why do you not see that as systemic, Ms Gartmann? These were about the processes that were being used within Rural Bank and the adequacy or inadequacy of those processes. That's a systemic issue, isn't it?---Well, the portfolio performance wouldn't suggest that it was a systemic issue.

Well, I'm not concerned with the performance of the portfolio at that stage. You might say that that justified some of the inadequacies that were pointed out by APRA, but APRA was concerned that the processes that you had in place were not adequate to assess the serviceability of customers' loans?---They were, yes.

So these are issues that were clear well before the engagement of KPMG to provide that report in March 2010?---That's correct.

Now, can I turn to some questions about the second set of problems or issues that you've referred to in connection with the 62 loans, which related to security and valuations. And you acknowledge in your statement that issues were identified with over-reliance on security values, failures to make appropriate inquiries, and verification of valuations and appraisals?---Yes.

Now, if we go back to the KPMG report at your exhibit 8, and return to the table at BAB.5022.0001.0254 – I'm sorry, the table is at 0257. If we consider, again, these breaches of lending standards identified by KPMG, we see that at least one of the issues identified by KPMG in this table expressly related to security and valuations. Three of these district banking managers were found to have engaged in instances of inflating the values of livestock in the appraisal form; do you see that?---I do see that.

And a number of other breaches that were framed in a broader way may also have been related to security and valuations, such as a failure to ensure that loan conditions were met prior to drawdown, and noncompliance with loan conditions?---Yes, I see those.

Now, at least one of the sample credit file reviews undertaken in the KPMG report provides an example of the sorts of security and valuation issues that were arising. Can I ask you to return again to the appendix to the KPMG report, and this time to turn to 0280. Now, this file related to a farmer from Victoria, so we know it is not one of the 62 that you've dealt with in your statement. And this farmer had a livestock mortgage with Rural Bank?---Yes.

Now, perhaps if you could explain what a livestock mortgage is. You did say earlier that at Rural Bank you lend against - - -?---We do against stock.

- - - assets other than property?---Property, yes. So the value of the stock, we will lend up to 50 per cent against the value of the stock.

Thank you. Now, this farmer had been an Elders client since 1994?---Yes.

And his principal banking was with another bank where he had an $11 million exposure?---Yes.

And from 2005 to 2008 Rural Bank had advanced various funds to the customer, and he struggled to operate within his approved limits. Do you see that at 0280:

> *Various funds approval to purchase fertiliser, provide working capital, and regularise account.*

?---Yes, correct.

Continuing:

Struggled to operate within previously approved limits.

?---Correct. That was also during the millennium drought in Victoria.

Yes. And in February 2009 the farmer applied to increase an existing facility by $100,000 to $800,000?---Yes.

And again we see that application was declined due to a lack of current financial statements?---Yes.

And we see also that the account had been out of order 177 days since the last review?---Yes.

And for 16 days it had been $110,000 over its limit?---Yes.

So we see on the following page, 0281, that that's described as evidence of hardcore debt in the overdraft?---Yes.

Now, just prior to the application being made, the district banking manager had appraised the livestock value for the customer at 1.735 million?---Yes.

And that figure had been confirmed by RSM. Is that a regional sales manager?---I couldn't tell you back in those days, I'm sorry.

Okay. So despite the fact that the loan facility had not been increased to 800,000 in February 2009, in June 2009 a revised temporary limit of $850,000 was approved?---Yes.

And the $1.735 million valuation was used to approve that increase?---Yes.

And Rural Bank formed the view that the facility could be increased due to pending sale of the customer's cattle?---Yes.

And the district banking manager made comments at the time that the sale of the cattle in October 2009 would clear the entirety of the customer's debt to Rural Bank?---Yes.

And then on 22 July 2009 the RSM conducted a further livestock appraisal?---Yes.

And at that time the livestock, that had been valued at 1.735 million in February 2009, were revalued at $728,500?---Yes.

So the upshot of that was that Rural Bank had loaned this customer more than the value of his security?---That's correct. And that date does coincide with the information I provided earlier around cattle prices. It wasn't just north Queensland.

So what we see from this is that – I want to put to you that the district banking manager responsible for the initial valuation shouldn't have increased the customer's facility in June 2009 in circumstances where that customer had been experiencing significant financial difficulty in February 2009, and where there were reasons to doubt the correctness of the valuation upon which the increase was based?---Potentially so. I'm unable to comment on this one, not understanding whether or not that increase was in order to continue to feed the livestock. I don't know what the conditions were in that region at the time in 2009. It was Millennium Drought and the last thing we want to do, particularly with livestock, is not advance funds in order to feed livestock. So that is one of the challenges in lending in agriculture.

But this was a borrower who, we see from these documents, was highly leveraged. He had $11 million in exposures with another bank?---Correct, yes.

And we see the differences in the valuations, and I want to understand whether, in your view, this district banking manager exercised the care and skill of a diligent banker when he increased the facility in 2009?---Well, not understanding why he may have increased the facility, if it was truly to support the operational costs for his livestock, I'm unable to say.

Well, we see that the request to increase the facility from 750 to 850 is described as "a request to cover excesses". Do you see that in the second last paragraph?---I do, yes.

So does that clarify that for you?---It certainly helps.

So I want to ask again whether you think this district banking manager exercised the care and skill of a diligent and prudent banker when he increased the facility on that basis in June 2009?---I believe his judgment wasn't appropriate.

And again, after receiving this report, did Rural Bank take some action in response to this district banking manager's conduct?---Yes. I know with this particular banker he was coached and oversighted, and his current portfolio is exceptional in terms of he only has, I think, in the last couple of years, there has only been two out of orders for his portfolio.

So he remains with Rural Bank?---He does.

And following receipt of these findings from KPMG about this file, did Rural Bank communicate to this client that their loan was affected by breach of the lending standards?---I'm sorry. Again, because it wasn't one of the Queensland ones, this is not one I have investigated and am unable to answer at this time.

But this was an exhibit to your statement, the KPMG report?---It was, and – yes.

But you don't know - - -?---No.

- - - whether there was a communication. All right. Can I turn to the third set of problems that you've identified as affecting those 62 loans, and if we stay within the KPMG report and go back to the table summarising the breaches of lending standards at 0254 within this document. I'm sorry, I did that before. 0257 within this document. We again see that many of the breaches of lending standards that were identified by KPMG related to loan management?---Yes.

All five of the district banking managers failed to report deteriorating features to Rural Bank in a timely manner?---Yes.

And all five failed to identify major signals of distress?---Yes.

And three of the five failed to follow up reporting conditions in a timely manner?---Yes.

Three of the five failed to advise of breaches of loan conditions?---Yes.

And two of the five - - -?---Sorry, I think that's actually only two.

I think we're looking at the row immediately above code of conduct breaches – personal conduct and honesty?---Sorry, yes, I was looking further down.

So you agree that that was three?---Yes. To convey loan conditions to customers.

To customers?---There's one - - -

I'm sorry?---There's one there.

I understand what the confusion is. That column relates to two individuals. Do you recall that, Ms Gartmann?---Yes, but that column is vacant in my copy.

For breach of loan conditions in the third last row on the page?---I'm looking at failure to convey loan conditions to customer and there is one cross there.

Sorry. If you could go down into the bottom part of the page now and the third last row?---Yes.

"Failure to advise Rural Bank of any breach of loan conditions"?---Yes.

There were three district banking managers for that failure?---Yes.

And two of them failed to follow up excesses and arrears as requested by the bank?---Yes.

Now again, can I just take you to one of the files that was reviewed by KPMG. If we turn to 0262. Now, this file related to a client that appears to have been a corporation that became a client of Rural Bank in late 2004?---Yes.

And at this time Rural Bank advanced about 2.61 million to assist this client with the purchase of a farming property?---Yes.

And over the next five years their debt increased to 2.91 million?---Yes.

And in June 2009 the lending manager requested monthly updates on financial performance, given a deterioration in the customer's position?---Yes.

And those updates were not provided?---Yes.

And if we turn to 264, we see that according to the observations of KPMG, this is part of the observations box for this file:

> *In about November 2009 the district banking manager had been made aware of the possibility that the customer may go into liquidation or administration.*

?---Yes.

And a Rural Bank review was due at that time, but it didn't happen?---Yes.

And if we go back to 0262, we see that in January 2010 the customer requested an increase in their overdraft from 200,000 to 360,000?---Yes.

And that would have taken the total exposure to 3.07 million?---Yes.

And at this time the customer's facility had expired?---Yes.

And at this time no Rural Bank review had been undertaken, despite a review being due in November 2009?---Yes.

So at the time the district banking manager lodged the submission in January 2010, he was aware of the risk of the customer's impending liquidation?---Yes.

And we see from 0263 that, despite this, he didn't draw the bank's attention to this, and nor did he accelerate the customer's review?---Yes.

And the credit and lending section of the bank subsequently wrote to the customer advising that the customer was in default and conveying the necessary action required by the borrowers?---Yes.

And on the same day, the request for an increase in the overdraft was declined?---Yes.

Then about five days later the district banking manager sent credit and lending a file note saying, among other things, that he had made the customer aware that, although he didn't agree with the credit team decision to refuse additional funding, he must now support them and pass on the conditions?---Yes.

And shortly after that the customer entered voluntary administration?---Yes.

And about two months later, Rural Bank's facilities were repaid via a property sale?---Yes.

And KPMGs observations included that it was unclear why the district banking manager would have supported the customer's submission for additional finance in January 2010, in circumstances where he knew the precarious financial position of the borrower?---Yes.

And it was also unclear why he would have advised the client that he did not agree with the bank's decision?---Sorry, could you repeat that?

KPMG said it was also unclear why the manager, the banking manager, would have advised the client that he did not agree with the bank's decision?---Yes.

And the district banking manager's monitoring of the account was, in the words of KPMG, "Extremely tardy"?---Yes.

And he didn't undertake his review of the account at the required time despite the fact that he had been aware that the customer might go into liquidation or administration?---Yes, they were the KPMG observations.

And KPMG also said that deteriorating features of the account were not reported to the bank in a timely manner?---Yes.

And generally there was limited communication from this banking manager to credit and lending regarding customer issues, despite requests for updates?---Yes, that has been observed by KPMG.

So again, based on these findings, do you accept that this district banking manager didn't act fairly and reasonably towards the customer in his failure to properly monitor their loan conditions?---I – well, with the benefit of – well, without the benefit also understanding how close the relationship was between this banker and the customer, and how aware he was of the – of the business's performance and conditions, I certainly recognise and acknowledge that there was poor timeliness in terms of reporting to Rural Bank of the performance and behaviour with his customer.

Was it fair to the customer to support an extension of funding in circumstances where the customer was in such a precarious financial situation?---Again, because I'm unclear as to what that financial increase would cover, I'm – I couldn't make an informed comment on that.

Irrespective of what it was going to cover, given the financially precarious position of this client, do you think it was fair to extend in that way?---Like I said, without knowing what they were attempting to do to trade out and address the production challenges, and how they were planning to utilise those additional funds, I cannot make an informed – but I would just purely be speculating, I'm sorry.

Well, what action did Rural Bank take in relation to this district banking manager?---They are no longer in the employment of Rural Bank.

And since when are they no longer in the employment?---I couldn't tell you. With this particular banker – I know, of the two in South Australia, one of them is no longer with the organisation, and the other one works within the Elders branch network, but not in agribusiness finance.

Now, do you say this is one of the South Australian district banking managers?---I believe so. Isn't this the South Australian – no, this might - - -

Perhaps if I can ask you to look at 0258, because you have the information that's obscured by the redactions?---Yes.

Can I ask you to consider whether this district banking manager was from Queensland?---You are correct with Queensland, and they left in 2009.

And I should ask you again, now that you've identified which banking manager this file related to, what action Rural Bank took in response to these findings from KPMG?---I'm sorry, because it wasn't one of the 62 that I looked at in depth, I couldn't say.

You don't know what action was taken?---No, I don't.

And do you know if the customers were told of the breach of the lending standards found by KPMG?---I am not aware of what customer communications took place.

Now, did the 62 loans to the Queensland cattle farmers that you've identified in your statement include any of the loans that were the subject of the KPMG report?---One.

Which one was that? Perhaps if you could identify - - -?---0265.

0265?---Correct.

I see. So the customer dealt with on pages 0265 through to – I'm sorry, yes - - -?---It's only that one page.

- - - I don't think there is another page. So a single page, 0265, is one of the non-performing 62 loans that you speak of in your statement?---Yes, correct.

Now, in your statement you acknowledge that about half of those 62 loans involved one of the three issues that you've identified. So either issues with security or valuations, issues with serviceability or issues with loan management?---Yes.

Is that right?---That's correct.

And two of those issues were present in 16 per cent of the loans?---Yes.

And that all three of those issues were present in eight per cent of the loans?---Yes.

Thank you. Now, the sorts of issues that were detected by KPMG in the review of these 10 loan files weren't restricted to these 10 loan files, were they?---I couldn't say if they were more broad. These were some individuals in isolated instances, and subsequent reports investigated things more broadly.

Well, subsequent investigations revealed that there were systemic issues with Rural Bank's loan management practices, particularly in the Queensland portfolio?---That was the view of a particular author.

Which particular author was that, Ms Gartmann?---That was for the credit framework report of May 2011.

That's Mr Corolis' report?---That's correct.

Are we going to hear, Ms Gartmann, that as well as disagreeing with the description of these events given by Mr Hirst in his explanation to the Commission, you take issue with the findings of Mr Corolis in his internal review conducted in 2011?---Well, I can put some context to Mr Corolis' review - - -

Yes?--- - - - in that Bendigo Bank had acquired 100 per cent of Rural Bank, in that was finalised in December 2010, and we had a distribution agreement with Elders Rural Services - - -

Yes?--- - - - to provide district banking managers and frontline staff support. And there was – there were some cultural challenges between Rural Bank and Elders at the time - - -

Yes?--- - - - and this report was certainly written to stimulate some action and some focus by Mr Corolis.

It was written to stimulate some action?---And focus.

And focus did you say?---Correct.

Are you saying the findings of Mr Corolis are not accurate?---I think they were overstated.

And what enables you to say that Mr Corolis' findings in 2011, which extend beyond the 62 loans that you've looked at for your statement, are overstated?---Because a number of years down the track now, in 2018, reviewing the issues that he highlighted and looking at some of the work that we did subsequent around enhanced training and development, some strengthening process and policy, I don't believe that all that he called out was as dire as it was – or as the report would paint.

But he was there at the time, Ms Gartmann?---He was.

And you were not?---Correct.

And he reviewed the material at the time and made a series of findings?---He did.

Which shaped a lot of work done by the bank thereafter?---Correct.

And Mr Corolis was promoted to Bendigo Bank shortly after that piece of work?---I'm not sure how shortly, but he has been employed across the group, yes.

I want to come to the findings that he made, but before I do that I have been asking you questions about loan management issues, the third of the categories that you identified as affecting these loans. That APRA letter from July 2009 that I took you to earlier also contained – that concern, expression of concern by APRA about loan management; did it not?---It did.

We see that, from 2009, APRA was raising concerns about whether early warning signs of credit deterioration were being adequately realised through Rural Bank's credit processes?---Yes.

And APRA said that it had obtained a sense from its reviews that Rural Bank's willingness to increase a borrower's debt:

> *…may at times be as a result of the bank's reluctance to more prudently enforce its credit program.*

Do you recall that finding or that statement by APRA?---Yes.

Thank you. And we see from the board credit committee meeting minutes that you've annexed to your statement that, between February 2009 and January 2010, Rural Bank had downgraded 194 clients by three or more grades on its nine grade credit risk rating system?---Correct, yes.

Now, six months before the KPMG report was delivered in March 2010, the board credit committee had expressed concerns that there had been no improvement in dealing with accounts in arrears and account management in the early stages of delinquency remained a major issue; do you recall that?---Yes, I do.

And one manifestation of that, as noted in the board credit committee minutes, was that credit and lending personnel in Queensland were undertaking what's described in the document as "increased AMU tasks". Does AMU in that context mean asset management unit?---I believe it does.

So by that time there were clear indicators there were a significant number of loans in need of active account management, particularly in Queensland?---Correct. Largely resulting from a number of the conditions that we've discussed earlier.

And do you accept that those minutes record that, despite this, Rural Bank was continuing to give priority – at least in Queensland – to new business and additional lending to existing clients over no increase annual reviews?---In terms of the priority of time allocated? Is that what you're asking?

Well, perhaps if I show you that entry from the minutes, and you can comment on it, Ms Gartmann. It's your exhibit 7, BAB.5022.0004.0001. So you see these are minutes of a board credit committee meeting on 16 March 2010?---Yes.

And if we turn to 0002 within that document – sorry, I'm just finding the document in my materials, Ms Gartmann. At 0002 we see the reference there – I'm sorry, I'm just trying to find the right part to direct you to, Ms Gartmann. 5022.0004.0002. You have it. My junior has it. I can't find it in my materials, so I am going to use Ms Zeleznikow's. Thank you. Now - - -

THE COMMISSIONER: Under Queensland bullet point 2.

MS ORR: Thank you. Thank you, Commissioner. Do you see there I had already taken you to:

> *Credit and lending personnel are undertaking increased AMU tasks.*

?---Yes.

Continuing:

> *Priority is being given to new business and additional lending to existing clients over no increase annual reviews.*

?---Yes, I can see that, and it's certainly - - -

How do you interpret that?---Well, I interpret it that where there is an annual review required, where it's maintenance, as opposed to working with existing customers that require additional lending to support their operations, and that could – again, I can't tell you whether or not it was for additional term lending or additional lending to support cattle operations or otherwise, then yes, their priority would have been to support people that were requiring assistance to work through.

I'm sorry, I'm struggling to understand how you read that into the words:

> *Priority is being given to new business and additional lending to existing clients over no increase annual reviews.*

?---I’m not disputing that. I’m putting some context as to supporting customers that may be requiring – I’m looking at the additional lending component.

What about new business? Why would priority, given everything that we’ve discussed about what was going on in this period for Queensland cattle farmers in particular, why would priority be given to new business?---Because we have equal weighting across compliance and annual reviews, customer retention, and also new acquisitions.

Because the KPIs required people - - -?---Yes.

- - - to sell more loans?---As part of their KPI - - -

Yes?--- - - - as well as – because if new business is important for any corporate operation.

But why would you give priority over these problems that we’ve been discussing, so we – we can see that you’ve got increased personnel undertaking AMU tasks, asset management tasks. Was that an appropriate time to prioritise generating new business?---It was not an appropriate time.

And we see that Mr Ormsby, who is referred to in the final dot point there, who is one of Rural Bank’s directors, noted in relation to Queensland that:

> *Unfavourable cycles have emerged over the years and whilst the issues need to be dealt with, the bank must also continue to focus on opportunities presented by these cycles.*

What opportunities do unfavourable cycles present, Ms Gartmann?---I’m sorry, not being at the meeting, I’m not – I could not say what Mr Ormsby meant, apart from - - -

Reading that, what do you interpret him to be referring to there?---I couldn’t – I couldn’t say.

Well, what do you say are the opportunities that emerge from unfavourable cycles for the bank?---Only to work through with customers.

Do you think that’s what Mr Ormsby is referring to there?---I could speculate what he is inferring, but I won’t.

And why is that?---I don’t think it is appropriate for me to pretend I am Mr Ormsby, I’m sorry.

No, I am asking you about your interpretation of that sentence there?---So I would imagine that he’s talking about working through with customers through an unfavourable cycle.

I see. All right. So even after the KPMG report was delivered in September 2010, it took Rural Bank some time to recognise that it had systemic loan management issues, didn't it?---It took some time to identify that we needed to improve our oversight and, therefore, application - - -

And that you had - - -?--- - - - of our loan management.

- - - systemic loan management issues?---I don't believe that we had systemic loan management issues.

And is that because you disagree with Mr Corolis and the findings of his report in 2011?---I do disagree with a number of – the severity with which he painted the picture.

Rural Bank at this time appears, from a number of the documents that have been provided to the Commission, to have put the marked increase in its level of impaired assets down to the adverse seasonal conditions. Do you agree with that?---They were exceptional contributing factors, yes.

And there was further engagement with APRA in 2011. Do you recall those documents?---I have seen them.

Could I show you BAB.5024.0001.1708. You see this is a letter from APRA to Rural Bank on 7 January 2011?---Yes.

And at 1709 we see APRA commenting on the increase in Rural Bank's impaired assets?---Yes.

And APRA observed that there had been a marked increase in the bank's level of impaired assets over a quite short period of time?---Yes.

And APRA noted that there were several drivers behind specific cases of impairment and downgrades of credit risk ratings, but the key driver appeared to be adverse seasonal conditions?---Yes.

And APRA required Rural Bank to provide various reports about its impaired assets?---Yes.

And we see from 1710 that APRA was provided with the KPMG report?---Yes.

And APRA noted that the KPMG report contained some concerning issues for the bank and requested copies of any response received from Elders in response to those matters?---Yes.

I tender that letter, Commissioner.

THE COMMISSIONER: Letter APRA to Rural Bank Limited, dated – Ms Orr?

MS ORR: Dated 7 January 2011.

THE COMMISSIONER: 7 January ’11, BAB.5024.0001.1708, exhibit 4.127.

EXHIBIT #4.127 LETTER APRA TO RURAL BANK LIMITED DATED 07/01/2011 (BAB.5024.0001.1708)

THE COMMISSIONER: Is that a point at which - - -

MS ORR: Just before we break, if you wouldn’t mind, Commissioner.

THE COMMISSIONER: No, of course not.

MS ORR: Following receipt of that report in February 2011, Rural Bank started querying whether it might have systemic issues in respect of loan management. Do you agree with that?---Through the Taso Corolis report, yes.

Mr Corolis’ report. So by this time a further 156 customers had been downgraded by three or more credit grades in the previous year?---Yes.

And there was then a meeting of the board credit committee on 2 February 2011 that was the genesis of Mr Corolis’ work?---Yes.

I will come to that meeting after the break, if the Commission pleases.

THE COMMISSIONER: Yes. 2 pm.

ADJOURNED **[1.01 pm]**

RESUMED **[2.00 pm]**

THE COMMISSIONER: Yes, Ms Orr.

MS ORR: Ms Gartmann, before the break I had asked you some questions about February 2011, when Rural Bank was starting to query whether it had systemic issues in relation to loan management. Could I ask you to look at exhibit 7 to your statement, BAB.5022.0004.0005. These are minutes of a board credit committee meeting on 2 February 2011. And do we see there, at the bottom of the page – do you have that there, Ms Gartmann?---I have on the screen, yes.

At the bottom of the page, we see some things that were highlighted by the GM for risk. We see higher up the page that the GM for risk – the general manager for risk was Mr Corolis?---Yes.

And Mr Corolis highlighted to this meeting of the board credit committee, on 2 February 2011, that there was:

> *A continuing trend of downgrades in the Queensland portfolio, within recent downgrades concentrated in one portfolio. The bank remains outside its target range for the CRR distribution of the portfolio, and in the absence of new growth, this is unlikely to be addressed in the short term, particularly given the prevailing conditions in the Queensland property market.*

And:

> *The majority of asset management unit resources are being devoted to the Queensland portfolio and further resource allocations are underway.*

?---Yes.

That was highlighted by the general manager of risk to the board credit committee on this date?---Yes.

And we then see over the page that, as a result of those matters being highlighted, the committee discussed in some detail, at the top of the page, the key points highlighted in the executive summary and the current state of the portfolio, which is outside the board credit committee's target credit quality parameters?---Yes.

The chairman then had some things to say about that:

> *The chairman expressed his disappointment with the findings in the APRA review report which I had taken you to earlier. The chairman queried whether the issues were isolated to a small number of loans, or whether the issues were more systemic, and also queried whether the general manager of risk has sufficient resources to allocate to resolving these issues. The chairman also noted that a proportionately large percentage of larger loans have proven to be problematic. These items were discussed by the committee, and the chairman requested that the general manager for risk provide the committee, at its next meeting, with the following: a paper outlining the key issues and what processes are being adopted to identify, rectify and address deteriorating, distressed and impaired assets, including resource requirements.*

And do you see that that paper was also to address:

> *Whether there are any systemic issues that need to be addressed and recommendations in this regard.*

?---Yes.

So that was what the chairman sought at this meeting on 2 February 2011?---Yes.

And the systemic nature of the loan monitoring problem became fully apparent to Rural Bank throughout 2011?---I still disagree that it was a systemic problem. I think before the break you mentioned 159 accounts had been downgraded.

156 in the year prior to this?---56. Out of 8000 customers, I don't believe that that's a systemic issue.

Well, that's about the number – that's about the volume of files downgraded. That's a slightly different matter, isn't it, to whether these are systemic or isolated issues that are resulting in the bank remaining outside its target range for the CRR distribution of the portfolio?---Well, when we're taking into account the Millennium Drought that broke in early 2011, and what had happened in Queensland cattle, conditions in Australian agriculture were challenged and, yes, our credit quality had deteriorated. However, they were in particular regions that were impacted by multiple events.

Okay. How many clients did you say that Rural Bank had at this time, Ms Gartmann?---In – what year was this?

2011?---2011, I think we had about 5000 customers.

Thank you. Now, this is the meeting – this is the discussion at the meeting on 2 February 2011. There's a further discussion of these matters at a meeting on 18 May 2011?---Yes.

Have you seen the minutes from that meeting, Ms Gartmann?---I have.

And that's your – it's part of your exhibit 11, BAB.5025.0001.0161. And if we turn to 0166 within that document we see that Mr Wilkinson, the head of asset management:

> *Advised that the majority of credit downgrades related to accounts which had not been reviewed for up to two years, and now reflected a deteriorated position that had not been brought to the bank's attention.*

Do you see that?---Correct. Yes, I can see that.

So was it acceptable for accounts to have not been reviewed for up to two years?---Excluding the term loans that only require – are only required to be reviewed every three years then, no, it's not.

So the loans should have been reviewed more regularly?---An annual review is required.

Thank you. And we see that Mr Wilkinson said that:

> *The credit downgrades related to accounts which had not been reviewed for up to two years and now reflected a deteriorated position that had not been brought to the bank's attention.*

So who should have brought that deteriorated position to the bank's attention?---The district banking managers.

And they were not doing that?---I'm assuming, from these set of minutes, that they were not.

So there was a systemic failure to properly monitor accounts?---Certainly, in the Queensland portfolio that I've looked at closely, there were delays across the portfolio in reporting.

And that failure to properly monitor accounts isn't surprising, I want to put to you, given that the bank had made a commercial decision in March 2010 to give priority to new business and additional lending to existing clients?---It was – there's still a balance between account retention and the annual review process and compliance, and new acquisitions, yes.

The balance wasn't working, was it, Ms Gartmann? You had matters where loans hadn't been reviewed for up to two years, and I'm putting to you that that poor loan management was a consequence of a commercial decision that had been made to prioritise new lending?---I think it was also influenced by lack of on-ground resources through our district banking manager network. There had – there were a low number on the ground at that time.

These - - -?---And also because we did have, in that 2011 period, customers that were under stress, and not always can we meet face-to-face to do those annual reviews. So, yes, there was poor focus from our staff on the ground, there were some reluctant customers to engage in looking and quantifying their position, and we didn't have enough people on the ground to do that.

So do you accept that that poor focus from the people you did have on the ground, as you've described it, was a result of the decision by the bank, the commercial decision by the bank to ask them to prioritise new lending over the management of existing clients?---I think we always have to have some focus on growth. And the balance is – and the lack of oversight and management of the frontline staff was that they were not putting sufficient focus on their annual review process. That's not to say it was not undertaken altogether.

Yes. But you appear to want to answer my questions by reference to the conduct of those on the ground staff. What I'm trying to ask you to engage with is the directive from above to them to prioritise on new lending – prioritise new lending rather than the management of existing clients?---The minutes that you showed me, where that was, it was a reflection of a conversation rather than a directive.

And - - -?---So I can't say that it was actually a directive.

Right. But that was the position of the board credit committee in that meeting?---From - - -

To make that prioritisation?---I think the bullet point was actually highlighting that there appeared to be a focus on those above – a prioritisation above annual reviews.

Perhaps if I can take you to some other documents that speak of the focus on growth in the Queensland portfolio in this period. Can we go to Mr Corolis' report which was produced in response to the request from the chairman in the meeting in May – I'm sorry, in February 2011 that I took you to. Mr Corolis' report is exhibit 9 to your statement, BAB.5022.0001.0009. So this is the report produced by the general manager of risk following that meeting?---Yes.

And it was produced for another meeting of the board credit committee in July 2011?---Yes.

And I want to put to you at the outset that this report, which you've annexed to your statement, and which you refer to in your statement as the credit structure report, put the existence of a systemic problem in respect of loan monitoring and, indeed, loan origination beyond doubt?---With the benefit of hindsight, I disagree, because much of what Mr Corolis suggested would happen did not happen to the portfolio.

Well, I want to focus on what he said was happening in the portfolio. Now, perhaps the best thing to do is to take you to some particular findings made by Mr Corolis in this report. Can we start by looking at the first page, 0009. And what I want to suggest to you is that, under the heading Discussion, Mr Corolis gives a somewhat sobering overview of the state of Rural Bank's loan portfolio. Do you see the references to the deterioration in the credit quality of the portfolio?---I can see that.

And do you see, underneath the dot points, his reference to the level and amount of problem loans being too high and outside tolerance in absolute terms?---I can see that, yes.

And if we turn to 0010, we see in the first paragraph below the dot points that Mr Corolis observed that:

> *Since April 2010, credit quality had continued to deteriorate across the rural and AMIS –*

AMIS?---That was a managed investment scheme loan program.

Yes:

> *…loan portfolios at a rate higher than expected. The discussion below focuses on the rural portfolio unless otherwise stated.*

?---Yes.

Now, we see that underneath that, in relation to rural lending, Mr Corolis stated that:

> *The majority of the deterioration has occurred in Queensland. The deterioration in the credit profile of the Queensland portfolio has been exacerbated by the depressed property market, which shows little sign of improvement. It is important to highlight that the Queensland property market has contributed to the current level of problem accounts, but in the main has not been a causal factor leading to defaults. The property market has, however, exacerbated losses and led to contracted and prolonged workout periods.*

Do you agree with that, Ms Gartmann?---I disagree with Mr Corolis' causal factor.

Why is that?---Again, with the benefit of hindsight and looking at the portfolio as a whole, and understanding agriculture – no disrespect to Mr Corolis – but understanding agricultural volatility, I disagree with his comment there.

So Mr Corolis was tasked by the chairman of the board credit committee to undertake this work. He was engaged to do that work in 2011, at the time of the deterioration of the portfolio?---Yes.

But you say you're in a better position, in June 2018, to assess what was going on with the loan portfolio in Queensland?---Certainly. I'm not in the moment and I'm taking a more objective view of the longer term agricultural cycle.

Why don't you think Mr Corolis was taking an objective view?---Because at the time we had – I believe that the business was only recently fully 100 per cent owned - - -

Yes?--- - - - as I've highlighted earlier.

Yes?---There were some challenges in the cultural alignment between Elders and Rural Bank.

Yes?---And certainly there had been a marked impact on the portfolio in Queensland.

But why do those matters about the relationship between the two entities in this period of acquisition affect the accuracy of the findings and observations made by Mr Corolis in this document?---Because this was a report also written to try and stimulate, as I said before the break, some greater focus and investment in the district manager – banking manager resources and their performance.

Why do you say that, Ms Gartmann? This was a report that was responsive to a request from the chairman for:

> *A paper outlining the key issues and processes that are being adopted to identify, rectify and address deteriorating distressed and impaired assets, and address whether there are any systemic issues that need to be addressed.*

?---Because from my investigations and review from material at the time, there were a number of cultural misalignment challenges between the two organisations.

I understand that?---And this report was to bring greater focus and attention to the credit quality of the portfolio and the investment and resources to undertake that.

But this wasn't a report directed to understanding cultural misalignment challenges. It was directed to answering the chairman's request to analyse whether there was systemic issues that needed to be addressed and recommendations made?---Correct.

All right. Well, let's look at page 0012, because we can see from that page, underneath the first graph, the last sentence in that paragraph that Mr Corolis recognised that:

> *The rate of growth in Queensland was much higher than every other state and well above national growth rates.*

Do you agree with that?---I do agree with that. If you look at the industry growth rates for Queensland agricultural lending at the time, you would also see that it was well above national growth rates. So we were tracking in line with the industry, which was investing on the back of a rising property market.

We see at 0013 that Mr Corolis observed, at the top of the page that:

> *The proportion of the Queensland portfolio in loans of more than $10 million had increased quite rapidly, moving from approximately 6 per cent in 2004 to over 22 per cent by 2009.*

You accept that those statistics are correct?---That is correct, and it also reflects the background paper that was released from the department highlighting the growth in agricultural debt, particularly in Queensland, at that time.

Well, we see from 0014, that - - -

THE COMMISSIONER: Just before we leave that, we see from the next sentence in 013 that the concentration, in fact, was well in excess of the national average, don't we?---The distribution of large loans.

Yes?---So national average for the Rural Bank portfolio, yes. And the Queensland portfolio and Queensland loans more broadly across the agricultural sector were substantially large compared to the rest of Australia.

MS ORR: We see from 0014, Mr Corolis' analysis of this growth in your Queensland portfolio. We see at the top of the page that:

> *Given the bank's position in the agribusiness lending market relative to its competitors, further investigation is warranted regarding the key drivers of the rate and nature of growth within the Queensland portfolio. In particular, relative to its competitors over that period of growth, the following points are highlighted: Rural Bank did not necessarily offer the best rates, competition for loans was strong, and Rural Bank did not have a premium brand or the sales capability to attract top end producers on a consistent basis.*

Do you agree with those matters?---I agree with the first two, and we still do not offer the best rates, because that's a race to the bottom. Competition for loans was strong because everybody was in that market. However, I would disagree with the premium brand. There was a partnership between Elders and Rural Bank, and one of the benefits of that partnership was having a number of Elders district banking managers located within community, connected to their community, and knowledgeable about the producers in that region and their systems of production. So I don't believe it was not a premium brand, because the value proposition of having a bank and a pastoral house partnering to support Australian agriculture, I feel, is actually a premium brand.

But Mr Corolis did not?---He did not.

The Corolis report suggested that this aggressive growth in the Queensland portfolio was accompanied by widespread deficiencies in both loan origination and loan management practices and procedures. Do you agree with that?---Certainly in the loan management practices, as we've talked about a little bit, there was certainly areas of substantial improvement. In terms of loan origination, having looked at the 62 loans that became non-performing, origination was appropriate, particularly in the earlier years and before they got into some challenging conditions from external factors.

Well, that wasn't the view of Mr Corolis, was it?---No.

Mr Corolis, in relation to loan origination, identified issues relating to a failure to properly assess loan serviceability?---He did.

And he said at 0014 that, based on the problem accounts that Rural Bank had been managing, he considered the consistent theme to be a lack of debt serviceability?---He did highlight that, and certainly looking at a number of those loans in the Queensland portfolio, when they are designed for a bridging purpose, serviceability assessment is impractical and not appropriate because of the strategy to then pay down debt via asset sale.

Mr Corolis found that a specific manifestation of this theme of lack of debt serviceability was the noticeable increase in debt serviceability ratios in Queensland loans from 2004 to 2006?---Correct, yes.

And within those two years he found that the proportion of loans with a debt serviceability ratio of over 50 per cent jumped from 13 per cent to close to 24 per cent?---Yes.

So that by 2006 the Queensland portfolio had almost doubled the national average of loans with a debt serviceability ratio of over 50 per cent?---Yes. That's stated in his report.

So that indicated a much greater reliance on security than debt serviceability?---Correct.

Now, this was reinforced on page 0015 by Mr Corolis' review of a number of performing and non-performing files, from which he determined that debt serviceability requirements were either waived or heavily subordinated in terms of importance in favour of security coverage?---Correct.

In other words, he found that a customer's ability to repay their loan was subordinated to Rural Bank's ability to recoup the money via the sale of the security offered in connection with the loan?---That's correct.

And we see at 0015 that the human consequence of this was that for a number of files and, in Mr Corolis' words, "a significant sample of stressed accounts", a customer wasn't able to service their debt at the first review date?---That's what's written here, yes.

And Mr Corolis considered that those serviceability issues were masked by the structure of the interest repayments offered by the bank?---That's what his view was, yes.

Now, do you agree with those views, Ms Gartmann?---No. Well, the masking by the interest repayment structure, I disagree with. These are half yearly interest payments, and very appropriate for Queensland cattle given the timing of their cash flow. And we still have about 30 per cent of our loans in Queensland cattle are on half-yearly interest repayment cycles.

What about Mr Corolis' finding about a significant sample of stressed accounts showing that the customer wasn't able to service the debt at the very first review date?---That's his finding, yes.

Do you have any reason to dispute that?---Well, I haven't looked at – I haven't looked at exactly the same set of files that he looked at.

No?---I looked at 62 specifically.

Yes?---And from my view and from my investigations on those files, they were serviceable.

Is there any reason why, Ms Gartmann, when you annexed Mr Corolis' report to your statement, you didn't mention the many issues that you have with the report, the areas of disagreement you have with the report?---No.

Do you understand that by annexing the report to your statement - - -?---Yes.

- - - and providing it as one of the aspects of the investigation that was conducted by Rural Bank - - -?---Yes.

- - - it's difficult for anyone to assess that you have any issues with the content of any of those reports?---No. I think that what I'm disagreeing with is some of the systemic nature.

Yes?---I certainly recognise that we did have an overreliance on security in Queensland, and that the emphasis and the balance between serviceability and security was not appropriately balanced. There was subsequently then substantial work to address this, largely through training and oversight. So I'm not disagreeing with any of that. What I am disagreeing with is the systemic nature and – of these issues across Rural Bank, and I'm also disagreeing with some of the elements which Mr Corolis points to as being inappropriate when I think, from an agricultural context they are appropriate, such as the half-yearly interest cycle.

But - - -?---So it's more in the severity and the – I don't believe it was a systemic issue. However, these reports are fact. They were tabled and discussed and, therefore, they did trigger a range of actions subsequent.

Well, they triggered a range of actions because these were regarded by the bank to be systemic problems that required systemic change, weren't they?---That is the view of the author, yes.

No, I'm not talking about Mr Corolis. You've referred to the steps taken following Mr Corolis' report. You've referred earlier today to the Willis Report, which set out a large number of recommendations to be made by the bank in relation to culture, in relation to governance, in relation to the handling of loans generally. They were systemic changes that needed to be made because these were systemic problems, were they not?---No. They were not – in my view, sitting here in 2018 and reviewing these files, and reading the minutes not as someone who was participating, and looking particularly at the 62 Queensland cattle loans, I do not believe that they were systemic.

So the bank was wrong to make the systemic changes in response to these matters?---They did not make systemic changes in response.

To culture, to governance?---There was certainly work and effort, as there continue to be, on policies and procedures, cultural alignment, training and oversight, that did take place. And they still take place, and it's not because we have a poor bank and poor practices, it's because there's continual improvement and there's always better ways of doing things.

They were very significant changes that were made as a result of this report and the Willis report that followed it, weren't they?---I think there was a lot of refinement because, when I look at the broader underwriting standards within the 2005 credit manual – and I've compared that to the 2013 credit policy manual and the 2018 one that we operate under now – largely, it's there. The changes that took place have largely been around articulation, greater guidance, greater clarity for each and every person within the lending value chain to actually have greater direction on what they should be doing, and doing what's right. So banking has – actually has a poor record for being clear and articulate, and putting things into plain English. And much of what I've seen, the improvements in the policies and procedures, has been greater guidance.

So the changes that were made – you describe them in your statement as including rebalancing of Rural Bank's focus on loan serviceability, improvements in staff training, tightened performance management, changes in relation to valuations and appraisals, and implementing new governance practices including significantly expanding the remit responsibility and membership of the management credit committee to monitor the credit risk profile of Rural Bank, establishing the lending standards review committee to investigate potential lending policy breaches, and establishing the compliance and conduct standards committee?---Yes, correct.

These are the changes that you referred to in your statement at paragraph 71 in response to Mr Corolis' report and the Willis report that followed?---Correct.

They were significant systemic changes?---I don't believe they were systemic – well, they were significant changes over a period of seven years.

And they were in response to the matters identified in Mr Corolis' report and the Willis report that followed?---And the prior report, yes.

Yes, the KPMG report?---Yes.

Thank you. So if I could just take you to a few other parts of the Corolis report, Ms Gartmann, at 0019 we see that, from Mr Corolis' review of a large number of poorly performing accounts, he identified 15 additional very troubling themes relating to loan origination and loan management, more broadly; do you see that?---I do.

And they included:

A strong bias toward asset lending on the assumption that rural property values would continue to increase and, accordingly, asset sales would provide a comfortable "first way out" in the event of recovery action.

?---Yes.

They included:

A failure to disclose, recognise and identify the true risk profile of the borrower.

?---Yes.

They included:

A compromised valuation process, with valuations having been instructed and/or influenced by sales.

?---Yes.

They included:

Appraisals being inflated due to the appraiser not visiting and inspecting the property and/or possibly compromised due to an inherent conflict of interest.

?---Yes.

They included:

Cash flows for clients having been prepared by sales and not sighted and/or agreed with the borrower.

?---Yes.

They included:

An overreliance and usage of temporary limits.

?---Yes.

Continuing:

Poorly structured credit approvals and waiving of conditions subsequent to approval.

?---Yes.

Continuing:

Lending against defective and/or poor securities.

?---Yes.

Continuing:

Obviously warning signs such as anomalies that were either not identified or overlooked.

?---Yes.

Continuing:

Permitting customer risk rating overrides without proper justification.

?---Yes.

And:

Credit allowing perceived pressure from sales and/or management to compromise the independence of credit decisions.

?---Yes.

Now, these were themes which had been a significantly material contributor to the credit issues which the bank found itself experiencing in 2011?---Those were definitely the views of the author, yes.

And these are systemic matters, not isolated matters?---Yes. Well, Mr Corolis highlights in the first paragraph that they are not restricted to the Queensland portfolio.

They were themes that impacted upon Rural Bank customers around Australia, weren't they?---According to the author, yes.

And we see - - -

THE COMMISSIONER: You say "according to the author". The author was the chief risk officer of the bank; is that right?---That's correct, yes.

Is there any reason you offer why I should not understand the chief risk officer of the bank to have made an accurate assessment?---I think when you consider – if you asked the Rural Bank leadership team, risk is one component, and they will always view things as a glass half full, as opposed to the full executive leadership team. So in the – with this particular report, it was drawing attention – strong attention – to a number of issues, but I don’t know that that was the view of the entire leadership team.

It was the risk officer doing his job, wasn’t it?---He was.

MS ORR: We see in the final sentence on this page, Ms Gartmann, Mr Corolis’ conclusion:

> *Based on my review, a number of these issues were clearly systemic, and not isolated, and have been a significantly material contributor to the credit issues currently faced by the bank.*

?---Yes, that’s written there.

You disagree with that?---I think that’s a common theme. The issues were there and they triggered a number of actions and improvements to systems process policy. In my view, sitting here in 2018 and reading the materials, it was not a systemic, across the board, issue.

I just - - -

THE COMMISSIONER: Well, can I understand better than I presently do what you mean by “systemic” in this context?---So I believe that if it had been a broad systemic issue, we would have seen a lot more non-performing files, we would have seen further deterioration of the credit profile of the bank, and – and not just in Queensland. It would have been seen across the board.

MS ORR: There were significant numbers of non-performing files, weren’t there, Ms Gartmann?---I know that in Queensland there were, yes.

Yes. And what about outside of Queensland?---I don’t have the numbers at hand, unless you’ve got them.

So you assume that there weren’t - - -?---Well, having a look at the broader portfolio, and also the portfolio performance in recent time, I cannot draw a conclusion that it was systemic at a national scale.

Although Mr Corolis did?---Yes.

Now, on 0020 we see that one of the final reflections by Mr Corolis was that a number of the loans should simply never have been approved. Do you see that in the second paragraph?---Yes.

Now, you didn’t exhibit to your statement the minutes of the board credit committee meeting at which this report was presented?---I don’t think so.

Why not, Ms Gartmann? You exhibited many, many board credit committee meeting minutes. Why did you not exhibit the minutes that considered this report?---I don't know, sorry.

The committee had a significant discussion about what had emerged from Mr Corolis' report at that meeting?---Yes, it did.

And if we go to BAB.50006.0004.0070 – 5006, I'm sorry. Now, we need to turn within this document to the minutes of 27 July 2011 meeting, which are at 0074. And we see at the bottom of the page there that, amongst other things – so, sorry, I should direct you first to the paragraph above that which shows that Mr Corolis presented his paper at this meeting?---Yes.

And highlighted a number of matters in relation to that report?---Yes.

And then noted that:

> *The overarching control framework had proved deficient and significant changes have been made in this regard.*

?---Yes.

And we see the chairman's response below that?---Yes.

Continuing:

> *The chairman noted that the current credit situation was unsatisfactory and that there appears to have been cultural issues contributing to the issues currently faced.*

?---Yes.

And that:

> *While in some circumstances lending outside the bank's preferred underwriting standards may be permissible, the report suggested that basic credit disciplines appear to have been ignored.*

?---Yes.

And at 0075 we see that the chairman noted, at the top of the page, that:

> *A presentation was made approximately five years ago which highlighted that the value of Queensland cattle properties were heading into a pure asset bubble, and these warnings appear to have been ignored.*

?---I tried to find that particular presentation, but I was unable to, so I can only go on what's written there.

And we see Mr Patton, a director, noting that:

> *Growth appears to have been an issue given the rate of growth and the size of the deals being written.*

?---Yes.

Now, the tenor of these minutes – which I assume you've read in preparation for giving evidence today, Ms Gartmann?---I have.

The tenor of these minutes is that the issues which had been identified by Mr Corolis in his credit structure report stemmed from the aggressive growth that had been pursued in the Queensland loan portfolio?---Following the market trends, yes.

Why is it important to you to add the qualification of following the market trends, Ms Gartmann?---Well, I think it was actually an industry-wide issue, and - - -

What was an industry-wide issue?---The growth in activity in Queensland, and the increased size of lending in Queensland cattle.

THE COMMISSIONER: Well, I don't understand why that makes it any better or any worse?---It doesn't make it any better or any worse. I'm just making sure that – I would like to highlight that we weren't above industry growth rates. We were tracking in line and we were following the crowd, unfortunately.

MS ORR: So you accept that there was aggressive growth that was pursued by the bank in the Queensland portfolio at this time?---Yes.

And we see that after a further discussion of the findings of the report on page 0075, including highlighting of the need for greater cultural alignment between sales and credit, the chairman notes towards the bottom of that page that:

> *The bank must take responsibility for resolving these issues and the focus needs to be on making permanent improvements to all facets of the credit process, including the oversight function.*

?---Yes.

That was the position of the chairman taken following the presentation of Mr Corolis' report?---Correct.

I tender that document, Commissioner. The minutes are within a larger document, Commissioner, which is the board credit committee meeting pack for a meeting on 17 August 2011.

THE COMMISSIONER: Board credit committee meeting pack – what date, Ms Orr?

MS ORR: 17 August 2011.

THE COMMISSIONER: 17 August 2011, BAB.5006.0004.0070, exhibit 4.128.

EXHIBIT #4.128 BOARD CREDIT COMMITTEE MEETING PACK DATED 17/08/2011 (BAB.5006.0004.0070)

MS ORR: So after the presentation of Mr Corolis' report the bank took significant steps to improve its policies and procedures; you accept that?---Yes.

And they related to loan serviceability, securities, valuations and loan monitoring?---Correct, yes.

And the first step in that process was obtaining a further external report, which you've referred to as the Willis report, and which is annexed to your statement?---Actually, the first step was, at that July meeting, forming a taskforce to investigate, and then they engaged a consultant.

And was that the consultant who produced the report you've been referring to as the Willis report? And that was provided in November 2011?---It was.

And many of the findings in that report are consistent with action items that had been identified by APRA as early as 2006?---Yes, correct.

So the key messages in the Willis report related to credit culture?---Yes.

Governance, approval processes, and portfolio management and monitoring?---Yes, correct.

Rural Bank then took steps to implement recommendations made in the Willis report?---Yes.

And the work project that followed took a number of years?---Yes.

And your statement charts developments up until April 2013?---Yes.

But further policy changes were necessary, even after that period?---Well, in light – in view of the continuous improvement program, yes. They weren't necessarily in response to the Willis report. There were – there are always policy reviews and further developments.

So, for example, in March 2012 APRA was still expressing the view that Rural Bank's number of outstanding reviews was far too high?---If that – if you say so, yes. I can't quite remember.

I am happy to show you that document, if you're not familiar with that one, Ms Gartmann?---Yes.

That's BAB.5032.0003.0278. So this is a letter from APRA on 14 March 2012. And if I could direct your attention to 0281?---Yes. So this was only a few months after the Willis report had been tabled, which identified similar issues.

Yes?---And there were a number of work streams underway.

Yes. So at this time in March 2012 we see from the middle of the page that APRA still thought that the bank's annual reviews were far too high and that the whole process should be re-evaluated?---Yes.

Particularly when it would appear that some large loans can go three years without a review?---Yes.

So that remained a problem in 2012?---Yes.

I tender that document, Commissioner.

THE COMMISSIONER: Letter APRA to Rural Bank, 14 March 2012, BAB.5032.0003.0278, exhibit 4.129.

EXHIBIT #4.129 LETTER APRA TO RURAL BANK DATED 14/03/2012 (BAB.5032.0003.0278)

MS ORR: Now, if we take the date of late 2011 as the time by which the critical issues were identified – that's the date that you assign in your statement – we can see that it took about a year and a half or more to complete the first tranche of reforms?---Yes.

Do you consider that was an appropriate length of time?---Well, one of the primary first steps was reviewing and considering changes to the risk appetite statement, because from that flows the framework for credit assessment. So that was a piece of work that took – took a substantial amount of time and went back and forwards to the board and board credit committee for a period of time. So it did, unfortunately, take that long, yes.

The work project that you describe in your statement focused almost entirely on revisions and amendments to your policies and procedures; is that right?---Along with training and oversight, yes.

There's no reference in your statement to any work relating to customer remediation?---No.

And you tell us that the only investigations that Rural Bank undertook in respect of the systemic issues that were identified in relation to origination and management were investigations that were undertaken in a general fashion rather than in respect of individual customers?---Well, for many of the customers in the Queensland cattle portfolio that had become non-performing, we were having direct and very close relationships with them as we were working through. So, aside from that, there was no communication around any of the issues that were highlighted in the Willis report because most of those were internal, and pertained to the amounts of funds that the bank was writing off, not that customers were writing off.

Well, the two are not mutually exclusive, are they, Ms Gartmann? There were serviceability issues with the capacity to affect the customers individually?---Correct.

And were the customers told about that?---No.

Should they have been told about that?---Well, I don't believe that serviceability alone was – or – or lack of appropriate serviceability assessment was the driving factor behind those loans becoming non-performing.

But you've conceded in your statement that the conduct of Rural Bank contributed to those loans becoming non-performing?---Correct. So we had not adequately assessed to leave sufficient resilience to weather a perfect storm of live export ban impacting markets for a substantive period of time and a five-year drought.

So do I understand that no Rural Bank clients whose loans were examined as part of the work that was done on these issues were informed of any issues that had been discovered in respect of their loans?---No.

I am correct that that did not happen?---I don't believe so.

Okay. And should it have happened?---As I said, because I don't believe that the serviceability assessment was causal, no, I don't believe it would follow through that we would inform customers of that.

And there was no remediation program set up?---Apart from working directly with the customers to get through a challenging external environment, no.

Now, if similar issues – which I want to describe as systemic issues, but I take it that you will cavil with that description – but if similar issues were identified by Rural Bank today, would Rural Bank respond in the same way as it did then?---It really does depend on the circumstance, in terms of if they are average seasons and we had this response of a credit portfolio quality downgrade, then yes. If it's due to external circumstances that are beyond reasonable, then no.

I just want to make sure that in answering my question, Ms Gartmann, you are taking into account the matters that were not external that contributed to the performance of these loans, including the 15 themes identified by Mr Corolis in relation to his assessment of the portfolio?---So when I've looked at the 62 loans, as I said, there are a very small number that I don't believe we would write today. And so, therefore, writing them and their performance, I don't believe is impacted by the assessment that we undertook.

So today, if you identified a failure to disclose, recognise and identify the true risk profile of the borrower, would you tell the borrower that you had identified that?---So if we were doing that today with no external conditions that were the perfect Storm, then yes.

Well, why does the presence of the external conditions impact on whether or not you should disclose to a customer that there has been a failure to disclose, recognise and identify their risk profile?---So if the risk profile is impacted by those extreme external events, it's not because of the serviceability or credit assessment that they're in financial difficulty, because I don't believe – if we truly considered the risk profile of Australian agriculture and factored in what – you know, millennial droughts, a political decision on markets, then no one would lend in Australian agriculture. It is the only – Australia is the only country that has not got – does not have any subsidised support for farmers to buffer them against many of these externalities, and I feel – it is my belief that that volatility needs to be considered, but you cannot sensitise and consider a credit assessment for that perfect storm otherwise you would never lend in Australian agriculture, and then you are financially excluding a large part of our community.

Yes. In answering my questions, I understand you to keep coming back to the external factors that were present in these loans. I'm asking you to put the external factors to one side. If you identified today that one of your staff had failed to disclose, recognise and identify the true risk profile of the borrower in making an assessment of a loan to that borrower, would you tell the borrower that that had occurred?---We would, yes.

Thank you. And if you identified today that a valuation process in connection with a loan had been compromised - - -?---Yes.

- - - would you tell the borrower that that had occurred?---Yes, and we have.

And you have?---Yes.

That's something that has occurred recently?---No, it's through the course of these activities.

So you have spoken to customers about these matters?---We have spoken to customers about a number of these issues. Like I said, through discussions, through asset management, we have had those conversations.

So you've spoken to customers about valuations that were compromised?---Not in the Queensland cattle industry, no.

There have been other valuations that have been compromised?---We have had one instance, yes.

And you disclosed that instance to the customer?---Yes.

And where you became aware that credit risk rating overrides had been implemented without proper justification, would you draw that to the attention of the borrower?---No.

And why not?---Because that is largely an internal rating, and I don't know that customers would take well to being informed that they are maybe on a watch list. That's not conducive to the relationship, and it largely impacts the oversight that we have on that particular loan.

And where you became aware that the independence of credit decisions had been compromised because of pressure from sales or management, would you draw that to the attention of the borrower?---It depends if there is impact on the customer. Then, yes. Largely, they would be the risk being carried by the bank.

Thank you, Ms Gartmann. I have no further questions.

THE COMMISSIONER: Yes, Mr Batt.

<RE-EXAMINATION BY MR BATT [2.54 pm]

MR BATT: One matter, Commissioner.

Ms Gartmann, just a few minutes ago you were asked a question by Ms Orr – and this is transcript 3685, line 1, Commissioner.

You were asked a question about the contents of your witness statement. The question was:

> *You have conceded in your witness statement that the conduct of Rural Bank contributed to those loans becoming non-performing.*

And you said in answer to that question about the contents of your witness statement, "Correct". Could you please take out your witness statement, Ms Gartmann, and go to paragraph 60 on page 13, which reads:

I do consider that the issues referred to at paragraph 54 above may have meant that some of the loans were more susceptible to the cumulative effect of external stressors than they otherwise would have been.

Is that the part of the witness statement that you had in mind when you answered "correct" to Ms Orr's question?---Yes, it is.

No further questions, Commissioner.

THE COMMISSIONER: Yes. Yes. Thank you very much, Ms Gartmann. You may step down. You're excused.

<THE WITNESS WITHDREW [2.55 pm]

MR BATT: Commissioner, if I might just deal with one documentary aspect. I've discussed it with Ms Orr. It just relates to the tender of a small number of documents which are, if I can encapsulate them, the responses of Rural Bank to the APRA letters that were tendered by Ms Orr. We seek to tender the bank's responses to those letters from APRA to the bank, and I understand there's no opposition to that. If I could give the Commissioner the references, we would seek to tender the five documents.

THE COMMISSIONER: Yes.

MR BATT: The first is BAB.5034.0001.0001, dated 24 August 2009. Rural Bank's response to the APRA prudential review report dated 1 July 2009. We tender that.

THE COMMISSIONER: That document is exhibit 4.130.

EXHIBIT #4.130 RURAL BANK RESPONSE TO 1 JULY 2009 APRA PRUDENTIAL REVIEW REPORT DATED 24/08/2009 (BAB.5034.0001.0001)

MR BATT: Commissioner pleases. The next is BAB.5024.0001.1713, dated 14 February 2011 entitled Rural Bank's Response to the APRA Prudential Review Report dated 7 January 2011. I tender that.

THE COMMISSIONER: That is exhibit 4.131.

EXHIBIT #4.131 RURAL BANK RESPONSE TO 7 JANUARY 2011 APRA PRUDENTIAL REVIEW REPORT DATED 14/02/2011 (BAB.5024.0001.1713)

MR BATT: And then, Commissioner, the other two documents – I may have said five a minute ago, I think I meant four. The other two documents are both responsive to what was exhibit 4.129. One is a letter and one is an attachment to the letter. The first - - -

THE COMMISSIONER: Do it as a single document – single exhibit, I think, Mr Batt.

MR BATT: Thank you, Commissioner. They do have different dates and document references, but that's no difficulty. I will just note that. The first document reference is BAB.5032.0003.0277, dated 26 April 2012, and entitled Rural Bank's response to the APRA Prudential Review Report dated 14 March 2012. And going with it on that basis, Commissioner, is BAB.5006.0014.0060, dated 24 April 2012, entitled an APRA Prudential Review Action Plan. We tender those two documents as one, if we might.

THE COMMISSIONER: Together those will be exhibit 4.132.

EXHIBIT #4.132 RURAL BANK'S RESPONSE TO 14 MARCH 2012 APRA PRUDENTIAL REVIEW REPORT WITH ATTACHMENT 24 APRIL 2012 APRA PRUDENTIAL REVIEW ACTION PLAN DATED 26/04/2012 (BAB.5032.0003.0277)

THE COMMISSIONER: Thank you, Mr Batt.

MR BATT: Commissioner pleases.

MS ORR: Commissioner, that was the last case study in the agricultural finance part of this hearing block. Before we move to the next topic in the hearing block, could I tender four statements obtained from CBA witnesses which will not be the subject of cross-examination. They are a statement from Mr Grant Cairns, C-a-i-r-n-s, dated 19 June 2018.

THE COMMISSIONER: That becomes exhibit 4.133.

EXHIBIT #4.133 STATEMENT FROM MR GRANT CAIRNS DATED 19/06/2018

MS ORR: A statement from Mr Mark Wlossak, W-l-o-s-s-a-k, dated 19 June 2018.

THE COMMISSIONER: That becomes exhibit 4.134.

EXHIBIT #4.134 STATEMENT FROM MR MARK WLOSSAK DATED 19/06/2018

MS ORR: A statement from Johanna White, J-o-h-a-n-n-a, dated 21 June 2018.

THE COMMISSIONER: That becomes exhibit 4.135.

EXHIBIT #4.135 STATEMENT FROM JOHANNA WHITE DATED 12/06/2018

MS ORR: And a second statement from Ms White dated 29 June 2018.

THE COMMISSIONER: Sorry, what date?

MS ORR: The 29^{th}.

THE COMMISSIONER: Thank you. Becomes exhibit 4.136.

EXHIBIT #4.136 STATEMENT FROM JOHANNA WHITE DATED 29/06/2018

MS ORR: Perhaps if the Commission would allow a short break to allow Rural Bank's representatives to leave and then I will deliver an opening statement in relation - - -

THE COMMISSIONER: Very welcoming to you, Mr Batt.

MR BATT: I won't comment on whether we would rather stay or go, but I will go.

THE COMMISSIONER: If I come back at five past 3, Ms Orr.

MS ORR: Thank you, Commissioner.

ADJOURNED [2.59 pm]

RESUMED [3.06 pm]

MS ORR: Commissioner, we turn now to the second topic of this fourth round of public hearings. The second topic we will examine involves issues that arise in the interactions between Aboriginal and Torres Strait Islander people living in regional and remote communities and financial services entities. As at 2016, 649,171 Australians identified as being of Aboriginal and/or Torres Strait Islander origin, comprising 2.8 per cent of the total population of Australia. Whilst the majority of Aboriginal and Torres Strait Islander people live in New South Wales and Queensland, the Northern Territory has the highest proportion of Aboriginal and Torres Strait Islander people, with 25.5 per cent of the Northern Territory population identifying themselves in this way. For this reason, and because a number of our case studies this week will involve witnesses from the Northern Territory, the Commission has chosen to hold this second week of hearings in Darwin.

As with the other topic explored in this round of hearings, the Commission has consulted widely in order to identify and understand the issues that arise for Aboriginal and Torres Strait Islander people in their dealings with financial services entities. We will provide further detail of this consultation later in this opening statement. The structure of this opening statement is as follows: first, we will explore some of the obstacles to accessing financial products and services that are experienced by Aboriginal and Torres Strait Islander people in remote and regional communities. Second, we will identify what the Commission has been told by representatives of those people, and by the regulator, about the experiences of Aboriginal and Torres Strait Islander people with financial services entities, including with particular financial products and services that are the subject of the case studies explored in these hearings.

Third, we will identify the particular financial products and bank practices that are the subject of our case studies, and will explain some of the key features of the legal framework governing those financial products and practices. Fourth, we will summarise what financial services entities have told the Commission about their practices relating to their Aboriginal and Torres Strait Islander customers. Finally, we will briefly address the nature of the evidence that will be given over the remainder of this week by providing an overview of the case studies that we will examine. We turn first to obstacles encountered by Aboriginal and Torres Strait Islander people living in regional and remote communities when accessing financial products and services.

Before doing so, we note that the Aboriginal and Torres Strait Islander population is as diverse as the broader Australian population, and not all Aboriginal and Torres Strait Islander people living in these communities will experience the obstacles that we will outline. As we explained last Monday, in our opening address for this fourth round of hearings, as at 30 June last year around 6.9 million people, or around 28 per cent of Australia's population, lived in regional or remote areas. Of all people living in remote areas, there is a significant proportion of Aboriginal and Torres Strait Islander people. In 2011, 45 per cent of people living in very remote areas, and 16 per cent of people living in remote areas, identified as Aboriginal and Torres Strait Islander.

As at June last year, only 4 per cent of all branches of ADIs in Australia were located in remote or very remote areas. Only 7 per cent of face-to-face services provided by ADIs were provided in remote or very remote areas. And finally, only 2 per cent of ATMs in Australia were located in remote or very remote areas. In general terms, access to a bank branch, other face-to-face services, and ATMs decreases as remoteness increases. A lack of access to appropriate and affordable financial services and products is often referred to as financial exclusion.

Financial exclusion is frequently graded on a scale. Three indicators of financial inclusion, which are used as markers on this scale are whether a person holds a transaction account, a credit card, and general insurance. People who hold all three of these are considered fully financially included; people holding two of the three are considered marginally financially excluded; and people holding one of the three are considered severely financially excluded; with people holding none of the three, fully financially excluded.

Research done by the Centre for Social Impact between 2006 and 2013 indicated that women, young adults, and those living in capital cities were more likely to be severely or fully financial excluded. However, the Centre for Social Impact's research also found that Aboriginal and Torres Strait Islander Australians were overrepresented in the severely or fully financially excluded group. The research found that indigenous Australians were around twice as likely as non-indigenous Australians to be financially excluded. The Commission will hear evidence in these hearings from people who work with Aboriginal and Torres Strait Islander people about the factors leading to financial exclusion.

Three important factors are financial literacy, geographic exclusion of people living in regional and remote Australia, and difficulties in providing the required identity documents to receive financial services. We will say more about each of these three factors, dealing firstly with financial literacy. Fundamental barriers can exist for Aboriginal and Torres Strait Islander people in accessing financial services, including language barriers where English is not spoken as a first language, lower levels of financial literacy, and limited exposure to people with high levels of financial literacy. A 2015 study by Gordon and Boyle notes that lower levels of literacy are present among Aboriginal and Torres Strait Islander people, particularly those from regional and remote communities where children have only participated in formal education in relatively recent generations.

The study also found that lower levels of literacy and numeracy disproportionately impact on the financial exclusion levels of Aboriginal and Torres Strait Islander people, who are continuously overrepresented in this category. Consumers with low financial literacy may have a limited understanding of how credit, insurance, and superannuation products work. This may result in inappropriate products being provided to consumers. We turn to geographic exclusion, which refers to a physical lack of access to banking and financial services due to the distance between where the consumer lives and the required services. In the 2016 Census, almost one in five

Aboriginal and Torres Strait Islander people lived in remote and very remote areas, compared to around 1 in 100 non-indigenous people.

By virtue of their location, Aboriginal and Torres Strait Islander people are more likely than the general population to suffer geographic financial exclusion. For all Australians, and particularly for Aboriginal and Torres Strait Islander people, geographic exclusion can be further compounded by a range of other practices and developments. We will highlight three of these: bank branch closures, ATM fees, and access to digital services. Dealing first with bank branch closures, in recent years there has been a reduction in bank branches and other face-to-face points of presence in these communities. The Commission heard in the first part of this hearing about the substantial number of branch closures in rural and remote areas of Australia over the last decade.

The removal of banking services from remote communities has had particular implications for the Aboriginal and Torres Strait Islander population, who represent a large and increasing share of the population of regional and remote Australia. The ABAs bank closure protocol recognises that losing a nearby branch may have implications for the local community, particularly for those who live a significant distance away from a branch. The protocol identifies the steps that should be taken by a bank if it is closing a branch and there is not another branch of the same brand within 20 kilometres by road. In those circumstances the protocol proposes that, where it is commercially viable to do so, a bank closing a branch will ensure that ongoing face-to-face access remains locally available. If it is not commercially viable to continue to offer face-to-face services, the protocol provides that the bank will undertake to identify other retail banking service options prior to bank closure and commence consultation with the community.

Turning to ATM fees, a lack of access to bank branches and to alternative methods of withdrawing cash may result in people living in regional and remote areas paying relatively high transaction costs to obtain cash. These transaction costs are largely referable to ATM fees. In a 2010 report, the Australian Financial Counselling and Credit Reform Association noted that the cost of ATM fees was having a significant and detrimental impact on indigenous people living in remote communities. This was due to withdrawal limits on ATMs, which forced people who needed larger amounts to make multiple withdrawals, incurring additional fees. It was also due to indigenous consumers having no choice but to use the single ATM in a remote community that charges fees to perform transactions or check account balances, and due to community stores charging fees of $2 per EFTPOS transaction.

In response to concerns raised about the impact of ATM fees, the government announced in December 2010 that the Reserve Bank of Australia and the Treasury would establish a joint taskforce to monitor and enhance ATM competition reforms. In May 2012, the ABA applied to the ACCC for authorisation of a proposed agreement pursuant to which customers of the proposed participating financial institutions would be provided with access to fee-free ATM withdrawals and balance inquiries at certain ATMs operated by the proposed participating ATM deployers.

On 8 November 2012, the ACCC granted authorisation for five years to 1 December 2017. On 21 December last year, the ACCC granted reauthorisation for a further 10 years.

Turning to access to digital services, as the physical distance to financial products and services increases, access to the internet and other digital services becomes increasingly important to facilitate dealings with financial products and services. Access to the internet and online banking services may alleviate some of the difficulties in accessing financial services when access to a branch or an ATM is limited. However, Aboriginal and Torres Strait Islander people living in remote communities may have difficulty accessing the internet, as it may be unavailable or costly. Other factors that impact on the ability of Aboriginal and Torres Strait Islander people to adapt to electronic banking systems include language barriers, levels of education, literacy, technical literacy, and unreliable phone or internet access.

We turn to the third important contributor to financial exclusion. As well as financial literacy and geographic exclusion, difficulties with identification documents can play a major role. As we have noted, the Centre for Social Impact has done significant work on financial exclusion. In a piece of work from 2012, considering people who were fully or severely excluded from access to financial services, the centre found that 17.9 per cent of Aboriginal and Torres Strait Islander people surveyed had difficulties in opening a bank account because they were unable to provide identity documents, compared with 8.7 per cent of non-indigenous people in the survey.

The Commission will hear from people representing bodies that work closely with Aboriginal and Torres Strait Islander consumers about the reasons such people have difficulty with identification documents. We highlight some of those reasons now. In 2015, the Indigenous Superannuation Working Group found that identification problems occur because for many Aboriginal and Torres Strait Islander people, particularly older generations, births, marriages and deaths were not recorded in official registers. The result of this is that some Aboriginal and Torres Strait Islander consumers do not have a birth certificate. If their birth was never recorded, it can be very difficult to obtain a birth certificate.

Some Aboriginal and Torres Strait Islander consumers have or use multiple names. These may include a traditional skin name or clan name, a birth name, and an adoptive name. Formal identification documents may contain different names or different spellings of the same name. It can be very difficult to have documents copied or certified in remote locations. Some Aboriginal and Torres Strait Islander people live many hours away from the nearest bank branch, making it difficult to physically attend a branch to provide identification documents.

Financial exclusion has a number of potential consequences. Amongst other things, financial exclusion makes day-to-day money management difficult, reducing people's ability to buffer against unexpected financial shocks, or to smooth consumption. Financial exclusion can mean that individuals who lack identification documents may have difficulty opening a bank account, accessing superannuation entitlements, and accessing mainstream credit. Financial exclusion also increases the likelihood that a consumer will resort to methods of obtaining finance beyond mainstream credit providers. As a result of being excluded from mainstream credit options, consumers may have few alternatives other than to turn to high cost, small amount lenders to source finance as quickly as possible from the first available lender at whatever cost and on whatever terms are offered.

In 2015, the Centre for Social Inclusion noted that, when compared to the broader population or financially included segment, between 2006 and 2013 people who were severely or fully financially excluded were consistently more likely to experience a number of poorer economic, social and health outcomes. Amongst other things, those who were severely or fully financially excluded were more likely to feel financially unstable. It is clear that Aboriginal and Torres Strait Islander people face unique obstacles to participation in financial services in remote and regional communities. We will hear evidence in these hearings about the significant consequences of financial exclusion for these people.

We turn next to some of the experiences of Aboriginal and Torres Strait Islander people in respect of the products and practices that we will address in these hearings. The Commission has consulted with a large number of bodies that provide assistance to Aboriginal and Torres Strait Islander people in their dealings with, or disputes with, financial services entities. The Commission has spoken with financial counsellors and lawyers from organisations across Australia who work closely with this group. In the Northern Territory we spoke with the Katherine, Central Australia, and Darwin offices of the North Australian Aboriginal Justice Agency, NAAJA, and with representatives of Save The Children in Katherine.

In Queensland, we spoke with the Indigenous Consumer Assistance Network ICAN including with financial counsellors who work with consumers on Palm Island. In Victoria, we spoke to the Consumer Action Law Centre. In New South Wales, we spoke with the Financial Rights Legal Centre and New South Wales Legal Aid. We also spoke with representatives of Financial Counselling Australia across the country, including its affiliates at Broome CIRCLE in Western Australia, Anglicare Northern Territory located in Darwin and Lutheran Community Care located in central Australia. We spoke with financial counsellors who work with clients in a number of remote communities across Australia including Groote Eylandt and Lake Evella in the Top End, and the Yuelemu Community in Central Australia. In addition, we spoke with the First Nations Foundation who work across Australia.

These bodies told the Commission about the key issues facing Aboriginal and Torres Strait Islander people in their dealings with financial services entities, some of which were common across a number of these organisations. The first common issue that the Commission heard about related to funeral insurance. Consumer bodies told the Commission about predatory sales practices of funeral insurance companies and about the provision of inappropriate policies to Aboriginal and Torres Strait Islander people. We were told that funeral insurance policies were often unsuitable to the consumer base.

The second common issue related to superannuation. The Commission heard about a number of difficulties experienced by Aboriginal and Torres Strait Islander people in relation to accessing superannuation funds. We heard that these people sometimes lack the necessary knowledge about their superannuation benefits and entitlements in order to make a claim. When they are aware of those entitlements, we heard that they often still have difficulty accessing entitlements due to the identification requirements and issues associated with remoteness. We were told that there can be a lack of acknowledgement within superannuation funds of indigenous kinship structures, meaning that consumers are unable to elect beneficiaries beyond their immediate family.

The third common issue related to consumer lending. We were told about instances of irresponsible lending that bore a number of similarities to consumer experiences that we examined in the first round of Commission hearings, in circumstances that involve the added challenges of remoteness, language, and cultural barriers. We heard that clients face problems with a range of consumer credit products including car loans, credit cards, consumer leases, particularly those taken out to obtain essential household items, such as furniture and white goods, pay day loans, and in-store credit arrangements, including the practice of book-up. Book-up is a practice by which a supplier allows a customer to run up a tab and to pay for the goods or services later.

Commissioner, we will not be considering consumer leases, payday loans or in-store credit arrangements in these hearings, because they do not fall within the terms of reference of the Commission. This is because, generally speaking, the entities providing consumer credit under those arrangements do not fall within the definition of a financial services entity in the terms of reference. Most relevantly for present purposes, those entities are generally not authorised deposit taking institutions, nor entities which are required under the Corporations Act to hold an Australian financial services licence.

The fourth issue identified by the groups with which we spoke related to banking fees and practices. We were told about issues associated with informal overdraft facilities and high dishonour and overdrawn fees. ATM fees associated with withdrawing cash and checking account balances appeared to be of particular concern in remote Aboriginal communities. We were also told about difficulties in meeting the identification requirements for opening a bank account. We were told that a significant amount of financial counsellor's time is occupied by assisting clients to verify their identity with financial services entities.

We also sought information from ASIC about what it considered to be issues of particular concern affecting Aboriginal and Torres Strait Islander people in their dealings with financial services entities. ASIC told us that it receives information and complaints about issues affecting Aboriginal and Torres Strait Islander people from four main sources: complaints received by ASICs indigenous outreach program in the course of undertaking outreach work, complaints received by ASICs indigenous telephone and email help line, complaints received by ASICs misconduct and breach reporting team, and through stakeholder networks of indigenous consumer advocates, financial counsellors, community legal centres, and other government agencies.

ASICs indigenous outreach program is a national team which undertakes surveillance and compliance activities, works with ASICs enforcement teams to pursue enforcement action, works with the MoneySmart team to produce financial literacy materials for indigenous consumers, and undertakes project and policy work to improve the provision of financial services for indigenous consumers. ASIC told the Commission that it has identified a number of issues in relation to the provision of funeral insurance policies to Aboriginal and Torres Strait Islander people. Since 1 January 2008, ASIC has received 37 complaints from consumers who identify as indigenous, or who were identified by their representative as indigenous, relating to funeral products.

The particular issues raised were the use of inappropriate sales practices when selling funeral insurance to indigenous consumers, 26 of the incidents, including misrepresentations and pressure selling tactics, and the sale of funeral insurance policies to indigenous consumers in circumstances where the policy may be of little benefit to the policy holder, such as sales to indigenous people under 20 years of age. ASIC identified that while over half of consumers with funeral insurance were aged 50 to 74 – this was 51.2 per cent – funeral insurance sold to indigenous consumers had a much younger age profile. 50 per cent were aged under 20. A higher proportion of indigenous consumers also had their policies cancelled for non-payment of premiums. ASIC has taken action against at least three funeral and life insurance providers in respect of their sales to Aboriginal and Torres Strait Islander customers. Two of these funeral insurance providers, ACBF and Select, will be the subject of case studies during these hearings.

ASIC also told the Commission that it believes a significant number of Aboriginal and Torres Strait Islander people have difficulty engaging with the superannuation system. ASIC told us that it received feedback from financial counsellors and consumer advocates, through its consumer advisory panel, about unmet needs among Aboriginal and Torres Strait Islander people for information about superannuation, proof of identity requirements, and tax file number issues. The feedback that it received also related to difficulties with accessing superannuation funds and finding lost super. ASIC told us that it has held information forums with representatives of the superannuation industry to raise awareness about the issues Aboriginal and Torres Strait Islander people face when accessing their superannuation.

ASIC has also changed trips to indigenous communities with senior people from some superannuation funds. ASIC also told the Commission that many remote indigenous communities are not serviced by ADIs, or by networks or intermediaries to connect ADIs with potential borrowers. ASIC explained that it is common in remote communities for credit to be provided by the vendor of the goods, including through book-up arrangements. ASIC told us that it has worked with regional indigenous communities in relation to loans and credit products, and that this work has primarily been directed towards providers of book-up and consumer leases for household goods.

ASIC told the Commission that consumer advocates have notified it of Aboriginal and Torres Strait Islander clients who spend significant proportions of their income on bank fees. In particular, the lack of services and choice of ATMs means that fees for withdrawals and balance checking are frequently unavoidable. ASIC participated in a taskforce with Treasury and the Reserve Bank in 2010 to 2011. As a result of a report produced by that taskforce, the ABA implemented the fee-free ATM response which we referred to earlier. This involved the provision of 84 ATMs by certain banks across very remote communities at which cash withdrawals and balance inquiries could be made without charge. ASIC told the Commission that the fee-free ATM trial has significantly reduced the impact of transaction fees in communities where a fee-free ATM is located.

A number of the issues raised by ASIC and by those bodies that provide assistance to Aboriginal and Torres Strait Islander people will be considered in this round of hearings. In particular, the Commission will examine case studies involving funeral insurance and bank fees and practices. Immediately after this opening tomorrow morning, we will hear from a representative of ASICs Indigenous Outreach Program, and a representative of Financial Counselling Australia, who will provide further information about some of the issues faced by Aboriginal and Torres Strait Islander people in regional and remote communities in dealings with financial services entities.

We turn now to the particular financial products and practices of financial services entities that we will examine in these hearings. In this part of our opening address, we will also outline some key aspects of the legal framework that relate to the subject of our case studies. The first product which we will consider in the case studies is funeral insurance. Funeral products assist consumers to ensure that there is sufficient money available to cover the cost of their funeral. In addition to funeral insurance, other types of funeral products include prepaid funerals and funeral bonds.

Funeral insurance is sold directly to consumers and is a type of life insurance. There are two types of funeral insurance: funeral life insurance and funeral expenses insurance. In general terms, when a consumer purchases funeral life insurance, they nominate a chosen benefit amount, such as 5000, 10,000 or $15,000. The sum insured is typically much lower than for other life insurance products as it is intended only to cover the cost of a funeral and burial or cremation. The consumer makes regular payments to the provider of the funeral insurance. Premiums are generally payable fortnightly, monthly or annually. On the event of the death of the person insured, if it occurs during the period of the policy, the benefit amount is paid to a nominated beneficiary who can spend the money however they choose.

This differs from funeral expenses insurance. Here, the benefit paid is an indemnity for funeral expenses up to a specified limit. This means that if an insured person has nominated a limit of $15,000, and has paid premiums in accordance with this amount but the funeral only costs $8000, the insurer will only pay $8000. In 2014 most funerals cost somewhere between 4 and $15,000. Despite the low sum insured, the cost of most funeral insurance coverage is relatively high, due in part to features such as an absence of full underwriting. Some funeral insurance policies have fixed premiums, but most do not. Therefore, the total cost paid for funeral insurance cover generally depends on how long the person lives after acquiring the insurance.

Funeral insurance products in Australia typically have the following features: the premium payable depends on the age and sometimes gender of the applicant, and the sum insured. Applicants are not usually subject to health or medical checks. There are often restrictions on when benefits are payable in the first 12 to 24 months of a policy. For example, benefits are often payable during this period for accidental death only. Similar to other types of life insurance, the premiums are ongoing and often stepped. That is, they often increase as the consumer ages, although in some policies premiums cease after the person reaches a specified age.

The sum insured also usually automatically increases in line with CPI or a fixed amount, such as five per cent. The insured person can sometimes opt out of automatic sum insured increases, and premiums are not refundable if the insured person stops making payments or cancels the policy. As we will see from the case studies, this feature often means that consumers are hesitant to cancel funeral insurance policies as they may have already paid significant amounts of money for the policy and stand to lose it all if the policy is cancelled.

As at 30 June 2014, there were a total of 437,274 active funeral insurance policies covering 743,421 insured lives. In the 2014 financial year, there were a total of 12,648 funeral insurance claims accepted by insurers. Over 103 million was paid out in claims with an average payout of $8143. This was a significant increase on the previous year in which 61.6 million was paid out in total. The amount paid out by insurers was around 33 per cent of the value of premiums collected over the same period. In the 2013 financial year the value of claims paid was 20 per cent of premiums collected. During the 2014 financial year, a total of 72,091 funeral insurance policies were cancelled, representing a lapse rate of 16.5 per cent of total active policies. Notably, the rate of cancellations as a proportion of new policies was 80 per cent.

Nearly 65 per cent of cancellations were initiated by consumers, while in the remainder of cases the insurer cancelled the policy due to non-payment of premiums. About 16 per cent of cancellations occurred during a cooling-off period, which is often 30 days, while a further 39 per cent occurred during the remainder of the first year of the policy. About 55 per cent of cancellations, therefore, occurred during the first year. According to most insurers, the main reason for policy cancellations is the cost of the policy. Nearly two-thirds, 65.2 per cent, of active policies had been held for less than three years. Only 17.5 per cent had been held for five years or longer, with just 4.7 per cent held for longer than eight years.

ASIC has regulatory responsibility for the conduct and disclosure obligations of issuers of funeral insurance. ASICs investigations into the industry have found that people who bought funeral insurance generally found out about the product through television advertisements. People who bought funeral insurance generally selected from a small number of insurance providers. Most people with funeral insurance policies had not thought to calculate the total cost or to estimate likely costs under the policy. Most consumers held policies with stepped premiums where premiums increased as the person aged. Average annual premiums quadrupled for consumers aged over 50, rising from $336 from those aged 50 to 54 to $1344 for those aged 80 to 84.

Despite the overall decline in new policies between the 2013 and ’14 financial years, nine insurers reviewed by ASIC received a total of nearly 315 million in premiums for the 2014 financial year, an increase of about 9 per cent on the previous year. And, as I’ve indicated, ASIC found that most funerals cost somewhere between 4 and $15,000. For the policies reviewed, the average sum issued – sum insured was 8859. For new policies, the average sum insured rose to $10,631. Nearly 13 per cent, or 92,532 people, were covered for an amount in excess of $15,000.

The regulation of funeral insurance differs depending on whether the particular insurance product is a funeral life insurance product or a funeral expenses insurance product. Both funeral life insurance products and expenses insurance products are life policies under the Life Insurance Act. They are also contracts of life insurance under the Insurance Contracts Act. The consumer protection legislation in chapter 7 of the Corporations Act includes funeral life insurance as a financial product, but does not include funeral expenses insurance. Issuers of funeral life insurance products are, therefore, subject to the requirements imposed by chapter 7 of the Corporations Act, whereas issuers of funeral expenses insurance products are not.

Chapter 7 requires entities to act in certain ways when providing financial services pursuant to Australian financial services licences, including doing all things necessary to ensure that the financial services are provided efficiently, honestly and fairly, complying with the financial services laws, taking reasonable steps to ensure that their representatives comply with the financial services laws, maintaining the competence to provide financial services, ensuring that their representatives are properly trained and competent to provide the financial services, to have a dispute resolution system for services to a retail client, and to have arrangements for compensating retail clients for loss or damage suffered because of breaches to financial services law.

Funeral insurance products are also subject to the consumer protection regime contained in part 2, division 2 of the ASIC Act, although the applicability of this regime to funeral expenses insurance policies appears less than clear cut. ASIC has regulatory responsibility for the issuers of funeral insurance, but ASIC does not have a product intervention power. Therefore, if conduct is not misleading, ASIC does not have powers to prevent funeral insurance products from being sold in situations where consumers may pay more in insurance premiums over a long period than the benefit that will be available under the policy, or have to cancel a policy due to unaffordable premiums, despite having paid premiums over a long period, and potentially in excess of the benefit available under the policy.

Another topic that will be considered in the course of this round of hearings is bank fees. Fees are imposed by banks on customers in respect of a number of financial products, including loans, credit cards, and transaction or deposit accounts in accordance with the terms of those products. The focus in these hearings will be on fees that are imposed in relation to the terms of transaction or deposit accounts. Fees imposed on deposit accounts can include fees for use of an ATM of a different bank or provider, monthly account fees, overdrawn fees, and dishonour fees, which are fees payable when a direct debit from an account is unable to be completed. Some financial institutions offer an account which has low fees or no fees for customers.

Accounts with fee-free features are sometimes referred to as basic accounts. A basic account provides eligible customers with an account into which they can receive their government benefit payment, and access free banking transactions. Basic accounts might offer no account keeping fees, free monthly statements, no minimum deposit amounts, and no overdrawn fees. The Reserve Bank conducts an annual survey on bank fees which provides information on the fees earned by banks through their Australian operations. The 2016 survey, published in June last year, included 16 institutions, being 90 per cent of the Australian banking sector by balance sheet size.

Fee income from deposits for the 16 institutions in the 2016 financial year was $1,104 million down from $1,109 million in 2015. Banks reported that the decline in fee income was due to more fee waivers, reduced ATM charges owing to customers' increased use of contactless payments technology, and EFTPOS cash out options, and reduced balance inquiries arising from increased use of mobile banking applications. As we will see later in this opening, these developments often do not assist Aboriginal and Torres Strait Islander customers living in remote communities.

We turn to the regulation of bank accounts, and particularly transaction accounts. Bank practices are subject to a number of different, commonly overlapping legal regimes. These regimes include general or judge-made law, including contract law, the ASIC Act – which contains prohibitions against misleading or deceptive conduct, unconscionable conduct, and unfair contract terms – and the Australian Consumer Law in schedule 2 of the Competition and Consumer Act, which applies to the supply of goods and services to consumers. The practices of financial services entities in respect of transaction accounts, including the handling of informal overdrafts and fees, are also self-regulated by codes to which these entities are signatories.

As you have heard in previous hearings, the Code of Banking Practice contains guidance around industry standards. It is a voluntary code published by the ABA that has been adopted by most banks offering retail products in Australia. The ABA has also developed an Indigenous Statement of Commitment which outlines efforts to enhance financial inclusion, banking support, and access to basic bank accounts and services for indigenous consumers. The ABA released the first Indigenous Statement of Commitment in 2007, and it was revised in July 2015. The current version of the banking code was published in 2013. As you have heard previously, in December 2017, the ABA lodged the new draft banking Code of Practice with ASIC for approval. An updated version of the new draft code was provided to ASIC in April this year. We will refer to some of the relevant provisions in the new draft code shortly.

Since 2014, the code has included a general clause concerning customers in remote indigenous communities. Pursuant to clause 8, subscribers to the code are required to provide special assistance to members of these communities. This clause provides that if a consumer is a member of a remote and indigenous community subscribers must take reasonable steps to:

> *make information about banking services that may be relevant –*

to the consumer –

> *....available in an accessible manner.*

At the consumer's request:

> *…provide details of accounts which may be suitable to –*

the consumer's –

> *needs, including in a remote location. This information may include details of accounts which attract no or low standard fees and charges.*

To assist the consumer:

> *…with meeting identification requirements, having regard to the obligations of the bank under the anti-money Laundering and Counter-Terrorism Financing Act; appropriately train staff who are regularly dealing with –*

consumers –

> *in a remote location to be culturally aware.*

And to:

consider publicly announced key Commonwealth, state and territory government programs, such as income management programs that may be relevant in providing banking services to the consumer

A customer can refer an alleged code breach by a subscribing bank to an independent compliance monitoring body, the Code Compliance Monitoring Committee, or to the bank's external dispute resolution scheme, such as FOS, if the customer has suffered a loss and is not satisfied with the bank's internal dispute resolution. As we have noted, the Code of Banking Practice is currently in the process of being revised following an independent review which was completed in February last year. The independent reviewer was provided with examples of insufficient support for vulnerable customers, including Aboriginal and Torres Strait Islander people, and recommended broadening clause 8 to apply more generally to that group. That is, not necessarily only people living in remote communities.

The reviewer also recommended that clause 8 of the code be redrafted to make the obligations on signatory banks more meaningful and clearer. The draft code contains a new provision, clause 35, dealing specifically with Aboriginal and Torres Strait Islander people. Clause 35 requires that if a person tells the subscriber that they are an Aboriginal and Torres Strait Islander customer the subscriber will take reasonable steps to make information about their banking services accessible to them. They will also tell those customers about any accounts and services that are relevant to them, tell them about any accounts or services that have no or low standard fees, and help them meet any identification requirements.

The draft code also contains clauses requiring subscribers to raise awareness of the basic – that is, low or no fee – banking products that they may offer, to take reasonable steps to make information about banking services accessible to customers in remote communities, including remote indigenous communities, to provide cultural awareness training to staff who regularly assist customers in remote indigenous communities, and to train their staff to treat diverse and vulnerable customers with sensitivity, respect, and compassion.

A further topic that we will explore in the case studies is in formal overdrafts. An overdraft is an arrangement that allows a person to withdraw more funds than they have in their account. There are two types of overdraft: one being an arranged or formal overdraft, and the other an unarranged or informal overdraft. An arranged overdraft is a credit facility connected to a bank, building society, or credit account which a person applies for or which may be given to a person as part of the account. In contrast, an unarranged or informal overdraft occurs if a person makes a payment but there are insufficient funds in the person's bank account to cover it. In that circumstance, where the person's bank honours the payment anyway, this creates a debt.

While financial services entities have different policies in relation to unarranged overdrafts, many cheque or savings accounts permit some form of unarranged overdraft to take place. Penalties fees for exceeding a person's available balance can be anywhere from 10 to $30. Some banks do not charge a penalty fee, but impose a penalty interest rate on the overdrawn amount. Unlike formal credit products, the amount overdrawn plus the penalty fee is usually repayable immediately.

The Department of Human Services, the Department of Veterans Affairs, and representative bodies have developed and endorsed a code of operation that applies to the recovery of debts from a person receiving an income support payment or Veterans Affairs payment. The code of operation applies to the recovery of debts that arise from customers' accounts where no repayment arrangement already exists, and applies to bank practices in respect of informal overdrafts. The code of operation is endorsed by the ABA for member banks, and is a non-legally binding statement of best practice between the Department of Human Services, the Department of Veterans Affairs, and the representative bodies on behalf of relevant ADI members.

Pursuant to the code of operation, the default position is that a customer should be able to retain at least 90 per cent of their income support payment or veterans affairs payments in any fortnightly period. Where the ADI is unable to contact the customer about the debt, the maximum repayment amount that may be deducted from the customer's fortnightly payment will be the amount equal to 10 per cent of that fortnightly payment. If the ADI does not contact the customer, or is unsuccessful after reasonable efforts have been made, the ADI may determine a deduction amount that is no more than 10 per cent of the customer's fortnightly payment.

Alternatively, an ADI may freeze the account in cases where reasonable efforts to contact the customer or their authorised agent have been unsuccessful. A frozen account must be reinstated as soon as the customer makes contact to arrange for the repayment of the debt. The ADI may contact the customer, or vice versa, and negotiate a payment arrangement for any amount agreed between them, subject to the following. The ADI will not require repayments that are greater than 10 per cent of the customer's fortnightly income support payment or Veterans Affairs payment without first establishing that a higher amount is reasonable and appropriate in the customer's circumstances.

When considering if a repayment amount of greater than 10 per cent of the customer's fortnightly payment is reasonable and appropriate, the ADI may consider factors including the customer's needs, taking into account that the intent of income support payments is to ensure access to essential items such as basic food and shelter, and the need to maintain this for welfare recipients. The ADI may also consider any prior deductions from the customer's income support payment or Veterans Affairs payment and, where a debt exceeds the usual payment being credited to the customer's account the ADI will consider, in accordance with this code, future payments as recovery of the debt. And finally, they may consider any other special circumstances which may impact on a customer's ability to repay the debt.

Having determined an appropriate amount for repayment, the ADI will deduct that amount from each fortnightly payment made to the customer by Human Services or

Veterans Affairs until the debt is paid. An arrangement between an ADI and a customer in respect of repayment of debts will be recorded by the ADI. The record will also include details of any disagreement between the customer and the ADI, and the advice given to the customer on his or her rights and further avenues for resolution of the disagreement. A customer, or their authorised agent, is able to request a copy of the repayment arrangement. And that the ADI reviews the repayment arrangement should the circumstances of the customer change.

Where a customer believes that their ADI has not complied with the code of operation, they can invoke the internal dispute resolution process of the ADI, and if the dispute cannot be resolved to the customer's satisfaction by their ADI, they can take their complaint to an external dispute resolution scheme of which the ADI is a member. We will see in these hearings that the code of operation is important for some Aboriginal and Torres Strait Islander people who receive income support payments. In some circumstances Aboriginal and Torres Strait Islander people may not have understood that they had an overdraft facility and the terms on which it was provided.

We turn to the information provided to the Commission by financial services entities about their services and practices relating to their Aboriginal and Torres Strait Islander customers. In response to a letter from the Commissioner asking financial services entities to identify cases of misconduct and conduct practices, behaviour or activity that has fallen below community standards and expectations, only a small number of entities disclosed conduct relating to Aboriginal and Torres Strait Islander people. This may, in part, be because financial services entities do not generally collect information about whether their customers identify as Aboriginal and Torres Strait Islander people.

We will summarise some aspects of the responses and statements received from the entities in respect of their interactions with Aboriginal and Torres Strait Islander people. We start with ANZ. ANZ provided two statements to the Commission from Tony Tapsall, general manager retail branch network northern Queensland and the Northern Territory. ANZ told the Commission that it operates branches and agencies in 19 remote communities in Australia and that it does not generally record the race or ethnicity of its customers. ANZ told the Commission about its operations on Groote Eylandt, where ANZ has an agency and operates a 24 hour ANZ fee-free ATM. ANZ offers a fee-free everyday transaction account to customers receiving certain government benefits, called an ANZ Access Basic account. This is an account commonly used by customers living on Groote Eylandt.

ANZ told the Commission that it offers two formal overdraft facilities. ANZ Assured and ANZ Personal Overdrafts. Informal overdraft arrangements are available on a variety of ANZ retail transaction accounts. ANZ told the Commission that in response to the code of operation applicable to the recovery of debts it has implemented what are known as "90 per cent arrangements" which are available to ANZ customers who receive specified payments from Human Services or Veterans Affairs into an ANZ transaction account. The key features of the 90 per cent arrangements are ANZ can apply no more than 10 per cent of the payments to reduce the overdrawn amount, including related fees and interest, with the consequence that the customer is able to withdraw the remaining 90 per cent; the customer can only withdraw funds over the counter at a branch or agency; any interest and fees applied to the overdrawn amount may be reversed; and, once the overdrawn amount is repaid, these arrangements are removed.

ANZ told the Commission that if a staff member becomes aware that a customer with an overdrawn account was receiving specified payments from Human Services or Veterans Affairs, the staff member will generally suggest to the customer that the 90 per cent arrangements be put in place on their account. Mr Tapsall will give evidence in the Commission this week about informal overdrafts, and about ANZs low fee and fee-free accounts.

We turn to Bendigo and Adelaide Bank, which we will refer to as Bendigo Bank. Bendigo Bank have provided a statement from Robert Musgrove, the executive engagement innovation at Bendigo Bank. Bendigo Bank told the Commission that it has many customers living in regional and remote communities, including Aboriginal and Torres Strait Islander customers. However, the bank does not collect data from its customers that identifies whether or not they are Aboriginal and Torres Strait Islander people. Bendigo Bank operates 608 branches, including community bank branches and agencies, and 720 ATMs across Australia. Of these, 374 branches and agencies, and 358 ATMs, are located in regional and remote communities.

Bendigo Bank told the Commission that since 2012 it has been a participant in the fee-free ATMs in remote indigenous communities initiative, facilitated by the ABA. Bendigo Bank told the Commission that it has certain practices or procedures by which it may refrain from applying fees and charges. For example, where a requested direct debit transaction would put an account with no overdraft facility into a debit balance which is sufficiently small, the bank will often allow the transaction to proceed with no overdrawn fee. By way of further example, where an account incurs a dishonour fee as a result of having had insufficient funds to enable a requested direct debit to be transacted, and the dishonour fee then causes the account to become overdrawn, it is the bank’s practice not to apply an overdrawn account fee in addition to the dishonour fee. In his statement, Mr Musgrove responded to the situation of a particular Bendigo Bank customer who had repeatedly been charged overdrawn fees of $21.50, and dishonour fees of $40, over a period of time.

We turn next to CBA. CBA has provided a statement from Sian Lewis, executive general manager, direct channels, within retail banking services of CBA. CBA told the Commission about its indigenous customer assistance line or ICAL. ICALs purpose is to provide support to geographically isolated Aboriginal and Torres Strait Islander customers who would otherwise not be able to access a CBA branch or online services to conduct their day-to-day banking. ICAL provides free balance inquiries, replacement cards, access to funds, and general support to assist customers with their banking requirements. ICAL employs a specialised identification process for remote customers to enable the delivery of account opening and other services. CBA currently supports 90 remote communities through its ICAL service.

In 2009, CBA identified that remote customers were relying on third party owned ATMs to retrieve their account balances and were incurring significant fees from those providers as a result. CBA launched ICAL on 25 May 2009. To address the fees associated with account balances, the launch of ICAL was focused around educating customers to telephone for their account balance rather than using ATMs. CBA told the Commission that customers have access to ATM services in remote communities through the ATM fee-free agreement, which has been operating since May 2012.

CBA recently identified that there have been instances where CBA customers incurred fees using the ATMs owned and operated by third parties under the ATM fee-free agreement. CBA told the Commission that it is working to identify the number of customers affected, that it will ensure the fees are refunded, and that it will continue to work with the ABA and third party ATM providers to ensure this does not happen again. CBA also told the Commission that financial assistance centres in remote indigenous communities had raised concerns with ASIC in relation to the difficulties that some customers had faced completing the identification process. CBA told the Commission that it is working on ways to overcome these difficulties and encourage further engagement.

We turn next to the Traditional Credit Union or TCU. TCU is an unlisted public company, limited by shares, registered under the Corporations Act. TCU provided a statement from Anthony Hampton, its chief executive officer. TCU told the Commission that it has branches in 14 remote communities in the Northern Territory, in addition to branches in Darwin, Katherine and Alice Springs. It owns and operates 31 ATMs across the territory which are mainly located at remote communities where there is a TCU branch. In 2017, 80 per cent of its members lived in remote communities. The vast majority of TCU members living in these communities are Aboriginal and Torres Strait Islander people.

TCU told the Commission that its business model is fundamentally different from that of other ADIs, because TCU relies on fee income rather than interest income. TCUs net interest income is very small compared to its transaction and account fee income. TCUs low net interest income means there is little capacity for TCU to cross-subsidise branch and ATM networks. Because of this, TCUs transaction fees and charges are relatively high compared to those of other ADIs. For example, TCU told the Commission that it charges a weekly account service fee of $5 for an everyday account, and a monthly account fee of $10 for a budget account and a loan saving account. A cash withdrawal fee of $5 per withdrawal is charged for cash withdrawals at a branch in relation to certain accounts. TCU charges members an overdrawn account fee of $20, and $30 for the dishonour of a direct debit or cheque. TCU members are not charged a fee for cash withdrawals or for checking an account balance from TCU owned ATMs.

We turn finally to Westpac. Westpac provided a submission to the Commission in which it acknowledged that ASIC had raised concerns in 2015 about its provision of car loans to two indigenous customers in remote communities. Westpac considered that these loans were unsuitable for the customers and should not have been approved. The loans were entered into in around February 2010 and July 2012 by Capital Finance Australia Limited prior to it being acquired by Westpac in December 2013. Westpac was of the view that the identified conduct, at least in part, could be attributed to insufficient control over the implementation of policy, process, or changes to policy or process by third parties.

Westpac waived all amounts owing under the loans and ensured that neither customer had a default listing against their name in respect of the loans. Westpac told the Commission that it has undertaken a review of a sample of regional accounts in a serious arrears position to identify any car finance responsible lending issues. In addition to receiving and analysing the submissions and statements received from these and other entities, the Commission issued 43 notices to produce documents to 18 entities. These notices yielded close to 17,000 documents about various aspects of financial services entities practices, procedures and conduct, both generally and in particular cases.

We turn now to the particular case studies through which the conduct of financial services entities in relation to Aboriginal and Torres Strait Islander people will be addressed. The first case study will examine the conduct of the Aboriginal Community Benefit Fund with respect to funeral insurance plans that it offers to customers throughout Australia, including Aboriginal and Torres Strait Islander customers. The Commission will hear evidence from Tracey Walsh, an Aboriginal woman, about her dealings with ACBF both prior to and following her signing up for an ACBF plan. The Commission will also hear evidence from Bryn Jones, a current director of ACBF.

The second case study will examine the practices of Select AFSL in selling funeral insurance to Aboriginal and Torres Strait Islander Australians. The Commission will hear evidence from Kathy Marika, a Yolngu woman who grew up in north-eastern Arnhem Land about her experience in being sold funeral insurance policies which she did not understand and could not afford, and her experience in respect of the referral sales program in use by Select at that time.

The third case study will examine the conduct of ANZ in connection with the fee-free and low fee accounts it offers to customers living in remote communities, including Aboriginal and Torres Strait Islander customers. The Commission will hear evidence from Thy Do, a senior family support worker at Save The Children. Ms Do will explain the difficulties experienced by one of her clients, an Aboriginal woman from a remote community, when trying to open a no-fee account at the Katherine ANZ branch.

The final case study will examine the conduct of ANZ in connection with the provision of formal and informal overdrafts to customers living in remote communities, including Aboriginal and Torres Strait Islander customers. The Commission will hear evidence from Mr Phil Bowden, a financial counsellor at Anglicare Northern Territory, about Aboriginal and Torres Strait Islander customers who have been granted overdrafts by ANZ. As we have already indicated, the Commission will also hear evidence from Tony Tapsall, the general manager, Retail Branch Network, northern Queensland and Northern Territory.

Commissioner, tomorrow morning, before moving to these case studies, we intend to call two witnesses with experience working with Aboriginal and Torres Strait Islander people in remote and regional communities. Those witnesses are Mrs Lynda Edwards of Financial Counselling Australia, and Mr Nathan Boyle of ASIC. That concludes the opening statement, Commissioner.

THE COMMISSIONER: Thank you very much, Ms Orr. What time tomorrow?

MS ORR: 10 o'clock should be fine, thank you, Commissioner. I hope.

THE COMMISSIONER: We're going soft in the Territory, are we, Ms Orr? 10 o'clock it is, then.

MS ORR: Thank you, Commissioner.

MATTER ADJOURNED at 4.19 pm UNTIL TUESDAY, 3 JULY 2018

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