A Submission to:

1. **The Productivity Commission Inquiry: Business Set-up, Transfer and Closure;**

2. **The Parliamentary Joint Committee on Corporations and Financial Services Inquiry into the Impairment of Customer Loans.**

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1.0 Overview

My three submissions enclosed focus on the interaction between Australian Banks and the Small and Medium Enterprise (SME) sector of the Australian economy. Australia needs strong banks and nobody would dispute this fact. Australia equally needs a healthy SME sector.

The recommendations I make in this submission are not intended to weaken our banking sector. On the contrary, our banking sector must remain strong and robust. The recommendations are however intended to strengthen the SME sector. Logically it follows that if Australia has a stronger and more dynamic SME sector that is increasingly productive, generating growth and increasing employment, then the banking sector will also benefit.

However, in recent years and decades the Australian banks and their solicitors have perfected the banks' loan documentation used for their commercial loans. The result of this is that an SME is unable to resist the will of a bank even in a court of law. This reality leaves the very existence of an individual business in the hands of a banker who on a whim can default a commercial loan and destroy that business. The directors of that business, the entrepreneurs of Australia, mothers, fathers, husbands and wives face total emotional and financial devastation at the whim of a banker and these entrepreneurial Australians have absolutely no defense.

These statements that I am making are not exaggerated. The sad fact is that what I have described above is absolutely true.

My philosophical position on these matters is quite simple. When the director of an Australian small or medium sized business goes to bed at night that director ought to be able to sleep soundly with the knowledge that when he or she wakes in the morning their commercial bank loan is still in place provided the interest payments have been made. In my view this basic fundamental position should be non-negotiable. This is how it is in the USA.

My first submission has already been provided to the Productivity Commission. However, I have modified and augmented it. Accordingly I would ask the Commissioners to review it with this in mind.

Please read my submissions where I discuss these matters in depth.

2.0 Recommended Reforms to Australia's Current Insolvency Regime

In order to prevent an insolvency event being manufactured by a bank, described by Hon Philip Ruddock MP as a "Constructive Default", I recommend:

1. If a client is paying interest on the loan, at the non-default rate, then under no circumstances should the bank be able to default the loan.
2. Six months prior to the expiration of a loan the bank must give notice that the loan will be required to be repaid on the due date. If notice is not given, then the loan continues until the 6-month notice is given.
3. If the secured creditor alleges that a monetary default has occurred and wants to default the loan, then this should be referred to a third party. This party should have the power to allow the borrower to rectify the default if possible and if not, then confirm the default.

When a genuine insolvency event does occur, I recommend;

1. Insolvent trading laws should not apply to SMEs.
2. A 'debtor in possession' voluntary administration model should be available for businesses to use to restructure.
3. Protection from secured creditors should be available during the restructuring process.
4. The hierarchy of securities mentioned earlier should apply.
5. There should be no bankruptcy period for company directors following the insolvency event provided always that the director has acted honestly.
6. Company directors should be able to retain certain assets that will enable them to recover and regroup and encourage them to try again.
7. Any assets sold by a liquidator should be sold by way of a public auction. Sale of assets by way of private treaty is currently permissible. This should be prohibited.

Personal Guarantees, I recommend:

1. Personal guarantees by a third party and directors' guarantees should only be available to a secured creditor to the extent of assets listed in the guarantee. In this respect the assets listed will form part of the security for the loan.

3.0 Submission No. 1 to the Draft Productivity Commission Report: Business Set-up, Transfer and Closure

24 June 2015

Points of discussion for the meeting on 30 July 2015

3.1 Introduction

My main interest in this report is to see meaningful reforms introduced into the insolvency industry. The catalyst for my interest was the appointment of receivers to one of my companies by a bank in 2013. The bank had no justification to do so other than it wanted to close down a particular fund that had been established pre GFC. I can provide more details at the meeting.

Through my research and meetings with politicians over the last 2 years, I have become familiar with a large number of business people who had their loans defaulted and as directors were bankrupted by the CBA and Bankwest, following the purchase of Bankwest by the CBA from HBOS in December 2008. I was just an observer and not a victim. It would seem that there were somewhere between 500 and 1000 commercial loans affected, and according to CBA records, may have been an average size of $8 million each. These figures will be confirmed during the upcoming PJC Inquiry into the Impairment of Customer Loans. Philip Ruddock, who you will recall was Australia's Attorney General under John Howard, has joined the PJC.

I have personal impact statements from about 100 of these victims and it would seem that the vast majority of them were paying the interest on their loans. Nevertheless, the loans were called in, assets sold and the directors bankrupted. Philip Ruddock has coined the term ***"constructive default"*** to describe this type of behavior by the banks.

My simple proposition is that this behavior by the banks is unacceptable. I discussed this issue with David Murray following my submission to the FSI. My submission and discussions with David Murray may have contributed to his recommendations 34 and 36 in the final report.

Your draft report is very comprehensive and useful. There are many subjects that I would like to discuss with you. However, I will make the following points and elaborate next Tuesday.

3.2 Protection from the Secured Creditor

The report discusses at length the insolvency process. I agree that the whole process needs reform. One of my objectives is to find a way to prevent companies falling into insolvency in the first place. The best way to keep a business alive is to prevent the bank, the secured creditor, from appointing receivers for their own commercial gain. If we can do this, then a large part of the problem would be fixed. In every case of which I am aware, it has been the secured creditor, the bank that has appointed the receiver. We can solve this problem by legislating to achieve the objectives of the following 3 points. You will find that these points are all very reasonable. The banks will have a different view.

1. If a client is paying interest on the loan, at the non-default rate, then under no circumstances should the bank be able to default the loan.
2. Six months prior to the expiration of a loan, the bank must give notice that the loan will be required to be repaid on the due date. If notice is not given, then the loan continues until the 6-month notice is given.
3. If the secured creditor alleges that a monetary default has occurred and wants to default the loan, then this should be referred to a third party. This third party should have the power to allow the borrower to rectify the default if possible and if not, then confirm the default.

Your report mentioned that Chapter 11 did not have a high success rate in saving companies. You need to remember that because of Chapter 11, secured creditors cannot appoint receivers at their sole discretion. This fact alone would have prevented the vast majority the CBA/Bankwest clients from having receivers appointed. Therefore the Chapter 11 data quoted in the report would reflect companies that are likely to be in genuine financial difficulty and accordingly, not all can be saved.

There are many aspects of Chapter 11 and Chapter 7 that I believe Australia should adopt.

3.3 Bankruptcy

I have been bankrupt so I can speak with some knowledge. I was bankrupted in the early 1990’s following the recession at the end of the Keating Government. My wife and I lost virtually everything and were left to start again with five dependent children. Prior to this my brother and I owned a manufacturing business employing over 100 staff.

Our current system adopts a penal approach. Your draft report discusses the need to ensure bankrupted individuals meet their responsibilities, are prevented from doing certain things like being a director or manager of a company, travelling abroad without permission and the like.

My comments here generally refer to company directors who have been bankrupted due to personal guarantees provided to banks. These directors are the typical victims of the Bankwest/ CBA event. The current impairments by the ANZ bank against the legacy loans of the Landmark loan book, purchased by the ANZ, are creating similar victims. There have been two recent segments on the Chanel 9 program 60 Minutes, investigating specific cases.

So who are these terrible people these ex-company directors and who are now bankrupt and need to be punished? Have you ever met one? If you associate with professional people like solicitors, teachers, surgeons, dentists, doctors and public servants then chances are that you may have never met a bankrupt person or a discharged bankrupt person. While these professions are extremely important, people in these professions are generally not entrepreneurs. These bankrupt ex-company directors are business people.

They have often built their own business and are an important part of this country's entrepreneurial group and they are vital to our economy.

So what are the sins of these people who need to be treated so harshly? These people are guilty of doing exactly what our Prime Minister and your minister, the Treasurer, have just implored us all to do. To get out there and have a go, borrow money. That is exactly what he said. These people, the entrepreneurs of this country are those of us who mortgage our homes, sign personal guarantees, put all our assets and savings on the line and we employ people, we take on contracts, we buy stock and we buy equipment. We generate the growth and the wealth for all Australians. Sometimes we make mistakes, particularly when we are young and inexperienced. Sometimes we encounter events that are not of our doing and out of our control, like the GFC or the recession that occurred at the end of the Keating period.

And how does Australia and Australian law treat these people if things go wrong? We treat them dreadfully. We treat them as though they are criminals or at least potential criminals, and restrict their activities accordingly. My wife and I battled through the 3 years of "purgatory" following my bankruptcy hoping that my trustee would not extend my bankruptcy to 5 or 8 years at his sole discretion. We did everything in my wife's name and pretended that I was the principle caregiver to our children. We worked extremely long hours and reestablished ourselves financially. But you must realize that we are the exception to the rule. Generally bankruptcy will destroy marriages and families and destroy any motivation to try again. It is totally and completely soul destroying.

If you are wondering what it may feel like to go bankrupt, contemplate this scenario. After lunch your employer tells you that you are being sacked for suspected fraud, even though you are innocent. You are told to leave the building and that you will be receiving no severance pay or accumulated holiday pay. You must leave with nothing. When you arrive home your spouse greets you in tears because a bank has taken possession of your house and all its contents and changed the locks to deny you access. You are not even allowed access to recover your personal possessions. You had given a personal guarantee to the bank to help a friend and the friends business failed. On top of this the bank that held the personal guarantee has also emptied your bank accounts so you have no money.

Welcome to the world of those of us who have had to start again. This is just the beginning of the nightmare. The bank will bankrupt you and your 3 years of punishment is about to commence.

We need to develop and enshrine in law a new attitude and approach that demonstrates far more respect for the entrepreneurs of our country. If they make a mistake, they need to be encouraged to try again. We are all the wiser and do better the second time. More importantly, as previously stated, often businesses fail through no fault of the entrepreneur. Look at the current case of the home insulation industry. This is currently being reviewed. How many businesses failed and company directors were bankrupted because of reckless decisions made by the then federal government early in the period of the GFC.

So, how do we currently treat our entrepreneurs when things go wrong? We:

1. Take all their assets.
2. Let them keep a car provided it is not worth more than $7,500.
3. Appoint a trustee, a bit like a probation officer, to make sure the bankrupt person does not go out and earn too much money or start in business or even manage a business again for 3 years.
4. If they earn more than $53,000 per annum, then they need to give some to their trustee who generally gives it to a bank.
5. Threaten to increase the bankruptcy period for up to 8 years if the trustee so chooses in his sole discretion.
6. Take their passports and have these people go 'cap in hand' to the trustee in bankruptcy and ask permission to travel.

3.4 Directors' Guarantees and Asset Siphoning

In my view, the comments in the report on this subject are misguided. The report states that *"some business owners siphon their assets to related entities such as family members".* This all relates to the issue of directors' guarantees and this matter needs immediate reform.

Directors' guarantees are generally given to banks or financial institutions, although they can also be given to other creditors. However, more experienced directors do not have other assets and very rarely provide personal guarantees to unsecured creditors. Other limited forms of security such as bank guarantees are available. In any event, the personal guarantee is useless to the unsecured creditor, once a receiver is appointed. At this time you can be sure that the receiver will find that there is nothing left for the unsecured creditors, once he has paid the secured creditor and himself.

The main issue is how a bank uses a director's guarantee. In the SME area, a bank will not provide a loan without a personal guarantee from all directors. The banks use these guarantees to vacuum up all the directors' assets and to bankrupt the directors, in the event the bank defaults the loan. This process must be stopped.

The fundamental problem is that currently a director's guarantee is not limited and it should be. At the time the loan is written the bank should advise the client:

1. The amount of the loan
2. The term of the loan
3. The loan to value ratio (LVR) they require
4. The interest rate they require

If a director's guarantee is required it should be limited and linked to the LVR. For example, if the bank will provide a loan with an LVR of 65% of the secured asset, then why is a director's guarantee required to provide additional security? If the value of the property is inadequate it terms of security then a limited director's guarantee could be provided for the balance, but it must be limited.

It must be remembered that the company is the borrowing entity and accordingly the company is directly liable for the loan as well.

My strong recommendation is that by law, ***a director's guarantee must be limited to a list of specific assets and not used as a 'catch all' by the banks.***

3.5 Chapter 11 and the Debtor in Possession Work Out Model.

I am very surprised to see the comment in the report that suggests, ***"almost all businesses get an extended opportunity to succeed before an insolvency appointment occurs.***" This comment implies a reality that is the exact opposite of what actually happens, based upon my knowledge and experiences.

In our meeting I will bring along 100 personal impact statements where the bank has appointed receivers with no discussion of restructure or refinancing with another institution, even though interest payments were being met. I will also discuss with you my two personal experiences.

In my view, any "work out" model where an external administrator is appointed will be ineffective. The business will be in the hands of the insolvency industry and the current situation will be maintained. The insolvency practitioner will look after the interests of his appointer first and foremost, and then consume in fees any surplus funds and leave the unsecured creditors unsatisfied.

The 'debtor in possession' model contained in Chapter 11 of the USA Bankruptcy Code is by far a superior model, and should be considered seriously.

3.6 Insolvent Trading

The problem with insolvent trading is that it is the insolvency industry that is there on the spot to make the claim of insolvent trading. They control the business and it is impossible for the directors "in exile" to obtain any financial information from the receiver. As all the assets of the director have been seized, the director is in a position where he cannot dispute the allegations of the receiver. Furthermore as the receiver has taken control of his bank accounts and taken the money, financially he is destitute and hardly in a position to fight the bank funded receiver.

Moreover, generally insolvency is based on a valuation of the assets of the business. All the receiver needs to do is ask his friendly valuer, to whom he regularly feeds work, to provide an appropriate valuation, and there you have it, insolvent trading. As an example, I will show you documents relating to the receivership of Colin Power's hotel. Colin is a victim of Bankwest/CBA.

The whole idea of a safe harbour for directors may well work for public companies, with independent directors and deep pockets.

However in relation to SMEs, I have a similar view to McGrathNicol, however for different reasons. I believe that SMEs do fear insolvent trading however their determination to succeed and pull through a difficult patch is stronger than the fear. These people are often fighting to save a lifetime's worth of work and all the assets of their family. Their greatest fear is losing everything and having to start again with nothing, when they could well in their later years. They will do whatever it takes to avoid failure. This is a good thing and for this reason I would advocate that insolvent trading laws should only apply to publically listed companies.

In the case of Colin Power and his hotel, he explained to me that he was meeting his interest payments in the early days of the GFC by laying off most of his staff and having his wife and 2 teenage children as well as himself, working behind the bar. This is what entrepreneurs do when things get tough. It didn't help, the CBA appointed a receiver who sold the hotel to the Director of Landmark White, Bruce McPherson, who did the valuations, at half the valuation price, by private treaty. I have all the documents. Colin is now living in the garage of a friend's home, his marriage has collapsed and he is driving a semi-trailer up and down the east coast. He is in regular contact with Senator Williams and will give evidence at the PJC.

I will repeat that earlier statement. The liquidator sold the hotel to the director of the valuation company Landmark White, Bruce McPherson, who carried out and signed the valuation for the liquidator. The sale price was half the value of the most recent valuation. The sale was by way of private treaty not auction.

3.7 Sale of Assets

Liquidators should not be able to sell assets under their control by private treaty. All assets should go to auction with a significant auction program. My understanding is that this is a requirement in the USA.

I look forward to discussing this further at our meeting on Tuesday next.

Kind Regards

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4.0 Submission No. 2 to the Draft Productivity Commission Report: Business Set-up, Transfer and Closure

6 July 2015

4.1 Introduction

Please accept my second submission to the Productivity Commission on the above mention subject. I make this submission to expand on the matters discussed in my first submission and also to comment on some of the matters raised at the public hearing in Sydney on 30 June 2015.

4.2 My area of Interest

My comments and suggestions relate to SMEs. This is where I have had considerable experience and where I believe that there is a need for substantial reform. Generally the businesses that I refer to are incorporated businesses where the principals provide company charges and personal guarantees to their secured creditors.

4.3 Consultation process for this Productivity Commission Report

I am a little concerned in relation to the public consultation process in relation to this inquiry. It was only by chance that I became aware of it three weeks ago. I immediately contacted the Commission. I prepared a brief submission, sent it to the Commission and then addressed the Commission at the public hearing on Tuesday 30 June.

I am surprised that I was not aware of the inquiry, as I have been actively involved in lobbying for reform in the area of "business closure" for the last three years. I have written and delivered a paper on this topic to the Menzies Research Center. I have written a paper titled *" A case for a Royal Commission to investigate the reason for the purchase of Bankwest by the CBA and the resultant impact on the stakeholders"* for the Minister of Finance, Senator Corman and discussed it with him. I have met with and discussed the problems of bankruptcy, insolvency and the imbalance of power between the banks and SMEs with many Ministers, Senators and Members of Parliament. I was instrumental in helping to establish the upcoming Parliamentary Joint Committee (PJC) for Corporations and Financial services inquiry into the Impairment of Customer Loans.

4.4 100 Personal Impact Statements

Following the public hearing, I presented to the Commission a bundle of personal impact statements from approximately 100 people whose lives and businesses were destroyed by the actions of the CBA when it defaulted loans from the Bankwest loan book. This is only a small fraction of the total number of people who had their loans defaulted in the immediate period following the purchase of Bankwest by the CBA. The vast majority of these loans were classified as “performing loans” with an average size of $8m, in the 2010 Results Presentation by the then CEO, Ralph Norris. I will submit this document in my Submission No 3.

I would urge the Commissioners to read these personal impact statements.

I would also urge the Commissioners to review the submissions made to the 2012 Senate Enquiry, titled *Effects of the global financial crisis on the Australian banking sector.* There were 158 submissions and the vast majority was from those who had their loans defaulted by Bankwest following the purchase of Bankwest by the CBA.

4.5 Comments on Matters Raised in the Sydney Public Hearing.

4.5.1 Conduct of the Banks

Without going over the material covered in my first submission, I will state again that without doubt the biggest cause of business insolvencies is the secured creditor, the bank, defaulting the loan. On face value this looks legitimate, however on deeper and closer examination one will find that the banks in Australia default loans when clients have been meeting and continue to meet their monetary obligations.

The question is then, is this behavior acceptable and should we allow this behavior to continue? **In America this cannot and does not happen.**

At the hearing it was suggested that in recent times the banks have had an “epiphany”. They now realise the error of their ways and that in fact the banks now realise that it is in all the parties’ best interests for the banks to work with their clients when a client is in financial difficulty. This is simply the banks’ spin-doctors endeavoring to cover up and gloss over the unconscionable conduct which the banks have been inflicting on their SME clients. We are talking about banks that have hundreds of years of experience lending funds to businesses. How is it possible that they would all wake up one morning and together decide that from now on we will not call in commercial loans?

In my experience the banks do work with their business clients if it suits them at that time. However, while they are allegedly working with them, they are charging exorbitant penalty interest rates and even in today’s low interest rate environment, it would not be uncommon for a bank to be charging in excess of 15 % penalty rates. In fact when the banks are allegedly working with an SME client, they are in fact gouging from their client with unjustified penalty interest rates.

However, when a bank decides that it would be in the bank’s best interest to default a performing loan, that is exactly what it will do. The banks have a history of acting in a way to maximise their own bottom line and the returns to their shareholders. On face value this would also seem a reasonable and responsible thing to do. However, when one looks at the contracts signed between a commercial borrower and a bank, it is clear that the bank has given itself the ultimate power to call in a loan at any time it so chooses.

In recent history there are many examples when banks have conducted mass defaults against SME clients because it suited their own commercial interests. For example,

1. The 1990-1992 recession. Foreign banks were given licenses to operate in Australia in the late 1980s. The competition resulted in banks' lending recklessly, which contributed to the recession *"we had to have".* The banks reaction was to extensively default loans because the contract terms enabled them to do so.
2. In the late 1990s some banks decided that they were "overweight" in property. Many viable loans were defaulted at that time.
3. When the CBA purchased Colonial State Bank it appears that loans were defaulted because of a warranty provision in the purchase agreement that enabled the CBA to reduce the purchase price by the value of any loan impairments. Evidence will be given in this respect at the upcoming JPC Inquiry.
4. The GFC event and in particular the many hundreds of commercial loans defaulted by Bankwest as already discussed. Evidence will be given at the upcoming JPC Inquiry of a similar warranty agreement.
5. The ANZ bank is currently defaulting performing loans that it acquired when it purchased the 10,000 loans that formed the Landmark loan book.

You may recall that at the public hearing I showed the Commission a 53 page document that was a part of a bank's commercial loan document. **These 53 pages were the default conditions.** They included positive undertakings, negative undertakings, conditions of default and common provisions. These 53 pages are nothing more than a long winded way of the bank saying, *"It is irrelevant what the terms and conditions of the loan are. We write the contract, we make the rules. We will demand the repayment of the loan at any time we choose."*

The banks and their solicitors have perfected their documents to such a degree that it is impossible for an SME client to challenge the bank in a court of law regardless of how substantial the client may be. Please refer to the examples of Rory O'Brien and Luke Saraceni in Appendix D. I know this for a fact because I have tried to do so. My solicitor and SC both advised me that I could not possibly win against the banks contract terms. These contracts have now become so unbalanced that they now only provide obligations to one party, and that is the borrower. In the example mentioned above there are 53 pages of obligations on the borrower. The lender has no obligations.

If a bank decides to default a loan and take possession of a secured asset, it can do so at its sole discretion. As one member of the current PJC for Corporations and Financial Services said to me, *"the process is totally unregulated"*

One needs to remember the following:

1. The bank writes the loan documentation. While competition allows some negotiation with the interest rate, in practice, the terms of the loan are non-negotiable.
2. The bank interprets the terms of the loan document.
3. The bank makes the decision to default the loan and instructs its solicitors to do so.
4. The bank's solicitor appoints the receiver.
5. The bank decides which security to enforce first, be it the secured asset, the assets of the borrowing entity or the guarantee of the director.
6. The bank decides when and if to bankrupt the director. When I was bankrupted, I was told that it was bank policy to always bankrupt the director.

This all takes place without the need of referral to any third party, so the process is totally unregulated.

In summary, in my experience, every case of insolvency of which I am aware was the result of a bank defaulting a loan. If the commission is looking for a way to prevent viable SMEs from being destroyed then the power of the banks needs to be considered. In my view the only way to protect SMEs from the inappropriate use of the extraordinary power of the banks, is by legislation.

Therefore, I restate the principles mentioned in my first submission,

1. If a client is paying interest on the loan, at the non-default rate, then under no circumstances should the bank be able to default the loan.
2. Six months prior to the expiration of a loan the bank must give notice that the loan will be required to be repaid on the due date. If notice is not given, then the loan continues until the 6-month notice is given.
3. If the secured creditor alleges that a monetary default has occurred and wants to default the loan, then this should be referred to a third party. This party should have the power to allow the borrower to rectify the default if possible and if not, then confirm the default.

4.5.2 Insolvent Trading

The representatives from the Law Society spoke about insolvent trading. They referred to large public companies such as Centro Properties and Fortesque. They also spoke about independent company directors who were quick to appoint a voluntary administrator (VA) to protect themselves from claims against themselves for insolvent trading. This behaviour is understandable as these directors are probably not the founders or owners of the company and would like to wash their hands of any involvement if the company was to fail. This is not my area of expertise so I won't comment on a solution to this problem.

However, the Law Society representatives did not mention anything relating to directors of SMEs who are also the shareholders of their own companies.

I did discuss this in my first submission and my view is the same. I would recommend that insolvent trading laws ***should not apply to private companies.***

4.5.3 Australian Bankers Association (ABA)

When questioned on the issue of a bank defaulting a loan based upon a breach of an LVR covenant, Mr. Ian Gilbert of the ABA said that this went to the viability of the business. This statement is illogical yet typical for a bank. A business could be trading very successfully and profitably, meeting all its debts when they fall due, and at the same time the LVR on a secured property may have dropped. It must be remembered that a bank will normally only lend to 65% LVR on a commercial loan. So, the bank has a 35% buffer built into the security. Yet the bank will argue that if the alleged value of the security drops at all then the client is in default and they have the right to default the loan.

The banks regularly use the LVR covenant default provision when they decide to default a loan because they can use the supposed independence of a third party valuer's report to justify the decision.

I had this discussion with David Murray in relation to my submission to the FSI. The comment he made at the time was to the effect *" so the banks are treating a commercial loan like a margin loan".* And this is correct.

The reality is that the value of a secured property will go up and down during the course of a loan contract. Historically, property prices increase over time and this will improve the banks position as compared to the day the loan was settled. However, in reality it is impossible to know the real value on a given day. Moreover, it is irrelevant if the client is paying the interest as required.

You will recall that I discussed the small commercial development that I did in Newcastle, when the bank appointed receivers to my company two years ago. I was three and a half years into a five-year loan when the bank decided that they wanted the loan repaid early. I refused to do so as I was not in default, my rent was $300,000 pa and my interest was $140,000 pa. The bank wanted the loan repaid early so that they could close down the fund that they had set up that was now too expensive for them to run.

The original valuation accepted by the bank was $4,000,000. The bank commissioned a new valuation that concluded that valuation had dropped to $2,300,000. I disputed this valuation, and had my own valuation done, which confirmed that the valuation was indeed still $4,000,000. I provided this to the bank.

Nevertheless, the bank appointed receivers to my property and company. I will repeat that, the bank appointed receivers to my company regardless of the fact that they did not have a charge over the company. My company was not security for the loan.

The receivers instructed my tenants to pay the rent to them. They requested a local agent to provide a sales program for the property. They demanded from a different bank that all the funds in my account with that bank be transferred to them. The receiver made this demand even though there was no company charge and any funds in a bank account were not secured funds.

As stated earlier, I would normally have defended my position in court. However my expert advice was that I could not win against the bank's contracts terms. Fortunately I was in a strong financial position, so I wrote a cheque and paid out the loan. The receiver then returned my property to me.

It is vitally important that the Productivity Commission understand how ruthless and totally unregulated this industry is.

4.5.4 Costs associated with Chapter 11

There were some comments regarding the cost of Chapter 11 in the USA Bankruptcy Code, and that accordingly it would be too expensive a solution in Australia. My experience with the Australian system and legal process is such that I cannot believe that any system could be more expensive. In the case of my Newcastle receivership, discussed in this submission, I paid $75,000 in costs to my lawyers just to get an injunction to stop the bank from selling my property for 3 weeks even before we had our day in court. My solicitors said that I would be liable for up to $500,000 to run my argument. You can see why I settled, paid out the loan and agreed to pay 50% of the banks costs as well.

I know of two ongoing court cases relating to the Bankwest matter and Project Magellan. I am told that in one case the legal fees are up to $5million and the other $15million.

4.6 Vested Interests and Both Sides of the Argument

Whenever this issue of insolvency and bankruptcy is being considered and discussed, it is very difficult to hear from both sides. On one side we have the banks. This is the side that inflicts the punishment. They are big and powerful with extremely deep pockets. Moreover, they have written the loan contracts, they interpret the contracts and they appoint the receivers at their sole discretion. They have their solicitors, insolvency practitioners and property valuers who are all there to feed on a lifetime's hard work and savings of the families of the entrepreneurs of our country. Naturally these vested interests would like the current system to remain as it is.

On the other side there are those who have had their lives and businesses destroyed by those mentioned above. So where are these people now? They have gone, dissolved into the background and forgotten. There is no organisation that represents them. Who wants to represent people who have no money to pay dues or fees and who are bankrupt?

When we look at the list of those who attended the Round Table on **Insolvency Arrangements**, held in Sydney on 9 February as part of this process, it proves my point precisely. There are representatives from the government, unions, the banks, the insolvency industry, but nobody representing those who have had insolvency and bankruptcy inflicted upon them.

As far as I can tell I am the only voice of a victim that the Commission has heard. I struggle to see how a balanced view could be formed about such a critically important matter as this with such uneven representations.

As far as I can tell I am the only person to make a submission or make a presentation who was not earning a living from the insolvency process or being paid by an organization involved in some capacity.

I receive no financial benefit nor do I seek any financial benefit for all the work that I have done and continue to do in this area. My only objective is to achieve meaningful sensible reform that will benefit and protect the entrepreneurial families of our country.

The victims of this process are generally broken destroyed people who have totally given up on the thought of receiving any justice through the system. As well, they have no assets, no money and very little income if any at all and are far too busy just surviving to contemplate coming along to the Productivity Commission to give evidence.

To assist the Commission, I have provided a folder of approximately 100 personal impact statements from victims of ***"Project Magellan"*** This code name was created by the CBA to describe *"a review of our portfolio*" that resulted in the mass impairments of Bankwest commercial clients following the purchase of Bankwest by the CBA. It is difficult to believe that this mass impairment was actually given a code name but it is true. This code name was discussed and acknowledged by the CBA under questioning by Senator Williams during the Senate Inquiry in 2012.

I would urge the Commission to look through these pages and to see and understand the full extent of the damage and the horror that the CBA inflicted on these business people and their families. These are not people who over spent on their credit cards, on excessive consumption. These are people who are aged in their 50's, 60's and 70's who have spent a lifetime in business. They have employed staff, generated growth in the economy, invested and have been successful. The CBA destroyed these people and their businesses for their own commercial benefit, whatever that might have been. The upcoming PJC inquiry may enlighten us all on this point.

It wasn't just the loans of the smaller SMEs that the CBA impaired. Two well know examples of far larger loans are Rory O'Brien and Luke Saraceni. My understanding is the O'Brien facility was for $178,000,000 and the Saraceni facility was for $330,000,000. I provide in my Submission No 3 some articles from the press on both of these people.

The ABC's 4 Corners program did a detailed and extensive documentary on this matter. Kerry O'Brien was the presenter. It was done on 5 April 2012 and it is on the Internet. The Luke Saraceni case was discussed in detail amongst many others. I would urge the Commissioners to review this 4 Corners documentary in order to have a better understanding of the power of the banks and the insolvency issues more generally. It also provides valuable insights into our side of the argument.

4.7 Parliamentary Joint Committee for Corporations and Financial Services (PJC)

The above-mentioned PJC is currently holding an inquiry titled “Impairments of Customer Loans”. The committee is currently taking submissions and the submission period closes on 24 July. Soon after the committee will start conducting interviews.

The Hon Philip Ruddock MP has joined the Committee for the purposes of this inquiry. The inquiry will be investigating in depth the issues surrounding the forced **“closure”** of businesses. I would suggest that this inquiry would be highly relevant to “closure” aspects of this current Productivity Commission inquiry. I would urge the Commission to take the opportunity to attend the PJC inquiry if possible.

4.8 Hierarchy of Securities

In my first submission I discussed directors’ guarantees, I would like to expand on this. A directors’ guarantee, even though it is a personal guarantee, it is still different from a personal guarantee. In the case where a company is borrowing funds against real property that is owned by the company, the company is liable for any shortfall when the property is sold. A directors’ guarantee is in addition to the real property security and the company’s liability.

However, the banks’ loan documentation is clever in that it defines all its securities as **“Primary Securities**”. This means that once the bank has defaulted the loan, (remember, at the bank’s sole discretion) then the bank can call on any security it so chooses, in any order. It is not uncommon for the bank to demand repayment of the loan made to the company, from the director of the company, even before the secured asset is sold. This way, the bank can bankrupt the director, keep the secured asset and the company, and the company can continue to trade in the hands of the receiver.

This is a dreadfully unreasonable and unjust situation and should not be permitted to occur. There needs to be a hierarchy of securities. If there is a genuine default and the business cannot be saved, then the secured property should be liquidated first, followed by the company and only then should the director be liable. However, it is my recommendation that the director should only be liable to the extent of assets listed on the director’s guarantee that would be linked back to the original LVR. Please see my first submission.

4.9 Chapter 7 and Chapter 11, USA Bankruptcy Code

In relation to the American Bankruptcy Code, I believe that there are many desirable features that could be adopted in Australia, including:

1. A bank cannot call in a loan if the interest is being paid.
2. When a business does fail there are assets that are exempt from creditors, to enable the entrepreneur to start again. There are different laws in each state. However, in Florida for example, the total equity in the family home is exempt.
3. Under Chapter 7, once all the assets have been handed over to the Court excluding the exempt assets, the bankruptcy is ended, and the entrepreneur is free to start again.

4. When a business is in genuine difficulty, the ***"Debtor in Possession"*** model of voluntary administration provides a genuine opportunity for the business to restructure without the external administrator draining valuable capital from the business by way of fees.
5. A bank cannot impose penalty interest rates on the business during the bankruptcy protection period.
6. The Single Asset Real Estate Debtor provision provides additional protection for a business such as a hotel or motel owner. This provides 90 days protection from the banks and if during the 90-day period, the business commences paying interest again at the non- default rate, the bank cannot default the loan.

4.10 Banks Will Resist Reform

The banks will undoubtedly resist any reforms that will change the current situation. The banks currently enjoy total control and total power over the SME sector so any reforms will only diminish that power and control.

I would anticipate the banks would make the following claims,

These reforms will increase our costs and we will need to pass these costs onto the SME sector.

I would respond:

1. If that is the case, so be it. If the interest rate on a commercial loan is slightly higher, then this is a small price for an SME to pay for certainty and security.
2. The Reserve Bank can have input into interest rate levels through monetary policy.
3. I would dispute the claim nevertheless. If the banks are now saying that they have made mistakes in the past and through their "epiphany" moment they now have decided to work with SMEs in financial difficulty instead of winding them up, then the end result will be the same and costs will not be any different.
4. In my experience the costs that the banks inflict upon themselves when defaulting and liquidating a viable business is extraordinarily high. These costs would be avoided.
5. The increased health of the Australian economy generally would flow through to the banks' profitability.
6. The American system reflects many of my recommendations and I don't read that the business sector in America is suffering in regard to the cost of funds.

These reforms will reduce the amount of capital available to be lent to SMEs.

I would respond:

1. APRA will decide the risk weighting to apply to individual assets classes on the banks' balance sheets. A bank does not determine it.
2. APRA and the Reserve Bank have different "levers" available to influence how and to which sectors money is lent.
3. The American system reflects many of my recommendations and I don't read that the business sector in America is suffering in regard to the availability of capital.

We agree that in the past we have acted too early when we have defaulted loans. Moving forward it is our policy to work more closely with our commercial clients and help turn around a struggling business. So these reform recommendations are not necessary.

I would respond:

1. History has demonstrated that in this regard the banks cannot be trusted. Given the opportunity of self-enrichment the banks will take this course of action at the expense of their clients.
2. If it is the banks' new policy to work in the best interests of their clients, then they should have no objection to any legislation preventing the inappropriate impairment of commercial loans as well my other reform recommendations.

4.11 Summary

My proposition is simple. All the insolvency events in the SME space that I have seen in the 35 years that I have run my own businesses have all occurred as a result of the secured creditor, the bank, calling in a loan. Therefore I maintain that the most effective way to reduce insolvency events in Australia and to preserve the value in Australian businesses is to prevent this from occurring whenever possible.

The contractual balance of power between the bank and the customer has moved so far in favour of the bank in recent years that it is impossible for an SME to challenge a bank in court.

I have had this discussion with the Australian Bankers Association and their spin position is that they would always act in the best interest of their client. They promote the ***"Benevolent Dictator's Defense"***, i.e. give us all the power by way of the contracts and we will always do the right thing. History has clearly demonstrated that the banks cannot be trusted with the absolute power that they currently enjoy. Please review the evidence that I have provided.

Moreover, if the banks claim that they will always do the right thing by their clients, then they should not have a problem with accepting legislative changes that oblige them to do so and at the same time protect the rights of Australian entrepreneurial families.

4.12 Conclusion

I recommend the following reforms to the current insolvency regime.

I have no doubt that the Australian banks will resist each and every one of my recommendations. They will push back with all the political influence that they have at their disposal. However in the final analysis, the only reason the banks really have to oppose these reform recommendations is that they do not want to lose the absolute power over SMEs that they currently enjoy.

I would be happy to debate these reform recommendations with the CEO of any bank at any time.

In order to prevent an insolvency event being manufactured by a bank, described by Hon Philip Ruddock MP as a "Constructive Default", I recommend:

1. If a client is paying interest on the loan, at the non-default rate, then under no circumstances should the bank be able to default the loan.
2. Six months prior to the expiration of a loan the bank must give notice that the loan will be required to be repaid on the due date. If notice is not given, then the loan continues until the 6-month notice is given.
3. If the secured creditor alleges that a monetary default has occurred and wants to default the loan, then this should be referred to a third party. This party should have the power to allow the borrower to rectify the default if possible and if not, then confirm the default.

When a genuine insolvency event does occur, I recommend:

1. Insolvent trading laws should not apply to SMEs.
2. A 'debtor in possession' voluntary administration model should be available for businesses to use to restructure.
3. Protection from secured creditors should be available during the restructuring process.
4. The hierarchy of securities mentioned earlier should apply.
5. There should be no bankruptcy period for company directors following the insolvency event provided always that the director has acted honestly.
6. Company directors should be able to retain certain assets that will enable them to recover and regroup and encourage them to try again.
7. Any assets sold by a liquidator should be sold by way of a public auction. Sale of assets by way of private treaty is currently permissible. This should be prohibited.

Personal Guarantees, I recommend:

1. Personal guarantees by a third party and directors' guarantees should only be available to a secured creditor to the extent of assets listed in the guarantee. In this respect the assets listed will form party of the security for the loan.

5.0 Submission No. 3 to the Draft Productivity Commission Report: Business Set-up, Transfer and Closure

8 July 2015

My third submission contains various documents that I would describe as evidence to support some of the arguments that I made in my earlier submissions.

5.1 Seven Personal Impact Statements

Please find attached a small submission of seven personal impact statements as a sample of those who have lost so much as a result of the impairments by the CBA of the Bankwest loan book. (Appendix A)

5.2 Two Articles by Sydney Morning Herald Reporter Michael West on the Insolvency Industry

In the first article Michael explains how a liquidator spent $500,000 in fees chasing a debt of $28,000. South Australia's Chief Judge found the liquidator PPB and its lawyers Minter Ellison enjoyed a *"loosely defined fee sharing arrangement"*

Michael goes on to say:

"The banks are running both ends of the insolvency spectrum, the administrations as well as the receiverships."
"Those who are getting the lion's share of the work lately PPB and Korda Mentha, never claim against the banks."

Please read the full article, it is quite unbelievable.

The second article relates to the receivership of Barrup fertilisers. In this case Michael West states,

"In just 14 months…the great fee hunters managed to clean out $56 million.
"PPB and Freehills alone helped themselves to almost $19m and 13.8m respectively"

Again, I would ask that that you read the full article. (Appendix B)

5.3 Commonwealth Bank of Australia Results Presentation

Please find attached three pages from the CBA Results Presentation in relation to the performance of Bankwest, following the acquisition of Bankwest by the CBA for the full year ending 30 June 2010.

You will see that these pages refer to the Bankwest loan book and that:

1. The "problem loans" were in fact "performing loans", i.e. they were not in default.

2. There were 11 loans (66%) of the book reviewed at this stage. We know from other evidence that somewhere between 500 and 1000 loans were defaulted.
3. The CBA having bought Bankwest had no regard for the terms and conditions of the original Bankwest loan documents. The CBA applied its own standards to the Bankwest loans and used these standards to default the loans.

This goes to the point I make in my second submission. The customer has all the obligations, in some cases up to 53pages of obligations.

The banks are not even obliged to honor the most basic terms of the loan contract. (Appendix C)

5.4 Newspaper Articles on Rory O'Brien and Luke Saraceni.

Rory O'Brien and Luke Saraceni were both businessmen with very large loans from Bankwest. In each case the loan facility was in excess of $150 million. Newspaper articles on both men are attached (Appendix D). Luke Saraceni was also the subject of a 4 Corners documentary on the fallout of the CBA purchase of Bankwest presented by Kerry O'Brien, titled "Happy Banking?" Produced on 5 April 2012. I would recommend that the Commissioners review this program on the internet. (Appendix D)

5.5 Summary

The only way the power of the big banks can be controlled in relation to their contracts and dealings with the SME sector is for the Federal Government to regulate relevant protections.

Again, I state that it is impossible for an SME to seek any justice through the legal system as I hope I have demonstrated.

For all these reasons, I recommend to the Commission all the reforms that I have explained and listed in the Conclusion to my Second Submission.