(AUSTRALIA) LTD

IMF (AUSTRALIA) LTD
ABN 45 067 298 088
AFSL 286906
www.imf.com.au

Introduction

a. In the last months of calendar 2007 the financial affairs of Bank of Western Australia Limited were inextricably attached to the future prospects of its parent company HBOS PLC in the United Kingdom. HBOS PLC depended, to a very large extent, on the wholesale market for its funding and Bankwest, in turn, relied for its funding upon HBOS to which, at the end of 2007, it owed some $8.7bn.

b. As HBOS foundered throughout 2008 and almost collapsed in September of that year, so too did Bankwest meander towards its own collapse.

c. At the moment, it is only possible to divine what happened to HBOS and Bankwest by reference to media documents. A timeline for those published documents is attached hereto.

d. It will take the power and reach of a Senate inquiry to reveal the full picture.

e. As part of its purchase arrangements for Bankwest, CBA extracted from the seller a warranty which enabled CBA to claw back part of the purchase price depending upon whether the assets of Bankwest had been accurately disclosed to CBA in the accounts of Bankwest.

f. Little is known about that warranty. In particular it is not known;

    i. If there was a time limit by which CBA had to make a claim under the warranty;

    ii. What categories of loan were covered by the warranty (were they just commercial property loans?)

    iii. What steps needed to be taken by CBA before a claim could be made under the warranty – was it sufficient for there to be a new valuation of outstanding loans or did CBA need to take enforcement proceedings i.e. call up the loans, appoint receivers and/or dispose of the security property?

    iv. Whether there was a cap on the amount that could be claimed by CBA?

g. What is clear is that CBA called upon the warranty and was paid some $200m.

h. At the same time some commercial developer clients of Bankwest believe they were hard done by when Bankwest revalued their security and called up their loans in the period after CBA took control of Bankwest..

i. If there was a time limit and if CBA had to call up the loans or take some enforcement action within that limited time in order to get the advantage of the warranty and if that warranty was unlimited then there is some risk that the CBA has been enthusiastic in its quest to have Bankwest identify and take action against commercial property developers whose loans were within the categories set out in the warranty.

Level 5, 32 Martin Pl
Sydney NSW 2000
GPO Box 5457
Sydney NSW 2001
T +61 2 8223 3567
F +61 2 8223 3555

Level 6, 37 St George's Tce
Perth WA 6000
PO Box Z5106
Perth WA 6831
T +61 8 9225 2300
F +61 8 9225 2399

Level 7, 320 Adelaide St
Brisbane QLD 4000
T +61 7 3108 1310
F +61 2 8223 3555

Level 31, 120 Collins St
Melbourne VIC 3000
GPO Box 5457
Sydney NSW 2001
T +61 3 9913 3301
F +61 2 8223 3555

Adelaide SA 5000
GPO Box 5457
Sydney NSW 2001
T +61 8 8232 4600
F +61 2 8223 3555

A Timeline for Bankwest

1. By the last quarter of calendar 2007 Bankwest had, for some time, been a wholly owned subsidiary of HBOS Australia Pty Ltd itself a subsidiary of HBOS PLC in the United Kingdom. From July 2007 Bankwest had been pursuing an extraordinary growth strategy based upon the opening of 160 bank branches across Australia within 4 years. **(Document A).**

2. **(Document B)**. In a report by HM Treasury entitled "Maintaining Financial Stability across the UK Banking System" the following passage appeared at paragraph 8 –"from autumn 2007, the Authorities were aware of the potential weaknesses at HBOS, the UK's largest mortgage lender, and as early as March 2008 had began to formulate specific plans should that bank get into difficulty."

3. During the last quarter of calendar 2007 and through the first three quarters of calendar 2008, Bankwest was reliant for financial support on its immediate parent HBOS Australia Pty Ltd and its ultimate parent HBOS PLC. As HBOS PLC came under pressure during 2008 and began to struggle financially so too did Bankwest.

4. **(Documents C and D)**. On 14 September 2007 a very strong run began on the funds of Northern Rock, a large UK mortgage lender. This run eventually led to the nationalisation of Northern Rock on 22 February 2008.

5. At the time, HBOS PLC was the largest mortgage lender in the United Kingdom so that what had happened to Northern Rock was not out of the question for HBOS.

6. **(Document E)**. On 27 December 2007 Bankwest issued 100m ordinary shares at $1 per share to HBOS Australia Pty Ltd to raise $100m. As Bankwest was already a 100% owned subsidiary of HBOS Australia Pty Ltd and already had loans of $8.7bn from another subsidiary of HBOS PLC a query arises as to whether any regulatory authority required or influenced this capital raising. Was Bankwest also under the regulatory eye as early as December 2007?

7. **(Document F)**. The financial year for Bankwest, at this time, began on January 1 and concluded on 31 December. As at 31 December 2007 the issued capital of Bankwest was 1,072,205,656 ordinary shares issued at $1 per share and 530m redeemable preference shares issued at $1 per share. Bankwest was indebted to Bank of Scotland PLC (another subsidiary of HBOS PLC) in the sum $8.71bn. The impairment losses charged to the income statements were $87.8m. The net assets were $3,014,000,000.

8. **(Document G)**. On 23 February 2008 the UK media announced that the practise of HBOS issuing loans in the UK representing 125% of the value of the security provided in support of such loans had ceased.

9. **(Document H)**. In February 2008 the manager of the Bankwest branch at Fremantle advised a property developer client that the HBOS head office had directed that no further loans would be made by the bank on commercial real estate in Australia. One statement to this effect made by one bank manager to one commercial property developer client does not mean that Bankwest in fact suspended commercial property loans across Australia. It is, however, a question which could be easily verified, one way or the other, by Bankwest.

Level 5, 32 Martin Pl
Sydney NSW 2000
GPO Box 5457
Sydney NSW 2001
T +61 2 8223 3567
F +61 2 8223 3555

Level 6, 37 St George's Tce
Perth WA 6000
PO Box Z5106
Perth WA 6831
T +61 8 9225 2300
F +61 8 9225 2399

Level 7, 320 Adelaide St
Brisbane QLD 4000
T +61 7 3108 1310
F +61 2 8223 3555

Level 31, 120 Collins St
Melbourne VIC 3000
GPO Box 5457
Sydney NSW 2001
T +61 3 9913 3301
F +61 2 8223 3555

Adelaide SA 5000
GPO Box 5457
Sydney NSW 2001
T +61 8 8232 4600
F +61 2 8223 3555

10. A decision by Bankwest to cease all new commercial property lending would only be taken in extreme circumstances so the question is whether this statement by the Fremantle manager was accurate and related to the whole Australian business of Bankwest.

11. **(Document I)**. On 29 February 2008 Bankwest issued a further 200m ordinary shares at $1.00 per share to HBOS Australia Pty Ltd to raise a further $200m. If Bankwest was cutting back on new commercial property loans then the issue of this capital is likely to reflect either regulatory encouragement or financial pressure arising from the decision to open 160 bank branches in 4 years.

12. There was no reference to any cessation of commercial property lending in the 2007 accounts for Bankwest (for instance in the section dealing with events occurring after the end of the calendar year) and nor was there any reference in the press to any such cessation occurring.

13. **(Document J and K)**. Upon the failure of Bear Stearns in the US on 17 March 2008 the shares of HBOS PLC fell 12.5% “amid concern about its exposure to investments linked to the US sub-prime mortgage markets.” The Bank of England injected £5bn into the financial sector amid concerns that HBOS PLC was in financial difficulty.

14. **(Document L)**. On 21 April 2008, the Bank of England announced that it would swap government bonds for mortgage backed securities to companies such as HBOS which had curbed lending because of the global financial crises. It is clear that HBOS PLC had stalled its lending in the UK which may lend credence to the proposition that it had ceased to advance funds to commercial property developers in Australia during the same period.

15. **(Document M)**. It is clear from reports in the media around this time that HBOS was already contemplating the sale of Bankwest. Such a sale would bring into HBOS both the purchase price and also repayment of the amounts due by Bankwest to the HBOS group (which, as set out in paragraph 7 above, stood at some $8.71bn by 31 December 2007.)

16. **(Document N)**. On 30 April 2008 HBOS announced a rights issue to raise £4bn and, at the same time, announced a writedown of £2.8bn on its assets. HBOS also announced that it was cutting future dividends and would pay the current interim dividend in shares rather than in cash.

17. **(Document O)**. By June 4 2008 Bankwest was forced to announce, in the Australian media, that it was “safe”. The “retail mortgages and savings boss Paul Vivian” went on record to say that “I would have to say that I think that we’re as safe as any of the major banks in Australia”.

18. **(Document P)**. On 12 June 2008 Bankwest was again required to make a public statement regarding its current financial position. “Retail Chief Ian Corfield” was quoted as saying “people who are investing in, or saving money with, Bankwest are absolutely safe. This business is supported by a very strong balance sheet of its own and, in turn, is backed up by the HBOS balance sheet. People, in my view, are safe as houses.”

19. **(Document Q)**. On 21 July 2008 the media reported that the rights issue by HBOS had only been taken up by “a tiny minority of existing shareholders in HBOS”. Shares issued for £1.2bn during that placement had been placed on the market. The rights issue had been shunned by major City institutions.

20. **(Document R**). On 28 June 2008 further media coverage referred to “burgeoning speculation” about a proposal for NAB to buy Bankwest from HBOS. Bloomberg claimed that NAB had met with advisory firms in London during June 2008 to discuss a bid for Bankwest.

21. **(Document S)**. On 31 July 2008 a report appeared referring to HBOS unveiling a 72% drop in pre tax profit for the first 6 months of 2008. HBOS announced that its share of new mortgage lending in the UK had fallen from 22% as at December 2007 to 7% as at 30 June 2008. HBOS also reported rising numbers of borrower defaults and warned of higher arrears to come.

22. **(Document T)**. On 31 July 2008 HBOS Australia Pty Ltd issued 1.6bn shares at $1.00 per share to raise $1.6bn. It is clear from this share issue that HBOS PLC was under continuing pressure to financially support its subsidiaries in Australia including Bankwest.

23. **(Document U)**. On the same day, 31 July 2008, Bankwest issued a further 250m shares at $1.00 per share to HBOS Australia Pty Ltd to raise $250m. This issue and a later issue referred to below meant that Bankwest was in a position between July and September 2008 where it required half a billion dollars in new capital from its parent in order to keep operating. At the same time, as will appear below, Bankwest was also drawing down billions of dollars from its parent by way of further loans.

24. It is possible that the media speculation in relation to the financial position of Bankwest lead to a regulatory requirement that Bankwest further increase its capital by the issue of these shares.

25. **(Document V)**. On 19 August 2008 a further report appeared in the media regarding the sale of Bankwest to CBA. The report set out that HBOS had appointed Morgan Stanley to investigate the sale of Bankwest and that CBA was preparing to make a bid.

26. On 15 September 2008 Lehman Brothers filed for chapter 11 bankruptcy protection in the US.

27. On 16 September 2008 the Federal Reserve Bank in the US created an $85bn credit facility to preserve the existence of American International Group.

28. **(Document W)**. These two events proved the end for HBOS PLC. On the verge of complete collapse the company was the subject of a merger with Loyds TSB. Had HBOS PLC failed on the 17th of September 2008 then Bankwest would have followed suit shortly thereafter. According to the report in the Telegraph the funding gap at HBOS was £198bn being the difference between loans made and customer deposits taken (i.e. the amount owed to other banks and financial institutions which were refusing to deal with HBOS.) Of that amount some $17bn was owed by Bankwest to HBOS (this amount had doubled in the 9 months between 31 December 2007 and the end of September 2008.)(refer paragraph 7 above and paragraph 46(d) below)

29. The question is – for how long had Bankwest been in this precarious financial position prior to 17 September 2008?

30. **(Document X)**. On 18 September 2008 the Reserve Bank governor declared Australia's financial system sound and that the condition of Australian banks was "light-years away from what is happening in other banking systems around the world." He did not specifically refer to Bankwest.

31. **(Document Y)**. This lead to further speculation on a takeover of Bankwest by CBA. The reports suggested that CBA and NAB had been "circling Bankwest for a possible tilt over the past couple of months".

32. **(Document Z)**. On 23 September 2008 Bankwest disposed of its factoring business in Australia to Allianz Finance. A report of that date set out that Bankwest had ceased all factoring business, was referring all new factoring enquiries to Allianz and would transfer its existing factoring contracts to Allianz. This was a bank under severe pressure which was badly in need of a saviour.

33. **(Document AA)** .On 30 September 2008 Bankwest issued a further 250m shares at $1 per share to HBOS Australia Pty Ltd to raise $250m. These monies were no doubt part of the fund which had been raised by HBOS Australia Pty Ltd in July 2008.

34. **(Document AB)**. At the end of each month in Australia banks lodge a form which is known as ARF320.0 Statement of Financial Position (Domestic Books). At section B(1) and (2) of the form the banks are required to set out their liabilities to "clearing houses and financial institutions." Under section B(2) the banks are required to report the amount due by them to the following;

    i. Reserve Bank of Australia;

ii. Australian Resident Banks;

iii. Australian ADI's;

iv. Registered financial corporation's; and

v. Other Australian Financial institutions.

35. From time to time APRA publishes "Statistics – Monthly Banking Statistics Back Data" and did so in a revision dated 31 May 2011. The statistics are gathered under numerous headings but one of them, in column X, is headed "Due to clearing houses and financial institutions" and, on its face at least, appears to be a collection of the amounts due by each bank under section B (1) & (2) of ARF 320 referred to above.(refer to attached)

36. The amounts shown for Bankwest under this column are as follows;

June 2008 – 0

July 2008 - 0

August 2008 - $29m

September 2008 - $859m

October 2008 - $2.234bn

November 2008 - $3.102bn

December 2008 - $3.752bn

January 2009 - 0

February 2009 - 0

37. These are amounts which were "due" at the end of each of those months by Bankwest to either Australian financial institutions or the Reserve Bank of Australia. One or the other or both of these two were keeping Bankwest alive while it awaited its saviour.

38. **(Document AC)**. On 8 October 2008 Commonwealth Bank announced that it had acquired Bankwest and St Andrews Australia Pty Ltd through a sale and purchase agreement with HBOS PLC. The purchase price was declared at $2.1bn. The purchase was conditional on the receipt of all necessary competition, regulatory and government approvals. CBA announced that it would fully fund the purchase by undertaking a $2bn institutional placement. CBA went so far as to say that part of the strategic reasoning for the purchase was that it "strengthens the competitive position in the growing and attractive Western Australia market." It appears that CBA meant it strengthened CBA's position in that market.

39. **(Document AD)**. This purchase of Bankwest by CBA was reported on 8 October 2008 as being at 20% below book value. A purchase price of $2.1bn (even if the whole purchase price was paid for Bankwest and nothing was paid for St Andrews) puts the agreed book value of Bankwest as at 8 October 2008 at $2.625bn (at the most). This represents a drop in book value of $389.6m from the position nine months earlier on 31 December 2007 (refer paragraph 7 above.)

40. This drop in book value occurred after the issue of $700m in share capital in the intervening period between 31 December 2007 and 8 October 2008 so the agreed drop in value of the Bankwest assets over this 9 month period was about $1.1bn.

41. These figures do not take into account any operating profit which had been made by Bankwest in that 9 month period. (later reported at about $500m)

42. On the face of it, therefore, the seller and the buyer agreed that between $1.1bn and $1.6bn of value had been eroded from the Bankwest assets in the first 9 months of calendar 2008.

43. There was no mention in the CBA announcement of any mechanism in the contractual documents whereby the purchase price could be reduced depending upon whether any of the loan assets of Bankwest were overstated in the books of Bankwest even after this $1.1bn/$1.6bn reduction.

44. **(Document AE)**. On 9 October 2008 the Chief Executive Officer of CBA commenting on the purchase of Bankwest said that "I think it was very important for Australia and for Bankwest to have a very strong parent." This was essentially the only contemporaneous comment which portrayed the purchase of Bankwest as being necessary to protect the Australian financial system.

45. **(Document AF)**. On 10 December 2008 the Australian Competition and Consumer Commission published its review of the competition aspects of the purchase of Bankwest by CBA.

46. The following points emerge from the ACCC document;

    a. In paragraph 1 the ACCC decided not to oppose the acquisition of Bankwest by CBA;

    b. From paragraph 26 the average price to book value for Australian banking acquisitions was 1.9 x the book value whereas the CBA acquisition of Bankwest and St Andrews was at .8x of the book value;

    c. From paragraph 57 parties other than CBA had been approached to purchase Bankwest – there are no details of which parties were approached or when they were approached;

    d. From paragraph 61 upon the sale of Bankwest, CBA was required to fund Bankwest so as to enable it to repay $16bn of intergroup loans from HBOS;

    e. From paragraph 62 an alternate buyer for Bankwest was unlikely; and

    f. From paragraph 63 "the rapid expansion being pursued by HBOS with the Bankwest business (160 branches over 4 years) was unprecedented in Australian banking"

47. The purchase of Bankwest by CBA was settled on 19 December 2008 and all of the issued shares of Bankwest were transferred to CBA ownership.

48. **(Document AG)**. On that same day CBA replaced the chief executive officer of Bankwest with an executive from CBA. The other two central roles within Bankwest were also filled by CBA executives i.e. the chief financial officer and the chief risk officer. In addition, four of the existing directors of Bankwest resigned and two new directors were appointed to the board. On the same day the company secretary resigned and a new company secretary was appointed. On the face of it these appointments were made by or on the recommendation of CBA as the new 100% shareholder of Bankwest. Thereafter Bankwest had six directors – three who had been in position prior to the purchase of Bankwest by CBA and three who had been added on the recommendation of CBA.

49. **(Document AH)**. On 22 December 2008 the new CEO Jon Sutton stated to the media that Bankwest would operate though its own independent board and would have its own independent chairman. "Although Mr Sutton has guaranteed there will be no effect to West Australian operations, the same guarantee cannot be extended to its operations in the East."

50. The financial year for Bankwest was about to come to an end on 31 December 2008 so that the accounts for the bank would be drawn up as at that date.

51. **(Document AI)**. On 30 April 2009 Jon Sutton as the new Managing Director of Bankwest signed off the 2008 accounts on behalf of the board. The accounts disclosed impairment provisions against loans of $825.3m an almost tenfold increase on the impairment position in 2007. The accounts also disclosed that Bankwest owed Bank of Scotland PLC $14.6bn which was novated to the CBA on 19 December 2008 (presumably on a dollar for dollar basis).

52. **(Document AJ)**. In a media release dated 30 April 2008 it was suggested that this huge increase in specific provisions "was driven by a small number of large property exposures in NSW and QLD together with a number of small exposures across business lending."

53. **(Document AK)**. In an update of 30 April 2009 CBA made the following statement –"the final purchase price for Bankwest will be determined over the next two months taking into account its capital position and provisions for bad and doubtful debts." This appears to be the first vague reference to a warranty included in the purchase contract back in October 2008. No further explanation was given as to what was to occur "over the next two months".

54. **(Documents AL)**. These cryptic comments from CBA were then expanded upon by Danny John writing on 1 May 2009 and setting out as follows;

    "Commonwealth Bank is seeking to cut the $2.1bn price it paid to buy Bankwest 4 months ago. When it emerged yesterday its new subsidiary had greatly raised its level of impairment charges to cover increasing bad debt."

    CBA has "activated a clause in the sale agreement to have the original price independently reviewed."

    It is believed that an independent expert will now review the claims from both sides with about $200m believed to be at stake in the process."

55. **(Document AM)**. In the meantime employees at Bankwest had been losing their employment despite what was said at the time of the Bankwest purchase. Tony Boyd writing for Business Spectator put it as follows on –"Commonwealth Bank's decision to cut 400 jobs at Bankwest signals the end of any East Coast expansion plans under the Bankwest banner." –"the job cuts are not a good look for CBA Chief Executive Ralph Norris and the new managing Director of Bankwest Jon Sutton. Both had said publicly that jobs would not go and gave similar assurances to the union." Of the 400 jobs that were cut 250 of them were in Western Australia.

56. **(Document AN)**. The other party to the sale agreement (HBOS PLC) had referred to the arbitration provision in the sale agreement during the course of its 2008 annual report and accounts published in the UK on 26 February 2009. The statement was as follows –"the share sale agreement provided for adjustments to the initial purchase price based on the risk weighted assets of Bank of Western Australia Limited and the net assets of St Andrews Australia Pty Ltd. As a result, the loss on sale of these businesses may be subject to adjustment for the contingent element of the commitment receivable." No provision had been made in the HBOS accounts at that stage.

57. **(Document AO)**. On 30 April 2009 Jon Sutton as MD of Bankwest was reported to have said –"since CBA acquired Bankwest, we have improved our credit underwriting standards in business and retail banking and have a strong focus on prudent and responsible lending." This certainly suggested that the $825.3m provision had been made because of pre-existing problems with credit underwriting and a lack of prudent and responsible lending by Bankwest.

58. **(Document AP)**. By early June 2009 questions were being raised in relation to the acquisition of Bankwest by CBA from no less a personage than the Chairman of the ACCC. He said on 3 June 2009 that, but for the global financial crisis, the ACCC would not have been in a position to have allowed the CBA/Bankwest merger.

59. **(Document AQ)**. This lead to a swift riposte from the chairman of CBA. Mr Norris said on 5 June 2009 that "it would have been "absolutely disastrous" for the domestic banking system if the West Australian bank had been allowed to fail." He was quoted in that article as saying that "Bankwest was close to collapse with $17bn in inter-group funding to roll over." And "I have seen the comments (by Mr Samuel), but I think at the time we made the offer there weren't too many options for Bankwest; it was failure or being taken over" and "it had an owner that was incapable of supporting $17bn in funding that had to be rolled over. So competition issues, I think, had to be pushed to one side, because it would have been absolutely disastrous for the banking system to have a bank fail."

60. So to this point in time the proposition was as follows - CBA had to buy Bankwest – it would have collapsed if it was not purchased by CBA – this would have been disastrous for the Australian financial system – as it turned out Bankwest had not been operated in a prudent manner and its credit practises were such that a huge writedown of $825m was required and large numbers of staff had to be re-trenched.

61. Whether or not this was a completely accurate picture and whether or not the large writedowns were absolutely necessary may be open to debate. The balance sheet for Bankwest as at 31 December 2008 discloses net asset of $3.54bn compared to the initial purchase price of $2.1bn. The annual accounts for CBA to 30 June 2009 (**Document AR**) contain the following description of Bankwest – "The groups financial strength (i.e. CBA) placed it in a unique position at the end of December 2008, to acquire at a substantial discount to book value, Bankwest and St Andrews. These excellent assets have enabled the group to realise a long standing strategic objective of strengthening its retail banking business in Western Australia and building an increased capability in business banking."

62. **(Document AS)**. On 2 July 2009 Jon Sutton was called before the Economics References Committee of the Senate. Some matters covered by him were as follows;

    a. At page E2 Bankwest maintains an independent board of directors and has its own business strategy independent of the Commonwealth Bank.

    b. At E5 of the 400 job cuts 137 transferred over to CBA.

    c. At E6 the previous owners of Bankwest (i.e. HBOS) were supporting other businesses within the HBOS group out of the Bankwest workforce.

    d. At page E6 Bankwest shared very few activities with CBA.

    e. The cost to income ratio for Bankwest prior to the purchase was 70% which was a lot higher than the major banks and some of the regional banks. The high cost base was as a result of Bankwest business supporting elements of the HBOS business and the Bank of Scotland business.

    f. At page 8 the Bankwest business had 'virtually stopped and stood still" and "the previous owners had to stop writing business; they could not continue to write business given the funding pressures they were under. So business lending and mortgage lending had stopped under the previous owners,"

63. Mr Sutton did not say when the business of Bankwest had stopped operating and nor did he make any reference to the impairment provisions against property development loans or the clawback by CBA which was then underway.

64. **(Document AT)**. On 4 August 2009 HBOS PLC published an Interim Management Report to the half year 30 June 2009. In that document the company disclosed an adjustment to the consideration received for its sale of Bankwest in the sum of £96m.

65. The £96m figure was later adjusted to £100m **(Document AU)**. The Australian equivalent of £100m in early august 2009 was about $200m.

66. **(Document AV)**. On 9 August 2009 Danny John wrote an article basically adopting the $200m payment and saying that it had been "resolved by mediation and both sides agreed to keep the result confidential." –"it was only after CBA completed the deal and sent in a team of auditors to review Bankwest's loan book that it discovered that the Perth based lender was under provisioned, driven by its exposure to the commercial property and business sectors. As a result Bankwest qualified its most recent financial performance from a $185m profit for calendar 2008 to a $139m loss because of a rise in its bad debt charges to $825m. According to a statement released at the end of April that announced the mediation process, Bankwest had returned to profitability in the first quarter of this year."

67. **(Document AW)**. CBA returned to this theme in August 2010. After the results to 30 June 2010 had been published the bank was quoted as saying that it had "dismissed several Bankwest executives including a former risk officer claiming the lender "systemically" inflated the credit quality of 100's of commercial property loans and mortgages when it was

owned by the British Group HBOS" and "we found a situation where the loans were incorrectly rated as far as we were concerned from a credit quality perspective, and also there were issues about the validation of the underlying security". The article set out the following proposition –"Commonwealth executives became alarmed when a number of Bankwest loans were found to be impaired. Usually problem loans move through the banks watch list, where several red flags are raised before the loans are classed as impaired. This was not happening in the Bankwest portfolio, which prompted Commonwealth to review 1,100 accounts."

68. **(Document AX)**. On 15 December 2010 Mr Norris from CBA appeared before a Senate committee and made the following points;

    a. At page E69 "Bankwest was, to a large extent, a failing bank. It would have been a failing bank if we had not bought it, because it was owned by an organisation that had carried out lending practises that were highly, I believe, inappropriate;

    b. "i think if you have a look at the other subsidiaries that were owned by HBOS, the quality of lending in all of those entities was of a poor quality."

    c. At page E76 to be fair, we had to provide $17bn in funding which no other organisation could have provided at that time in taking that organisation over." – "or it would have collapsed" –"yes. Potentially it would have collapsed."

69. One measure of a bank's enforcement activity is the amount of collateral it repossesses in order to ensure that loans in default are repaid to the bank. As shown in Document F (note 27) Bankwest repossessed $6.1m of the commercial property in 2006 and $6m of commercial property in 2007. As shown in Document AI at note 26, Bankwest repossessed $127.6m of collateral in 2008. CBA took over Bankwest in the dying minutes of 2008 so the interesting question was how much collateral was repossessed by Bankwest over the 6 months after CBA took control of Bankwest?

70. **(Document AY)**. Is an extract from the accounts for Bankwest to 30 June 2009. For some reason, by that time, Bankwest had ceased reporting on the amount of collateral it had repossessed during the accounting period. The accounts simply set out –"
in the event of customer default, any loan security is held as mortgagee in possession and therefore the Group does not hold any real-estate or other assets acquired through the enforcement of security."

Hugh McLernon
Managing Director
6 February 2012