

Questions on Notice

Question 1: Chair - You said that there is only one case where LVR alone was the reason for a default. Most of the submissions we have received indicate that there several conditions, LVR being just one of them. So, how many times have you taken action against a borrower where LVR was one of the conditions?

...with an indication, and particularly where it is one of perhaps only two or three areas.

Beyond the one instance described where an LVR was the sole reason for the event of default, NAB will only use non-monetary events of default in limited circumstances to commence enforcement action, most commonly confined to an insolvency event associated with the customer (that is where the customer, its directors or another third party has placed, or has taken formal steps to place, the customer in external administration).

If NAB is required to commence enforce action on a facility, it will ordinarily issue a notice setting out the event of default relied upon. As NAB generally relies on monetary events of default when enforcing its facilities, those notices set out those monetary defaults and do not also include any other events of default, including any breaches of financial covenants, such as LVRs.

To determine each instance where there also existed a breach of a non-monetary default, in addition to a monetary default, NAB would be required to undertake a manual review of each of its files and its electronic records (which record defaults). This data cannot be extracted without such a manual review.

Larger syndicated institutional lending is usually cashflow based rather than security based and would be quite unlikely to have an LVR covenant at all. However, again, to obtain any data around instances where this has occurred in larger syndicated institutional lending, again, NAB would be required to undertake a manual review of each of its files and its electronic records (which record defaults). This data cannot be extracted without such a manual review.

Question 2: You said that you apply quite a number of factors [referring to the factors upon which NAB assesses risk noted in its opening statement], and I would like to ask you to give that to us on notice in writing about the factors that you do consider

Set out below are the factors that NAB may consider in assessing the risk of a customer file:

- Cash flow
- Profitability and margins
- Management and board capability – operational, business, strategic, financial, industry
- Working capital management
- Debtors/creditors profile
- Stock turnover and aging
- Covenant compliance
- Governance and compliance regimes
- Bank facility management information reporting
- Overdraft excesses and days past due
- Key supply contracts and achievement of contract KPIs
- Interest rate, F/X, commodity hedging strategies
- Any major litigation
- Animal health and welfare
- Tenancy profile
- Organisational structure – key operating subsidiaries, holding company and financial company
- Debt and capital structure
- Operational gearing and balance sheet leverage
- Licencing and regulatory compliance
- Loss of key executives
- Actions of other creditors
- Receipt of an ATO garnishee order

- Market/political/regulatory/legal restrictions which impact a customer's ability to operate
- Issues with competitors which may have a contagion impact
- Inability to generate accurate and useful financial information
- A "going concern" comment or qualification by an auditor
- Deterioration in security values, significant asset write-down or impairment
- Externalities such as currency movements, adverse seasonal conditions, failure of major debtor or customer, regulatory change, application of sanctions.

Question 3: Let us assume that you are a model banker and your practices are the best and most appropriate... In what way have you assured your customers that if your bank is taken over by another those practices will remain in place?

...
I want to know how you ensure that those codes of behaviour that you have assured us might be in place have been documented, that your clients can see them and are aware of them and that if you are taken over will bind any successors?

At present, NAB does not anticipate being taken over by another bank. However, in relation to NAB's codes of behaviour and practices, these are embedded into our policies, training and culture.

NAB maintains a Code of Conduct (**Code**) which sets out the standard of responsible and ethical conduct expected of every NAB employee (permanent and temporary), as well as contractors, consultants and directors working at NAB. NAB requires its employees to review and acknowledge that they will abide by the Code, as part of their training requirements.

The Code is published on NAB's website, so there is transparency for our customers.

Question 4: Referring to section 420A. You describe it as a strict legal obligation. Mr Williams or Mr Green, can you tell me whether any liquidator or any financial institution has ever got into serious trouble for breach of section 420A, because I have never heard of one?

As set out in NAB's submission to the Inquiry, NAB's view is that section 420A has been the subject of extensive judicial consideration. As a result, this law has been well tested and there is clear guidance around what practical steps and identifiable processes (for example, advertising and the sale process conducted by the controller) may be appropriate to employ in order to discharge the duty.

There are also various instances where a controller has been found to have not sufficiently discharged its obligations under the provision, for example, see *Investec Bank (Australia) Ltd v Glodale Pty Ltd* (2009) 24 VR 617, *Kyuss Express Pty Ltd v Sellers* (2001) 37 ACSR 62, *Artistic Builders Pty Ltd v Elliott & Tuthill (Mortgages) Pty Ltd* (2002) 10 BPR 19,565 to name a few.