COMMONWEALTH OF AUSTRALIA

Official Committee Hansard

JOINT COMMITTEE ON CORPORATIONS AND SECURITIES

Reference: Provision of bank statements to customers

WEDNESDAY, 16 AUGUST 2000

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JOINT COMMITTEE ON CORPORATIONS AND SECURITIES

Wednesday, 16 August 2000

Members: Senator Chapman *(Chair)*, Senators Conroy, Cooney, Gibson and Murray and Ms Bishop, Mr Cameron, Mr Rudd, Mr Sercombe and Dr Southcott

Senators and members in attendance: Senators Chapman, Conroy, Cooney, Gibson and Murray and Ms Bishop, Mr Cameron and Mr Rudd

Terms of reference for the inquiry:

Provision of bank statements to customers.

WITNESSES

Committee met at 9.29 a.m.

FORD, Mr Bruce Raymond (Private capacity)

MURRAY, Ms Wendy Ann (Private capacity)

CHAIRMAN—I declare open this public hearing of the Parliamentary Joint Statutory Committee on Corporations and Securities and welcome the witnesses who will be appearing before the committee today. The purpose of the hearing is to take evidence on the provision of bank statements to customers. In June the committee resolved to invite the witnesses who will be appearing today to address the committee in relation to this issue. The committee will examine and consider the evidence it receives at this hearing with reference to its statutory duties as set down in section 243 of the Australian Securities and Investments Commission Act 1989. The committee prefers to conduct its hearing in public. However, if there are any matters that a witness wishes to discuss with the committee in camera, we will consider such a request, and I note that we have had one such request in advance. I also remind witnesses that the giving of false or misleading evidence may constitute a contempt of the parliament. I welcome as our first witnesses, Mr Bruce Ford and Ms Wendy Murray. We do have some material from you in the form of a submission, but I invite you to open the proceedings with a statement if you choose to do so and then we will proceed to questions.

Mr Ford—Thank you, Mr Chairman. Firstly, Wendy is going to read our speech. Before Wendy reads that speech, I would just like to say that we feel it is not possible in the time that we have today to cover every matter that we have looked at. What we have done is prepare a submission representative of the practices of the Commonwealth Bank with the relative substantiating documents to assist the committee's understanding. I am sure this will substantiate to everybody present today that what we are saying has some substance. I would like to table these documents, and we request that they be placed on the public record. We have prepared a representative sample of the documents.

CHAIRMAN—Yes, and we will receive those additional submissions.

Mr Ford—Yes, we want to table those now so that they are placed on the public record.

CHAIRMAN—That is fine.

Mr Ford—Thank you. Wendy is going to read that out now if you will bear with us.

Ms Murray—Thank you for this opportunity to present before you here today a matter that has occupied the lives of a majority of us for the past five years. Honourable members of parliament, what we are about to submit to you represents a culmination of many years of exhaustive research and work. We have dedicated all our resources towards seeing that our grievance with the Commonwealth Bank is dealt with in a fair and just manner. Along the way, we have met and spoken with hundreds of people who are also aggrieved by what the bank has done to them. We have encountered many whose experience mirrors the persecution and fraud which we are currently fighting. We are convinced that what we are about to submit to you is part of an extensive and fraudulent operation conducted by the CBA, which is in fact systemic

and potentially affects thousands of their customers. Honourable members, our experience has highlighted a litany of blatant practices designed to maximise bank profits at the cost of small and innocent customers like ourselves.

As background to our current plight, we were previously in primary production until the bank asked us to repay our debt. The CBA's refusal to provide proper statements and details relating to our debt forced us to conduct extensive research that not only covers our own personal experience on issues with the Commonwealth Bank but also includes a number of other customers around Australia in the same situation. However, we do not purport to represent a particular group of people; we are simply putting to the committee a bank practice that we have seen impact in an extraordinarily adverse manner on farmers and small business people.

What we wish to exemplify and provide evidence of is the practice of the Commonwealth Bank relating to the following matters. Firstly, there is the non-issuance of bank statements to its customers, or what purports to be bank statements that are nothing more than what the bank terms 'shadow ledgers'. These ledgers are not provided to the tax office and do not form part of its audited accounts. Bank statements are not shadow ledgers and shadow ledgers are not bank statements. I refer to, secondly, the circumstances in which the bank does not issue bank statements; and, thirdly, what the ramifications are for its customers. Fourthly, the Commonwealth Bank has taken prematurely the benefit of bad debt write-offs from customers' accounts while at the same time preventing the customer accessing any information or statements. This is all done without advising the customer. Fifthly, this is not an isolated case. Sixthly, there is a lack of transparency and honesty as a result of this practice and, when these issues are raised with the Commonwealth Bank, the bank deliberately covers up its practice and engages in dishonest conduct. Seventhly, the bank gains tax advantages by applying this practice, such as premature write-off, non-declaration of interest income and false accounting. The seven points that I have listed represent breaches of the Trade Practices Act, the Income Tax Assessment Act and the Crimes Act.

We are now able to identify a scheme of arrangements that the Commonwealth Bank has entered into in order to minimise its taxation liability. Under this arrangement, the bank has elected to adopt a policy of discontinuing to provide customers with their usual bank statements without the customers' knowledge. This occurs in most instances when the CBA decides to classify a customer's account as a bad debt and make a write-off to claim a tax deduction. The question must be asked: why would the CBA be so determined not to provide statements to customers? The answer is provided from the CBA's own court affidavits and records, copies of which we have obtained. These documents state: first, following write-off, account statements were readdressed to ensure that statements did not issue to the borrower; secondly, readdress statements to issue to branch; thirdly, do not post statements; fourthly, customer never to be told that an account is a loan account. You can refer to tabled documents Nos 1 and 8.

The CBA has been advised that when effecting a write-off upon customers' accounts, for it to be deemed a bona fide bad debt under section 63A of the Income Tax Assessment Act, the CBA must make a book entry upon a customer's account showing the written-off amount in order to satisfy the Commissioner of Taxation. However, the CBA cannot send this adjusted statement to the customer as there would be a number of obvious difficulties, both practically and legally, for the CBA. During our meeting with the CBA's Mr Terry Austin, he advised us that if the bank sent these statements it could mislead the customer. Hence we have a situation whereby the

bank has stopped sending any statements that may divulge information that we are lawfully, ethically and morally entitled to know. As a result, customers are unaware that they are being treated as a bad debt and unaware of any fees and charges being applied to their account. In many cases, these customers' accounts were not bad debts as per section 63A of the Income Tax Assessment Act; they are purely a premature tax advantage for the bank to the detriment of the customer.

The CBA records show that 57 per cent of these bad debts are recovered and in fact are not bad—I refer the committee to tabled documents No. 1, Greenwood Challoner. The real outrage is that, when any of those unfortunate clients go to any branch of the CBA seeking information on their account balance, they would be given the figure from the CBA's mainframe computer which does not include the amount written off. The customer is not told that the written-off amount is accruing interest in a manual ledger known as the 'shadow ledger'. If the customer requests a statement, the CBA gives what purports to be a statement, which is an off balance sheet account referred to as a 'shadow ledger'. The CBA will no doubt tell the committee that it provides customers' statements from its shadow ledgers. These are not true statements: a shadow ledger is not a bank statement and a bank statement is not a shadow ledger.

The bank does not pay tax on the interest accrued in these shadow ledgers until it collects that interest from the customer. The CBA has already advised the *Sydney Morning Herald* and the *Sun-Herald* that it does not pay tax on shadow ledgers until it collects the money from the customer—which is often some years later. Greenwood Challoner, the bank's consultant accountants, advised the CBA that despite using these ledgers it would be liable to pay tax on the accrued interest each year. They also advised that operating such a system could be grounds for the ATO and the court to find that tax should be paid. The ATO law states that tax must be paid on interest in the year it was derived, which is quite different from when it is actually paid by the customer. Australian Tax Office documents confirm that this advice is current today—I refer the committee to tabled documents No. 1. As such, the CBA accrues interest on these bad debts that have been written off without paying tax on the interest—despite the tax law saying that tax must be paid on the interest accrued.

The CBA then proceeds to pursue people into financial ruin on an amount of interest that it should have declared for tax as well as the amount that it has told the tax office it has written off under section 63A of the tax act. The bank's own consultative accountants, Greenwood Challoner, cautioned the bank about the activities that it is considering engaging in: discontinuing to provide the customer with bank statements and not divulging the factual situation to the customer. The CBA knows that this is a deliberate practice and that it deceives the customer into paying amounts that are not a true reflection of the bank's accounts.

Rural and small businesses rely on the integrity and prudence of their respective banker working openly and honestly through the inherent difficulties and variables such as drought or excessive wet seasons of primary production and associated industries. The alarming fact is that anyone banking with the CBA who is, or has been, experiencing financial difficulty could be subjected to this process and, because they have found themselves in a compromised position, the CBA may deliberately avoid providing them with their usual bank statements. This practice of not issuing bank statements is deliberate. It deceives the customers, and CBA gains a tax deduction.

In May 1997, we submitted our matter to the House of Representatives Standing Committee on Industry, Science and Technology and is recorded as submission No. 165. The report titled *Finding a balance* identified problems as follows: firstly, the banks refused to explain why an account had been manually adjusted, even when solicitors for the client made a formal request; secondly, the banks refused to provide information about their accounts when the amount of interest levied and the outstanding balances were in dispute; thirdly, the banks being secretive and evasive; fourthly, the refusal by banks to disclose information about clients' accounts; and, fifthly, the practice of banks opening new accounts for clients on their own initiative and transferring credits and debits between accounts without the permission or knowledge of the clients.

At the time of our submission, it was unknown to us and the committee why the bank was determined to refuse providing the customer with bank statements. Our research has proven that the CBA has a deliberate policy to withhold statements for the sole purpose of deceiving every customer whose account the bank elects to make a write-off upon. There can be no legitimate reason this bank can force customers into spending millions of dollars in legal expenditure just to obtain honest explanations from their bank about their true debt. The CBA must be made to explain to its customers what it does to their accounts. If they are not prepared to be honest then they are not fit to hold a banking licence. Please refer to page 39 of tabled document No. 7.

I will now turn to case studies. In the time we have today, it is not possible to cover every matter. We have prepared a representative sample of CBA customers that illustrates how the bank manipulates these people's accounts whilst not providing statements and pursues them to bankruptcy without substantiating their debt. Briefly, the matters are as follows. Mr Steve Heinrich, a grain producer of South Australia, has been involved in legal proceedings with the CBA since 1992. The CBA transferred a bank bill facility to 12 fully drawn loans without his knowledge or consent. One year prior to litigation and in the course of these proceedings, the bank has not provided bank statements. The bank obtained judgment for an unsubstantiated debt and is now attempting to bankrupt Mr Heinrich. On 1 August 2000, the bank wrote to Mr Heinrich and advised him that, as they now had judgment in their favour, the provision of statements was no longer relevant. The CBA is currently pursuing Mr Heinrich to bankruptcy. Please refer to the last page of tabled document No. 8.

Rothmore Farms Pty Ltd director, Mr Richard Cooper, a grain producer of Moonta, South Australia, disputes the amount the bank claims. Bank statements were never issued when requested. The CBA opened accounts without the knowledge of the company or directors. The Coopers made funds available to pay out the debt to the bank, but the bank refused to enter into settlement. The Coopers were subsequently bankrupted on an unsubstantiated debt. I refer you to tabled document No. 9.

Davridge Pty Ltd, developers of Sydney, borrowed money from the CBA by way of bank bills for approximately $3.5 million. CBA, without the knowledge or consent of Davridge, transferred the bill facilities into fully drawn loan accounts. In 1994, Davridge asked the CBA to explain unauthorised amounts in excess of $7.5 million withdrawn from its accounts. From this point on, Davridge did not receive any statements. The bank then pursued the directors of Davridge to bankruptcy in 1998 for a total amount of $27.95 million, a figure that is unsubstantiated. Refer to tabled document No. 11.

Mr and Mrs Robert Coddington, sheep graziers from Dubbo, New South Wales, requested statements in October 1996 whilst involved in litigation with the bank. Over one year later the bank sent statements showing a zero balance on one of the accounts. The Coddingtons agreed to settle their matter with the bank, reliant on the bank's representations of the level of their debt. CBA now claims Mr Coddington owes an additional $106,000 and has failed to advise him of debt write-offs in excess of $300,000 during the settlement. Refer to tabled documents No. 10.

Mr Brian Jarvis, squash court proprietor from Alstonville in New South Wales, was promised refinance from the Commonwealth Development Bank in late 1996. CBA then advised Mr Jarvis they were taking over the account and were not prepared to refinance. Mr Jarvis did not receive bank statements from June 1998 onwards despite requests from his accountants. He was bankrupted in April 1999 without ever receiving statements. Refer to tabled document No. 12. It should be noted in these studies that the CBA has debited and credited these customers' accounts without their knowledge or consent.

Finally, for our own personal matter, refer to tabled document No. 7. Traztea Services Pty Ltd, horticulture enterprise of Sawtell in New South Wales, was dealing with the Commonwealth Development Bank, the rural arm of the CBA since 1979. We had received a government interest subsidy as the company had been assessed long term viable. In 1993, the bank provided the government with written confirmation it would refinance the company for a further 15-year period. The company was not in default, no letter of demand was issued, and the company's assets far exceeded the bank's lending. However, the bank requested repayment of the loan in full within eight weeks and we were treated as a bad debt so the bank could claim its tax benefits. To this day the bank insists our selling of assets and subsequently closing of our business was voluntary, which is untrue. We were told if we did not repay the money in eight weeks the bank would sell us up.

We agreed to pay the bank because it was our belief that if the bank took possession we would end up with nothing, even though our assets were many times greater than our debt. On 8 January 1996 we contacted the CDB and requested an amount to clear our loans. We were then provided by fax with a figure of approximately $430,000, which was principal and interest to date. On 18 June 1996, we received a fax showing balances of our loans of approximately $563,000, an increase of $134,000 in only five months. As we had paid the agreed interest-only payments on our loans, we phoned the bank and asked the bank to please explain. The bank said that, back in January, Sydney had computer problems.

The bank then ignored requests from our solicitors and us to provide bank statements. As a result we sought the assistance of a member of parliament to request our statements. In September 1996, the CBA attempted to cover up that the bank had mistakenly issued internal bank statements to us. We were told the sum of $134,000 had been set aside when it had actually been written off. Instead of explaining the bank had erred, the bank made a deliberate effort to cover up the use of its shadow ledgers. The CBA then wrote to us inferring the bank would consider charging us interest on the written off sum of $134,000, despite the fact that we were paying the full interest. The bank then created a document, purporting to be a bank statement, alleging the account still reflected the amount of $134,000 inclusive in the outstanding balance, despite the fact it had been written off and was recorded in its shadow ledgers.

The CBA advised on a statement the account as having been divided into portion A and portion B, with portion B being the written off amount of $134,000 and the total debt balance being roughly $490,000. However, bank statements following the portion A and portion B statements do not reflect the portion B sum of $134,000. It has vanished; there is not even a credit entry, nothing.

On 25 September 1996, an amount of approximately $404,000 was paid to account No. 4, yet the account only reflects a credit entry of approximately $355,000. Our bank statement does not reflect the difference being $49,000. Where did the money go? If the bank declared this as income, the $49,000 should be shown as a credit entry on our statement. The bank is exposed, having two sets of accounts running concurrently—one set being the live system which is the true reflex of the bank's records for shareholders and the ATO; the other being the shadow ledgers used concurrently to pursue a customer whilst claiming a tax deduction. We have been writing to the bank's senior managers and board of directors, including the present and previous chairman, for the past four years. We have also met with the bank on two occasions requesting direct explanations as to why we were treated as a bad debt and how the bank could justify what they did. We are yet to receive a full explanation.

We now realise that the bank has been lying to us and covering it up. This is a very serious allegation. We have documents to table that show that the bank's own solicitor, Mr Lanser, who was dealing with us, has shown us that he is prepared to defend matters when he knows that the CBA staff committed acts of fraud. Mr Lanser has illustrated that he and the CBA staff will make honest people spend large parts of their lives trying to uncover what he knows is fraudulent. I refer you to tabled document No. 7, page 39. If there was no problem for the bank, they would have given us honest answers four years ago. In fact, the bank admitted to the chairman of this committee that a junior officer had made an error in handling our account but that we were compensated for this error when it came to the determination of our final debt payout. Why now, after four years of time and money spent by us, does the CBA say this to the chairman and not tell us directly? I refer you to tabled document No. 7, page 2.

We have seen the explanation and the error of a junior officer time and time again—refer to tabled document No. 1: Dearing affidavit. In fact, this is an untruth. These errors are made because the bank has written off money, thereby adjusting the customer's bank statements without telling the customer. When these customers go into any branch in Australia, they are given incorrect balances because the amount on the CBA's mainframe computer does not include the amount written off as this has kept accruing interest on the shadow ledgers. Such write-offs are authorised by branch managers and head office. Further to this, the bank's records show—by fax from the general manager—that we did not agree with the figure that we paid to the bank and that we would be allowed the opportunity to remedy this with the bank. However, the bank knew that we were under contract to settle on the sale of our property. We were in no position to argue. Nonetheless, the bank has never allowed us the opportunity to show in excess of $40,000 interest being overcharged. As recently as two weeks ago, we requested copies of our final bank statements. To our amazement, what we received was completely different to the final bank statements received three years ago. These statements have been fabricated—they are false accounting and a breach of the Crimes Act. The bank must be asked to provide their microfiche to show true entries passed in the bank's general ledger reports to substantiate the true situation and the trail of entries that follow.

Conclusion: we have sought the help of many bodies, such as the Banking Ombudsman, to no avail. The bank has continually beckoned us to take legal action knowing full well that people cannot afford to endure the protracted process. We are not in default; we are not in litigation. We have tried for five years and cannot get answers from the bank. Recommendations: compensation for the people that have been subjected to the practices we have outlined. There are too many people in Australia affected by the issues raised today. The cost to the community is enormous and the cost to taxpayers of Australia is millions of dollars. A royal commission is needed now.

Mr Ford—I have some documents that I would like to circulate for the committee. These documents will give you a graphic illustration of what we have just been trying to outline. I think that will fix the matter clearly for everybody.

CHAIRMAN—We will receive those.

Mr Ford—Could we circulate those and then I will go through them.

CHAIRMAN—Mr Ford, you may proceed.

Mr Ford—The first document, at page 1, represents when we received our original payout figure. It is dated 8 January 1996.

CHAIRMAN—This is the cover sheet.

Mr Ford—Yes, the facsimile cover sheet.

CHAIRMAN—Perhaps if you can identify them each time you refer to a document.

Mr Ford—Okay. It is sheet number one. It shows a payout figure of $435,000 approximately. You will see on page 2 handwritten facsimile advice from the Commonwealth Development Bank, $563,000.

CHAIRMAN—Before we proceed, Ms Bishop would like to ask a question of clarification.

Ms JULIE BISHOP—On document 1, who wrote the handwritten figures, $435,901?

Mr Ford—That was written by ourselves.

Ms JULIE BISHOP—So that was not on the fax when you received it?

Mr Ford—No. That is the only adjustment there. We put that there and highlighted it.

Senator CONROY—That is the addition of those two numbers.

Mr Ford—Yes. Then on page 2, you will see the highlighted figure and the respective date, 18 June 1996, up in the top left-hand corner. The figure there is $563,000. That figure has increased from 8 January that year to 18 June that year by $134,000. That relates to the

submission that Wendy read out. We were servicing that debt and paying all the interest, which was what the bank's request was at the time. If you turn to page 3—

Ms JULIE BISHOP—On document 2, are there any of your figures on this or is this how it appeared?

Mr Ford—The $563,000 is our addition. When we received this figure, we sought to get advice from the bank as to what was going on. We were given the following explanations: the bank had computer problems back in January; the bank wrote the money off—

CHAIRMAN—This was the $134,000?

Mr Ford—Yes. Then the bank wrote to us in June or thereabouts that year claiming that they had set the money aside—the $134,000. The bank had stopped sending us bank statements at that point. We got our solicitor to request from the bank our statements and that request was ignored. That is tabled in the relevant documents. The solicitor tried twice and then we engaged the assistance of a member of parliament—at that time, Mr Eric Ellis. It was only after that that we received this. If you look at page 3 you will see, highlighted down the column there, figures showing that we were paying interest on a monthly basis for the total sum of the debt. That is the sum inclusive of this $134,000 figure. We were servicing our debt interest-only in total as the bank had requested and the tabled documents are there to substantiate that. With respect to the portion B, we allege that this is an off-balance sheet figure and it is just a synthetic account to suit the bank's own purposes.

When we settled with the bank—and we can go through that point—there was a great deal of questioning between ourselves and the bank to try and get an explanation, which was never forthcoming. The bank went out of their way to give us every excuse to cover this thing up. Eventually, we engaged in discussions with the General Manager of the Commonwealth Bank, Mr Russ Weaver. Discussions there transpired where Mr Weaver, the bank says, compromised on its debt. There was a reduction in the payout figure. So we, under duress we say—we certainly do not accept the practices of the bank at that time—were in a position where we could not argue with them. We had exchanged the contracts on our property and we could not back out of the deal. The bank knew that. Nonetheless, they knew that we were starting to ask a lot of questions. The bank compromised on the debt. The comments from Mr Weaver—which are on the public record in finding the balance documents for the standing committee—were, 'Take it or leave it. We'll see you in court,' which is effectively the tactic of the Commonwealth Bank. They seem to say that to most people.

When you get to page 4, there is a most interesting development from this point. We settled on our property in September 1996 and paid the bank the sums reflecting the compromise with Mr Weaver. We received this statement in August 1997 and the portion B had vanished—it had disappeared. This statement was issued on 4 December 1996 and the portion B had vanished. The credit entry shows $355,000, which is highlighted at the top. We in fact paid the bank $404,000. That raises the question: where did the $49,000 go? We started writing to the bank and we have done that for the last four years to try to get answers in relation to this. To this day we have been met with responses like, 'If you give us a meaningful reason as to why we should give you bank statements and explain all this—' We have to give them a meaningful reason as to where our money went! Eventually—since this hearing has been announced—on 18 or 20

July this year we received page 5. Amazingly, this statement was issued on the same day—4 December 1996—and the portion B had reinvented itself.

If you look at page 4 and page 5 together and look at the left-hand corner, you will see that these statements were issued on the same day—4 December 1966. They are completely different. The $505,000 credit entry there is completely different to the total credit entry on the statement received three years prior, but they are dated 4 December 1996. So we are looking at this now and saying, 'How do you have two bank statements on the same day issued three years apart that are meant to be the same bank statement?' and we are saying that the page No. 5 is only a result of this hearing. That is the only reason they have put this up. This is a complete fabrication. If it was right, we would have got the page No. 4 prior.

The documents tabled from the Commonwealth Bank, dated 27 November 1997, signed by Mr Terry Austin, confirm that page No. 4 was, in fact, the final bank statement and that it was correct. We questioned it. The bank has had three tries at getting it right here and they still cannot get it right. I think it has got something to do with what they are trying to tell us.

We met with the bank's Mr Lanser and other officers. We asked for explanations at that meeting, which was at about March 1999. We wrote on four occasions to the bank's Mr Ross Griffiths, Mr Robert Wawrzyniak, Mr Anthony Higgs and Mr Peter Dicker. All of the answers that came back were not telling, unless you refer to Mr Griffiths's letter, which responded that they would only tell us if we litigated. It is an extraordinary situation that we have to sue them for the truth. It is clearly a cover-up. This is what we have had to go through, and we are not in the litigation process.

That, senators and members of the committee, is the short version of our battle with the Commonwealth Bank to get honest answers. There is a moral issue here; there is an ethical issue here. People are entitled to get the truth from the bank's mainframe computer, not from shadow ledgers; they have a right to get their statements from the bank's mainframe computer, not from shadow ledgers, which are two separate things. We want bank statements from the bank's records that they provide to the ATO, not from some off balance sheet record that bears no reflection to their books of accounts for taxation purposes. If the bank wants to have its tax practices the way it does, it has no right to do this to people. And it has no right to bankrupt people on a debt that it will not substantiate.

CHAIRMAN—Can I just encapsulate what I see as the issues coming out of the evidence that you have given this morning. Correct me if I am not on the right track. As I see it, what you are telling us is that the first issue is the refusal of the bank to provide you with statements. The second issue is that the statements that were provided were inaccurate. The third issue is what you alleged to be tax rorting through the maintenance of shadow ledgers. Is that a correct encapsulation of the issues?

Mr Ford—Could you run that by me again, Senator.

CHAIRMAN—Failure of the bank to provide statements.

Mr Ford—Yes.

CHAIRMAN—The inaccuracy of statements that were provided.

Mr Ford—Yes.

CHAIRMAN—And some rorting of tax through the maintenance of shadow ledgers by the bank.

Ms Murray—Not only the failure to provide statements. Sometimes they do issue statements that purport to be statements that are not: they are fabrications.

CHAIRMAN—That is covered by my comment about inaccurate statements.

Ms Murray—Well, as long as we are clear.

Mr Ford—Inaccurate statements, Senator, versus synthetic statements—

Ms Murray—This is the problem.

Mr Ford—Are they really statements? They know they are not statements. There is a big difference there. You can say, 'The bank gives the customer the statement.' Is it a real statement?

Ms Murray—Is it the one that everyone else gets: that the tax office, that the shareholders get?

Mr Ford—We are talking about a bona fide document and it does not constitute false accounting. We are talking about mainframe statements that they would provide to the authorities—the ASIC or the ATO—for whatever purposes. They are the statements we are trying to clarify. That is the real issue that we are trying to get across here. We do not claim to have any claim upon the bank's accounting practices. If there is a tax issue here and if we are wrong—that is not the issue. We are saying that people have a right to get statements that are a true reflection of their account from the bank's mainframe system. There should be no reason—if the bank does not have any problems—why they would object to that. And the question must be asked, 'Why?' The answer to that lies in the documents we have tabled.

CHAIRMAN—As I recall, in the earlier discussions I had with you when you raised this issue with me, you acknowledged, I think, at the end of the day, that the settlement you reached with the bank meant that you were not, in effect, financially disadvantaged by what had occurred.

Ms Murray—We were. We did not agree with what we paid the bank.

Mr Ford—I never said that.

CHAIRMAN—You didn't?

Mr Ford—No.

Ms Murray—We are saying that we were under contract to sell our property but the bank compromised the debt and said, 'Take it or leave it.' We got one chance, one offer, and that was it.

Mr Ford—We were told, 'That's the deal. Take it or leave it, or we'll see you in court.' In our situation, what does one do? The position we were in was one of being subject to the exploitation of power. The bank said to us, 'This is how it is.' Now we do not accept that, and we never have. So I did not say that.

CHAIRMAN—So, even though the amount that was paid out was less than the bank said was the total amount owing, you would still dispute that that was the correct amount?

Ms Murray—That is right.

Mr Ford—That is right.

Ms Murray—We say that the amount we paid them is not right. When we spoke to the general manager at that time, we also made him aware that we had been overcharged interest, as well. He said, 'We'll come back later on and sort that out.'

Mr Ford—And he has put that in writing.

Ms Murray—So clearly the bank knows that we were not happy.

Mr Ford—The bank knows full well that what they are saying—to say that we were adequately compensated—is an absolute farce. It is all there on the record.

CHAIRMAN—Are you claiming that the maintenance of shadow ledgers is, itself, illegal?

Mr Ford—I am not a lawyer but I find it highly dubious, at best, to say that it is ethically or morally acceptable. If the law does not classify it as illegal, I am saying that it should be changed.

CHAIRMAN—I will read to you from the bank's letter in response to my raising your issues with them:

When a borrower is complying with the contractual obligations they agreed to when the Bank advanced money to the borrower, we add interest as it accrues to the loan and report it as income in our financial statements.

When we have reason to doubt that the borrower is going to meet their obligations, we may (based on our assessment of whether the borrower will deal with their financial difficulties) stop recording the interest as income in our financial statements as we do not want to mislead shareholders.

We may also record a provision internally against the amount of the loan balance owed by the borrower to reflect any shortfall that may arise in the ultimate recovery of the loan (taking into account the value of any security given by the borrower). However, the borrower is still legally bound to repay the loan balance outstanding, including any interest due in accordance with the loan contract.

The Australian Taxation Office (ATO) does not allow the Bank to record the loan provision as a deduction against taxable income. The ATO takes this view because at law, the borrower is still liable to honour their commitments to the Bank and

the deduction is not available until a debt is written off as bad. Further, in some circumstances the ATO requires the Bank to pay tax on this ongoing accrued interest, even though it is not recorded as income in our financial statements.

The ATO only allows the deductions to be taken when the Bank can demonstrate it has taken appropriate steps but failed to recover the loan balance outstanding and has subsequently written the debt off as bad.

Accordingly, for legal and tax reasons, the Bank is required to keep separate records of the amount owed by the borrower (which differ from the records used to prepare the financial statements). The record maintained of the borrower's ongoing legal obligation has become known as the "shadow ledger".

If a borrower whose loan is judged to be in doubt makes repayments (cash, security sale proceeds, etc) their legal debt to the Bank will be reduced accordingly, and any interest paid regarded as income in the financial statements. These amounts are separately disclosed in our financial statements on a basis agreed to by APRA.

That is the bank's explanation of what happened in your case. Would you like to respond to that?

Mr Ford—I would, Senator. If I have captured the points that you have read to me—

Ms Murray—It is quite a lot to respond to—

Mr Ford—I am going from memory so I stand to be corrected. What the bank says there is absolutely correct; I do not argue with that. It is a very precise definition of what they should be doing. They use the word 'provision', and they may well provision as they will; it is a perfectly legal process and it is not in dispute.

On the question of the securities, the bank may if, by its own judgment—whatever the words were—it feels that the borrowers' securities are not adequate or they justify their reasoning for making a provision—reflects or relates to the amount of security held. How one interprets that value is open to question. However, in May the year previous to making that provision the bank received an assets and liability statement from us in excess of $1.5 million on a debt that we were servicing and which the bank statements clearly show. They had a claim to us, on these statements, of approximately $560,000—and let us give the bank the benefit of the doubt. However, the securities that we held at their behest were all insured. The stock is insured for $750,000—one-third of its wholesale value. The point is that, because they had enough securities there for a provision to even be made, the suggestion is that it was a bit overzealous at best. Now, we were making our payments on that loan, and the interest payments are meant to be book entries. Under tax law they have to make book entries to make the entries deemed correct—not an off balance sheet ledger brought backwards and forwards onto two sets of books.

If it was a write-off, it was a write-off, and the bank has to justify it, I think you said, in accordance with APRA's regulation. If it is a write-off, it is not meant to be accruing interest. I have shown you the bank statement at page 3 of the documentation where the bank is collecting $5,490 per month interest—as per the letter which I think I faxed to you, Senator, on the eve of the hearing. That letter clearly showed that the bank was saying, 'Provided that you make interest only payments, we will continue doing what we are doing.' We had a buyer for the sum of $560,000, which was going to completely clear their alleged debt. There were other securities in terms of real estate—a home and other land. There were adequate securities there. Payments were made. I agree with that letter, Senator; however, there is a question as to what they were doing with this account.

CHAIRMAN—With regard to the statement that appears on page 3 of the documentation you have given us, you are saying that $5,490 was an interest only payment on the total debt, including the $134 set aside?

Mr Ford—Yes.

Ms Murray—We relied on the bank to tell us that figure.

Mr Ford—The bank advised us of that in writing.

Ms Murray—The bank said in letters to us, 'You pay this much money.' At the time, we did not know what that amount covered. We relied on them.

CHAIRMAN—But from looking at the statement, it seems to me that they have in fact credited this as both an interest and principal repayment of portion A—

Ms Murray—That is correct.

CHAIRMAN—rather than interest only on portion A and portion B.

Mr Ford—That is correct.

CHAIRMAN—Why do you have the understanding that it was an interest only payment on the total amount if the statement shows that it is—

Mr Ford—This is the wonderful benefit of hindsight. This statement had not been invented when we were paying that $5,000-odd a month. We did not know about portion B—they had not told us—until we got the statement of 18 June, which is at page 2 of the documentation. I will come back to that statement, if you like. We were servicing the debt on a figure that we did not know anything about. We did not know anything about this $134. That is the first time we got to find out about it.

CHAIRMAN—When you got this statement?

Mr Ford—Yes, that is when we found out what they were doing.

CHAIRMAN—Again, that reinforces my question: what lead you to the conclusion that that was an interest only payment on the total amount rather than a P and I payment on portion A, if you did not know that portion B even existed?

Mr Ford—There was the letter that I think I faxed to you—I cannot recall what number it is on the tabled documents—saying that the 'interest only' repayments would continue to be maintained.

CHAIRMAN—Yes, I do recall seeing that. I think the fact that that letter was sent to you needs to go on the record.

Mr Ford—We were doing what the bank asked us to do.

CHAIRMAN—This is the letter of 17 May?

Mr Ford—That seems to be correct: signed by Mr A.W. Higgs?

CHAIRMAN—Yes. It states:

In the interim, we trust the "interest only" repayments will continue to be maintained ...

Mr Ford—Yes.

CHAIRMAN—And this was the amount of $5,490 that that letter is referring to?

Mr Ford—Yes, and we have documents to say that that figure has been sighted.

CHAIRMAN—What is your evidence, or is it purely supposition, that the bank was doing anything untoward in regard to taxation arrangements, given the comments they made in that letter that I quoted to you?

Mr Ford—We are not accountants and we do not profess to be. Our understanding of this has evolved out of just wanting to know what is going on and getting down to find out. In the responses we received from the bank when we started to question this, the bank were clearly trying to cover up. If there was not a problem at the start as to what was going on, they would have just told us.

When we asked, we got told things like computer problems being set aside. The bank put it in writing. Just after we asked the question the bank wrote to us in a letter I think dated 20 June 1996. I do not believe you have a copy of it there but it is certainly in the tabled documents. The bank said that, in response to our question as to what was going on, the difference between the two payout figures of $430,000 and $560,000 of approximately $134,000 had been set aside as an internal accounting procedure. That is not a provision and a write-off. Senator, can you clarify your question if I was getting off the point?

CHAIRMAN—It was whether you had any hard evidence to support your allegation that there was some untoward tax arrangement involved here, given the letter and the explanation in that letter I quoted to you.

Mr Ford—We were told by the Commonwealth Bank in writing in 1997 that they had inadvertently given us the incorrect figures and that the money was written off. When we met with the bank's Mr Ross Griffiths and Mr Robert Wawryzniak, we were told that the money was provisioned in June and July 1995 and written off on March and June respectively of 1995 in that financial year. We were told by the bank that they wrote the money off.

CHAIRMAN—They had written off rather than set aside.

Mr Ford—Absolutely. They told us and they have put it in writing. I think they have forgotten that, Senator. It is getting a bit complicated for them to keep track of what they have written. They wrote to us in November 1997 and told us that they wrote the money off.

CHAIRMAN—Do we have that letter?

Mr Ford—No. I do not think you do have it.

Senator COONEY—They have written off or set aside?

Mr Ford—They wrote to us in a document dated 27 November 1997, which is one of the tabled documents here.

Senator COONEY—The only reason I asked that is that in that letter of 24 June 1996 they talk about 'setting aside' rather than 'writing off'. I was wondering whether they used the phrase 'setting aside' rather than 'writing off'.

Mr Ford—Initially they used the phrase 'setting aside'. That is when we asked for an explanation. They open that letter up by saying, 'We respond to the question of what has been going on'. It acknowledges that we were asking.

Ms JULIE BISHOP—An explanation of the loan balances.

Mr Ford—Yes. They come back with 'setting aside'. They could have just told us—

Senator COONEY—I want to get some clarification. Do they later use the words 'writing off'?

Mr Ford—Yes, they do.

Ms Murray—At that time we were told a number of things. We were told the bank had computer problems. We got that letter. We were told it was set aside. Also we have a fax confirmation for a conversation with the bank's Mr Peter Dicker that says that the bank wrote the money off. At that period of time we had many different explanations within two weeks and we could not fathom it out.

CHAIRMAN—In this letter of 27 November 1997 they are responding to points that you have raised with them. In 1a) it says:

As previously advised **the loan balances** have inadvertently omitted the $134,000 written-off by the bank

Then in b) they say:

As previously advised **the payout figures** in this facsimile include the $134,000 write-off.

Are they referring there to the payout you provide to the bank?

Mr Ford—They say it includes the write-off. They say it was written off.

CHAIRMAN—So they have written off, but then they have written it back in?

Mr Ford—Yes.

Ms Murray—But the pay-out figure in January does not include the written off figure.

Mr Ford—Senator, this is the letter signed by Terry Austin, who we met with, and his offsider confirmed it. The top paragraph of the last page, from my memory, will speak of it, but it confirms the write-off again. But what I was wanting to draw to your attention is—

CHAIRMAN—Page 3?

Mr Ford—Page 4.

CHAIRMAN—The bottom of page 3, isn't it, where the bank elected to write it off?

Mr Ford—The bank there is confirming the money was written off. On the bottom of page 3 it says:

The bank elected to write off on the 10 March $100,000 and $34,000 on the 19 June 1995 ...

This was confirmed in our meeting with the senior bank staff, including Mr Griffiths.

Ms Murray—And this is all while we are paying the loan.

CHAIRMAN—What do they mean there? It goes on to say, 'which you appear to have attempted to claim were deposits initiated by yourselves'.

Mr Ford—Yes, they are trying to say that we are saying that we paid the money. We are not saying that we paid the money; we never have. On the back page, page 4, giving the bank every benefit of the doubt here, the third last paragraph from the bottom says:

On the issue of statements, I have verified from the Bank's files that the statements you have been provided are correct and cover the full period of the loan from funding until settlement.

Those statements he is referring to, which are termed by the bank as final bank statements—

CHAIRMAN—This is page 4 of this document?

Mr Ford—Yes, page 4 of that document as well, yes.

CHAIRMAN—Sorry, just go over that again. That is the amount there, is it?

Mr Ford—The letter of 27 November—

CHAIRMAN—Is it referring to these amounts?

Mr Ford—It is referring to those statements. That bank statement in the tabled document comes with a cover letter. If you look at the copy of that bank statement, page 4, it comes with a cover page, which is tabled, confirming in writing that these were, in fact, the final bank statements. This brings us back to an interesting situation. I am going to point out something to you. The bank has gone to every effort to say that they have written the money off to us. They have put it in writing, they have substantiated what we confirmed at a meeting and there is a statement, page 4, issued to say that that is your final statement.

Ms JULIE BISHOP—The letter you are referring to—you said that has a fax cover sheet?

Mr Ford—A cover letter, yes. I do not know if it is in there.

Ms JULIE BISHOP—Not the one of 18 September enclosed?

Ms Murray—It is in the tabled documents in the tab highlighted 'bank statements'.

Ms JULIE BISHOP—Because we have got one that includes a statement on page 3.

Ms Murray—The third page from the back, Senator.

CHAIRMAN—This is a fax of 20 August 1997?

Mr Ford—Correct.

CHAIRMAN—It says:

I refer to your facsimile dated 20 August 1997 regarding the final statements for the above Term Loans. We now enclose the final statements for the above Term Loans as requested.

Mr Ford—That is page 4.

CHAIRMAN—It is page 4 on this document.

Ms Murray—But you will note that we paid the loan out in 1996 and we did not receive those final bank statements until we requested them, and you will also note that we received them August 1997. So those bank statements did not come out to us until one year later upon our request.

Mr Ford—To simplify it and so it is very clear for you, because it is fairly simple when you can see it as clearly as we do, this statement, page 4, where our final statements were issued, it must be noted, said they were issued on 4 December 1996. Page 5 is purporting to be the same bank statement issued on 4 December 1996 and, hey presto, you have got another $134,000 back. It comes and goes at will.

CHAIRMAN—Received three years later?

Mr Ford—Yes, received three years later. I do not know whether they produced this batch in the morning and this batch in the afternoon of 4 December 1996 but, obviously, there is a big

question here that the bank is going to have to address as to whatever their accounting practices are. We spend four years of our lives writing for answers, and we get it varying three years at a time and digressing each way. It is clearly a question of what is going on, and why so many variances to the truth, and I do not believe the truth is there. I think this exemplifies the treatment that everybody has been getting on this matter.

CHAIRMAN—I guess there is the old comment that, if you have a choice between a stuff-up and a conspiracy, you choose the stuff-up. But you are saying, in fact, saying that it is a conspiracy.

Mr Ford—There is a bit of Shakespeare in there too isn't there—something about tangled webs?

Senator COONEY—You seem to have another problem. Following on from the chairman's question as to whether it is a conspiracy or a stuff-up, you seem to be saying that the bank uses the legal process as a threat rather than as a means of resolving matters. In other words, instead of using the law or the legal system—the court system or whatever expression you want to use—as a means of disposing of a matter fairly, they use it as a threat to make sure that you are not able to take the matter any further. Is that what you were saying?

Mr Ford—I think that is an excellent question. That is what I am saying and that is what we are saying. That is what people have been put through. We have not been through the court process as most people have. In one of the cases that we put here—Davridge—the company spent $3 million on legals only to find out that they were going to be bankrupted on a debt that was in the vicinity of $5 million in 1995. They were bankrupted and the bank has effected that bankruptcy on something like $27 million. That is a fairly hefty increase; I think it is in the order of 700 per cent over the period. But to answer your question—is the bank abusing the process and using their legal muscle?—on page 39 of the submission that we have tabled for Traztea—

CHAIRMAN—It is a letter from Mr. Griffiths.

Mr Ford—It is Mr Griffiths's letter in response to me. I think I mentioned earlier that we asked four senior members of staff for an explanation about the bad debt: how they treated our account and why they were doing this when we were servicing the debt. We sent faxes to four of the senior officers who were handling this matter and they responded to us. In this letter they said, 'You are not going to get told unless you initiate legal proceedings'.

Senator COONEY—So the culture that you are detecting in the bank is not a culture of someone trying to help you to create wealth and then going along with it. As somebody put it the other day, they are more into sales than services. My understanding of what you are saying is that their culture is one of getting what they can from their customer and, if the customer fights back, threatening them with heavy legal expenses.

Mr Ford—That is a fact, Senator. I recall my initiations in dealing with this bank and I can only speak with praise, but there has been a definite transition from a great bank to a bank that has lost some sort of scruples in terms of that very point of dealing with the customer. I do not see how the bank can reasonably justify putting honest people through this process. This is all

about four years of writing to the board of directors and saying, 'Please tell us.' This is why we are sitting here today. We are someone who has stood up and said we are going to keep asking until we get to the bottom of it. There are many people who have been bankrupted and are just too humiliated and their lives devastated. So on that point we say yes to your question.

CHAIRMAN—Your dealings were actually with the Commonwealth Development Bank weren't they—the actual financial transactions.

Mr Ford—Yes, the rural arm of the Commonwealth Bank. But when you talk Commonwealth Bank or Commonwealth Development Bank you still feel like you are dealing with the same bank.

Ms Murray—The same people were dealing with us as the Commonwealth Development Bank as if you were a Commonwealth Bank member, so it was the same section.

Mr Ford—To clarify that point further, in the people's matters that we have looked at, the people that we are dealing with are the people that these other customers are dealing with the same. So it is a sort of—I am not sure of the word, but—

Ms Murray—The same section in the bank seems to be handling both the Development Bank and the Commonwealth Bank.

CHAIRMAN—The Development Bank no longer exists as I understand it.

Ms Murray—That is right.

Senator COONEY—You seem to be saying that the same culture is across both.

Mr Ford—Definitely.

Senator COONEY—There might be a distinction in location but there is no distinction in attitude and approach.

Mr Ford—That is correct, yes. There is a section in the bank—I think it is the Group Credit Policy Control Section; the name changes.

Ms JULIE BISHOP—Mr Ford, you refer us to a letter of 8 April 1999 from Mr Griffiths to you and you use that as an indication of the bank's attitude to providing information; that is, that it will not unless it is part of a litigation process. By that stage, you had made a number of very serious allegations against the bank, had you not?

Mr Ford—No, I had not. We met at that stage with the bank because of dialogue we had had with the bank and because of legal advice that we had taken. We were not in the litigation process per se. We had prepared an actuary to put to the bank to get us a bit more of an objective direction in order to resolve it. The actuary was prepared by Horwarth Services.

Ms JULIE BISHOP—Yes, I have seen it.

Mr Ford—It cost quite a lot of money. That was them saying to the bank that they would take it prematurely—that advantage. That was not us.

Ms JULIE BISHOP—Could I just clarify that point. Had that document from Horwarth Services been seen by the bank by this stage?

Mr Ford—Yes.

Ms Murray—When we settled with the bank, the bank clearly knew that we were not happy and we did not agree with the amount. That led us to prepare this Horwarth Services report and that went on from there. Once we gave the bank the Horwarth Services report, we wrote to the bank and they agreed that we would have meetings to discuss a resolution. Once we presented this report to the bank, there seemed to be no resolution and we received this letter, page 34, saying that we would have to litigate to get the answers.

Mr Ford—That was after our meeting.

Ms Murray—We were endeavouring to sort out this problem. We had spent a lot of money preparing an objective report for the bank to tell us that we had to litigate to get the answers.

Ms JULIE BISHOP—I just want to get that letter in context. Their response was that they would not provide additional information other than as part of a litigation process. At the time they wrote that letter, they had received a copy of the document from Horwarth which indicated that your companies had suffered economic loss to the tune of $1.2 million and that your solicitors had indicated that the bank could be liable to pay unliquidated damages as well.

Ms Murray—That is correct.

Ms JULIE BISHOP—So the bank was well and truly on notice that there were some very serious claims being made by you at that point. Are you aware that there are requirements of insurers and others that once an entity is on notice of claims they must take an extremely prudential approach in terms of ensuring that there are no admissions of liability outside the legal process?

Mr Ford—I accept what you are saying.

Ms JULIE BISHOP—I am just saying that the letter that you referred to should be put in the context of a fairly substantial claim having already being made against the bank.

Mr Ford—Yes, I accept that and I take your point. The letter that we are talking about—page 34—also referred to a fax dated 7 April.

Ms JULIE BISHOP—You are saying that the material requested is very relevant to your claim. In other words, you are asking the bank to provide documentation to support the claim that had been set out in the Horwarth report. Their response was, ‘We are not going to provide you with any more documentation other than as part of a litigation process.’

Mr Ford—Yes.

Senator COONEY—How did you get to the point where there was litigation in contemplation?

Mr Ford—There is no litigation in process, Senator.

Senator COONEY—No, but in contemplation. You got to the point where the issue of litigation was raised.

Mr Ford—Just to give you an understanding of our mind at the time, Senator, the last thing we wanted to do was to get involved in litigation because our experiences have shown that you just do not win in a legal process with the Commonwealth Bank. They will deep pocket you.

We were not contemplating litigation. We prepared that Horwarth Services report to show the bank what we thought was an objective, honest view as to how we felt. The other thing was that the general manager of the bank, after we settled, said, 'Subject to you coming back and clarifying your claim for interest overcharges, the bank will view that with fair consideration.' The bank knew we were not happy with the payout. We were addressing where we left off. The point was—and I hope this clarifies the matter for you and Ms Bishop—that we were not contemplating litigation. We were trying to be objective. We honestly believed that the bank was going to be sincere about it. I think that was a serious mistake on our part.

CHAIRMAN—But you could understand from the bank's perspective they might interpret that as a first step on the road to litigation and therefore their response is based on that conclusion.

Mr Ford—Yes, I do.

Senator MURRAY—I apologise to the committee; I was caught up in a debate in the chamber and I will have to return to that. I have a question which will probably back up on all the other information you have given to the committee, Mr Ford. Am I given to understand that your motive in raising the issue of how banks deal with bad debts, the statements attached to it and the shadow ledgers allegation, is because you think that that is improper behaviour on the part of banks?

Mr Ford—Absolutely, Senator. We are saying that if the customer is to be treated as a bad debt, banks have a right to do that. However, if there is a question as to whether the debt is bona fidely bad, that is for the ATO to assess and we leave it with them. We are saying that their application of tax law and accounting law should not impact on customers. With respect to what they want to do with their books, all we are saying is none of this would be going on and none of these people would be suffering if the bank provided bank statements from the mainframe ledger, the true ledger, the true reflection of the company accounts, which would immediately clarify what they are doing.

Senator MURRAY—And am I given to understand that two threads come from this: one which reflects the private interest and one which reflects the public interest? The public interest is an extension—I am not sure you have made this allegation—that banks are, through this

device, avoiding their proper taxable declarations and, at the private interest level, the consequence is to put bank customers in a position of having insufficient information about their financial and legal status and in a situation of stress and uncertainty when their financial affairs are revealed later to be different from what they understood them to be. That is my understanding of the two themes.

Mr Ford—Absolutely. Just to reinforce that, it is a very serious statement that we have put forward in these documents regarding tax but we are not just coming out and saying this without substantiation. The documents that we have tabled to date clearly show that the bank took advice on this very issue and they were told that they could not do it because it was going to be in breach of the law. On top of that, the internal memos that were circulated through the bank, while they were circulated in 1985, confirm that their acknowledgment of this advice would be in contravention of the tax act and that if it went to court, they would be found guilty of what we are saying. That is for the ATO to assess and we have tabled those documents. On the private issue of the stress and how it impacts on people's lives, it is immeasurable and there must be a social cost to the community and to taxpayers as well.

Senator MURRAY—In raising this matter, are you raising it as the leader of a group of people who have had similar experiences or in your own right?

Mr Ford—Both, but not as the leader of a group of people. We did not choose to get propelled into this position. Certainly our own matter represents, we believe, a lot of people—in fact, many Australians. It is to the credit of a lot of people who joined hands to have got to this stage and expose what has been going on. A lot of people have had trouble talking about it.

Senator MURRAY—The chair might have thought of this but has omitted to mention it: you would not be experienced with these forums, so I suggest that if, as a result of your discussions today, you feel that there are further points you could have made or would like to make, committees like ours will always accept supplementary submissions.

Mr Ford—Thank you. I appreciate that.

Senator GIBSON—In your business or businesses, undoubtedly you would have had bad debts.

Mr Ford—No. I have never had to deal with this sort of accounting treatment until now.

CHAIRMAN—You are talking in relation to your clients?

Senator GIBSON—Yes, your own business.

Mr Ford—I can honestly say no. I should be grateful when you ask me that question, but no.

CHAIRMAN—There being no further questions, Mr Ford and Ms Murray, thank you very much for your appearance before the committee this morning and for your answers to our questions.

[10.48 a.m.]

MADIGAN, Mr Bernard Ernest (Private capacity)

CHAIRMAN—Welcome, Mr Madigan. We have before us some documents that you have presented to the committee today. Do you wish to make an opening statement?

Mr Madigan—I have presented the documents as an affidavit. That is the way that I am used to doing these sorts of things these days. I am currently in litigation with the Commonwealth Bank of Australia over a number of matters. Among those matters is the withholding of statements and bank statements.

CHAIRMAN—That is the issue that is before the committee in this inquiry—the withholding of statements, the issue of shadow ledgers and so on—so I would appreciate it if you would keep your remarks specifically to the terms of reference.

Mr Madigan—I will read out the affidavit that I have submitted because I do not think that everybody has got a copy of it. It is a factual document—it is an affidavit—and it is supported by annexures which I do not know if everybody has got. I have kept the affidavit to matters within the terms of reference of the inquiry.

CHAIRMAN—I do not think you need to read the affidavit because enough of us have it and can share it around.

Mr Madigan—I did not know if you had enough.

CHAIRMAN—Perhaps you could just summarise the issues that are in the affidavit.

Mr Madigan—I will run through it quickly. My business with the Commonwealth Bank started in October last year in the Supreme Court when the bank issued a summons on me and a default notice. I satisfied the default notice within the default period, which was seven days. Since I satisfied the default notice and I had paid the loan off, I asked the bank to provide me with the closing statement of my account.

The bank refused to provide me with the closing statement of my account. I paid the account up and closed the account on 10 November. If you look through the annexure you will see that the bank manager gave me a letter to say that the account was closed on 10 November. I will give you the page number, because I actually closed the account a few times. It is annexure J. This is all very hard-hitting evidence which you are about to see. On annexure J you will see a letter given to me by the bank manager of the Ermington branch on 15 November. The first sentence says:

This letter serves to confirm the above loan was repaid on 10 November 1999.

He goes on to say that ‘documents have been requested to be forwarded to this office’ and will be given to me on their receipt. I discovered in December that, even though the account had

been closed on 10 November, withdrawals were still being made from it. On 16 December—and this is on annexure K—I wrote a letter to the bank requesting, in part 4: how is it possible to apply a debit—

Senator COONEY—I am sorry, I am a bit lost here.

Mr Madigan—Annexure J is where the bank confirmed that the account was closed on 10 November. On 16 December I found out through a telephone help-line inquiry that the account was not closed and I said to the bank, in the letter on 16 December: how is it possible to apply the debit to a closed account? That is on annexure K. The bank replied in a letter that they wrote on 11 January. Mr Lanser from the bank replied to me with an explanation—

CHAIRMAN—Do we have this in here?

Mr Madigan—Yes, that is on page 1 of annexure L. The explanation was of how the account was still accruing withdrawals after it was closed on 10 December. His explanation—I am looking at clause 3 of the first page of annexure L—was that on 15 November 1999 $65 was taken, being the fee for procuring a transcript of the argument before Justice Santow. So there you have a situation where $65 was taken out of the account five days after it was closed, to procure an argument before Justice Santow. That would be all right except that the argument before Justice Santow did not happen until the 16th, the following day.

Ms JULIE BISHOP—That may well be the day that they were required by the Supreme Court to pay for the transcript—

Mr Madigan—No, because the argument—

Ms JULIE BISHOP—because you often order transcripts in advance.

Mr Madigan—You order transcripts in advance, but the matter before Justice Santow was an unlisted matter. It was a hearing for directions in front of the registrar which was redirected to Justice Santow on 16 December. The matter in front of Justice Santow was a matter in which I was awarded two court orders against the bank: one of the court orders was for the bank to file its defence to my cross claim; and the second court order, most importantly, was for the bank to return my certificate of title, since I had already paid the loan.

Ms JULIE BISHOP—Was there an order for costs at the end of the hearing before Mr Justice Santow?

Mr Madigan—No, there was no order for costs. I did not apply.

Ms JULIE BISHOP—Did the bank apply?

Mr Madigan—No. What happened then was that the bank withheld my statement; the bank withheld their defence—they did not supply their defence as Justice Santow had ordered—and the bank did not supply me with the certificate of title, either. So I pulled them into court

another time in front of Justice Bergin to explain their reasons for breaching two of the court's orders. Ultimately, the certificate of title was returned to me.

Talking about statements, once again here we have an account which I had closed on 10 November, which you saw as annexure J, I think it was. At annexure M, we again have the same account that I closed down. Three times I closed this account, and I was still unable to get statements. I closed it a third time, and received a letter from the bank manager at Ermington, which says:

This letter serves to confirm that the above housing loan was paid out on 10 February 2000.

He might have it as a form letter on his computer, because he would be getting pretty used to writing this by now. So, once again, 'closed on 10 February'—still no statements. So I went before Justice Bergin again in the Supreme Court, without notice, and asked that the bank provide me with statements. I got a court order on the bank to provide me with statements.

Now I am going to show you something that will amaze you, because I finally got the statements that the bank was withholding. Justice Bergin ordered the bank to provide me with statements: all the outstanding statements up until the loan was closed. The bank provided me with what they call a 'transaction history inquiry' which is at annexure N. There is a mysterious debit of $4.76 applied to it after the account was closed. So, of course, the account was still open. It was like the evil dead, you couldn't silence it. It kept coming up by itself and it was still open. Closed it once, on 22 October; closed it twice, on 10 November; closed it a third time, on 10 February this year. Miraculously, it had a debit of $4.76. That is at annexure N.

A little later I went to the office of Mr Lanser, who is sitting over there, and spoke to them, because they had to answer. I wanted the original statements—that is, not a bank statement; I wanted the original statements. Scott Atkins filed this affidavit in the Supreme Court. This was an affidavit filed by the bank's legal department. On page 3 of annexure O—this is written by the bank, in their words—Mr Lanser says:

"What do you mean 'the originals'? The Bank would no longer have the originals."

I am asking him for a statement which is one month old, and Mr Lanser says to me, 'What do you mean "the originals"? The bank no longer has the originals.' Turning to page 4 of the bank's affidavit at annexure O, there is something which is even more interesting. Mr Scott Atkins, who is also one of the bank's solicitors, said:

Mr Madigan you do not understand, the statement copies provided to you are addressed that way because the Bank's computer is no longer programmed to address the statements to your home.

An account which has closed and has a $32,000 redraw facility overpaid because it has closed early? The letter says:

... the Bank's computer is no longer programmed to address the statements to your home.

Do not forget that we had a court order for these statements. Ultimately, when I fronted up in front of Justice Bergin on 1 March 2000, the bank provided the statement. I want you to have a look at the statement that the bank sent me. Have a look at whose name is on the top. It is not

mine. It says ‘C O Home Loans Management’ sent back to the bank. That is what the postman saw when the bank’s computer put it in the envelope and sent it back to the bank.

Mr Lanser argued in court that these statements are electronically generated. Justice Bergin said to Mr Lanser, ‘If that is electronic generation, Mr Lanser, why is the bank’s logo visible on the statements?’ You can see the bank’s logo quite plainly there, it being orange and black. We all know that computer statements that are electronically generated only store data. They do not store pictures. The bank’s logo would not appear on a computer generated statement. That statement is a photocopy of the master. There is no question in my mind about that. Have a look at it there on the same statement. The statement is not in default. It has, ‘You are ahead in your payments of $32,500’. There is no reason why I should not be given that statement. It is not in default. The address has been changed up the top, as I showed you before, and this statement was only produced by an order from the Supreme Court of New South Wales.

Turning to page 2 of the statement you will see something which is very interesting. We are talking about a statement I cannot get access to that has been mailed back to the bank, as you can see. Turning to page 2 of annexure P we can see there on 17 October a withdrawal of $41.70 and a withdrawal on 19 October for $509. Mr Lanser explained in his letter of 11 January that those withdrawals were the filing fees in the Supreme Court. Mr Lanser should know that part 52A rule 9 of the Supreme Court rules says that fees are payable on the conclusion. Here we have a situation of the bank taking its unawarded fees out of my account, without my consent and knowledge, in advance in October in defiance of the Supreme Court rules. That keeps the account open.

Let us go to page 3 of annexure P. On page 3 of annexure P once again we have the logo up the top, which you can see, which indicates to me it is a photocopy of an original. It indicates to me that it is not a computer generated statement. Page 3 of annexure P on 10 November has my fee for closing the account of $752. On 15 November you will see that there is the fee attending to settlement, which is $150; the early repayment adjustment of $3.27, and the interest correction of 63 cents. You will see that the balance at the close of trade on 15 November was zero. The account was closed. The bank manager at Ermington was correct when he said to me, ‘This stands to serve that the account was closed on 10 November.’ There it is. Look here. He has taken money out on 16 November but he has backdated it to 15 November. How do you explain that?

How can you take money out of somebody’s account on 16 November and backdate it to 15 November if you do not want to do something fraudulent and make the account look like it was still open after it had been closed? There it is. I describe that as a bogus transaction. There is no other explanation for this. He was asked in court in front of Justice Rolfe on 19 January, ‘Mr Lanser, how do you explain a withdrawal of $65.00 on 15 November to buy a transcript of a case heard on 16 November, an unlisted matter?’ Do you know what Mr Lanser said? He said, ‘I do not know; you would have to ask the bank.’ Come on! This is the bank’s solicitor being questioned by a Supreme Court judge and saying, ‘I do not know the answer to that, you would have to ask the bank.’

Let’s go a bit further. We have that on page 3. Let’s go to page 4 of annexure P. Once again you can see the address at the top and the change. This statement was given to me on 1 March this year. I had to go to the Supreme Court to get an order on the Commonwealth Bank of

Australia to give me my statement, which was $32,500 in advance payments. What did they say there? The bank received that statement on 22 February. But you will remember from annexure N, which I showed you before, that is what they faxed me out on 23. The day after they had received this they faxed me this telling me that was not their statement. Of course that is not their statement.

This one is more interesting. Have a look at the reversal. The $4.75 which had miraculously appeared to keep the account open disappeared with as much mystique because this statement all of a sudden had to be produced to the Supreme Court. So the $4.75, which was put there for no other reason than to keep the account still open, disappeared. It disappeared as a credit reversal. There is nothing I can say. I think the evidence virtually speaks for itself. You can see there on page 5 of annexure P that on 20 February the balance of that account is nil. That is an account which I closed on 10 February. We have a letter from the bank manager to say that this account was closed on 10 February as annexure N. I have already shown it to you. It was closed on 10 February. Look at all those deductions in the meantime from 10 February right through to 20 February when the account was effectively closed by court order in the Supreme Court.

I do not mind going to the Supreme Court. I take a bit of pride in the way that the laws are administered in this country and I have a lot of respect for Supreme Court judges. I am not scared of doing that, as you can tell from the way that I talk. I am quite articulate. I do a lot of study on what I am doing. But I know there are a lot of people who do not have the gumption to get up and go and who do not have the skill and the drive that I have. I go to the Supreme Court to get a statement that is mysteriously kept open for no other reason than, in my view, fraud. There are people that cannot do that.

They are the issues there in terms of the statement. You have my affidavit there. The whole matter did start over matters of the bank changing the frequency of charges on statements. But if you do not want to address that we will not look at that either.

CHAIRMAN—Thanks very much, Mr Madigan. Senator Cooney, do you have a question?

Senator COONEY—I think the point has been made quite clear.

CHAIRMAN—In taking us through that, you have made your particular issues clear. I know that sometimes when accounts are closed there are additional fees incurred—

Mr Madigan—They are all paid.

CHAIRMAN—government charges or whatever that might have to be added at the end because of pay-outs.

Mr Madigan—Sure, I agree with you. And there they are there.

CHAIRMAN—But there is nothing of that nature in these?

Mr Madigan—There certainly is. There it is there—the settlement fee.

Senator COONEY—In which annexure?

Mr Madigan—This is annexure P, on page 3, which is the statement. You can see there that we have a 'settlement to repay your loan,' an 'early payment adjustment,' and an 'interest correction.' You ask me and I will pay it. I said to them, 'Pay it out. Close it.' However, on 10 November it does a Lazarus. It is a funny thing to say about your bank account, you would not think that it would get up and walk around again after it has been dead, but it does. On 16 November it resurrects itself with a mysterious fee of $65 to procure a transcript of a case heard the following day as an unlisted matter.

Senator COONEY—Did they write to you and let you know that they were going to make these changes?

Mr Madigan—No. I had to get all this information by a Supreme Court order.

Senator COONEY—That is what you say, you say that there was no notice and the only way you could get it was to go to the Supreme Court.

Mr Madigan—That's right. You have only got to have a look at the address on the statement to know what their intention was. There was no intention to notify me. If they wanted to notify me they would not have changed the address.

CHAIRMAN—Your concern is that in reopening the account which was supposed to be closed that it was incurring costs for you.

Mr Madigan—The Commonwealth Bank of Australia at the moment does not have a claim against me, as much as Mr Lanser argues that they have. I was issued a default note, along with their claim for $32,000, or whatever it was. I paid the default amount within the seven days that was stipulated. Section 81 of the Consumer Credit Act of New South Wales says that if I pay the default demand within the time allowed then the bank cannot proceed with any acceleration clause, which means that that is the end of the story. They wanted $32,000: they got $32,000.

Mr Lanser would have you believe that the account is not closed, that it is still going, and as long as the account is still going then they can pursue me. But the account was finished. The default value was paid. It was closed. But it was in their interest to keep the account open. That is why they withheld my certificate of title, and that is why I got a court order to supply it.

When that matter came before Justice Burgin on 2 and 3 December last year, and where Justice Burgin described the bank as flouting the law and she ordered Mr Lanser to provide an affidavit explaining why the bank chose to flout the law in respect of certain rulings that had been handed down, the bank eventually provided my certificate of title. They handed it up for destruction.

I should not have had to do that. Going to the Supreme Court costs money, and Justice Burgin awarded me costs. She said to the bank, 'Mr Madigan has undergone certain costs and I think it is fair that he be reimbursed.' Of course, the judge has the right to apportion costs on the day. She told the bank to pay my costs. She said to me, 'How much will they be?' I said I wanted $150 a day for two days, a tradesman's rate. I am not trying to capitalise on this. I said that I

wanted $150 a day and I wanted the money for a pair of black K-Mart shoes, $29.95, that I bought to come to court. I was not trying to make money out of the bank. That is what she awarded.

Out of the goodness of my good heart I waived the cost of the K-Mart shoes. I put a cost on the bank for two days in the Supreme Court of $300, but I did add my cost for the bus fare and the train fare which brought it up to $313. The bank then refused to pay me. The bank refused to pay me the $313. When I said to Mr Lanser, 'I think it reasonable to pay me in a reasonable time,' he said to me that the costs were not payable until the end of the proceedings, and he quoted part 52A of the Supreme Court rules. So here we have a situation where the bank takes out over $500 of its unawarded costs from my account, without my knowledge, without my consent, at their liberty because they have got control over my account, but I am not allowed to take my $313 from the bank as awarded costs in the Supreme Court.

There is no answer to that. I think the evidence speaks for itself. I hope you will demand answers from Mr Lanser—if he gets up and speaks to you—because I certainly cannot get any answers, especially in the Supreme Court, when he tells Justice Rolfe, 'I do not know the answer to that. You will have to ask the bank.'

Mr ROSS CAMERON—In this instance, the bank employees are not deriving any personal benefit. What do you think is going on in keeping the account open?

Mr Madigan—My observations for keeping the account open?

Mr ROSS CAMERON—Yes.

Mr Madigan—I do not know the reason for that. It seems strange to me why somebody makes such a concentrated and focused effort to keep the account open. To take $65 out of the account five days after it has been closed, to my way of thinking, does not make sense. But there is a reason for it, and I hope you can find that reason. I just do not know. I hope the bank will answer those questions for you.

Mr ROSS CAMERON—Is it your view that the bank is seeking to derive some kind of tax benefit from the provision and arrangements?

Mr Madigan—They are, because while the account is still open and while the bank are in control of the account and I am not in control of the account—I am not in control if it; the bank are in control of the account, a ledger with my name written on the top—there is nothing stopping the bank from putting any amount of fees onto that account. As a matter of fact on 19 January I showed my concern to Justice Rolfe in the Supreme Court after the account had been closed twice but was still open. I said to Justice Rolfe, 'I want you to pass an order on the bank to stop them from putting their fees onto my account. We had already seen the situation where the bank had put over $500 worth of fees onto my account, and for every appearance that I was going to have against the bank, once again, they were going to put fees onto my account.

Mr Lanser told me just last week that he was getting $250 an hour. Mr Lanser is an employee, and he seems to think that he is allowed to charge a scale of fees. The scale of fees was abolished in 1997. He can charge only what he gets paid, yet he is preparing fees at $250 an

hour, not for appearing in court but for researching the law. He researches the law for four hours at $250 an hour, he makes inquiries amongst solicitors and officers at $250 an hour; he photocopies—the whole lot. If I ring the bank and I make an inquiry through the helpline, he charges me $250 an hour. You will see in the letter that I wrote to the bank manager that I will not be requiring Mr Lanser's bogus fees at $160 an hour—that is what it was in those days; I do not know where he gets his $250 from, but that is what he told me last week—for answering my genuine inquiries as a customer of the Commonwealth Bank.

Mr ROSS CAMERON—You referred to the Supreme Court rules in relation to payment of costs at the completion of a matter.

Mr Madigan—Yes.

Mr ROSS CAMERON—There the court would be regulating the payment of court order costs between litigants. Isn't it possible that, under the terms of the loan agreement, if the bank incurs disbursements through the duration of a matter, that may be lawful? I am not talking about whether it is good commercial practice.

Mr Madigan—I know what you are saying and I understand your question, but here we are talking about something which is unawarded.

CHAIRMAN—Mr Madigan, please excuse me. Senators will have to go to a division briefly, but we will return. Mr Cameron can keep the dialogue going.

Mr Madigan—We are talking about unawarded costs. With regard to the transcript that Mr Lanser bought, or the bank bought, for $65 on 15 November, the day before the case was heard, if I had applied for costs that day I would have been awarded costs, because Justice Santow hand wrote the court order. He was so determined that this would go down on the record and would not be mistaken that he hand wrote the court order ordering the bank to supply me with my certificate of title, ordering the bank to file their defence. It was all handwritten. I got a court order telling them to give me a certificate of title; I got a court order telling the bank to file a defence. I would have won the costs had I asked, but I did not ask. I am not capitalising. So here we have a situation where the bank could easily have turned around and put another $500 onto my account—because we are talking about unawarded costs.

Mr ROSS CAMERON—I have not read your loan agreement, and I am not commenting on Mr Lanser's fees in terms of value for customers of the bank—whether he is worth $150, $250 or whatever his salary is. I am saying that, if the bank, for example in the course of your loan facility, incurs a cost, for example a transaction related cost in a real estate conveyance, presumably they are entitled under the loan agreement to withdraw that immediately from—

Mr Madigan—That is in terms of the loan agreement, but we are not talking about those sorts of costs. What we are talking about here are costs which are regulated by the Supreme Court rules. The Supreme Court rules say one thing and, effectively, that is what you have to abide by. You cannot draw up a contract to turn around and say that we can overrule the Supreme Court act, and I certainly cannot approve of that any more than I can give you authority to park your car on the footpath. I cannot say, 'Go and do a delivery; park your car on the footpath,' because it is not lawful to do that. In the same way it is not lawful for the

Commonwealth Bank to draw up a contract which circumvents the effectiveness of the Supreme Court rules. It is just not lawful. In terms of any costs which they incur in the sale of the property, I can understand that but, in unawarded court costs, no, I do not agree with that at all.

Mr ROSS CAMERON—I would not get into a dispute about the reach of the law of contract in relation to court orders. In relation to your loan, there is one statement which says that you were $32,000-odd ahead of your loan repayment schedule. Then you said that subsequently you received an order for repayment for payment of indebtedness, which you complied with—

Mr Madigan—It was $4.75 or something, yes.

Mr ROSS CAMERON—What was that claim for? How much was that for?

Mr Madigan—It was not a claim. The bank said that I was one payment behind in my loan, and the bank wanted repayment of the whole lot. So I paid, within seven days, all the money that I owed them. Effectively, to my way of thinking, that would close the account.

Mr ROSS CAMERON—You were behind by one repayment—by what period of time?

Mr Madigan—One month. I was $600 behind.

Mr ROSS CAMERON—At that point the bank were within their rights to—

Mr Madigan—Sure.

Mr ROSS CAMERON—And you complied with that?

Mr Madigan—Sure, and I paid them the money. They wanted the full payment within seven days of the letter. I said, 'All right, there it is.'

Mr ROSS CAMERON—I am trying to understand why the bank would do this, and the bank is going to have their opportunity to give their evidence, as will the ATO, in relation to provisioning for bad and doubtful debts.

Mr Madigan—There is a very good reason why the bank would do that, but it is really out of your terms of reference and I did not include it. It is in the affidavit. I will talk to you now about it. This is something that is going to surprise everybody.

In July 1998 the bank changed the frequency of the annual fee on home loans to a monthly fee. In May 1999, when I was preparing my statements for taxation, I noticed that the annual fee had been changed to a monthly fee, so I rang the help line at the bank and said that I had not got the notice. They are supposed to give 30 days written notice and I did not get that 30 days written notice. She said somebody from the bank would contact me. They contacted me all right—I got a threat from Scott Atkins of the legal department of the Commonwealth Bank telling me not to ask any more questions in regard to this matter or else the bank would take an injunction against me in the Supreme Court. I contacted the ombudsman's office and said to the

ombudsman that the bank changed the frequency, from being an annual fee to a monthly fee, in July 1998 without giving me 30 days written notice.

So the bank did an investigation on that and the ombudsman did an investigation on that. The ombudsman's determination is in my evidence that I have filed. He determined that the bank had changed the frequency but had not introduced a new fee and, as such, the bank was not obliged to give me 30 days written notice. In June this year I uncovered that section 61 part 1 of the Consumer Credit Act of New South Wales says that the bank does have to give me 30 days written notice. The bank wanted to keep that part of the investigation hush-hush, so the bank started legal proceedings against me to stop the ombudsman from inquiring any further, because the ombudsman's terms of reference will not allow the ombudsman to inquire once legal proceedings are in position.

You could say there is no big deal about that. Well, there is a big deal about that. Let me explain. The penalty for changing the frequency on a home loan without giving the customer 30 days written notice is 100 penalty units. A penalty unit is $110. That is a $11,000 liability on the Commonwealth Bank of Australia for not giving me 30 days written notice. They did not give you, you, you, you, you, anybody in this room, 30 days written notice—$11,000 penalty. So the Commonwealth Bank of Australia has a liability which I estimate at somewhere between $10 billion—that is 10 thousand million dollars—and $20 billion for not giving their customers 30 days written notice of the frequency change. Why do you think the Commonwealth Bank wanted this matter pulled into court so quickly?

Mr ROSS CAMERON—Your account was a home loan account?

Mr Madigan—Yes.

Mr ROSS CAMERON—What happened when it went to court?

Mr Madigan—When it went to court I paid it off.

Mr ROSS CAMERON—Yes, but has that assumption of liability for non-notification been tested in court?

Mr Madigan—It will be tested. It is a matter I have just filed—a new claim against the bank which I filed last Friday. They are not in the terms of reference of this inquiry, but they are quite substantial, and there is a point there in my claim, part 1.02, as Mr Lanser knows.

Mr ROSS CAMERON—You think that may explain why the bank did not want to give you—

Mr Madigan—Most definitely. That is very substantial. The bank knew it. The bank threatened that if I continued inquiries with the ombudsman's office they would take an injunction against me. I thought that was very strange because my inquiry to the ombudsman's office was quite legitimate. All I did not do was that I did not get that letter and I was just saying why.

Mr ROSS CAMERON—I am mindful of the fact that in this forum the bank does not have an opportunity to immediately respond to—

Mr Madigan—I can understand that, but there will be a forum for that.

Mr ROSS CAMERON—I do not want to just protract the evidence until the senators return. Thank you for your very comprehensive presentation.

Mr Madigan—Thanks very much for the inquiry. It is overdue and it has been a very good thing for the Australian public.

Mr ROSS CAMERON—We will take a short adjournment until the senators return.

Proceedings suspended from 11.28 a.m. to 11.31 a.m.

GRIFFITHS, Mr Ross Edward, Head of Credit Management, Commonwealth Bank of Australia

LANSER, Mr John Morris, Solicitor, Commonwealth Bank of Australia

ULLMER, Mr Michael James, Group General Manager, Financial and Risk Management, Commonwealth Bank of Australia

CHAIRMAN—I welcome the representatives of the Commonwealth Bank. We do have certain items of correspondence from the bank that I have received as chairman. Do you wish to make an opening statement in relation to the issues raised?

Mr Ullmer—Yes, I would like to make an opening statement and then take the opportunity to make a few comments in response to the two matters that the committee has heard already.

The vast majority of Australians pay back their bank loans on time, on schedule and without issue. Unfortunately, a very small minority is unable or unwilling to repay their loans. I have been asked to respond on behalf of the Commonwealth Bank Group to allegations made by some members of this small minority of organisations and individuals who have breached their contractual commitments with the bank. Specifically, those allegations are that the Commonwealth Bank failed to inform certain rural customers that their debts had been written off; wrote off loans as bad debts while still receiving interest payments to service those debts; refused to issue bank statements to customers who had continued to service their loans; and used a shadow ledger system to improperly claim tax benefits.

Before addressing these four items, I would like to comment on the process that has been given the emotive title of 'shadow ledger'. For those customers who continue to meet their contractual obligations to the bank, details of activities on their account movements would issue through the normal bank systems, including, where relevant, periodic bank statements. Where the bank or, for that matter, any other credit provider has formed the view that all or some of the debt owing will not be repaid, it will, to ensure compliance with accounting requirements, make an accounting entry to reflect provision for the possible loss or write-off of this amount as a bad debt. Clearly, just because a credit provider forms the view that a debt is irrecoverable or bad does not extinguish the liability of the borrower to repay the moneys owed under the loan agreement. This would include interest that continues to accrue on the debt. In these instances, the credit provider will need to keep a separate record of the legal debt owed under the contract. It is this separate record that has been referred to as the 'shadow ledger'. Thus the shadow ledger relates only to impaired loans and records a borrower's ongoing legal obligation where all or part of a debt has been written-off by the Commonwealth Bank Group or any other credit provider. The accounting ledgers that include the provision for possible loss of the debt are used to prepare the financial statements.

I turn to the specific issues of concern to the committee: firstly, that the Commonwealth Bank Group failed to inform certain rural customers that their debts had been written-off. The Commonwealth Bank Group does not as a matter of policy inform any of its customers that their debts have been written off for accounting purposes. Any decision by the Commonwealth

Bank Group to write-off all or part of the debt recorded in its books is an internal accounting matter and is undertaken to ensure that the books and records of the Commonwealth Bank Group are maintained in accordance with generally accepted accounting standards and other regulatory requirements.

Any debt write-off by the Commonwealth Bank Group does not reduce the amount legally due and payable by the customer. There is, therefore, no need for the Commonwealth Bank Group to inform the customer of this internal accounting entry. The evidence before the committee today would illustrate the confusion that arises when inadvertently customers are made aware that accounting write-offs have been made. The actions of the Commonwealth Bank Group in this regard are no different from those we understand to be undertaken by any other commercial organisation.

The second concern is that Commonwealth Bank group wrote off loans as bad debts while still receiving interest payments to service those debts. This response follows from my first point. The Commonwealth Bank Group has received interest payments in respect of amounts which have been written off in its books. The payment of interest by those customers where the Commonwealth Bank Group expects it would incur a bad debt is not a frequent occurrence. However, as has been indicated, the writing off of a debt is an accounting entry and does not reduce the legal obligation of the borrower to repay the amount due. Interest continues to accrue and be due on the total amount of principal outstanding, including any amount written off for accounting purposes. When such interest is received in cash from the borrower, the amount is treated as income for both accounting and taxation purposes. As a consequence, the Commonwealth Bank Group pays income tax on the interest payments that have been received.

The third concern is that the Commonwealth Bank Group refused to issue bank statements to customers who continue to service their loans. We are unaware of any circumstance where the customer has continued to service their loans in accordance with the loan agreement where the Commonwealth Bank has refused to issue statements, but when dealing with an impaired loan, the relationship between the bank and the borrower may be vexatious. The borrower may dispute the amount owed and the Commonwealth Bank may cease to issue further statements as in the past there has been little purpose in providing information that the customer may perceive as incorrect and may further inflame the dispute that may well be in place between the customer and the bank. I note that the consumer credit code in dealing with personal loans at section 31 addresses the obligations of credit providers to provide statements of account. Section 31(3) provides that a statement of account need not be given where the debtor is in default or where an amount has been written off the debt and no further amounts have been debited or credited to the account.

In dealing with business customers, we are aware of a small number of instances where officers of the Commonwealth Bank Group have refused to issue statements on request to borrowers who are in default of their loan obligations. In terms of the dimension here, the Commonwealth Bank Group has over 600,000 business customers and the number of customers at any one time where we may be looking at writing off all or part of their debt would today be of the order of 100. To the best of our knowledge, these instances are ones where the Commonwealth Bank Group has obtained judgment from the court for the debt which the customer is unable to pay or where the Commonwealth Bank Group has agreed with the customer an amount in full satisfaction of the legal debt owing.

The bank has already announced, in June this year, that it will provide the very small number of customers who are having difficulty in repaying their loan with details of their account indebtedness on request. The bank is now prepared to go further and issue statements on these loan accounts—that is, loan accounts where the borrower is in default of their loan agreement—in line with the bank's regular statement cycle for that loan until there is either a court judgment or agreement has been reached between the parties, which is normally signified by a legally enforceable release document. The statement we will provide will be a full statement of the borrower's account indebtedness, including the principal outstanding, interest, fees or any other cost charged to the account pursuant to the loan agreement and any interest rate changes. But I would note it will not include any amounts that have been written off for accounting purposes, to avoid the very confusion that has been the subject of the discussions this morning. This arrangement will commence on 1 January 2001 or sooner, depending on the appropriate changes that will be required to our systems. Until that time, we will stand by our commitment issued already to issue statements on request to these borrowers.

My fourth point is the use of a shadow ledger system which it has been asserted was to improperly claim tax benefits. As to whether any of these matters is in any way driven by taxation issues, I would note that the Commonwealth Bank Group is one of Australia's largest taxpayers and, in the last financial year, paid income tax to the federal government in excess of $900 million. We reject any assertion that there has been any impropriety on the part of the Commonwealth Bank Group in any of the matters referred to. Our treatment of impaired loans is strictly in accordance with the taxation laws.

Before I respond to a number of the comments made by Mr Ford and Mr Madigan, I would like to hand out an information sheet outlining our response in summary form, a statement of the position I have just articulated as to what we will do going forward and a copy—for those members of the committee who do not have them—of the letters on this matter that we have already referred to.

CHAIRMAN—Thank you.

Mr Ullmer—If I can now briefly give some summary comments in response to the commentary of the two previous individuals appearing before the committee. With respect to shadow ledgers, those ledgers are available to our independent auditors as part of the annual audit process undertaken by the bank. In fact, in a number of matters that have been referred to today, our independent auditors have specifically reviewed the accounts in question and confirmed that the activity on those accounts is in accordance with accounting requirements and taxation requirements. I would also note that those ledgers are available to the tax office in the course of their normal reviews of our affairs.

There was a statement made that we have bankrupted individuals with respect to unsubstantiated debt. This is incorrect. When a borrower defaults in a way that requires us to go through a court process of bankruptcy, then clearly it is an obligation upon the court to ensure that the amount of the debt that has been claimed and is finally settled to the bank has indeed been substantiated.

With respect to Mr Ford and his business, the bank had a relationship, as Mr Ford alluded to, going back many years with his company. The business had a history of trading difficulties and

the bank had responded to those by a process of continual deferment and restructuring of amounts due under his various loan agreements over many years. Mr Ford commissioned an expert's report to investigate the business in July 1993. That expert commented that there were extreme cash flow difficulties and that the business could not trade out of its current difficulties without an orderly asset sale. I have mentioned already that our independent auditors have specifically reviewed Mr Ford's account and confirmed that it is in accordance with accounting and tax treatments. That is both the accounting records and the records of the legal debt due.

Issues about the statements were raised by Mr Ford—and this is really the nub of the whole issue—that is, the statements should be a reflection of the amount that customers owe the bank. There has been a lot of discussion today that it should be a statement of what our mainframe computer has within it but, as I have already indicated, that would not be a true reflection of the amount owed by the customer. The very important point is that customers should have an understanding of their financial affairs. Those financial affairs would not be illustrating in Mr Ford's case the fact that $134,000 had been written off. It had been written off for accounting purposes. That write-off did not absolve Mr Ford from honouring his obligations under the loan contract to repay the amount of principal, interest and fees that were due. I detected towards the end of Mr Ford's evidence that in fact he seemed to acknowledge that that was the case. On this question of the issuance of the statements to Mr Ford, I would observe that these requests are being made some 3½ years after the matter was settled by agreement between Mr Ford and us. In terms of the realisation of Mr Ford's assets, that was a process undertaken by Mr Ford himself. The final matter I would note is that there was a reference to the state of tax law in 1985. The relevant tax laws in fact changed in 1992 in their treatment of impaired loans.

With respect to Mr Madigan, over the last decade, he has conducted a campaign of trying to prove that there are weaknesses in the Commonwealth Bank's policies and systems. To summarise a number of matters that Mr Madigan referred to, there is a circumstance where Mr Madigan obtained $4,000 by deception in knowingly drawing a cheque against an account which had insufficient funds. That matter went to court. The verdict was in favour of the bank and ordered Mr Madigan to repay the funds and also the bank's legal costs in the matter. There was much discussion about Mr Madigan's home loan with the bank. The situation there is that Mr Madigan swore a false statutory declaration with respect to obtaining a land title. He stated that no person or corporation held security over the land title. That is the reason why we were in court on that matter with Mr Madigan. The court granted an injunction restraining Mr Madigan from dealing with the proceeds of the sale of that property. That is how that money came to be returned to us within seven days. The $32,000 referred to on the statements is part of our normal process where we advise customers as to how much additional borrowing capacity there is having regard to the security they have offered by their home. It was not a question of $32,000 being paid in and somehow that being appropriated by the bank.

With respect to these matters that have been before the court, a number of orders have been made against Mr Madigan. One included a confirmation of an interim apprehended violence order that had been taken out by the female manager of the Ermington branch based on the way she had been harassed by Mr Madigan. The other matter, which is also very important, is that the deed that was signed required Mr Madigan to close all of his accounts with the Commonwealth Bank. Mr Madigan seems to take delight in trying to show that he can keep those accounts open. I am happy to take your questions.

CHAIRMAN—Thank you, Mr Ullmer. You just commented that, in relation to Mr Ford, the statements had not been requested and some 3½ years had passed after finalisation of the actual matter. Are you are telling us that, at the time of these dealings, there was no request from Mr Ford for a statement?

Mr Ullmer—As Mr Ford alluded to, his relationship was with the Commonwealth Development Bank. As it happened, throughout the process leading up to the settlement with Mr Ford, statements were issuing in the normal course through the Commonwealth Development Bank. It is through that process that Mr Ford received a statement showing the $134,000 write-off. The point I am making is that the Commonwealth Development Bank did not actually have the system in place of keeping a separate record of the accounting debt as opposed to the legal debt. That clearly caused confusion, although I would suggest that Mr Ford must have been perfectly aware that he had not made a repayment of those two amounts aggregating to $134,000. I should also note that at the final wash-up of all of the relationships with Mr Ford and his businesses, the bank ended up suffering a loss aggregating $110,500.

CHAIRMAN—When Mr Ford did actually ask for these statements, can you tell me what the time lag was between their request and when they were available?

Mr Ullmer—As has been alluded to, we are in a situation here where our policy has not been to issue these statements that have within them accounting write-offs. It would appear that there has been a reticence to provide those statements for fear of further inflaming the situation with Mr Ford. When the requests came through, as I say, some 3½ years later, whilst those requests were initially rejected on the basis that `This matter was settled some considerable time ago; why are we reopening old wounds?' eventually all those statements were provided.

CHAIRMAN—I take it from what you have said that, even though a debt is written off by a bank internally for accounting purposes, does not mean the debt is cancelled in terms of the liability of the borrower?

Mr Ullmer—Exactly.

CHAIRMAN—Is reason for not advising the customer that the debt had been written off the fact that you would not want the customer to misunderstand or gain the impression that the debt had been cancelled? Are there other reasons?

Mr Ullmer—We have an obligation to our shareholders and, indeed, to our capacity to provide cost effective finance to the vast majority of Australians who are able to service their loan agreements, to ensure that we recover the appropriate amount of moneys from all debtors. So when a debtor is in default of their loan obligations, to advise them that we have taken this view would simply create in their mind an impression that they no longer had to repay this amount of money. That is inappropriate and it would be unfair on all of those people who do meet all of their loan obligations.

CHAIRMAN—You said that Mr Ford, in a sense, took the initiative or handled the sale of assets to meet the liabilities. As I recollect, Mr Ford, in his evidence, suggested that there was pressure from the bank that caused him to sell some, if not all, of that property in a time frame or to a buyer other than a buyer who had indicated they were willing to pay more for that asset.

Mr Ullmer—As I mentioned in my opening statement, the situation with Mr Ford's business is that it had trading difficulties for many years and the bank had facilitated the continuation of the business by deferring repayments and restructuring various loan facilities, but a point in time came where we were clearly concerned at the ongoing financial difficulties. A review was undertaken by an expert commissioned, as I understand it, by Mr Ford. That expert concluded that the business was not viable, carrying the level of debt it that it did and without realisation of assets. So, at that point, my understanding is that there were discussions between us and Mr Ford as to how this matter was going to be resolved. It did not go to court; it was settled outside of any court process. Clearly, I would say that, where we were concerned, as to the capacity of a borrower to repay, naturally we seek, at some point in time, to say that we now have to bring this matter to a close.

CHAIRMAN—With regard to the issuing of statements, they ceased at the time that Mr Ford was in default of the loan.

Mr Ullmer—Chairman, can I ask Mr Griffiths to respond to that in terms of the detail?

Mr Griffiths—Mr Chairman, no, they did not. Mr Ford, strictly speaking, was not in default of the loan at any point. He was substantially in arrears at the contractual arrangements. Indeed, by June 1994, those arrears were over $100,000. But the arrears had come about with the agreement of the bank, which had been trying to assist Mr Ford in the orderly wind-down of that business. But statements had continued to issue in the normal statements cycle which, for the Commonwealth Development Bank, was annually—soon after 30 June in each year.

CHAIRMAN—And those statements still indicated the total amount of the debt?

Mr Griffiths—As we have already heard, one of the issues was that the statement that was issued for the period of June 1995 did include those write-offs.

CHAIRMAN—And how did that come about?

Mr Ullmer—It was an error.

Senator CONROY—Would you take me through the general procedure from when you make a decision to make a provision for a bad debt, to what obligations that has on you and the customer and then move on to debts. I am neither an accountant nor a lawyer, so I am starting behind the eight ball here. You make an assessment that you think someone is not going to be able to pay, you decide to make a provision. What happens next?

Mr Ullmer—I will take you through the process. We will assume we are dealing with a business customer where normally there would be an individual account officer within the bank responsible for managing the bank's affairs with that customer. One of the account officer's obligations is to monitor the financial performance and the ongoing capacity of the customer to repay their obligations. There is a process where, at least annually, those account officers are required to grade the loan as to its credit worthiness. Where that account officer forms a view that there may be some difficulty in repaying a particular loan, then it is identified with a particular grade within our system. That then flags up in aggregate across the whole of our portfolio of over 600,000 business loans a requirement to establish what we call a general

provision. That general provision is our assessment based on many years of historical loss experience as to what is the likely loss that may occur from that general portfolio of loans. That amount is not individually tagged to any specific loan. There is an important point there. The raising of that provision, whilst treated as an expense in our financial statements, is not a deduction for taxation purposes, because the tax office takes the view that it is not specifically attributable to any particular loan and therefore it is just a prudent accounting provision so that we do not mislead our shareholders. The next stage would be reached when the officer judges that, on this particular loan, there is now actually a high likelihood that a loss will be suffered. At that point in time—

Senator CONROY—May I ask what the grade is without revealing anything that is commercial-in-confidence? Is it a Z grade; is it a D grade?

Mr Ullmer—Yes. In those sorts of grades, we are talking about an F, if it is in doubt; a G—

Senator CONROY—First, 'the provision being raised' is an F grade. In 'high likelihood', the next one, is a G.

Mr Ullmer—In a G grade, what we would then start to do is to say that we would no longer accrue interest on this account for accounting purposes because we have formed a view that there is a high likelihood of loss. But at this stage, we take a prudent view and say we will no longer record interest on that account for accounting purposes, although clearly the borrower still has an obligation to pay the interest as it is accumulating under the loan agreement.

Senator CONROY—The borrower still has to pay.

Mr Ullmer—The final grade would be an H grade in our system—and I should say that all banks in Australia have similar grading systems, as they do in the United States—where we expect that this loan is likely to then go into a realisation process. This is where we expect that we may actually lose money on the principal that we had advanced and on the accrued interest that had not been paid and that had been recorded prior to us stopping recognising interest from an accounting point of view. It is at that point that we would consider making a write-off against that particular account. From a taxation law point of view, the tax office need to be satisfied that we have made every reasonable endeavour to recover the moneys from the customer before the Taxation Office will allow us to treat that as a deduction in deriving our taxable income. So it may be some years between when we recognise it in our accounts as a loss and when we are able to recognise it for taxation purposes as a loss. One of the areas that the tax office will audit when they do come in from time to time is whether we are doing that in a reasonable way so that when we make these write-offs, there is indeed a reasonable prospect that we will in fact incur the loss for taxation purposes.

Senator CONROY—And that is not sort of between G and H use. It is not that you become a G classification and then you have a few years. You say 'H grade' and then you have the capacity, providing you have made attempts and satisfied the tax office, then to make a tax—

Mr Ullmer—To make a write-off.

Senator CONROY—write-off, which gives you the tax deduction.

Mr Ullmer—Yes.

Senator CONROY—But you do not just go 'H grade. Okay, tomorrow that's it, we write it off.'

Mr Ullmer—No. That is where the taxation laws quite properly require us to have made very serious attempts to recover this money and also to have then specifically made an entry in our books to show that we are writing off this amount. It is then that that gives the cause for the concern that has been expressed today, where individuals are saying, 'Some of my loan has been written off. Shouldn't I be made aware of that?' Our view—and I think that of all other credit providers—is no. As a borrower, that would mislead you. But we also have obligations to our shareholders and to the financial markets generally not to overstate the value of the assets that are recorded in our balance sheet.

CHAIRMAN—What happens when a debt that you have written off internally is either wholly or partly recovered? In other words, it comes back off the shadow ledger and is recovered. At what stage do you bring that back in, if perhaps it has been written off for tax purposes as well as for internal accounting purposes?

Mr Ullmer—It could happen in two ways. Firstly, if the circumstances surrounding the borrower's financial position improved—and that may happen through movement in market values of properties, et cetera—then we may increase the quality of the grade of that customer so that they are no longer in the circumstances where we feel that the provision is required. We will write back that provision at that point in time when those circumstances have eventuated. If it is a situation where the facility is fully cleared—through the realisation of security property, for example—and the cash proceeds exceed the written down amount, then we will bring that to account as income, both for accounting and for tax purposes when those proceeds are received.

Senator CONROY—When that happens, if you have already written it off and therefore you have already claimed the tax deduction, how do you balance off with the tax office? Do you remit back to them? What is the accounting transaction there?

Mr Ullmer—In the year of income in which the cash is received, it would be included in taxable income for that year. In the circumstances we are talking about, based on a genuine assessment over a period of time, say, two years before, if we have judged that we are going to incur a loss and have gone through all the other procedures, we are entitled, under the taxation laws, to take a deduction. If, two years later, markets have improved, et cetera, and we have actually physically realised the property, we will bring to account as income in that year the cash proceeds. By way of example, there is a much larger facility than we are talking of with the borrowers today. But we, as all major banks do, would still have facilities relating to, say, property developments in the late eighties and the early nineties.

Senator CONROY—Still hanging in there.

Mr Ullmer—There is one where, as late as December last year, we actually received some cash a decade later. I do not think anyone could criticise us throughout that period—and this is still a hole in the ground in Sydney—for taking the somewhat cautious view that, in all

likelihood, we were not going to get this money. And here, 10 years later, circumstances change.

Senator CONROY—I appreciate and understand all of what you have said, but you did not answer my question. I accept that once you receive income you have got to declare it, and therefore you pay tax as you would on any of your income. The question I asked was this. You have received a tax deduction that is valued at X dollars, and you have now received income. How do you reverse the X dollars that you have already gained for the write-off? Do you net it out in some way, or are you not required, under the law, to net it out?

Mr Ullmer—If I understand your question, Senator, we do not go back, in the example I gave you earlier—

Senator CONROY—And reverse?

Mr Ullmer—and resubmit a tax return for that year. We would include it in the tax return that we submit for the year in which the cash is received.

Senator CONROY—What is your definition of include it? That is what I am trying to get an understanding of.

Mr Ullmer—It would be added to our amount of income for taxation purposes. Our taxable income will have within it an amount relating to the cash that has been received.

CHAIRMAN—So if the write-off two years before for tax purposes was, say, $200,000, that is $200,000 that you would claim as a deduction. If the $200,000 was then repaid two years later, you would add $200,000 to your income for that one year.

Mr Ullmer—Or more likely, Chairman, if we say that in that example $180,000 is the actual loss and we have therefore recovered $20,000 more than we estimated ten years ago, that $20,000 will be added to our taxable income and we will pay tax on $20,000.

Senator CONROY—I am struggling to understand this. In my mind at the moment I am seeing this as a double dip. You gained a $200,000 tax deduction two years previously, you then receive $180,000 and, even though it is $20,000 short—

Mr Ullmer—No, sorry, Senator. In the example I am giving we would in fact have received $20,000. I am sorry for confusing you.

Senator CONROY—No, I misunderstood what Senator Chapman was saying.

Mr Ullmer—In the example I am giving, we assumed we were going to lose $200,000, and we are entitled to take that as a tax deduction. If we only lose $180,000 two years later when all the properties are sold, et cetera, we have therefore actually lost $20,000 less than we had anticipated. That $20,000, quite rightly, comes back as income to the Commonwealth Bank Group, and we pay tax on it.

Senator CONROY—But I guess you had a tax deduction two years earlier of the $20,000.

Mr Ullmer—Yes.

Senator CONROY—That is what I am trying to get to. In my mind you should remit that back to the tax office, the tax deduction rather than just—

Mr Ullmer—Well we pay tax on it in the year in which it is received so the effect is the same.

Senator CONROY—No, but you have received it as well. You may lose some in your income, depending on whatever tax you were paying at that time. I see a capacity for you to have made not a substantial profit but a—

CHAIRMAN—One offsets the other.

Mr Ullmer—Senator, if I could give a very simple example. Assume that we had no other activity. In the first year when we believed that we were going to suffer a loss of $200,000, we get a tax deduction of $200,000 at 36 cents in the dollar in those days. When we eventually lose $180,000, we have already taken a deduction for $200,000, we cannot take another deduction for $180,000, but instead we have to go back to the tax office and say that our estimate was $20,000 too high. Two years ago we took a deduction with hindsight that was $20,000 too much, we must now pay back to the tax office the tax relating to that $20,000.

CHAIRMAN—So it balances out.

Senator CONROY—I will have a think about that. At what point—(f), (g) or (h)—do you or did you stop sending accounts? I understand what you are saying you will be doing in the future, but at what point in the (f), (g), (h) process does somebody stop receiving automatically their monthly or weekly or whatever it is—

Mr Ullmer—The policy has been, where we are in a situation effectively of being sufficiently concerned that we are going to make a write-off on the accounts, so therefore a write-off has been processed—it has been through all of this evaluation process, which may have occurred over a number of years—and the situation then arises that we have made this write-off on the accounts—

Senator CONROY—So this is an (h) grade?

Mr Ullmer—Yes. It is required to flow through our accounting system, and we are then in a situation where, if we send that statement to the customers under our current systems, they will see, as Mr Ford did, that there is an amount reducing the loan balance by $134,000 and they may be misled into thinking that that is a repayment or some other windfall on the account. And so what has been the practice in the past is to redirect those accounts to the lending officer who is responsible for collecting the debt, and that is why the address has changed to send it to that lending officer, to ensure there is no mistake in it being inadvertently sent to the customer. Then the situation in the past has been that, typically, we are in some process of either dispute or compromise with the customer whereat they are provided with detailed accountings of how

much their obligations are to the bank. So, clearly, as I alluded to with bankruptcy, the court will not grant an award for us of bankruptcy in an amount of money without rigorously going through what we put before the court as being the amount owed.

What seems to be the request here is to say, 'But we also want a bank statement.' The issue with the bank statement is that then if there are differences, which may well be these accounting write-offs, it creates confusion. What people may be suggesting is that we should only pay the amount on the bank statement. Our view is that what is legally due, what the courts would always look to see, is what is the amount that is due under the loan agreement. What we have put on the table today is that we will now put in place the systems to ensure that we can continue to advise these customers of their amounts due to the bank under their loan agreements, notwithstanding that we will continue to do the proper accounting and taxation processes with respect to write-offs.

CHAIRMAN—Do you know what the practice of other banks is in relation to this matter in terms of provision of statements? Is it the same as yours has been historically, or is it the same as you are now proposing to do?

Mr Ullmer—My understanding is that what the Commonwealth Bank does is representative of industry practice.

CHAIRMAN—So the initiative you have announced today is ahead of game, in a sense?

Mr Ullmer—I believe it is, but it is not done for that reason.

Senator CONROY—You mentioned that when you reach the (g) grade you no longer accrue interest on a daily basis, which then affects some accounting procedures.

Mr Ullmer—If I can just clarify, we do not accrue interest for accounting purposes because there is sufficient doubt about the receipt.

Senator CONROY—No, I understand.

Mr Ullmer—We do accrue it for the borrower.

Senator CONROY—There was a ruling in December 1994, income tax and non-accrual loans, so you get to make the judgment following the 1994 ruling about when to stop accruing the interest on a daily basis, effectively.

Mr Ullmer—That is my understanding.

Senator CONROY—What happened prior to the 1994 ruling? I think that would cover most of Mr Ford's case, from the sound of it. I know it kept going for a little while. So how did you book it up in terms of accruing the interest, prior to the tax commissioner making the ruling in December 1994?

Mr Ullmer—I may ask Mr Griffiths if he is familiar with that far back. But the one point I would emphasise with respect to Mr Ford's specific account is that that has been reviewed by our independent auditors, Ernst and Young, who have confirmed that the account has been treated in accordance with appropriate taxation law and accounting requirements. So it has been specifically examined.

Senator CONROY—I understand the concept of the non-accrual loan, that you stop making income from it in your balance sheet and profit. But what actually happened prior to the tax commissioner giving you the capacity to create what became known as a 'non-accrual loan'? Did you keep accruing each day on your books up until that point? Was there are an industry procedure?

Mr Griffiths—From an industry perspective and an accounting perspective we have to make sure that what is recorded in our accounts reflects the amount that we expect to receive. So, if we do not expect to receive the amount, we need to either stop accruing it, or create, in effect, what we call a 'reservation' of that interest. You will see in our financial statements 'reserved interest'. That is the term we have used where interest is still being booked, if you like, but we are backing out for accounting purposes on a global basis the amount of that interest reserved. Regardless of what we do there, if the interest is received in cash—whether it is a G account or an H account—it is always taken to profit; it is always treated as interest income for both accounting and tax purposes.

Senator CONROY—I am not trying to catch you out, I am just trying to find out what happened. You may want to take it on notice and come back to us about what you think used to happen. They seem to have created a new category for you to deal with this, called 'non-accrual loans'. I am just trying to find out what was the accounting practice before the tax ruling came about. Did the G grade not exist? Did you have to go from F to H, in effect?

Mr Ullmer—In terms of general banking practice, for many years—I am going through from the seventies onwards, based on my experienced—banks have always had these sorts of procedures in place.

Senator CONROY—I am sure there must have been some procedure—

Mr Ullmer—There have always been procedures which, in substance, do the same as we are doing today. What has happened through the nineties is that those procedures have tended to become more codified from a taxation point of view. The Australian Prudential Regulation Authority, which regulates banks and other financial institutions, has also taken steps to ensure that the way in which this information is disclosed in financial statements is consistent between banks. Over the nineties, APRA, or the Reserve Bank before that, has issued guidelines which all banks in Australia follow as to how these things are going to be disclosed in their financial statements. So the substance has not changed. Today what you see is a much greater uniformity between all financial institutions on this matter.

Senator CONROY—Could you take on notice what the banking practice was, what the accounting practice was. I am not asking for a 200-page explanation. I just want a rough explanation of how it was handled prior to the creation of the non-accrual loans. I accept that there had to be some practice, I am just interested in what it was.

Mr Ullmer—Certainly, Senator.

Senator CONROY—I turn to the letter which I think Mr Ford referred to where you make reference to the fact that something was written off. I think you were here when he was talking about that—where a staff member wrote and informed Mr Ford that some amount written off by the bank had been inadvertently omitted. Are you familiar with the letter I am talking about?

Mr Ullmer—Based on the discussion of references to 'written off' and 'set aside', I would imagine that was a colloquialism that was being used. So there was no mistake made in terms of the amount being written off but, as I mentioned, through the Commonwealth Development Bank system, the statements were issued together with that write-off to the customer, and that is what occurred and that is what has caused this confusion.

Senator CONROY—Do you have a copy of what Mr Ford was referring to as 1, 2, 3 et cetera?

Mr Ullmer—I do not have a copy of it. Is it possible to have a copy?

Senator CONROY—I am sure that you have seen them, or that someone has reviewed them all for you. Document No. 1, dated 8 January 1996, has an amount which, in Mr Ford's handwriting, totals $435,901.40. He has received another document on 18 June, which is in handwriting. Is it an old practice to issue handwritten statements? Does it still happen now?

Mr Griffiths—I suppose it could happen in the interests of expediency more than anything else. It is most unusual to issue it in hand but, if there is no-one around or if the computer is not working, it may, to get the statement out, be issued in hand.

Senator CONROY—You have heard Mr Ford refer to the mainframe. Are shadow ledgers maintained on a separate computer or does somebody literally sit there—I presume this is not the case—and does it all by hand?

Mr Ullmer—Over the years, the processes have evolved. In the Commonwealth Bank, they are maintained on a computer system today but in days gone by they have been maintained manually. Our understanding is that at some other banks even today they are maintained manually. This all goes to the point that our mainframe systems are designed to produce, in the normal course for the vast majority of Australians who meet their financial commitments to the bank, their normal statements. Those systems are used to develop also our financial statements which we release to the market. With the small number of borrowers that we are talking about here where write offs are required, those write-offs are processed through our mainframe systems and at the same time we need to maintain the separate record of what amount is actually due to the bank, based on the terms of their loan agreements. It is this record, which records their amounts due to us under the loan agreements, which is kept separately in our case on a separate computer system. I do not think anything turns on whether it is a mainframe system or a manual system.

Senator CONROY—I just wanted to understand how it works. Do you know if it was computerised by June 1996? Your shadow ledger maintenance: was it still by hand or was it by computer?

Mr Griffiths—It is substantially by computer but not the same sort of system as the normal statement system.

Senator CONROY—You cannot just press a button and print someone's out?

Mr Griffiths—No. People would have—

Senator CONROY—You call it up on a screen, presumably, and then you write out this material.

Mr Griffiths—We can actually produce a form of statement from it—yes—but people have to go in and put in the various increases that have occurred, because it is not being processed through that system in the normal course. With things like interest charges for the month, we would have to go in and add those in.

Mr Ullmer—Our mainframe systems are dealing today with over nine million customers. We are talking here about a very small population of customers who are having these financial difficulties, therefore they are part of a separate system where those records are maintained.

Senator CONROY—Do you think it has been good business practice not to advise people what their actual liability is?

Mr Ullmer—In terms of our position going forward, I think that illustrates that we have changed our view on that. What we do need to be aware of is that for a number of customers they could well react adversely where they are in financial difficulties, they are perhaps in dispute with our bank or any other bank and they are then receiving constant reminders of what the bank sees its position as being. So I think you have to acknowledge that, in taking this matter forward, there may well be people who find this considerably irritating and in fact may feel that the bank is trying to put pressure on them by continually reminding them.

But, on balance, if we stand back and say, 'Is it better for these customers in totality to understand their full financial position through that regular issuance of statements?' I think we would have to say, yes, it would be better. But I would note that many of these customers are receiving, through the process of litigation or dispute, documents which set out their obligation to the bank. What a lot of this seems to be turning on is to say, 'No, it is not acceptable that we receive this document,' which may well have been prepared by a very senior professional taking a lot of care. 'We would rather receive something that is churned out of a system.' I cannot understand what the difference is, unless people are trying to see what differences there are between the two and saying, 'We will then use those differences to exploit some advantage with the bank.'

Senator CONROY—At what points in F, G or H are you able to start invoking the penalty provisions of your contract, in terms of higher interest rates and those penalty provisions? Firstly, what are the penalty provisions, usually, and at what point are you able to start invoking them?

Mr Lanser—I do not quite grasp what you were getting at.

Senator CONROY—There was one case quoted earlier of somebody having a $5 million loss to you and they ended up being bankrupted for $27 million or $29 million. Presumably, these penalty clauses have kicked in there, in terms of a higher level of interest rate than they otherwise would have been paying.

Mr Ullmer—I would be very surprised if that was due to interest charges. I think you may find that there were a number of other factors with respect to that matter.

Mr Lanser—Were you referring to the matter of Davridge?

Senator CONROY—I think that the gentleman was actually here but no-one was actually named. But Mr Ford referred to a $5 million loan which ended up being a $29 million debt.

CHAIRMAN—It was $27 million.

Mr Ullmer—On that specific matter, without the facts, it is totally impossible to comment.

Senator CONROY—No, but what I am trying to get to is: what are the sorts of penalty provisions that are available to you when someone is in breach and at what point is the trigger for them to be invoked? To start off, what are the penalty provisions?

Mr Lanser—Are you talking about interest penalty provisions?

Senator CONROY—Any penalty provisions; that is what I am asking.

CHAIRMAN—If someone is in default or arrears.

Senator CONROY—Luckily, I have never been in default, so I have never had to get into the situation. But if interest rates keep going up it could be the case.

Mr Lanser—It depends, obviously, on the terms of the loan facility itself. The facility will have, in the loan agreement, provisions for the rate of interest which will be charged and provisions for the rate of interest which will be charged if the loan goes into default as defined in the agreement.

Senator CONROY—They would be pretty standardised though—you would not make them up for each individual contract. What is the penalty rate of interest in your usual contract?

Mr Lanser—That is really a question for Mr Griffiths.

Senator CONROY—I do not mind who answers it.

Mr Griffiths—In a normal commercial business, our default rates are stipulated to be 4½ per cent over the overdraft index rate.

Senator CONROY—Are there other penalty provisions in your standard commercial contract?

Mr Griffiths—In terms of interest rates or provisions generally?

Senator CONROY—In terms of provisions generally.

Mr Griffiths—Again, it would be a contractual thing but not that I can think of, no.

Senator CONROY—That is about the only one, barring unusual circumstances?

Mr Ullmer—There are various costs of realisation of security property and potentially costs of investigation.

Senator CONROY—You are trying to recoup your costs, I understand that.

Mr Lanser—If there has been litigation and there has been a judgment for a debt, then there is a legal doctrine of merger, which is that the debt merges in the judgment. Thereafter, it is more likely that rates of interest prescribed in the court rules from time to time will apply. You may then find that whatever was contractual merges into a different rate of interest applying. And of course, if years flow on, by the time that bankruptcy proceedings or something or other are ultimately taken, interest will have accumulated at that rate. But they are simple interest rates, if they are court rates; there is a provision saying they are not compounding.

Senator CONROY—On page 3 of that document, where you break Mr Ford's account into a portion A and a portion B. Could you take me through what led you to turn something into an A and a B.

Mr Griffiths—This was a policy adopted by the Commonwealth Development Bank at that time. What you have in front of you is actually a record of legal debt or a shadow ledger statement. Effectively, the portion B has isolated that amount that we have taken as a write-off and kept it separately. Portion A is the normal part, which should be recoverable in the ordinary course.

Senator CONROY—Somewhere in these pages of documents, and please do not ask me to find it because I could not, there is a figure of $5,490. The confusion in the minds of the Fords was that they believed that this presumably negotiated and agreed figure of $5,490 actually paid off A and B. You would argue, 'No, it only really paid off portion A.'

Mr Griffiths—At that time what we had agreed to do was to accept interest only on the debt and yes, the $5,490—I have not done the calculation—I am assuming would have represented the interest on both the portion A and the portion B. Instead of reducing the amount of the interest charged, that amount has continued to be paid. The extra amount, you will see, is actually coming off the principal debt so that all amounts received from Mr Ford at the time have been applied in a reduction of the total debt, albeit that we had said that we would accept interest only. We have actually received and accounted for some amounts as principal reductions.

Senator COONEY—When you do that portion A and portion B do you write and say, 'We're going to do it this way'? Is there any explanation to the customer that this is what you are going to do? Is there any explanation given of how the account is set out?

Mr Griffiths—No, not a clear explanation because, again, of the habit of not trying to disclose the internal accounting write-off that we had taken.

Senator COONEY—You do not want to do that. Who don't you want to tell about the internal write-off?

Mr Griffiths—The customer.

Mr Ullmer—As we explained earlier, we feel it is misleading for the customer if they have a sense that the amount—

Senator COONEY—That is what I thought. So it is your judgment of what the customer would want.

Mr Ullmer—This is purely our judgment that the customer needs to understand what is the amount they owe the bank. The fact that we have taken an accounting write-off does not affect the amounts they owe the bank.

Senator COONEY—But that is a judgment you make.

Mr Ullmer—Yes. It is a judgment we make and I would suggest that—

Senator COONEY—So the decision to set out the accounts this way is a decision of the bank.

Mr Ullmer—Exactly. I would also say that it is to our understanding consistent with common banking practice. But I would also go further: I would be surprised if there would be many commercial organisations that have trade debtors where they expect one of those trade debtors to not pay them back fully and they would write to that trade debtor and say, 'We are making a provision against your trade debt.' In my experience I have never encountered that.

Senator COONEY—I want to establish this as a matter of fact. I think you are drawing inferences from what I am asking. What I am asking is that that is a decision that you or any other bank or any other creditor, as you understand it, would make. It is a decision that you make to set out the accounts this way and to treat the money owing, as far as the paperwork goes, in this way.

Mr Ullmer—Yes.

Senator CONROY—Having looked at page 3—and you have made the point that the $5,490 was paying both A and B and a bit of the principal, I think you said.

Mr Griffiths—The amount was calculated such that it would pay the interest on both A and B. But as you can see it is actually applied against the debt in A only.

Senator CONROY—The problem there is that the $134,000 looks like a fixed amount of principal that is not being reduced.

Mr Griffiths—Yes, that is right. It is not being reduced and nor is interest being added to that. The amount of interest that was notionally being charged, if you like, against that $134,000 is actually being used to reduce the principal in portion A so that, in this case, Mr Ford has got the advantage of having principal reductions even though he may not have wanted to reduce the principal but only make the interest only payments.

CHAIRMAN—Was that done by mistake because that letter that Mr Ford referred to talks about interest only payments?

Mr Griffiths—Yes. I think it was an oversight to not reduce the amount such that it did represent interest only on portion A. But as I have said, the money, in full, has been credited against the total debt owed by Mr Ford on that portion A.

Senator COONEY—What was the level of the officer or officers dealing with this act? Clearly, people at your level would not be doing it. Can you give us a picture of the sort of person who is dealing with this—what sort of qualifications he or she has and what experience?

Mr Griffiths—It is a bit hard. Again, it varies—

Senator COONEY—So it could be really almost anybody dealing with this—it varies?

Mr Griffiths—Yes.

Mr Ullmer—Senator, it would have to be an officer appropriately qualified for the particular position.

Senator COONEY—That is what I asked, but it seemed to me that the answer I got was that it varies—in other words, you could not point to a band of people who had particular qualifications. That is what I understood the answer to be.

Mr Ullmer—It varies depending on the complexity of the lending arrangements with a customer. If you are looking at major loans to major corporations in Australia you get account officers with particular qualifications to do that. If you are dealing with business customers at another level you get account officers with qualifications appropriate to that level.

Senator COONEY—You would understand what I am getting at. What has clearly appeared today is that there are misunderstandings. If a system could be developed where at least the misunderstanding did not arise that would be a help. But, for a misunderstanding not to arise, I think you probably need people who are properly trained, properly qualified and who can communicate these issues. You might have the greatest banking system in the world in your mind but, if the people executing the scheme in your mind are not up to it, I think you are going to get problems.

Mr Ullmer—With respect to this particular issue, it was the Commonwealth Development Bank. The Commonwealth Development Bank had their system running in a particular way—and we are going back to the middle of 1990s now. In terms of the policy that was in place, it was not the policy to provide statements with write-offs sitting on them. Going forward within

the Commonwealth Bank we will put in a system to ensure that these things are dealt with properly.

Senator COONEY—If you and I were going to have heart surgery and they said, 'We've got a well qualified young man who got his degree three years ago and has shown considerable merit and we reckon he will be a star in the future; would he do?' we would probably be a bit inclined not to take him or her. It is the same sort of thing here. I often wonder who is actually carrying out the processes that the bank put into operation.

Mr Ullmer—In that regard, Senator, we obviously strive very hard to provide uniformly high levels of service, but we are dealing, as I have said, with over 600,000 business customers—and over nine million customers generally—and mistakes, unfortunately, will occur.

Senator CONROY—We established before that the penalty interest rate was about 4½ per cent on your standard situation. The second question I asked, which I forgot to come back to, was: when do you decide to invoke that?

Mr Ullmer—It would be set out in the loan agreement. So when there has been a default under the loan agreement we would have the capacity to charge the penalty interest. In a number of situations we will waive that right, depending on whether we feel that, by doing so, it would enable our customer to get out of the financial difficulties they may be in at that stage. In other circumstances where it is clear that, at the end of the day, the matter needs to be pursued through to realisation of property we may well charge the penalty interest.

Senator CONROY—You make, in a sense, a commercial judgment? For example, Mr Ford would never have paid this. I think you said that, because he had never been technically in default, he would never have been subject to a penalty.

Mr Ullmer—We had waived those problems by giving concessions on interest. A successful outcome for us is to have a customer who can, in some cases with our assistance, pull through their financial difficulties so that they become a successful financial business again, which is beneficial for the customer, the community and ourselves.

Senator CONROY—If I could then turn to page 4, which is the first of the statements and is dated 4 December 1996. If I can use Mr Ford's jargon, is this a 'mainframe' or a 'shadow' ledger?

Mr Griffiths—That would not be a mainframe statement.

Senator CONROY—This is also a shadow ledger?

Mr Griffiths—It is.

Senator CONROY—On page 5, which again is a statement dated 4 December, is that a mainframe, if I can use that term, and a shadow?

Mr Griffiths—No, a shadow, if we stick to that terminology. They look different.

Senator CONROY—They are obviously different; dated the same day and both presumably taken off the same computer, albeit not the mainframe. It is the shadow ledger computer.

Mr Griffiths—I guess the shadow ledger at that time could have been produced on a number of things, including in some cases being typed on a typewriter. I cannot be certain whether that document No. 4 is not something that has just been typed on a typewriter. Document No. 5, while it has a statement date of 4 December 1996, it was done that way to show that it was effectively as at the same date as No. 4, but it was only done just prior to it being issued in July this year.

Senator CONROY—I guess the critical difference between the two is that most of the other numbers are consistent, and obviously you are back to portion A and portion B, but your total credit figure is substantially different between pages 4 and 5, and they were both reconciled on 4 December. How can you get a situation where there is a fairly substantive difference in that total credit figure? I would have thought if you went back and looked at it on the same day, even if you did it four years later, you still should have had a figure on the screen that was consistent across—

Mr Ullmer—As Mr Griffiths has said, Senator, these statements are produced off a separate process—if I can call it a process—which has evolved over time, and it is not a situation where one is pressing a button and up on the screen pops a number. It is a situation where—from my understanding, Mr Griffiths—the second statement was being done in response to these requests to say, 'Provide me with a statement of my account.' Clearly, with the passage of time, every effort was made to make sure that there was no confusion as to write-offs appearing on that statement, and obviously any other various charges that had occurred as part of the process of settling commercially the arrangements between Mr Ford and ourselves were put through on that statement. So, as people ask for a statement of account, our understanding of that is that that is a presentation in a documentary form to a customer of what their position is with the bank. It does not mean that it has to be produced by pressing a button on a mainframe computer.

Senator CONROY—I understand that. I guess the problem still continues to be that the figure under the heading 'Total credit' is $140,000-odd different. This time you are actually supplying the information to the customer as opposed to the previous policy which was not to. How confident are you about the processes when there can be $140,000 difference in total credit?

Mr Griffiths—Firstly, if I can, the statement form was issued and provided and inadvertently left out the portion B. It was a statement issued after the settlement of the property transactions, at which point we had had an exchange of letters between the bank and Mr Ford agreeing that the receipt of a certain amount of money, some $478,000, was going to be received in full extinguishment of the debt. So at that point, we have to say, as long as the balance gets to zero, that presumably ought to be enough for the customer—there is no more money owing by the customer.

What we did not do, and it was alluded to in Mr Ford's presentation, was credit the full amount actually indicated. As you can see on page 4, there is a credit of $355,416, and we paid $404,809. It is notated there, and that difference of $404,000 was actually paid. What we have done, though, part of this was the bad debt recovery, and we have treated it as a bad debt

recovery in the bank's general ledger, the set of accounts that prepare our accounting records and our income tax record, but we have not put it through this subsidiary system. So, if you like, in terms of Mr Ford's statement, it did not properly reflect the amounts that had been received on his account. The correct numbers were, though, processed through the bank's general ledger system.

Senator CONROY—Did you supply him with a general ledger?

Mr Griffiths—No.

CHAIRMAN—At that stage the total debt was cancelled, as distinct from simply an amount being written off.

Mr Griffiths—Yes. There was an exchange of letters between the two indicating that the amount would be received in full extinguishment of the debt and the release of securities.

Senator CONROY—You can understand if I paid you $404,000 and I received a statement from you—albeit some time down the track—that indicated I had only paid $350,000, that that would certainly cause me enormous concern: 'Firstly, what does this mean? I have paid it back.' It would certainly distress me if I received a statement indicating that I had actually paid back less.

Mr Griffiths—Exactly.

Senator CONROY—There is actually no argument, I understand, between all parties that $404,809 was actually paid.

Mr Ullmer—And there are the letters from Mr Ford to the bank in September 1996 saying that these amounts fully discharged all of his obligations to the bank, and there has been no dispute on that. The issue is, when subsequent requests were made up to 3½ years later saying, 'Please, can we have a statement of account,' in a situation where it has been quite clearly established that all obligations have been eliminated, that initially the lending officers were saying, 'Why do you need this? This amount has been settled; you've written to us confirming that it has been settled.'

Senator CONROY—I would have more confidence if I had not listened to Mr Madigan earlier who seemed to be able to get nil balances and then find that he kept ending up in debit. I would have a bit more confidence if I had not heard Mr Madigan when you say a nil balance means it is over.

Mr Ullmer—Mr Madigan contrives to create those situations.

Senator CONROY—I know Mr Cameron wants to ask some questions on Mr Madigan.

Senator COONEY—You seem to be saying there—or it is coming across to me and I want to correct it—'Look, you are asking for this 4½ years later. That is a bit beyond what is reasonable unless you can give us a reason.' Is that the attitude you were taking? Did you have

that information and say, 'Look, we're not going to give it'? That is one situation. Or did you say, 'Look, we haven't got this information; it is going to be terribly difficult to get it,' which would be a different situation again. I was wondering whether, if it was the first, you were simply saying, 'Well, look, even though we have the information we are not going to give it to you because this matter is all disposed of and why should you be coming around now and worrying us?'

Mr Ullmer—As came out in the discussion of Mr Ford's evidence, a point in time was reached where we were put on notice of potential claims that would be flowing against the bank, so caution was naturally then brought into play—'Well, you have put us on notice that you may potentially be claiming substantial amounts of money against the bank and, at the same time, requests are being made to say, "Can you please send me statements?"'

Senator COONEY—So you were saying this is sort of discovery by stealth almost; wait until the court case before we give discovery. Is that the problem?

Mr Ullmer—I note that we have offered on a number of occasions to go through a process of mediation with Mr Ford to settle these matters, and those offers have been rejected, so the environment that has been created from the bank's perspective is why is this happening.

Senator COONEY—That is so; I can follow that. So you are saying the climate that had been created by the time he asked for those was such as to lead the bank to think, 'Litigation is in contemplation and therefore we will not help in any way except what the law requires.' Would that be a reasonable assumption?

Mr Ullmer—Ultimately, in fact, we did provide the statements last month, I believe. Yes.

Senator COONEY—Yes, I can follow that but why did you ultimately do it? Was that according to legal advice, was it because you thought, 'It's not going to hurt us,' or 'It's the right thing to do'? I suppose what I am really asking about—and we got on to this before—is the culture with which the bank comes to this. I think there is nothing wrong with people saying, 'I'm going to defend a court action and I'll take every legitimate legal defence I can,' but that does indicate a particular attitude. Other people say, 'What's your problem? Let's see if we can answer it.' It is a different way of going about it.

Mr Ullmer—I think there are degrees here. With over 600,000 business customers, the relationship is extremely positive in the vast majority of cases. We are dealing with situations here where borrowers are quite rightly concerned at the loss of their financial assets that has occurred through what emerged in their businesses. Clearly, it is a very difficult time for those individuals. Our approach to that, as I think we indicated through our actions, is very often to endeavour to assist customers through those difficult times. When we get to a point in time where our judgment is that there is no prospect for recovery of the customer's business, we have no option other than to seek to recover the money that we have advanced. Clearly, that is not going to be a happy environment, certainly for the customer, but also for the bank officers, who do not enjoy this sort of situation.

Senator COONEY—Who are the decision makers in this? Who makes the decision to foreclose on a debt and, if need be, to go through the legal process and even end up ultimately

getting an order for bankruptcy? Who makes that decision? At what level is that sort of decision made?

Mr Ullmer—I will ask Mr Griffiths to give you the detail on that but I would note that there are a whole range of what we call delegated authorities within the organisation and a matter such as that would not be taken lightly and would be subject to review by a more senior individual than the account officer.

Senator COONEY—Before you answer that, I will go further; this may help you to answer. I think it was said before—and quite rightly—that the bank has got obligations to shareholders and to the integrity of the bank itself. There are a whole series of pressures on a person who is a decision maker to work out what is going on. Clearly, the person cannot act as Father Christmas but, on the other hand, there is a relationship between customer and bank and traditionally, at least in the old days, there was almost a friendliness—particularly in the country—in the event of this sort of thing. It seems to me that that has changed. What I am trying to get at is a feel for how a decision maker would go about his or her process.

Mr Griffiths—Firstly, in respect of who makes the decision, as Mr Ullmer has said, we have people with credit approval authorities within the bank. Those amounts will increase depending on seniority, experience et cetera. In terms of the management by those people, they will manage a file. If they are entitled under their approval authority to make a decision, then they will do so. That will always be subject to a hindsight review by their next most senior officer anyway. On an annual basis, we would review the delegations held by those people. If they have shown and demonstrated more experience and skills, they might be awarded a higher delegation. If there have been problems, they might actually lose their delegation if they are seen to not have been exercising them in the appropriate way. That is how those decisions are made and those are the reviews that are in place.

Senator COONEY—And if the matter gets to court, I take it that you send it off to some firm of solicitors. Does the firm of solicitors then take over the decision making?

Mr Griffiths—No, the firm of solicitors just take instructions. The account manager will still manage the outcomes. So, during that period, they may offer mediation, get involved in mediation or decide to accept a compromise amount.

Senator COONEY—With respect to every legal step that is taken, whether interlocutory or otherwise, that decision is always made, ultimately, by the decision maker in the bank?

Mr Griffiths—Yes.

Senator COONEY—Whether you decide to go to court and what tactics are used in court, those decisions always come back to the decision maker in the bank?

Mr Griffiths—Ultimately that is right.

Mr Ullmer—Based on legal advice, which may be either internal or external legal advice.

Senator COONEY—So the lawyers just perform the task of carrying out the technical functions. Am I correct in saying that?

Mr Griffiths—That is correct.

Mr ROSS CAMERON—We did have quite a debate inside the committee about whether to proceed with this inquiry, in part because we did not want to just trawl the bank's reputation through a group of vexatious litigators or disgruntled defaulters or whatever it is. But it is fair to say that people come to their MPs pretty much as a last resort and that quite a few of us have had people coming to us about this specific set of issues with a felt sense of personal injustice, which said to us that we ought to at least investigate it.

There is a range of things which seem to me intuitively to support the bank's position. One is we accept the fact that you are a very good taxpayer. On behalf of the Commonwealth, we appreciate that. We assume your affairs are audited every year as a public company and we are not receiving complaints from the auditors or from the ASX. But there is a question about the management practice and about how to avoid this situation continuing. You say 'shadow ledger' is an emotive description. How does the bank describe the ledger?

Mr Ullmer—I suspect that is how historically we have described it.

Mr Griffiths—In some places, record of legal debt; in other cases, it has become, just colloquially, a shadow ledger.

Mr ROSS CAMERON—That is the way you describe it, but it makes people apprehensive. I think Senator Conroy is right that if people receive two different statements of the nature of a commercial relationship involving hundreds of thousands of dollars and in which up to $60,000 just disappears, then they feel nervous.

I appreciate your point that you do not want to send a signal to a customer which says, in effect, 'You shouldn't feel obligated to repay this because we've written it off.' At the same time, if you have some trigger in a relationship with a person who in many instances takes a great deal of pride in their character and reputation and who wants to do everything in their power to repay, and you just say, 'At this trigger, the cone of silence falls and you get no information,' then I just feel that management practice of saying, 'We don't want to inflame the situation by giving people information,' is why we are here today—because, in part, you have inflamed the situation. When an environment of suspicion develops where people cannot get information, then when they get it they get two quite different stories and then that is attributed to inadvertence on behalf of junior staff but it is clearly happening as a systemic thing in the whole organisation, then people wind up in here.

Mr Ullmer—I do not think people in my position can blame junior staff; we have to take responsibility for what happens within the organisation. With respect to the relationships that build up with customers, I think it is unfortunate that we are dealing in specifics here. As an aside, I should say we thought long and hard about whether this is appropriate because there is a very important issue of banker-client confidentiality, but we felt that in a sense that had been waived by Mr Ford and Mr Madigan coming forward in the way they did. We felt, having regard to our reputation and the fact that we are an institution that means a lot to people,

whether they be shareholders, pensioners, superannuation funds, et cetera, in this country, we have an obligation to defend our reputation.

Mr Ford acknowledged that the relationship that had gone back a long time with the Commonwealth Development Bank had been a good one, and certainly from our perspective our view would be that in quite a number of cases we had given concessions to accommodate Mr Ford through a difficult financial situation. So, if the discussion was being held before those concessions reached a point where we said, 'We cannot see the light at the end of the end of the tunnel,' and in fact Mr Ford's own expert said that he could not see the light at the end of the tunnel—if this discussion was happening before that point in time, I would hope everyone would say that this is a good example of how this should all work. But the reality is, when we are dealing with over 600,000 customers, you will not in every single case manage to achieve a situation where those concessions can be given and given until a point in time when things start to get better.

Mr ROSS CAMERON—Is it the case that you always held security over assets sufficient to meet the debt?

Mr Ullmer—Based on our assessment, no, and based on the assessment of Mr Ford's expert, who said that he had to realise assets for his financial viability. I would note that Mr Ford handled the sales process and at the end of the day we ended up writing off in excess of $110,000. So at the end of the day we, I would put forward, were correct, that there was a loss to be suffered. We had slightly overestimated it some years earlier.

Mr ROSS CAMERON—Why was there this practice of the shadow ledger that became this handwritten—what was the basis of that protocol?

Mr Ullmer—In a sense, the genesis of Mr Ford's complaint with the bank has actually got nothing to do with shadow ledgers, because it was the Commonwealth Development Bank system which in the normal course sent out a bank statement, or Mr Ford obtained a bank statement, which showed the write-off being processed. So in a sense that was nothing to do with a shadow ledger, and that was what created all the confusion. Subsequently, when it was brought within what was the policy at the time, this distinction started to be drawn between the amount that was owed to the bank under the loan agreement and the amount that we are properly reflecting in our accounting records.

Mr ROSS CAMERON—We have evidence from one of the other witnesses, though, that there was historically in the industry for some time—

Mr Ullmer—That is correct.

Mr ROSS CAMERON—That once the decision is made that whatever the grade is that has been reached, you then revert to this kind of on the back of an envelope thing—it feels amateurish for an organisation like the Commonwealth Bank, to me.

Mr Ullmer—It is a question of looking at the volumes that are being dealt with at any one time. In today's environment, where obviously the credit conditions are quite good, it may be approximately 100, or indeed less than 100. Then there is a question to be asked: do we go out

and build a system to maintain that in these circumstances where write-offs are being processed?

But, going forward, because of the concerns that have been raised, we will put in place whatever is the appropriate system that is required, having regard to the volumes and the complexity, to advise all borrowers as to what their position is—all borrowers who are defaulting on their lending agreements.

Mr ROSS CAMERON—To be fair, I am assuming you are not setting out to run a business to get more people into shadow ledgers, and I think intuitively that supports the proposition that the banks are putting. But it has been argued, for example, that this method of recording transactions in this area assists the bank to avoid discovery obligations and provide a transaction trail in the event that we do get into litigation. Since the allegation has been made, you should at least have the opportunity to respond.

Mr Ullmer—Mr Cameron, I am astonished that there would be any such assertion in discovery proceedings. Clearly, all relevant material, other than anything under legal privilege, has to be brought forward. These ledgers are not maintained under legal privilege. As I have said on a number occasions, at the end of the day, if we are into bankruptcy proceedings, a court is going to want demonstration through factual evidence of the amount that is owed to the bank.

Mr ROSS CAMERON—There was another suggestion which I think you should have the opportunity to rebut. I understand it may be subject to litigation at the moment but we are not prohibited by sub judice from raising it since it has already been raised. It is that the bank changed its fee policy in relation to home loans from a longer period to a shorter period without notification to customers. Do you want to respond to that?

Mr Ullmer—I may ask Mr Lanser here to see if he can elaborate on that.

Mr Lanser—I can only elaborate to the point of saying it has been pleaded in an amended cross-claim filed in the proceedings between Mr Madigan and the bank. It has not even been served on the bank yet. He had to go through the process of getting leave of the court to do it and the court granted him leave last Friday. I have not even received a sealed copy of the document. I have to say I do know now what is in it. There is an allegation of that kind. It relates to events a couple of years back. Clearly, I have to get instructions from the relevant part of the bank before I can plead a defence to it. I am not at the moment sufficiently instructed to be able to respond on a factual basis to that matter. But it has literally within the last 10 days been pleaded by Mr Madigan in his present dispute with the bank.

Senator CONROY—You will be happy to know I am almost finished. I was talking about incurring penalty interest rates. When that happens do you advise the customer that it has happened? I am talking in a general sense.

Mr Griffiths—It is always difficult in these things. If you say yes, you will find a customer who has not been advised. Ordinarily, I would have to say that we would.

Senator CONROY—That will be in the form of a letter. Bearing in mind that you are no longer sending them statements when you have reached this point, how do you advise them, and how do they then know what is the ongoing debt incurring to the bank?

Mr Griffiths—Firstly, we may still be sending statements at that point.

Senator CONROY—It is not a matter of practice. I think it is agreed. I am not trying to put words in people's mouths.

Mr Griffiths—Once a customer first goes into default, we may not have, and probably have not, taken a write-off that would have caused anything to happen to move a customer's statement outside the normal system. In those circumstances they would continue to get a statement in the ordinary course which would disclose the interest rate.

Senator CONROY—So it is not possible for someone to be accruing an amount of money that they are unaware they are accruing. Maybe someone phones you up or sends you a quick note saying that it is 4½ per cent compounded or not compounded. You would not necessarily be receiving a statement that tells you it is an extra $10,000 this month and an extra $10,000 next month. It is not possible for that to occur?

Mr Ullmer—As Mr Griffiths has said, there are a number of customers who are in default of the lending obligations to the bank for whom we have not charged a write-off because, at the end of the day, we may feel we are well secured and can help the customer through these difficulties with the comfort that we know the security is there. In that situation, the statements will continue to issue through the normal course. We are talking about that very small number where write-offs have been taken which then move out of the normal system. That is what we have undertaken to do. Today any of those customers in default can ask for statements if they are not receiving them. They may well be receiving them anyway. Going forward as a matter of practice, we will continue to issue statements to everybody that will detail their facilities, including any additional interest charges. It is also obviously spelt out in the loan agreement what the charges are.

Senator CONROY—If I was incurring a debt to you of an extra $10,000 a month, even though it might have been in the contract I took out with you 10 years ago, you say it might irritate but to me it would certainly reinforce in my mind that there is an extra $10,000 this month, and there is an extra $10,000 next month. I am just conscious of wanting to make sure the customer is informed that their liability is increasing. The fact is, as you have indicated, what you are now putting in place will leave no doubt, but certainly there seems to have been in some of the instances—

Mr Ullmer—It would be a very small number where that may be the case. Until such time as the proceedings are moving, at which point the legal process—

Senator CONROY—Sure, I accept the legal process.

Mr Ullmer—Probably it is well before the legal process in terms of exchanges between solicitors.

Senator CONROY—Does the bank write off as expenses, as you incur them, legal and debt recovery expenses and get a deduction for them?

Mr Ullmer—Expenses as incurred will be taken as a deduction from taxable income.

Senator CONROY—Do you add them to the shadow ledger, as well as the total figure, to determine whether you have fully recovered all costs?

Mr Ullmer—If they were appropriately recoverable from an individual we would not be charging them off as an expense, it would only be where they were not recoverable from the individual, or alternatively, where in accordance with the taxation requirements we had good reason to believe that whilst they were theoretically recoverable they would actually not be paid because of the financial position of the individual. In that case it would actually be a write-off, as opposed to the expenses themselves being charged.

Mr ROSS CAMERON—In relation to the question of a $500 withdrawal for costs while an action is on foot, Mr Madigan's case, before a court award for costs, what is the bank's policy on accounting for those expenses?

Mr Lanser—That is contractual. There is a clause, E14 of the mortgage in Mr Madigan's case, the bank's standard form of mortgage. It has a provision which in shorthand says that the bank is entitled to debit to the account the legitimate costs of any realisation. In the particular instance, as Mr Ullmer told you, what actually triggered the whole situation with Mr Madigan was that the bank held a mortgage over his Harris Park property but the mortgage was unregistered. Mr Madigan swore a false statutory declaration to the Land Titles Office in which he declared that he had lost his certificate of title and, most particularly, that it was not held by any financial institution as security. The Land Titles Office issued him with a duplicate certificate of title and he used that to sell the bank's security.

When the bank became aware of it, it obtained an injunction from the Supreme Court restraining Mr Madigan from dealing with the proceeds of sale and requiring him to disclose the whereabouts of the money. Mr Madigan did forthwith pay out the entire loan. In effect, he sought not to defend the injunctive proceedings brought by the bank. The filing fee, which was $509 for the proceedings in the Supreme Court, was certainly charged to the account pursuant to the provisions of clause E14 as an arguably legitimate expense.

While I am on that point I might deal with the transcript matter which so agitated Mr Madigan. During one of the interlocutory proceedings, because of the Land Titles Office's potential involvement, Mr Justice Santow directed the bank to procure a transcript of the proceedings before him that day and send it to the Land Titles Office to ascertain whether the Land Titles Office wished to be joined in proceedings. We did that, and the Land Titles Office did become a party to the proceedings and the duplicate certificate of title was delivered up to the Land Titles Office for destruction. It is true that the charge for that transcript from the Court Reporting Service was also debited to the account, pursuant to clause E14.

Mr ROSS CAMERON—I do not think there is any doubt that the bank's relationship with Mr Madigan had deteriorated very considerably and that he is a person determined to expose what he regards as the deficiencies in the bank's business practices. That is not a defence. I am

obviously not in any position to comment on the swearing of the affidavits and so forth. How does a person contrive to keep open an account which the bank has told them has been closed, on several occasions?

Mr Ullmer—The Commonwealth Bank, in terms of customer service, has the most access points of any financial institution in the country. We have approximately 1,050 branches and 3,500 post office agencies all over the country that act for us. If an individual is so determined to maintain an account with us and chooses to come into, say, a post office and deposits 65c to an account for which there was at one time a valid number in our system, it is very unlikely that somebody in a post office is going to look at that and say, 'No, you are Mr Madigan, we are not going to accept that deposit.' By this time, therefore, 65c is wending its way through our systems, at which point in time some operator will call it up on a screen and say, 'That was a valid number, we had better deposit it,' because we like to make sure that the money goes to the account of people who have deposited it.

I imagine that success in Mr Madigan's eyes would be something coming up and saying, 'We don't recognise this number. We cannot read what the name says on the deposit slip. We'd better pay this 65c into unclaimed moneys.' I am sure we would then start to get a range of claims about, 'Where is my 65c?'

Mr ROSS CAMERON—We will obviously hear from the tax office soon. We appreciate the time you have given today. I do not want to prolong it unnecessarily, but I was reading Peter's book on customer service and he used banking as one example. He said that best practice in a bank filled with customers standing in a queue was that the bank ought to nominate an officer to periodically go down the queue and give them an indication of how many minutes it would take to get to the front of the queue, on the basis that people get most angry in an environment of least information. And, for what it is worth, I think that would be a good practice in my electorate of Parramatta, particularly lunch times on Thursdays and Fridays.

But we are separately investigating the question of banks declaring their fees on electronic transactions and the reluctance of banks to indicate to customers the fee they are likely to incur in such a transaction. I do not want to open that here, but it does seem to me that quite a lot of these problems are self-inflicted wounds where the bank may be acting lawfully, but the environment of secrecy foments hostility. Respecting the problem you have with seeking to give an implicit permission for someone to default, it does seem to me you have got a management problem to address there.

Senator CONROY—Which they have.

CHAIRMAN—Which they have addressed in the statement today.

Mr ROSS CAMERON—Yes, and I do think we appreciate that. I think it is a useful gesture. I think, in particular, you sense from quite a number of the witnesses that they want to do the right thing and they feel that they are being frustrated in some way by the banks. So I think this is a very welcome step forward.

Mr Ullmer—Mr Cameron, I make the observation that, on pension days, we actually do have retired bank officers going up and down the queues encouraging the pensioners there to use the

electronic facilities and actually showing them how to use them. So we are trying to improve all the time and we will continue to improve going forward.

Senator COONEY—What sorts of audits do you carry out through the system? I am fascinated, perhaps needlessly, by this decision making process, and there are two things about that. A good decision maker needs to know—I just propose this as my thoughts—what the law is and what the facts are and also needs to have a proper disposition. What do you do about those sorts of things? Do you have any quality audits that look at these sorts of things?

Mr Ullmer—Yes. I will address that issue on two fronts, specifically with respect to lending. As Mr Griffiths observed, we have an independent unit within the bank called our risk review unit. That unit is made up of very experienced lending officers who periodically go around and visit every aspect of the bank which is involved in lending processes—from individual branches that make loans to business banking centres et cetera. In that process they will draw a selection of files with respect to loans that have been made and, using their experience, review those files to see whether the lending decisions have been taken in accordance with what in their experience—both policy practice and good commonsense—would be the appropriate way to treat that file.

That is also used at that point in time to confirm, in that experienced lending officer's judgment, whether the account officer has appropriately graded the loan, which then flows on to the earlier discussion we were having about whether provisions may be required. That process is also used as an on-the-job training exercise, so those senior officers will then spend time with the individuals taking them through their findings and hopefully a process of continual improvement. Overlaying that, we have a separate internal audit department of some size covering all aspects of the bank's operations but including this area so that they ensure risk asset review are doing an appropriate job. Finally, we have the external auditors who, given the level of controls and review that we have in operation, address their mind to whether these controls and processes are operating effectively.

Senator COONEY—Does that include the sorts of things that Mr Cameron was raising? You could have a quality audit that looks at whether or not people are making the right decisions about loans and doing all that sort of thing. But what about the issue that he was raising of 'customer comfort', if I could use a fairly colloquial term?

Mr Ullmer—On that point, yes. Our internal audit mandate goes to the whole issue of sales and service in our branches. It will go to such issues as the appearance of the branch—cleanliness—and whether staff are being appropriately mentored; whether they are receiving proper commentary on their performance feedback et cetera. It is quite a sophisticated process but, remember, we are dealing with an organisation with of the order of 30,000 employees.

Senator COONEY—Do you have a litigation policy? Has the bank got a policy set out that talks about its litigation policy? The Commonwealth is supposed to be what they call 'a model litigant'—whether it is or not is another matter, but at least that is what it proposes. Have you got a philosophy in the way you go about your litigation?

Mr Ullmer—In terms of our attitude to litigation, each matter will be judged on its merits. Unlike most banks, we have a reasonable internal legal capacity ourselves, so we are handling

many matters on our own. The benefit of doing that is that we are not being driven by a legal process where perhaps there is an incentive for people to quickly get into aggressive litigation and into court. Certainly we are very mindful to avoid court situations where it may well be futile—where it may be better to settle the matter and get on with life.

Senator COONEY—You wouldn't have any figures showing how many cases you have going now and how long they have been going for? Have you got any idea how long an average case goes—although that is probably something you could not answer because there would be no average cases. Put it this way: how long has the longest piece of litigation that you now have going been going for and what is the cost—or would you prefer not to talk about that?

Mr Ullmer—I do not have at top of mind those statistics, although those statistics are maintained in the normal operations of our legal department.

CHAIRMAN—You can take that on notice.

Senator COONEY—Yes, I can. I think a lot of the problems arise here through people getting into litigation, and the complaints seem to be the cost—the fact that the banks have massive resources—and the length of time the process seems to take. Of course this can well 'starve' former customers out of pursuing what they see as their rights.

Mr Ullmer—I think our record would show that we do not endlessly extend litigation. I would note that, in the Ford case, that matter did not go to court. It was settled between the parties.

Senator COONEY—I do not want them now, but do you keep diary notes of what happens—what decisions are made and how they are made? If somebody says, 'We will take this to court,' do you make notes about the decisions you make and why and how—what you think this will cost, how long you think it will take and what witnesses you will need?

Mr Lanser—In the legal department we operate on instructions received from the bank.

Senator COONEY—What I want to get at is this: a lot of the problems come around because of the threat of litigation. It seems to me that you say, 'No, we are good litigants.' That is how you would see it, but it is a matter of how others see it. Can we get some way of assessing what sort of litigant you are by evidence other than your own words? I do not doubt your own words, but we all see ourselves, quite rightly, in a good light. I am wondering whether you have diary notes or anything like that in your department. I do not know if you do it, but with a lot of lawyers if somebody rang them up they would take a diary note and say so-and-so rang or 'Mr Lanser rang and he said this.' You might not do that, in which case you would not have these diary notes. Lots of lawyers keep diary notes of telephone conversations—what has been said and what have you—mainly out of a sense of self protection, but you do not seem to do that.

Mr Lanser—In the legal department I keep diary notes of instructions received. Certainly on an ongoing basis we are evaluating the case as it proceeds along and we will render appropriate advice if we feel it is appropriate that the case should be either mediated or otherwise resolved.

Senator COONEY—So those diary notes would be available if people wanted to have a look at them?

Mr Ullmer—On a particular matter, yes.

Senator COONEY—You ought to say no to that, I would think.

Mr Ullmer—It depends what agency is asking to look at them.

Senator COONEY—Do the decision makers in the bank take diary notes of what is happening too?

Mr Ullmer—I, for example, would maintain a pad like this one here. I have these pads going back for 10 years.

CHAIRMAN—As there are no further questions, I thank each of you for appearing before the committee and particularly for the extensive way in which you have answered questions. We appreciate that.

Mr Ullmer—Thank you, Chairman, for the opportunity.

[1.28 p.m.]

BURROWS, Mr Scott Andrew, Assistant Commissioner, Large Business and International, Australian Taxation Office

KILLALY, Mr James Michael, Deputy Commissioner, Large Business and International, Australian Taxation Office

DUCRET, Mr Alan Raymond, Queensland Regional Director, Australian Competition and Consumer Commission

CHAIRMAN—Welcome. We are running quite short of time. We have about 20 minutes before we finish the hearing, because we have question time at 2 p.m. Senator Conroy has some general questions that he wants to ask the ATO, which he thinks he can do in public. I might give him that opportunity. If you think we need to go in camera so you can answer even those general questions, we will do so.

Senator CONROY—I have no specific questions on the Commonwealth Bank's taxation arrangements to raise with you. I would ask you to take us through, from your perspective, how the provisions for bad debts, as opposed to the actual writing off, operate and how they interact with the tax system. That is really all I am interested in. Would you take us through your version or view of how that interaction takes place.

Mr Killally—I might just broadly outline the income tax provisions and then go into a bit of detail about how they work in practice. With the normal lending arrangement, there is a principle amount and interest accruing on it. There are certain provisions in the Income Tax Assessment Act—sections 51 and 63 of the old act and sections 25-35 and 20-20 of the 1997 act—which deal with the writing off of amounts considered to be bad debts. Those provisions in both the old code and new code also have clawback provisions where amounts are recovered in respect of debts previously written off and they are included assessable income.

The established practice of the Australian Taxation Office in looking at a financial institution is to examine whether, in fact, the debt is bad wholly or in part. That requires a further examination than simply the writing-off in the journals of the bank. We need to be satisfied that the amount is, in fact, bad. That is a commercial judgment, looking at the circumstances of the particular case. Prior to a debt actually becoming bad, it may become doubtful or somehow impaired. There is then a practice in the banks of creating what they call non-accrual line accounts. They are accounts in which the loan is booked and interest does not accrue on those particular loans. The net effect in tax terms is that, once that judgment is made—and assuming it is made on a reasonable basis—the accounting treatment for tax purpose changes from a situation where previously interest was booked in assessable income as it accrued over the period of the loan to one where the interest is brought to account only when it is received. In other words, it moves from accrual basis accounting to a cash basis accounting. The reason for that is the judgment that there is something that is impairing the collection of the interest amount. With respect to the principle, as I said previously, there has to be a physical writing-off in the books of the account and there has to be a satisfaction from a tax point of view that it was

appropriate to do that. If a debt, for example, is fully secured, then we would not accept a writing-off as a bad debt.

Senator CONROY—You might have heard me ask this question of the previous witnesses. I understand that in 1994—I think 22 December 1994 was the actual date—you introduced the concept of non-accrual loans. What was the practice before the tax ruling on non-accrual loans in terms of how you booked up the interest?

Mr Killally—That practice had actually been followed for a long time. I can recall back in the 1980s that this was an issue. The ruling in 1994 simply formalised the matter, published it for the public at large, and addressed some situations where there were differences between the approach taken by the Reserve Bank at the time in terms of prudential requirements and the tax office threshold requirements for the writing off of bad debts and for the accounting of recoveries. There is a handful of situations where there were differences. For example, if the security was sufficient to cover the debt and the interest, we would not accept that you could have a non-accrual loan in those circumstances. There were two other situations: where there is an expectation that the debt would be repaid in full, albeit the term would have to be renegotiated to allow that to happen; and where there was no breach of any clause of the loan agreement—for example, a situation where the debt had not actually become due. In those circumstances, the tax office took the view that you could not write off amounts before they became due. They were essentially the three differences between the treatment by the tax office and the Reserve Bank in those days. In all other respects, they were common approaches. The difference is more to do with capital adequacy and the need to have a very conservative approach there and the requirement in the tax legislation that the writing off has to be a commercial judgment on the balance of probabilities.

Senator CONROY—You used the word 'formalised' in regard to what was in effect industry practice. What did the law actually require as opposed to what was industry practice?

Mr Killally—Section 63 required that the debt be bad and that it be written off as such in the year of income, but there is another general provision. Section 51—the general deduction provision which applied prior to 1997—in the case of money lenders, also allowed for losses and outgoings to be deductable. If a bank formed a commercial judgment on a reasonable basis that it had taken a loss either completely or partially in respect of a loan, then section 51 could give rise to a deduction for a financial institution.

Senator COONEY—Who would make the judgment in the tax office? Would that be done in the legal department? Was it proper to write that debt off?

Mr Killally—The matter would generally arise on a review of the bank's accounts in the course of an audit. In those circumstances it would be the audit team leader or his or her supervisor.

CHAIRMAN—Perhaps we will take the evidence that you are able to give in public and then we will move to in camera evidence.

Mr Ducret—Thank you, Chair. The ACCC's Brisbane office, for which I am responsible, is currently investigating complaints from Mr Ford and others involving possible contraventions

of the Trade Practices Act. We are looking at these issues today as to whether they amount to contraventions. To that extent these issues are a work in progress for the commission. We have not reached a final decision on whether or not there are contraventions, but I would like to add that our approach is to try to find an industry-wide solution to the problem. I am heartened to see that the Commonwealth Bank today have said that they are going to make information available. That is the first I have heard of it. I assume that they mean not just a level of indebtedness, that they are going to give full statements, but that is a great start. We do not see this is a problem just for the Commonwealth Bank. This is an industry-wide problem and we would like to get industry-wide solutions.

Senator CONROY—In seeking a solution, you must believe there is a problem.

Mr Ducret—We believe there is a consumer problem. There is no doubt that there is a problem for the customers of the bank. Looking at it from that view, there are ways and means. It does not mean that you have to prosecute someone for it. There may be ways of improving the situation for consumers. Our eyes are not just on litigation; they are on trying to get a better outcome for consumers.

Senator COONEY—Have you been conscious of the fact that they have audits that go around the whole time trying to improve customer service?

Mr Ducret—Every business would do that.

Senator COONEY—On this specific one, were you conscious when you were—

Mr Ducret—No.

Senator CONROY—You have not considered shaming them, as Mr Fels is regularly doing with the dreaded price exploiters?

Mr Ducret—When we do that sort of thing, do we it in terms of litigation or contraventions of the act. We would not shame them. If we came to the conclusion that there was no contravention of the Act, shaming them becomes fairly difficult.

Senator CONROY—Mr Fels is shaming them before he litigates.

Mr Ducret—He reaches a view first that there is a breach of the law. He does not shame people without saying that they have done something wrong.

Senator CONROY—There is a reverse of the onus of proof in those situations. He just has to say, 'I think they are guilty,' and they have to prove they are innocent.

Mr Ducret—Yes. It is not in these instances.

CHAIRMAN—Do you want to give the rest of your evidence in camera?

Mr Ducret—I would be happy to talk to the committee about where we are going and so on, but we would like to do that in confidence.

CHAIRMAN—Before we move to in camera evidence, can I first dismiss the bank. Senator Murray would like have some questions put on notice, but he had to leave. There was a request from another member of the rural network to give evidence, but because of the time we will not be able to do that. Again, perhaps that submission could be given in writing. We will now move to in camera evidence.

Evidence was then taken in camera—

Committee adjourned at 1.39 p.m.