PART 6

TRAINING AND SUPERVISION

The effectiveness of HFC's efforts in training and supervising its staff became an issue in these proceedings for a variety of reasons.

HFC itself put it forward that certain conduct on the part of its employees such as pursuing bankrupts for amounts owed to HFC and threatening to repossess goods over which HFC had taken no security was attributable to a lack of adequate training. Other conduct by HFC's staff also raised the issue of whether the conduct was caused wholly or partly by a failure in training or supervision.

It is important in examining this issue to bear in mind that HFC's operation is a highly decentralised one. Much of its lending business is solicited, managed and collected in branch offices. HFC branch offices have very small staffs, typically a branch manager, either one or two assistant branch managers and one or two more junior staff. Some branches are even smaller. Branches are under the supervision of district managers.

According to Mr. Vona the typical district manager has had two years service in that role preceded by three years as branch manager and, it would seem, one year as assistant branch manager, since his total service with the company is six years (6070). In its opening statement to the Authority the Applicant stated that the typical branch manager was between 23 and 25 years of age. It is thus evident that even up to the level of district manager the periods of experience are relatively brief.

Interestingly, the Authority was also informed that by comparison with the staff of Household of the United States, Australian staff have less experience at comparable levels of responsibility. That does not surprise the Authority since extremely low morale and heavy staff turnover are said to have been major problems within HFC.

It follows from -

(i) the relative isolation of branch staff that is inherent in the de-centralised branch structure;

(ii) the relatively short periods of service and experience of persons appointed branch managers and district managers; and

(iii) the high level of staff turnover,

that the demands on HFC to implement and maintain effective systems of training and supervision are extremely high.

The Authority was informed that the HFC business system or method of operation was largely modelled upon the Household system in the United States. As such it is designed to be highly dependent upon manuals as the prime guide or instructional tool for branch staff. The dependence of the system on adequate manuals was made especially clear by Mr. Vona on the 16th November, 1988 (6052). It is, therefore, convenient to examine first the adequacy of the manuals which HFC had in use.

In October 1988 the Authority was provided in the form of Exhibit A156 with a complete set of manuals, training guides and instructional memoranda that had been issued by HFC up to that time. There were 22 manuals, 12 training guides and 2 large volumes of loose or unbound memoranda and instructions.

On 28 October the Applicant provided the Authority with a document which listed the manuals and training guides contained in A156 in the categories of current and superseded. According to that document, 20 of the 28 manuals were current and 11 of the 12 training guides were current.

It should also be noted that of the 20 manuals designated as current, 3 of them were publications entitled Duties and Responsibilities of particular positions within HFC, namely Branch Manager, District Manager and Area Manager, respectively. One of the 20 manuals was a general "employment folder" which dealt with more general matters such as ethics, general standards of conduct, duties to retain confidentiality and so forth.

The other current manuals covered topics such as insurances, lending policy, collections, product selling, accounting procedures and real estate lending.

Some of the manuals designated as current appeared to be very old and had been incorporated into the Australian HFC operation from Household of America publications without first eliminating references to expressions or concepts that are simply not applicable in Australia. It was also noted that many of the manuals did not appear to bear dates of issue with the result that where one manual had been superseded by a subsequent manual, it was not obvious that that had occurred.

But those are really minor criticisms. The true state of the manuals as they were in force in October 1988 or shortly thereafter is best illustrated by the evidence of Mr. Vona and Mr. Shafferman. Mr. Vona stated in November 1988 that only three of the existing manuals "I endorse as being current" (6052). He also said "All of the other manuals, texts, have to be reviewed and rewritten. They are manuals that are there but have to be rescrubbed, so to speak" (5964).

Mr. Shafferman on 14 December, 1988 said that "We have only four manuals today that are quite up to date." Mr. Shafferman said this of the manuals - "some of the manuals are not accurate" - "they have not been updated for some time" - "sometimes the manuals contradicted the Credit Act." (7559/60). He described one of the Duties and Responsibilities manuals, namely the Branch Managers, as "a worthless piece of document" (7672). Of the same manual he said that it was "a manual obviously that nobody in their right mind could really follow to any degree of accuracy because it has had the United States in it and a bit of Australia and a bit of Canada and a little bit of everything else" (7758/9).

The Authority regards this as a very serious matter. It is inconceivable that HFC did not appreciate the absolute necessity of its manuals being in proper form. It is also inconceivable that the deficiencies so evident to Mr. Vona and Mr. Shafferman would not have been evident to other senior HFC management for a considerable time. In the Authority's opinion this constituted conscious neglect and is indicative of a lack of intention and willingness on the part of HFC to take the steps obviously necessary to ensure that it could conduct its business efficiently and fairly.

A related difficulty was the failure to follow up critical instructions issued in the form of memoranda with the issue of replacement pages for the relevant manuals. In the Authority's view this problem eventually became insoluble, short of re-issuing manuals, because of the extent to which the manuals had become out of date.

It is clear that from the latter period of 1988 onwards and particularly after the appointment of Mr. Shafferman, HFC has made considerable efforts to remedy the deficiencies in its manuals. By the end of the closing of the evidence in April, a considerable number of the manuals had been rewritten and re-issued, including manuals dealing with credit and Take 5 insurances, collections, lending policy and retail loans. In addition HFC had determined a timetable by which revision and re-issue of all of its manuals, including its Duties and Responsibilities manuals, would be completed. Under that timetable the process is estimated to be completed by end November, 1989.

Training

The first thing that was apparent to the Authority on this topic was the serious inconsistency in the Applicant's statements in the AC2 proposal documents. In paragraph 3.1 of that document , under the heading "Training", the Applicant admitted (or, strictly speaking, the Authority was asked to assume the truth of statements) that -

"(a) HFC has failed to train its staff properly.

(b) HFC has threatened to take possession of goods in circumstances where no security interest existed.

(c) HFC's staff had not been adequately trained as to the legal effect of bankruptcy."

Yet in the same document (see para 3.2) it is claimed that -

"(b) HFC has trained its employees in all aspects of the finance business carried on by HFC including its obligations under the Credit Act 1984 and related legislation."

It is surely ludicrous for a major national finance company to claim that it has trained its staff "in all aspects" of its finance business when it concedes that it has failed to educate them about such fundamental matters as the legal effects of bankruptcy or the most basic aspects of repossessions.

The evidence is that to a considerable extent the training of branch managers was left to district managers. At page 5225 Mr. Wilson told the Authority "It (ie. training) was a big part of the district manager's job" and again at page 5226 "Training was part of the district manager's job, he's responsible for training the people within his group. He has that responsibility."

Yet the evidence of Mr. Vona is to the effect that people become district managers typically after three years as a branch manager and one year as an assistant branch manager. One might wonder where Mr. Wilson expected the district managers to have gained the breadth of knowledge necessary to train their branch managers. Certainly not from the manuals, as we have seen.

The obvious fallacy in that approach to training has at least now been recognised by Mr. Miller whose evidence we will discuss in more detail shortly.

The Authority was provided with what at first sight was an imposing list of training sessions and meetings and the like conducted from 1985 onwards but particularly in 1987 and 1988 . We have serious doubts as to the utility of those training sessions and our reasons for so doing lie in the evidence of Mr. Shafferman and Mr. Miller.

Mr. Shafferman is the person put forward by HFC as a real expert in business control systems and regulatory compliance. On 15 December, 1988 Mr. Shafferman gave evidence about the task of revision of manuals, the relationship between manuals and training and the role of the Business Control department as headed by him. It is plain from Mr. Shafferman's evidence that the existence of proper manuals is an absolute prerequisite to building training programmes.

At page 7759 Mr. Shafferman said "... First of all before you can build the training programmes you have to build the documentation. Now, obviously when you have a lending manual and a collection policy and real estate loan policy and you have a legal policy those policies have to be developed and well defined. Once they're well defined then they're given to the expert training people to build the training programmes." He then went on to say that certain action had already been taken notwithstanding the limitations of the existing manuals. But nonetheless the point to be appreciated is that for the whole of the period from 1985 to December 1988 such training as had been carried out or attempted had suffered from the lack of the necessary basic material, namely adequate manuals.

Mr. Miller's evidence reveals an even more serious deficiency in HFC's past training methodology insofar as it was heavily reliant upon district managers training branch managers. In his first written statement to the Authority (A208), he stated that what HFC needed was people skilled in the art of training and development to teach the trainers in the skills of training, to educate those who will then go in the field in the ways of teaching, as well as in developing the programmes that they will use. He said "What we must avoid is a system in which an inadequate trainer trains a new employee - a system like that just feeds on itself. It is essential that employees are trained from the top down . Another way of saying that is that HFC must be more conscious of "training the trainer". I don't think there has been enough emphasis on that in the past." (A208)

There is also some reason to question the sincerity of HFC's commitment to training, even with flawed materials, prior to late 1988. The

Credit Act brought about important changes to the obligations of financiers and insurance companies relevant to insurance written in connection with regulated loan contracts. We understand from Mr. Hood's evidence that prior to the commencement of the Credit Act regular training sessions had been conducted in Australian capital cities for assistant, branch, district and area managers on insurance matters relevant to HFC.

In the first half of 1985 when the need for these training sessions would have been greatest, they were terminated by Mr. Carter, a Household based employee, then serving as head of HFC operations division in Australia. Mr. Hood said "We can assume ... that Mr. Wilson did not see fit to overturn Wal Carter's decision." Mr. Hood believed that the reason for Mr. Carter's action may have been the stresses and strains of the BFC merger but while that may have been the original "justification", it does not explain the failure to re-instate the training sessions until 1988.

In summary the evidence shows that -

(a) HFC failed to train staff about such basic matters as the legal effects of bankruptcy and rights to repossess;

(b) HFC cancelled its insurance training programmes at a critical time and failed to re-instate those programmes for three years;

(c) HFC's training system lacked the basic materials, principally suitable manuals, which were a necessary prerequisite to effective training; and

(d) HFC lacked persons skilled in the art of training and that its training was heavily reliant on district managers whose own knowledge had been developed under a defective training system.

The Authority finds that for almost the whole of the period since the Credit Act came into operation, HFC's training was seriously deficient and to a large extent the deficiencies were known to and tolerated by HFC.

As to the future, it is clear that there has been, albeit belatedly, recognition by HFC that it must overcome its past deficiencies in training. Considerable efforts are being made to complete the introduction of the new manuals, a specialist training officer and other new personnel have been appointed to provide the specialist training skills that Mr. Miller described as being essential to break the past circle of inadequate trainers training new employees. Other steps have been taken such as the introduction of the new Coburg training school to improve the initial training of assistant branch managers and to relieve branch managers of some of their responsibilities for training branch staff. Overall there now appears to be a commitment by HFC's most senior management to effective training.

In the short term, however, we think it follows both from Mr. Shafferman's and Mr. Miller's evidence that it will be some time before the impact of most of these measures works its way down from the top (as it must do in order to succeed) to where it ultimately matters most, namely to the branch managers and other staff who deal directly with the borrowers.

Supervision

The supervision of HFC's decentralised lending business has been conducted principally by a hierarchy of branch managers supervising other branch staff, district managers supervising branch managers, area managers supervising district managers and the divisional general manager controlling the area managers.

In the examination of HFC's training it has been seen that district managers typically have had three years prior experience as branch managers. It has also been seen that until very recently district managers were largely responsible for training branch managers and the deficiencies in training which resulted from that have been noted. Many of those deficiencies are equally applicable to district managers in their roles as supervisors, since it is scarcely possible to supervise properly unless one has been first trained adequately in all of the responsibilities of the position occupied by the person one is expected to supervise.

A vivid illustration of the damage that flowed from deficiencies in HFC's supervision is the stamp duty problem.

Stamp duty ceased to be payable on mortgages securing obligations under regulated contracts on 10 December, 1985 but HFC overlooked that change in the law. As a result HFC branches continued until late 1987 (when HFC first became aware of the 1985 change of the law) to collect stamp duty on account of goods mortgages which were entered into by way of security under regulated contracts.

Material provided from HFC establishes that between December 1985 and 1987 borrowers were wrongly charged stamp duty on 961 goods mortgages. The material provided by HFC showed that HFC has been able to locate only 829 of those mortgages - 132 have not been located. Of the 829 mortgages that have been found only 250 (30%) had duty stamps affixed and 579 (70%) were not stamped.

The extent of the failure to pay stamp duty on mortgages where the consumers were charged the duty varied considerably between individual branches. Set out hereunder is a table showing, with respect to branches at which more than 20 mortgages have been located, the extent at which duty stamps were affixed.

PART I - BRANCHES WHERE NO MORTGAGES STAMPED

Branch	Number of mortgages located
FOOTSCRAY	47
SPRINGVALE	34
WARRNAMBOOL	31

PART 2 - BRANCHES WHERE SOME MORTGAGES STAMPED

Branch	Number of mortgages located	Number stamped	Percentage of mortgages unstamped
FRANKSTON	121	2	98
RICHMOND	39	2	95
DANDENONG	64	6	91
CORIO	23	3	87
BORONIA	21	3	86
MOONEE PONDS	39	8	79
GLENROY	39	15	62
MOORABBIN	131	51	61
PRESTON	26	17	35
MORWELL	69	52	25
BALLARAT	56	50	11
BENDIGO	42	39	7

At the eight branches where fewer than 20 mortgages were located, the overall picture is certainly no better - at six of those branches none of the mortgages were stamped, at one branch (Ringwood) 1 mortgage out of 16 was stamped and at the remaining branch (Sunshine) 1 mortgage out of 8 was stamped.

From the viewpoint of examining the effectiveness of HFC's supervision, the fact that borrowers were wrongly charged stamp duty in the first place is not relevant.

What is directly relevant is that the failure to buy the duty stamps went undetected by district managers, area managers, internal auditors and anyone else in HFC with some responsibility for supervision. It is important to note that the problem went undetected for the whole of the period of almost two years in which HFC believed the mortgages to be still dutiable. It is also important to note the number of branches involved - almost every branch in Victoria had this problem.

In its final submission the Applicant said -

> "21.8 HFC also accepts that the failure to stamp the documents reveals a defect in its supervisory procedures. One might have expected that a supervisor alert to the point would have discovered some time ago that mortgages were not being stamped. But no-one in HFC was alert to the stamp duty point and consequently it was given no attention."

We fail to see the relevance of "no-one in HFC was alert to the stamp duty point." What we are examining is the very large number of cases in which money was charged to consumers but not spent for the purpose for which it was charged. The questions of stamp duty law have nothing to do with this but rather it is a straightforward issue of supervisors checking whether monies collected have been properly applied and accounted for.

The stamp duty matter also exposed what the Authority regarded as a serious deficiency in HFC's accounting system. Monies appropriated from borrowers on account of stamp duty were credited in HFC branch books to an account called a stamp duty account.

When the Authority asked why HFC's accounting system did not throw up the fact that monies taken on account of stamp duty on goods mortgages were being credited to that account but were not being matched by expenditure for that purpose, Mr. Shaw said that the HFC accounting system did not require a reconciliation of individual branch stamp duty accounts or of the aggregate of stamp duty accounts for all the branches. Any overall surplus or deficit in any particular financial year was merely swept into HFC's profit and loss result.

A similar deficiency occurred in connection with the charging of registration fees charged to borrowers to meet the cost of registering HFC's mortgages over motor cars in the Victorian Vehicles Securities Register. The particular problem here was that HFC branches had misread a memorandum from HFC's company secretary of March 1984 and as a result had charged borrowers $9 in lieu of the correct fee of approximately $6. HFC paid the Road Traffic Authority, which maintains the Vehicles Securities Register, on a monthly basis from its Sydney head office and billed individual branches for the amounts paid on their behalf. Accordingly, branches were generating an excess in their own accounts because they were charging the borrowers $9 but ultimately being billed only approximately $6 for each registration.

Again because the branch accounts in which these fees were recorded were not required to be reconciled the surplus did not come to light and it was only from the CCLS objection that HFC became aware of the overcharging.

During the course of his evidence Mr. Shaw refused to concede that HFC's accounting system was deficient in not requiring reconciliation of these types of accounts. The Authority expressed its concern about Mr. Shaw's view of proper accounting requirements and at the very end of the hearing the Applicant indicated to the Authority that it would make changes in its accounting system so that these types of accounts, where monies were charged to borrowers for third party purposes, would be required to be reconciled.

An entirely different type of failure in HFC's supervision concerned the completion of the budget information section of loan applications. The purpose of the budget information section is to enable HFC to assess whether the intending borrower can afford the repayments under a proposed loan.

The evidence of some of the borrowers suggested that there may have been a practice of branches writing in standard amounts for common items of household expenditure rather than the amounts actually expended by individual borrowers. The consequences of such a practice to sound credit assessment are obvious, as are the risks of over-commitment by borrowers.

However, paragraph 31 of Mr. Wilson's statement to the Authority made the position clear: "I now understand that in recent years the practice developed of using standard amounts for these common items. This was not the way in which the company intended these budgets to be prepared." (A157). In the Authority's opinion this is another telling example of the failure of HFC's supervision processes, since it is obvious that it developed without other persons in HFC's senior management team being aware of it either.

In our view the most telling material came from Mr. Miller. In his statement he said that when he came to Australia in August 1988 he spent some days visiting branch offices in Sydney and other States. He then said "Having done so, I was struck more than anything by the lack of discipline and organisation in the company. Morale was low and staff turnover in the branches was very high ... I was also disappointed to see the untidiness of many of the offices, even of the personnel themselves. Generally I did not have a good feeling about the company. We had let our standards drop." (A208, para 5)

Supervision is one of the important ways in which a company achieves a proper level of discipline and an effective operational organisation. Mr. Vona made it plain at page 6064 that supervision is the key to the successful operation of the company. It seems beyond argument that there had been a major failure in supervision for the company to be in the state which Mr. Miller found it in in August 1988.

As with training, there is clear evidence of a recent recognition by HFC of the necessity to remedy past deficiencies in supervision and steps are being taken to that end.

The new Business Control Department headed by Mr. Shafferman is attending to the production of new manuals and the revision of procedures which will improve the knowledge and understanding of the supervisors of both what they are expected to supervise and how they should achieve effective supervision.

Mr. Vona has explained that irregularities detected by district and area managers are to be more effectively followed through. A reduction in the number of branches over which each district manager is responsible has been put forward as a step which will lead to more effective supervision.

One important new proposal is for the appointment of a Compliance Officer who will receive copies of all relevant reports from supervisors, training officers and auditors. The Compliance Officer will also visit branches and be required to make quarterly reports to the Board of HFC's Audit Committee and to the Corporate Attorney.

There seems no reason to doubt that these measures will in the long term produce a marked improvement in the effectiveness of HFC's supervision but we believe that the improvement will be gradual and take some time to achieve. This is so because district managers remain the prime source of supervision of branch staff and their capacity to supervise is dependent upon their own levels of training and on the availability of up-to-date and adequate manuals.