B. Dissenting Report - Labor Members of the committee

1. Introduction

This inquiry was established by the Government to avoid a Royal Commission into Australia's banking industry. It has been a stage managed circus from its beginnings. The banks had full knowledge of the committee's hearing dates and schedule before the Labor members were appointed to the committee. One Bank CEO had discussed the committee's proceedings with the Treasurer during the same time period:

> Mr THISTLETHWAITE: You mentioned earlier that you had met with the Treasurer about this inquiry and a potential tribunal.
>
> Mr Hartzer: I would not characterise what I said that way.
>
> Mr THISTLETHWAITE: Sorry—about a banking tribunal. You admitted that earlier.
>
> Mr Hartzer: What I said is that I did not meet with the Treasurer to talk about this inquiry.
>
> Mr THISTLETHWAITE: No, but it came up as a topic of discussion in other discussions.
>
> Mr Hartzer: The tribunal was mentioned in passing.
>
> Mr THISTLETHWAITE: Okay. Did those discussions also include as one of the topics avoiding a royal commission?

> Mr Hartzer: Not in detail.
>
> Mr THISTLETHWAITE: In detail? At all?
>
> Mr Hartzer: I do not remember who said what exactly, but in the course of the conversation it would have been noted that there was a proposal to have a royal commission and that the government has instigated this set of meetings.
>
> Mr THISTLETHWAITE: As an alternative.
>
> Mr Hartzer: That would be one way to characterise it. I do not remember it being put that way.

When Labor members were appointed and sought to alter the hearing dates to allow more time for preparation and to provide additional days for questioning, the Coalition members used their voting majority to press ahead with dates pre-determined with the banks.

The banks have ridden roughshod over their customers, the Australian people, and the Turnbull Government is providing cover to protect the banking industry from further scrutiny.

Change in this industry only happens when you shine a light on those with power. Even now CBA is using its power to silence and punish whistleblowers,[1] a claim it denies. There is no authority in Australia that has the ability, resources or capacity to stop them from doing this.

Each of the Banks CEO's began these hearings with an acknowledgement of wrongdoing and a statement of contrition. Yet in place at all of the major banks are the same systems that drove their organisations to engage in unethical behaviour.

The one question the Coalition members' report fails to answer is why Australia should not have a Royal Commission into the banks?

The allocation of 20 minutes of questions for each member once every year is simply not enough. It is clearer now than ever, a broader inquiry is needed. The

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[1] Commonwealth Bank whistleblower Dr Benjamin Koh alleges smear campaign, ABC AM business editor Peter Ryan Posted 28 April 2016, 5:38pm, http://www.abc.net.au/news/2016-04-28/commonwealth-bank-whistleblower-alleges-smear-campaign/7368442

banks argue that a Royal Commission could drag on. This is not an argument against conducting a Royal Commission. This is a statement of fault, a frightened thought for years of misbehaviour. The only way to achieve any form of justice for the victims of the banks, and the only way to truly shine a light on the practices that drive unethical behaviour in the banking industry, is to hold a Royal Commission.

2. Banks have been acting unethically and ripping off customers

Recently, RBA Governor Philip Lowe noted that poor outcomes were a frequent occurrence within the industry:[2]

> Mr THISTLETHWAITE: Would you change anything?
>
> Dr Lowe: APRA is the financial regulator, so it is not the Reserve Bank. And APRA has made many changes to the nature of financial regulation recently—really around capital and liquidity. So I think the finance sector feels like it has gone through a period of very accelerated regulatory change. It is best, probably, to kind of let that settle and see how the system adjusts to it. I sense that you are asking about other types of regulation that really go to the issue of bank culture.
>
> Mr THISTLETHWAITE: Is there anything you want to say about that?
>
> Dr Lowe: I cannot help but agree with you that there have been too many examples of poor outcomes, particularly in the wealth management and insurance industries. That is disappointing to us all.

The head of the Australian Bankers Association, Steven Münchenberg, has said: "there are legitimate issues in the industry" and that "banks accept that in the past they have not always lived up to their own standards, let alone those of their customers."[3]

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2 Hansard, Standing Committee on Economics, 22/09/2016, Reserve Bank of Australia Annual Report 2015

3 http://www.smh.com.au/business/banking-and-finance/labor-calls-for-royal-commission-into-finance-20160407-go1dnr.html

The Apologies

Each of the banks CEO's admitted poor behaviour in their organisations:

Mr Ian Narev, CEO of CBA: "I have said before how sorry I am for the pain we have caused them. I say so again today."

Mr Shayne Elliott, CEO of ANZ: "Each time we fall short, we potentially harm a customer or a member of the community. For that, I apologise. When we fail our customers, it is my job to take accountability, apologise, fix it for the customer as quickly as possible and make the changes required to stop it happening again."

Andrew Thorburn, CEO of NAB: "Our advice was poor and wrong and not right, and I have apologised to them. We will continue to implement our customer response initiative. We believe it is being led well, it is comprehensive, it is thorough and it is has got lots of independence in it."

Mr Brian Hartzer, CEO of Westpac: "Westpac is not perfect. In recent years we have had operational errors, and we apologise for those. We have made some difficult decisions on pricing and at times we have not done a good job of communicating why we have made those decisions."

While the CEO's offer some level of apology there are still many questions that remain unanswered and many victims who have not received justice for the actions of their organisations.

ASIC Banning Orders

All four of the banks have been investigated by ASIC as part of its Wealth Management Project investigating financial advisers. As a result ASIC has issued temporary or permanent banning orders against multiple financial planners at each of the banks.

In the last year (October 2015 to October 2016) CBA Wealth Management Advice licensees have reported 15 advisers to ASIC and terminated 20 advisers.[4]

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[4] Financial Planners – sacked or reported to ASIC, 12 QON

NAB noted that 21 planners were dismissed for conflicts of interest, bad advice and compliance issues in a 2014 management report.[5]

Add to this ASIC has issued temporary or permanent banning orders against at least three ANZ Financial Planners in recent times: Wayne Meadth, Ben Cheung and Craig Miller. As well as banning orders against at least two Westpac Financial Planners Amanda Ritchie and Martin Hodgetts.

Open Advice Review

As well as the CommInsure scandal the CBA has the Open Advice Review Program which was established following the Commonwealth Financial Planning Scandal. CBA undertook to review client files back to 2003 to identify potential misconduct and bad advice:

> Mr Narev : Chairman, I will take a couple of those things specifically. No. 1: I have said before—indeed, I have said before in front of committees in Canberra—we did not act with the requisite speed many years ago, and even in more recent years, on the financial advice matters. We have acknowledged that and I repeat that to the committee today. Again, what I will say is this: as recently as Friday, Promontory, which is a globally recognised independent firm, produced its sixth report on the Open Advice Review Program. Actually, we got updated numbers since then that said that, of the 8,000 people, roughly, who wanted their advice review, 6,000 reviews have now been done. So far we have seen that in nearly 90 per cent of those cases the advice given was proved to be correct, but we paid an additional $11 million in relation to other claims. Bear in mind that a number of years ago, when we first undertook the remediation, we already paid out about $52 million. I want to emphasise one important aspect of this, and then David might speak specifically about the banned advisers. The Open Advice Review Program at the time was put in place not only to provide remediation to customers who did not receive advice of the standard they should have but to actually give confidence to everybody who received advice during that period that the advice they received is good.

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5 Financial Planning matters – sacking of 37 financial planners 22QW

Many clients of Commonwealth Financial Planning remain unhappy regarding their treatment by CBA and the Open Advice Review.[6]

Some clients considered legal action against CBA and their cases remain outstanding.[7]

The RBA Cash Rate

The cash rate and the banks' refusal to pass on full rate cuts to customers have always drawn media attention.

When the Reserve Bank of Australia cut the cash rate in August 2016, CBA did not pass on the full value of the cut. Instead, the bank highlighted that it was passing on about half the cut while raising interest rates on some of its term deposit products.

It has since emerged that CBA has quietly unwound those rate rises again – cutting one-year rates from 3 per cent to 2.4 per cent, and two-year rates from 3.1 per cent to 2.45 per cent. This means the higher rates that CBA promoted as justification for not passing on the full rate cut on a much larger number of mortgages and business loans were in place for just two months.[8]

Westpac claim that the cash rate is not a significant determinant for their interest rates:

> Mr Hartzer: Each bank has a different funding situation. As has been noted in the discussions with the other banks, we do not fund off the cash rate.

ANZ also argue there is no connection between the cash rate and mortgage rates:

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6 http://www.smh.com.au/business/banking-and-finance/97yearold-fights-cba-for-compensation-after-shoddy-advice-from-dodgy-don-nguyen-20160902-gr7fut.html

7 http://www.smh.com.au/business/banking-and-finance/victims-of-commonwealth-bank-financial-planning-scandal-and-consumer-group-choice-question-schemes-independence-and-reach-20150120-12uncb.html

8 http://www.theaustralian.com.au/business/financial-services/commonwealth-bank-unwinds-term-deposit-rate-rises/news-story/e20b7c3c6e84155a686dd196db9f75bb

> Mr Elliott: When you say 'delaying', as I said, there is no direct link between the RBA cash rate and what we charge customers.

On Wednesday 19 October 2016, ASIC chairman Greg Medcraft confirmed that the main determinant of bank mortgage interest rates is the RBA official cash rate.

Mr Medcraft, himself a former banker, tabled a briefing note showing the banks funding costs "completely tracked" the cash rate, which he said reflected the fact that "60 per cent or more of their funding comes from deposits, which are based on the cash rate."[9]

This evidence from Mr. Medcraft shows the big banks' justification for not passing on a greater proportion of full RBA rate cuts to customers is weak. The banks have been short-changing Australian mortgage holders and making additional profits on the back of it.

CommInsure

The committee asked questions about the CommInsure scandal. Because of time constraints these questions barely scratched the surface of the issues at CBA's insurance arm.

Various media reports note that following whistle-blower revelations, CommInsure had systematically denied legitimate life insurance claims and relied on outdated medical definitions to do so. Commonwealth Bank committed to amend these definitions and review historic claims going back to at least 2014.

Dr Benjamin Koh, CommInsure's former chief medical officer detailed in a Four Corners report in March of 2016 that:

> Insurers pressured doctors to change medical opinions in order to deny payouts, that medical files went missing and outdated medical definitions were used to deny claims.
>
> Dr Koh said he repeatedly tried to raise his concerns with senior managers at CommInsure, and even went to the insurer's board, but he was dismissed in

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9 Mr Greg Medcraft, Economics Legislation Committee, 19/10/2016, Estimates, TREASURY PORTFOLIO, Australian Securities and Investments Commission

> August 2015, after less than two years in the role, for breaching the company's IT policy by emailing records to a personal account.
>
> Koh said he did it because files were going missing and he'd tried repeatedly and unsuccessfully to have the matter investigated before taking it to the board.
>
> He told journalist Adele Ferguson that legitimate claims were denied in a systematic fashion in order to boost CommInsure's profitability, including pressuring doctors to change their reports.[10]

Another shocking example is the case of Mr Mathew Attwater, who was medically terminated from his position at CBA after suffering from mental health issues. Yet CBA's own insurance arm, CommInsure, assessed him as capable of returning to work and denied his claim on that basis.

On the day before the committee hearings began the ABC 7:30 program uncovered the shocking case of Peta Ouutzen who was denied a life insurance claim by Comminsure:

> Mr CONROY: ….I want to go back to CommInsure for a second, in particular the tragic case of Peta Outzen that was explored last night on 7.30. The response quoted in the story yesterday was that the Commonwealth Bank, in declaring that Ms Outzen's death was a suicide in direct contradiction of a death certificate stating accidental overdose and a coroner's finding stating accidental overdose, simply made a mistake. Is that Commonwealth's position?
>
> Mr Narev : In the case of Ms Outzen, yes, that is correct. We are aware of the circumstances, and I might say they were tragic circumstances. The nature of the circumstances gave rise to an initial view from the claims manager that this had been a suicide, which obviously was incorrect. The coroner found that it was death caused by accidental taking of the drugs. As it happens, that in itself is also excluded from the policy, but having looked at the circumstances behind the way this determination was made I do not think it is a good example of dealing well with a customer, and, to come back to what I said

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10 http://www.businessinsider.com.au/the-cba-now-faces-new-investigations-over-its-insurance-arm-2016-3

> before in response to Mr Thistlethwaite and the chairman, the bank needs to be doing a better job at those sorts of circumstances.
>
> Mr CONROY: How can the bank maintain it was simply a mistake when the claims assessor, post their initial claim, clearly ignored the coroner's finding and the death certificate? That is not a mistake. A mistake is losing someone's paperwork. It is not a mistake to say, as a claims assessor, 'I know more than the coroner.'
>
> Mr Narev : I will take this aspect on notice, but I have not yet been made aware that any claims manager wilfully ignored a determination of a coroner. What I have been made aware of to date is that, based on the circumstances of the case, the claims manager made a conclusion which was mistaken and did not take into account other factors. There actually is a process to make sure that if that happens it receives additional oversight, which did not happen. Regardless of whether or not the circumstances of what was a tragic death would or would not have been covered, I come back to saying that that is a process which was not a customer-friendly process.

CBA's focus is clearly not on every individual customer. These cases are all too common. Only a broader inquiry with the powers of a Royal Commission will be able to fully investigate these matters and the many who don't receive media attention.

This year ASIC conducted a review of the life insurance market. The report, released in October, noted that there were issues of concern in relation to higher claims denial rates and claims handling procedures associated with particular types of policies. For instance the rates of declined claims were highest for TPD cover, with an average declined claim rate of 16 per cent, and TPD denial rates being as high as 37 per cent.[11]

2016 ASIC Matters

Throughout the course of the year ASIC has investigated a range of matters resulting in fines and repayments to customers. The Labor members of the

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[11] http://asic.gov.au/about-asic/media-centre/find-a-media-release/2016-releases/16-347mr-asic-issues-industry-review-of-life-insurance-claims/

committee wish to highlight some of the enforcement functions of ASIC and the size and scope of the compliance failures that are all too common at the big banks.

CBA Infringement Notices

In September 2015 it was announced that CBA had paid four infringement notices worth $180,000 in relation to breaches of responsible lending laws when providing overdraft facilities.

As a result of the error, between July 2011 and September 2015, CBA failed to take into consideration the declared housing and living expenses of some customers. CBA informed ASIC that between July 2011 and September 2015, as a result of the error, CBA approved: 9,577 people for overdrafts which would have otherwise been declined; and 1,152 people for higher overdraft limits than would have otherwise been provided. CBA has written off $2.5 million in loan balances as a result of this error.[12]

ANZ Transaction fee refunds

In September 2016 ASIC announced that ANZ had refunded $29 million to hundreds of thousands of accounts after failing to disclose certain periodical payment fees.[13]

Westpac Transaction fee refunds

In September 2016 ASIC announced that Westpac had refunded $9.2 million in bank fees that should have been waived in one case, and $20 million in credit card foreign transaction fees in another.[14]

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12 http://asic.gov.au/about-asic/media-centre/find-a-media-release/2016-releases/16-308mr-cba-pays-180-000-in-penalties-and-will-write-off-25-million-in-loan-balances/

13 http://asic.gov.au/about-asic/media-centre/find-a-media-release/2016-releases/16-291mr-anz-to-refund-nearly-29-million-to-more-than-390-000-accounts-as-a-result-of-unclear-fee-disclosures/

14 http://asic.gov.au/about-asic/media-centre/find-a-media-release/2016-releases/16-304mr-westpac-refunds-92-million-after-failing-to-waive-bank-account-fees-for-eligible-customers/

CBA financial advice refunds

In October 2016, ASIC announced CBA would repay $105 million to customers who had been charged for financial advice that was never provided.[15]

3. The banks' structure and culture promotes bad customer outcomes

Each of the banks gave evidence to the committee that they have remuneration structures and targets that incentivise cross selling of bank products to customers, particularly insurance and credit products, even though they may not be in the customer's best interests.

Sales targets

Sales targets are included for frontline staff. Frontline staff can include – branch managers, customer service managers, customers service representatives etc. Sales targets are part of a 'balanced scorecard' that is used to determine performance. Sales targets typically make up to 30 per cent of the balanced scorecard metric for frontline staff. Balanced scorecards include metrics measuring an individual employee's performance.

Through this metric staff are required to meet a rate of at least 100 per cent is the sales target. The only metric that is discussed everyday by managers is the sales target. Failure to reach the required sales target will result in the implementation of performance improvement mechanisms and may result in the removal of underperforming staff from the business.

Targets are employed at every level of the business and are the key driver of poor behaviour.

Sales are also measured and compared to co-workers and other branches, regions and business units. This process is compiled into functional ranking systems known generally as league tables.

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15 ASIC Report 499, Financial advice: Fees for no service October 2016, Page 20, http://download.asic.gov.au/media/4054607/rep499-published-27-october-2016.pdf

Culture

At the centre of the problem is a cultural issue within the sector, that is geared towards selling products to customers. There is little to no understanding of the best interests of the customer. Drivers such as performance targets and bonus payments exist to push staff to make sales and drive profits for the banks. Customer need is a secondary issue. The bank CEO's will argue that customer needs are taken into account by employees because they utilise a balanced scorecard for all employees' performance management.

However this balanced scorecard still means that if you're an employee that is failing to reach your sales goals you may be managed out of the business. An employee may face the prospect of a choice between selling bad or unsuitable products and losing their job:

> Mr THISTLETHWAITE: So, if they are struggling and they are not meeting their targets, does that include perhaps using that information to put them on a performance improvement program?
>
> Mr Thorburn: The performance improvement program is something that comes quite a way down the process, and what a leader should do is look at the balance scorecard. How is the individual doing on customer, risk, financial, and leadership and people—working with colleagues? And then they should be sitting down with them regularly…
>
> Mr THISTLETHWAITE: And that performance improvement program can include warnings about behaviour and ultimately dismissal, can't it, if they do not improve?
>
> Mr Thorburn: Yes, that is true, but I think all businesses in Australia would have that sort of discipline, and that comes at the end of a long process of coaching and counselling and helping people to get better.

4. The current regulatory framework is inadequate to prevent poor customer outcomes and provide redress for victims

The heads of ASIC, APRA and the ACCC admitted that they do not have the legislative foundation or the funding and resources to properly regulate and scrutinise the banking industry particularly in respect of their culture, behaviour and competition.

The Australian Reported in March 2015 that ASIC chairman Greg Medcraft was quoted as saying "It's frankly quite clear that we're very thinly resourced across the board" following budget cuts in the 2014-15 and 2015-16 Budgets.[16]

ACCC can't look at competition on its own initiative

The ACCC has a range of limitations including an inability to begin self-initiated market studies and a lack of resources for dealing with investigations. The Chairman, Mr Rod Sims detailed his frustrations when appearing before the committee on 14 October 2016:

> Mr THISTLETHWAITE: the UK's Competition and Markets Authority has the power to conduct extensive market reports of its own volition. Is this something you think the government should consider in Australia in terms of your powers, rather than having it done through referrals or compliance work?
>
> Mr Sims: I think it would be a good idea, to be honest about it. The United Kingdom regulator is probably more advanced than in most other countries in its use of market studies. Certainly we had them out here trying to convince Ian Harper that it was a good idea, and we did not succeed.
>
> At the moment we can do market studies under one of two headings. One is that we can self-initiate, in which case we can get information only voluntarily. The only way we can get information using our compulsory powers in a market study is if the government refers the matter to us, as they have done with petrol, as they have done in the east coast gas market and as they are now going to do in dairy. Our beef market study is one that relies on voluntary information and clearly we have had limitations in the information we have been able to get in terms of understanding where the money is made in the value chain. You are not going to get that information voluntarily. That is such a crucial ingredient in many of these sorts of studies. Firstly, I think having that sort of power would be helpful. I emphasise again, though, that with our resources we would still be doing one or two a year, and that is roughly what the UK does as well. They are able to do only one or two a year.

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16 http://www.theaustralian.com.au/business/latest/asic-slams-penalties-budget-cuts/news-story/c37addc981d397c9de4bb24e4db86102

> Mr THISTLETHWAITE: That was going to be my next question: do you think it would require additional resources?
>
> Mr Sims: Just to go back to the chairman's original line of questioning, it depends on the government and how much they want us to do. I think personally if we were to get more resources I could use it most in the investigation area on breaches of the consumer law and breaches of the competition law, because it is frustrating that we do see breaches of the law that we cannot deal with or we are trying very hard to deal with it but because we have so many priorities things take longer than they should. So, it is a serious problem for us.

A lack of Executive Accountability

A key community concern in relation to bad behaviour by banks has been the lack of accountability of senior executives and directors for failings within banks:

> Mr CONROY: But some of these cases are over three years old. The media stories that broke this are somewhat old now. I appreciate you have got a formal process to look at the broader issues, but you have already acknowledged that the bank did the wrong thing in some of these cases. Are you not able to tell me whether anyone suffered any consequences—any disciplinary action—over any of these matters?
>
> Mr Narev : There is a range of disciplinary action and it is all taken into account when we get the full facts and circumstances.
>
> Mr CONROY: Is that a yes or a no, Mr Narev? Has anyone been disciplined?
>
> Mr Narev : At this stage, there are certainly individuals who we know enough about that we have had discussions with and who have had some consequences relating to remuneration. At this stage, we have not had individuals terminated as a result of this, because we have not seen the need to do that. If we do, we have got very clear principles on it. We will make sure that happens.

The United Kingdom has recently introduced reforms – the Senior Managers Regime – that create a statutory duty of responsibility that requires senior managers to take reasonable steps to prevent regulatory breaches from occurring, or continuing to occur, in their area of responsibility. This is leading many senior managers to reassess the appropriateness of the scope of their responsibilities and to review their approach to controlling and managing these areas of responsibility.

The UK Prudential Regulation Authority and UK Financial Conduct Authority new rules establish a framework to:

- create focused accountability on individual senior executives within banks;
- encourage such senior executives to take greater individual responsibility for their actions; and
- make it easier for banks and regulators to hold individuals to account.

Key elements of this framework include:

- identification of Senior Management Functions, being board director and senior executive management positions, which require pre-approval by regulators;
- requirement to allocate prescribed responsibilities among the Senior Management Functions;
- creation of key governance arrangements in a Management Responsibility Map with Statements of Responsibility for each Senior Management Function;
- requires banks to annually certify the fitness and propriety of key employees; and
- imposes codes of conduct on senior managers and all other employees.[17]

The potential for the introduction of a statutory responsibilities and transparency as to which senior managers are responsible for certain activities within banks in Australia was raised by the committee with bank CEOs, ASIC and APRA.

Both ANZ chief executive Shayne Elliott and Westpac chief executive Brian Hartzer expressed a level of support for a strengthened accountability regime for senior executives and managers, similar to Senior Managers Regime recently introduced by the UK Financial Conduct Authority:

> Mr KEOGH: The UK Financial Conduct Authority has brought in this strengthening accountability framework. I am sure as an international bank, as

[17] Deloitte EMEA Centre for Regulatory Strategy. Senior Managers Regime: individual accountability and reasonable steps. 2016.

you are, you would be aware of this—their process of having rules on individual accountability, the senior managers' regime and the remuneration code. Do you see some merit in that approach?

Mr Elliott: Yes.

Mr KEOGH: Is that something you think should be considered here?

Mr Elliott: I think that that tightens accountability for senior executives and is something that should be looked at. That is only reasonable.

Mr KEOGH: I think the key thing here about what I am asking you though is—we are not saying do not take risk and we are not saying do not innovate—that where people take that risk, or the bank as an organisation decides to take that risk, with what is effectively other people's money by advising them to put it into certain products or to buy certain products from the bank, that the advisers are responsible for it, but also that their senior management are responsible for the culture that surrounds that and for the systems that are in place and the training that has been put in place, so where that advice is given and risks may be advised to be taken, that there is a chain of accountability and responsibility for that.

Mr Hartzer: And I support than wholeheartedly.

Both the ASIC and APRA Chairmen, Mr Medcraft, and Mr Byres, also expressed favour to the concept:

Mr KEOGH: Okay. Ms Banks mentioned earlier—probably in quite a different context—the UK senior managers regime. I asked all of the banks about that during the course of the hearings we had last week. I would just be interested to know: in terms of being able to add to the arsenal that ASIC has at its disposal, does ASIC see that form of regulatory regime—I am not talking about the absolute specifics of what the FCA have introduced in the UK but, if you like, a statutory or regulated requirement on senior management personnel within a financial service, banks or otherwise, to take responsibility for their areas of responsibility, and the requirement for a financial service to identify the people who are responsible—as a useful way forward for the regulatory regime in Australia?

Mr Medcraft: Clearly that is a matter for government, but the—

Mr KEOGH: Well, I am asking you as the regulator.

> Mr Medcraft: No, that is okay. That is just a preface. But I have looked very closely at that because, as you know, I was headhunted to run FCA this year. With the senior manager regime, first of all, I think personal accountability is really important, and I think we have seen what happened with Wells Fargo this week.
>
> Mr KEOGH: Yes.
>
> Mr Medcraf: So I think that is important. I am not really philosophically at a view of trying to micromanage companies. I think they are responsible, they should be held responsible and they should make people responsible, clearly, and I think they want to. With the senior manager regime to date, they changed the onus. It seems to be working well, but again I think it is premature to judge whether it is a success or not. But the results to date are quite positive.

While the Chair's report claims the committee is "committed to increasing executive accountability in the financial sector", the recommendation to address this – public reporting of AFSL breaches, is flawed and would be ultimately ineffective at addressing the need to make executives accountable.

The Chair's report notes the introduction of the Senior Managers Regime and that its progress will be monitored but like much of the report, this is a meaningless statement.

The intention of the UK regime could be replicated in Australia, but differences in the financial systems of the two countries and their regulatory structures mean the regime itself could not simply be copied.

The complexities of introducing such a regime need to be thoroughly investigated in an Australian context. The only vehicle to run such an investigation is a Royal Commission.

5. The Government Members' Report Recommendations

Recommendation 1

The recommendation for the creation of a tribunal to replace existing EDRs is essentially half formed and pushes responsibility for its development to yet another government inquiry.

Indeed, the genesis of this majority recommendation appears to have been prior discussions between the Prime Minister, Treasurer and bank CEOs:

> Mr KEOGH: Mr Hartzer, have you had any conversations with anyone in the government about this idea of setting up a tribunal to deal with customer complaints prior to today?
>
> Mr Hartzer : I think I was at one meeting a couple of months ago where the idea was mentioned. It was certainly not an extensive conversation.
>
> Mr KEOGH: Who was that with?
>
> Mr Hartzer : I would guess that it might have been the Treasurer.
>
> Mr KEOGH: It might have been?
>
> Mr Hartzer : As I say, it was several months ago. I would say I have probably had a very short conversation with the Treasurer about it, but I could not swear to that. My memory is a bit hazy.
>
> Mr KEOGH: What sort of suggestion about the tribunal was put to you in that conversation?
>
> Mr Hartzer : There were no details. Actually, I do remember—sorry. I know where this came up. There was a meeting with representatives of the banks. It was in the press. It was April, May—I cannot remember exactly— and there was a discussion and one of the issues that was raised was about resolution of complaints and whether that whole thing needed to be looked at. We agreed, as I said in my earlier response, that it is important that there is an appeal process. If there is a gap between the different institutions then it is reasonable to look at that.
>
> Mr KEOGH: So the idea of a tribunal was raised at that meeting. The Treasurer was present at that meeting and you said representatives of other banks were also present at the discussion?
>
> Mr Hartzer : Yes. It was in the press at the time that there was a discussion between the Prime Minister and the Treasurer and representatives of the banks. I believe that that was one of the items that came up in that discussion.
>
> Mr KEOGH: What was the view that you and your bank expressed about that idea at the time?

> Mr Hartzer : It would have been what I said in my response earlier, which is that we are very happy with the idea that the architecture of appeal, to use my own word for it, should be looked at. If there is an issue of people falling between the stools or having limits that are too low, we are very supportive of that being looked at.
>
> Mr KEOGH: Initially your response was you thought that that was a few months ago. You then said there was a discussion in around April or May. Has this issue been raised with you subsequent to April and May but before today?
>
> Mr Hartzer : I could not tell you definitively. What I can absolutely say is I have never had a long conversation about the topic of a tribunal. I am not really even aware of what the details are of what is recommended. My immediate response is that I am very happy for that issue to be looked at—whether there is a gap in what sorts of customers are eligible to go to a review process. I accept that there might be places where there is overlap or gaps in coverage and it seems perfectly sensible to us that that would be looked at. As to whether the answer to that is a tribunal, a new institution, a merging of some institutions or a reframing, I am completely agnostic.
>
> Mr KEOGH: But you cannot rule out that there has been a conversation more recently where that may have been raised in some degree of detail that you cannot properly recall at this point?
>
> Mr Hartzer : Correct.

The Labor committee members note that a range of sector stakeholders and consumer advocates have raised very strong concerns about the tribunal approach.

A coalition of consumer advocates, made up of Care Inc, Caxton Legal Centre, Consumer Action Law Centre, Consumers' Federation of Australia, Financial Counselling Australia, Financial Rights Legal Centre (among others) went so far as to write to the Prime Minister stating that they are 'very concerned that a new tribunal may in fact deliver worse outcomes for consumers'.[18]

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[18] http://www.afr.com/business/banking-and-finance/financial-services/credit-ombudsman-says-new-bank-tribunal-would-be-a-huge-mistake-20161010-grzco8

Furthermore, the current Credit Industry Ombudsman, Raj Venga, stated publicly that a new banking tribunal would be a huge mistake.[19]

These stakeholder concerns are significant and should not be brushed aside by the committee or the Government without addressing their substance.

On the face of it, the tribunal model proposed by the majority report also falls short in several significant aspects of the law. For example, the detail provided in the majority report, appears to give rise to conflicts in structure that may make the creation of the body envisaged by the majority run into issues in respect of Chapter III of the Australian Constitution.

For instance, the proposed structure of a board and members gives the appearance of a the tribunal being a private body, such as the FOS, where members who volunteer to be members make a contractual agreement to be bound by FOS determinations.

However, the proposal also envisages compulsory membership and that decisions are binding by force of statute. This statutory compulsion to participate in tribunal proceedings and comply with decisions begins to take on judicial like qualities, similar to the SCT, which is a statutory body. Further, the nature of the decisions that such a tribunal would be making may well require that the body be invested with full judicial power. In either event, it would be improper for such body to be a private member based organisation, but rather a judicial one.

These conflicts require resolution in determining:

- who will preside over such a tribunal;
- the jurisdictional limits that apply;
- the scope of matters that may be dealt with by the tribunal;
- what procedures would apply; and
- what avenues of appeal may or may not exist.

There is a further issue created by the suggestion that lawyers not be permitted to be involved in respect of the tribunal. Like many well intentioned suggestions of

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19 http://consumeraction.org.au/edr-review/

this nature by committees and other bodies before it, this fails to account for the involvement in advising banks in proceedings of an army of internal lawyers at the disposal of each bank. Merely preventing lawyers appearing in a tribunal will not create a level playing field. Indeed, funding for legal assistance for customers would be of greater assistance in levelling the playing field, as well as ensuring the adoption of customer friendly procedures.

- As can be seen, the committee's recommendation opens more questions than it addresses and is a further demonstration of the requirement for a detailed and in-depth look not just at the sins of the past but also how they can be remedied in the future. An inquiry, such as the Ramsay Review, into EDRs in isolation to all other issues will be insufficient to properly address these concerns. These matters can only be addressed holistically through a Royal Commission.

Recommendation 2

There are a number of practical flaws with this recommendation:

The Chair's report has not made it clear how this would work in practice without compromising larger investigations or examination of misconduct.

While there is a clear need for more and better public reporting of breaches of corporate law or licensing requirements within financial institutions, and for greater accountability by senior executives where these occur, the model proposed in this report displays the same rushed and ill-thought-through approach as the Turnbull Government has demonstrated throughout this entire inquiry.

Recommendation 3

Recommendation 3 proposes the creation of a new team within the ACCC, without making any recommendation for additional funding to the ACCC to fund this work. In October the committee heard from the Chairman of the ACCC about its market studies program and that the ACCC is limited in the number and scope of market studies that it conducts to analyse levels of competition in a particular market space due to funding constraints.

This recommendation appears to effectively create a team to run regular market studies of the banking sector. It would appear more effective if the ACCC was

properly funded by Government to run market studies and directed by Government to conduct market studies into the banking sector. However, given the size and scope of such a study, the ACCC would be greatly assisted if an initial examination of competition issues in the banking sector was conducted through resources available to a Royal Commission.[20]

Recommendation 6

The proposal for the Council of Financial Regulators to review licensing requirements for ADIs and for a 'two phase' licensing process appears superfluous as the majority report does not consider evidence provided to the committee in a separate hearing by Mr Byres, Chairperson of the Australian Prudential Regulation Authority:

> Mr Byres: The $50 million is not actually a prevention to be an ADI. It is a threshold below which you are not able to use the word 'bank' in your business name. But we have a large number of ADIs that operate below the $50 million—typically credit unions and building societies— but there are some other organisations that choose not to have the word 'bank' in their name. They have an ADI authority, they meet the prudential requirements and they can do banking activity without the $50 million.
>
> CHAIR: Yes, but, if you are proposing to set up a bank, you would be required to have the $50 million prior to lodging the application with you?
>
> Mr Byres: The second thing is, no. The way our application process works is that when it comes to ADI licences we actually have what I would call a fairly iterative process. We work with applicants. The only thing you need to pay up-front is an $80,000 application fee, which is a cost recovery measure. It covers our costs for processing the application. You have to have the $50 million, certainly, before we sign the licence over to you, but it is not the case that you have to show a bank statement when you first roll up at APRA. Those are my two clarifications on the $50 million.

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20 Hansard, Standing Committee on Economics, 14/10/2016, Australian Competition and Consumer Commission annual report 2015

Recommendation 7

As the majority report notes at table 3.1, all AFSL holders are required to "have adequate risk management systems" and to not do so would amount to a significant breach, that such AFSL holder would have to report to ASIC.

Furthermore, APRA Cross-industry prudential standard (CPS) 220 – Risk Management requires an APRA-regulated institution to have systems for identifying, measuring, evaluating, monitoring, reporting, and controlling or mitigating material risks that may affect its ability, or the ability of the group it heads, to meet its obligations to depositors and/or policyholders. These systems, together with the structures, policies, processes and people supporting them, comprise an institution's risk management framework.

In addition, APS310 (ADI Prudential Standard 310 – Audit and Related matters), APRA can require an ADI (i.e. a bank) to audit its risk management systems. As such, it would be more appropriate to recommend that APRA direct banks to audit their risk management systems, with such audit report to be provided to APRA. However, the concern in relation to risk management system implementation and compliance discloses a larger concern, regarding whether APRA and ASIC are properly enforcing their regulatory domains, given that ineffective risk management would result in serious breaches of AFSL conditions and prudential standards. It is such concerns that support the need for a broader inquiry in the nature of a Royal Commission.

Recommendation 9

The Labor members agree that additional transparency measures via public reporting are much needed for the wealth management industry. However the recommendation as it stands may be unworkable. A properly formulated recommendation of this nature would need to focus on breaches that relate to client files or work performed on behalf of or in relation to a client.

Interbank ATM fees

An issue of continual frustration to many banking customers is the level of fee charged by a bank for using its ATM when a customer of another bank.

During the course of the committee hearings NAB and Westpac were asked to provide information as to the marginal cost to banks for allowing customers of another bank to access the bank's ATM network. All banks were requested to provide more detailed information in writing after the hearings.

During the course of the hearings, Westpac informed the committee that such marginal cost was approximately 20 cents. Given that the fee charged to non-bank customers for using an ATM is approximately $2.00 or more, this fee appeared to represent a mark-up of approximately 900 per cent.

NAB provided information on a public basis that such marginal cost was approximately 62 cents, showing a margin of at least 222 per cent.

It is disappointing therefore that in responding to these questions in writing CBA and ANZ only provided information on the basis that it was kept confidential.

While noting that the cost base for providing their ATM networks is one that not only increases over time but also increases on a per transaction basis as the number of ATM transactions continues to decline, this is effectively a cost that the banks would meet in order to service their own customers in any event. It is therefore apparent that the fees charged to non-bank customers are not related to the additional cost of servicing those customers but rather a way of mitigating the overall costs of the banks' ATM network. The existence of non-bank ATMs which also charge a fee for ATM use to all customers, appear to have set a market price for such a service which has allowed banks to charge a similar fee, disconnected from the cost base.

While the pricing of such services is a matter for each bank, the lack of transparency about the calculation of this charge has increased customer scepticism with banks.

Issues relating the responses to questions in writing:

Members of the committee sought further information following the 20 minutes of questioning allowed under the flawed structure of the inquiry. Some questions were then taken on notice or in writing.

Some of these questions in writing were answered fully and properly. For example NAB answered one question from the Deputy Chair on Bank staff performance

measures and incentives and balanced scorecards with significant attention to detail and seven annexures.

However some of these questions were answered poorly or need follow up to clarify their meaning and the committees understanding of them. This cannot happen until the CEO's appear at next year's hearings, if at all.

26QW - Banks staff performance measures and incentives

Despite claiming not to use leaderboards CBA acknowledged providing data to managers for coaching and performance purposes. However no detail was provided as to how this data is used by managers with their staff or how widely available this data is to other employees.

This answer raises further questions which cannot be asked under the current restrictions relating to this inquiry.

27QW - Accountability - code of conduct breaches

In response to this question CBA tabled the number of investigations undertaken into suspected beaches of their Statement of Professional Practice and then a further table outlining the number of employees no longer with the group.

No senior executives were investigated despite the fact that they have benefitted through bonus payments linked to financial outcomes derived from the alleged wrong doing of staff reporting to them.

Again, this answer raises further questions that cannot be asked until the banks appear before the committee again.

27QW - Bank staff performance measures and incentives

In response to this question regarding bank staff performance measures and incentives NAB provided an average figure. The use of an average for all NAB employees is misleading. By providing an average figure it is not possible to understand the at-risk component of the employees at different levels within the bank. For instance a comparison between a teller and the CEO might show that decision makers have around 60 per cent of their remuneration at risk while tellers may have less than 5 per cent at risk.

40QW - Bank staff performance measures and incentives

In response to a request to provide a copy of a balanced scorecard Westpac chose not to provide this information. Westpac's failure to provide the scorecard requested raises questions as to how balanced the scorecards actually are.

6. The House of Representatives Economics Committee is no substitute for a Royal Commission.

This inquiry exists as a mechanism to avoid further scrutiny through a broader inquiry. Each member of the committee had around 20 minutes to question the Bank CEO's over 3 days. The Labor members of the committee all ran out of time.

The one question the Coalition members report fails to answer is why Australia should not have a Royal Commission into the banks?

The process the Government undertook to set up this inquiry was flawed and put the committee at a disadvantage. The inquiry was announced and banks provided with dates prior to committee membership even being finalised, and committee members were only given a few short weeks to prepare.

This inquiry process effectively locks the public into a process of needing to wait 6 months for another hearing to seek more information. This is unreasonable and further proof the government is shielding the banks from scrutiny.

There are thousands of documents provided by the banks that are sealed – these secret documents deserve greater scrutiny. These documents cannot even be referenced in this report.

7. Labor Members' Recommendation

This inquiry process was initiated by the Turnbull Government as a distraction from the need for a banking Royal Commission.

Having achieved nothing but to emphasise the inadequacy of this approach for holding Australia's major banks to account and identify the significant scope of concerning malpractice which remains to be examined, Labor committee members recommend the Government immediately move to establish a Royal Commission into the Australian banking and financial services industry.

Such a Royal Commission into the financial services industry should examine issues such as:

- how widespread instances of illegal and unethical behaviour are within Australia's financial services industry;
- how Australia's financial services institutions treat their duty of care to their customers;
- how the culture, ethical standards and business structures of Australian financial services institutions affect the behaviour of these institutions;
- whether Australia's regulators are really equipped to identify and prevent illegal and unethical behaviour;
- comparable international experience with similar financial services industry misconduct and best practice responses to those incidents; and
- other events as may come to light in the course of investigating the above.

This Royal Commission should be initiated without delay to ensure justice for victims of banking misconduct and restore public confidence in the Australian banking sector which has been badly damaged by the string of scandals in recent years.

Signed:

Hon Matt Thistlethwaite MP

Deputy Chair

Mr Matt Keogh MP

Ms Madeleine King MP