

Additional comments—Australian Greens member of the committee

As stated in the Chair's report, the fourth round of hearings of the review of the four major banks has focused on the banks' response to the Royal Commission's Interim Report. This is appropriate. The point of a Royal Commission was to be able to undertake an exhaustive inquiry of the industry in a way that parliamentary committees have neither the time nor resources to do.

However, the Greens are concerned that there is a gulf developing between the rhetoric about reforming the financial sector, and the commitment to actually reforming the financial sector. Bank bashing is not an end unto itself. Policy reform is the goal.

The Chair's report fails to make any recommendations for reform, despite all of the evidence considered during the fourth round of hearings. While some members of the committee might be relying on the Royal Commission's Final Report to provide definitive guidance, this does not and should not preclude parliamentarians from putting recommendations, particularly through the committee process. That is what we are elected to do.

The best way to ensure victims of misconduct by the banks are not forgotten is to undertake reform to stop it happening again.

The Royal Commission is laying bare many of the problems with Australia's banking and financial system. Fraud, bribery, lying and dishonesty have been an all too common in stories of misconduct within once venerable institutions.

This conduct has been driven by the pursuit of profit above customer interest. But it is not just a problem of individuals and culture. It is a failure of structure and a failure of regulation. The banking system has become too complicated and too interwoven to properly serve the interests of consumers or the economy.

Overwhelmingly, financial complexity has been of more benefit to the finance industry than it has been to consumers or society.[1] The GFC showed that no-one truly comprehends the level of interconnectedness between complex financial products and everyday life. Risk is everywhere and it's everyone's problem, whether you signed up for it or not.

The Greens want to overhaul the structure of banking and finance and the regulatory and governance system so that it serves people rather than serving itself.

We are now one of the most heavily financialised economies in the world.[2] The banking and finance sector accounts for 9% of GDP and is the largest single sector

in the economy.[3] An oversized banking and finance sector can even constrain the real economy.[4]

The growth in the size and scope of banking has not been matched by an increase in financial stability or in the distribution of economic prosperity. In fact, both risk and economic inequality have increased.

Reordering the institutions

At the core of the problem with the current system of banking and finance is the rise of universal banking, where everything from saving accounts to derivatives are created and sold under the one roof.

Most people only ever want or need basic banking services at a fair price. Yet universal banking has allowed banks to prey upon customers' trust and loyalty to them. This is because universal banking creates an inherent conflict of interest within institutions. When a bank can make more profit by selling more products to their customers, then history has shown the bank's interest will prevail over the customer's interests.[5]

In Australia, the big-four banks acquired and developed wealth management businesses that both create financial products as well as sell them through financial planners and superannuation funds. Within these vertically integrated institutions, staff have been routinely encouraged to cross-sell a bank's products, regardless of the needs of the person walking into their local branch.

The deregulation that created universal banking also failed to ensure market discipline or protection against systemic risk through market concentration. These mergers brought our banks enormous political power; they are 'too-big-to-fail' and riddled with moral hazard. They know governments will get them out of a tight spot, so they are more willing to take risks, which only increases the likelihood of a financial crisis.

In Australia, too-big-to-fail has helped the whole economy become hostage to an inflated property market. The banks have pushed up property prices by getting loose with lending standards and writing ever bigger loans. This means that the next person looking to buy a house has had to borrow even more money to stay in the market, which in turn means greater bank profitability.

Australia's household debt is now at world-record levels.[6] The big-four dominate with an almost identical business model of mortgage dependency.[7] ACCC Chair, Rod Sims, recently said that the major banks' interest rate behaviour "resembles synchronised swimming more than it does vigorous competition." [8]

The banks are creaming it off home loans with no due regard for the systemic risks they have created. They are reaping super profits and paying themselves obscene salaries. Since the GFC, the average margin between the RBA cash rate and

standard mortgage interest rates – the spread – has doubled from just below 2% to now just below 4%.^[9] Meanwhile the Reserve Bank has insured the liquidity of around \$250 billion worth of bank assets because the economy is neck-deep in property.^[10]

Back to basics banking

The Greens want to bring banking back to basics. To get the economy working for people instead of the finance industry, we would end universal banking in Australia. Instead, a financial institution will only be able to own and operate financial services in one of these four exclusive classes:

- **Deposit and loan banks** that provide basic banking for individuals and business, including savings accounts, credit cards, mortgages and business lending.
- Large-scale **superannuation** funds, including default funds and choice funds.
- **Insurance**, including life insurance and general product insurance.
- **Complex and sophisticated** financial products tailored to high net worth individuals and large businesses. It includes wholesale and retail wealth management products used for investment banking, shadow banking, hedge funds, self-managed super funds, financial markets, and auditors and liquidators.

Doing so would distinguish between the **simple and essential** products and services that the vast majority of Australians use – deposits and loans, superannuation and insurance – and the more **complex and selective** activity that is the domain of big business, the wealthy, and the adventurous. This split will create a high level of consumer protection and a low level of financial system risk.

Re-ordering the regulators

This new regime will require a realignment of the regulatory authorities. The Royal Commission has exposed the failure of financial regulators to prevent misconduct. In particular, the Australian Securities and Investment Commission (ASIC) has not been up to the task. ASIC has prosecuted only one financial services licence holder in the last decade.^[12] The banking fraternity does not fear ASIC. They are almost indifferent to its existence, as evidenced by AMP's flagrant deception regarding the conduct of its financial planning arm.

While budget cuts have impacted upon ASIC's ability to do its job, various reviews into the corporate regulator have found that the problems go beyond a lack of funding. A recent government review found that ASIC's culture was "more defensive, inward looking, risk averse and reactive than is desirable for a conduct regulator".^[13] Similarly, a 2014 Senate Inquiry concluded that ASIC was a "timid,

hesitant regulator, too ready and willing to accept uncritically the assurances of a large institution”.[14]

A core problem with ASIC is that it has a conflicted mandate. ASIC is tasked with ensuring the efficiency and strength of the financial system as well as its fairness and integrity. These two objectives are frequently at odds with each other. What is good for markets is not always good for customers.

ASIC’s conflicted mandate came about at its inception, when the Howard Government took consumer protection powers for the financial sector away from the Australian Competition and Consumer Commission (ACCC). The wisdom of this decision has been questioned ever since. One of the key members of the Wallis Inquiry which recommended this structure, Ian Harper, recently admitted that it was likely to have been a mistake to disempower the ACCC.[15] ASIC’s former chief economist, Alan Erskine, has also called for the reinstatement of the ACCC’s powers over the financial sector.[16]

The Australian Prudential Regulation Authority (APRA) has a similarly conflicted mandate that requires it to take into account stability, efficiency and competition. The lax lending standards exposed by the Royal Commission and the state of Australia’s housing market point to a failure of any financial regulator to be safeguarding individual homeowners.[17] Instead, it has been the ACCC and the Productivity Commission which have both recently highlighted the lack of competition within the mortgage market in Australia.[18]

A return to a strong consumer watchdog

The Greens want to see the ACCC reinstated as the conduct regulator with responsibility for ensuring consumer protection and competition within savings and loans banking, superannuation and insurance, as well as over retail-level intermediators such as financial planners and mortgage brokers. This would include transferring powers currently vested with ASIC and APRA to the ACCC. The government has tacitly acknowledged the ACCC’s suitability for the role of conduct regulator when it tasked them to inquire into any impact the Major Bank Levy had on mortgage rates.[19]

APRA would continue to be the system regulator with prudential oversight over ordinary banking, superannuation and insurance, as well as investment banking. ASIC would continue to be the conduct and system regulator over the remainder of the financial system that is tailored towards sophisticated and wholesale clients.

The Greens would also reform the relationships between regulators and the regulation of regulators themselves. The Greens would give the ACCC a permanent position on the Council of Financial Regulators, along with ASIC, APRA, the Reserve Bank and Treasury, appoint an independent Chair, and require the Council to publish minutes and make public statements regarding decisions of the Council.

The Greens would also implement one of the few recommendations of the Financial Systems Inquiry that the government failed to accept, namely the creation of a Financial Regulator Assessment Board (FRAB) to advise Government annually on how financial regulators have implemented their mandates.[20]

Who this approach would affect

This policy would require banks to divest themselves of financial advisory and brokerage services, such as CommSec and Nabtrade. The Greens would also ensure that the wealth management companies that the banks are selling are split so that superannuation is separated from product issuance and financial planning. A failure to do so would still leave an inherent conflict of interest within essential service providers.

Within the remaining complex and selective components of the finance industry, separation would be primarily on the basis of whether products are retail grade or investment grade, and whether customers are retail investors or sophisticated investors, as it currently is.

But the Greens would introduce a range of measures to increase protections for retail consumers including:

- Financial planners will have to establish an industry-wide indemnity scheme.
- Financial planners will have to be individually licenced and need to be owned and operated separate from any product issuance firms if they are to call themselves a financial planner.
- Mortgage brokers will need to be owned and operated separate from any lending institution.
- Financial planners and mortgage brokers will no longer be able to receive commission-based sales.

Westpac:

It would have to divest its wealth management arm, BT Financial Group, and break-up superannuation, insurance and wealth management.

ANZ, CBA and NAB:

ANZ, CBA and NAB are on the way to divesting their wealth management arms. But they will be compelled to finish the job and also have to divest their trading platforms.

Macquarie Bank:

It will no longer be able to operate as a retail bank (ADI) and investment bank.

AMP:

It will have to break-up. Currently it is an ADI, as well as offering superannuation, insurance and wealth management. It will need to choose one area to operate in.

MLC:

Currently owned by NAB, but is being sold off. In addition to this it will have to break up superannuation, insurance and wealth management.

OnePath:

Currently owned by ANZ, but is being sold off. In addition to this it will have to break up superannuation, general insurance and wealth management.

It is time to break up the banks.

Mr Adam Bandt MP

[1] See: Kay, *Other people's money: masters of the universe or servants of the people*, 2015.

[2] Maddock, *Is the Australian financial sector too big?* ANZ Bluenotes, 16 April 2014.

[3] ABS 5204.0 - Australian System of National Accounts, 2016-17.

[4] Cecchetti & Kharroubi, BIS Working Papers No 490, *Why does financial sector growth crowd out real economic growth?* February 2015.

[5] See: Akerlof & Shiller, *Phishing for phools: the economics of manipulation and deception*, 2015.

[6] IMF, *Global Financial Stability Report*, October 2017.

[7] See: *Financial System Inquiry: Overview - Box 5: Systemic and housing risk in Australia*, 2014.

[8] Sims, *Synchronised swimming versus competition in banking*, AFR Banking and Wealth Summit, 5 April 2018.

[9] Productivity Commission. *Competition in the Australian Financial System - Draft Report*, January 2018.

[10] The Reserve Bank has established a Committed Liquidity Facility to, in effect, grade bank issued securities as high-quality liquidity assets under the rules of the Basel Accord. Australia is unusual in having had to establish such a facility as a result of the high ration of private debt to public debt.

[11] Irvine, Yeates, Danckert & Hunter, ['Stamp out this behaviour' - banks should not offer advice says Fels](#), Sydney Morning Herald, 18 April 2018.

[12] Royal commission into misconduct in the banking, superannuation and financial services industry, Witness statement of Louise Anne Macaulay, Senior Executive Leader, ASIC Financial Advisers Team.

[13] Chester, Gray, & Galbally, *Fit for the future: A capability review of the Australian Securities and Investments Commission - A report to Government*, December 2015.

[14] The Senate Economics Reference Committee, Performance of the Australian Securities and Investments Commission, June 2014.

[15] Martin, ['Benefit of hindsight': ASIC may have been wrong body to protect consumers, Sydney Morning Herald, 24 April 2018.](#)

[16] Erskine, Funding Australia's Future: Regulating the Australian Financial System, July 2014.

[17] Bryan, *New type of poverty hurting middle class*, Sydney Morning Herald, 26 April 2018.

[18] ACCC, *Residential mortgage products price inquiry, Interim report*, 15 March 2018; Productivity Commission, *Competition in the Australian Financial System – Draft Report*, January 2018.

[19] ACCC, Residential mortgage products price inquiry.

[20] Financial Systems Inquiry: Final Report, 2014, Recommendation 27 – Regulator accountability, 2014.