Levy on the Major Banks:

Submission to the Inquiry into the Major Bank Levy Bill 2017 and the Treasury Laws Amendment (Major Bank Levy) Bill 2017

Discussion paper

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INTRODUCTION

The Australia Institute welcomes the opportunity to a submission to the Inquiry into the Major Bank Levy Bill 2017 and the Treasury Laws Amendment (Major Bank Levy) Bill 2017. This submission should be read in conjunction with some earlier submissions to Senate Inquiries. In particular we refer to our submission to the Senate Economics Committee inquiries 'Competition within the Australian banking sector' and 'Consumer protection in the banking, insurance and financial sector'. Those submissions will be forwarded to the Committee Secretariat.

The government aims to introduce a bank levy to raise $6.2 billion over the forward estimates. The levy itself is 0.06 per cent on banks with total liabilities of $100 billion or more. But those liabilities will exclude among other things deposits less than $250,000. By excluding those liabilities the government may be signalling that it does not expect to see the levy passed on through fees on customer deposits under $250,000.

The levy will apply to five big banks - Westpac, ANZ, Commonwealth Bank, National Australia Bank, and Macquarie Group.[1] There is a good case for taxing the rents or super profits extracted by the big banks. Before tax underlying profits of the big four alone amounted to $46.1 billion in the four quarters to September 2016. That amounts to almost three cents in every dollar spent in Australia. Not only do the big banks dominate a concentrated banking sector but they have a common ownership which tends to nullify any tendency for genuine competition. In addition they have shown a willingness to dupe customers with strategies such as pretending St George is an independent business through to the various scandals that have come forward recently.

Australian Banking Association CEO Anna Bligh has vowed that 'every Australian is going to have to pay the bill' for the new levy. Her promise of revenge goes to prove that the Australian big banks have too much economic and political power. We can only hope the government empowers the ACCC to respond effectively to Bligh's revenge. The ABS household expenditure survey shows that low income groups pay higher proportions of their incomes in bank fees.

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[1] These five were identified by News. See http://www.news.com.au/finance/economy/federal-budget/bank-levy-in-federal-budget-2017-will-australians-end-up-paying-more/news-story/0358fd95eb25ca292936a7881d961e87 Macquarie may seem to be an unusual addition being an investment bank with a relatively low profile in its 'normal' banking business.

THE IMPACT ON AUSTRALIANS

The Australia Institute has also released a paper that has looked at the impact of the bank levy if it was passed through to customers and also if it was passed through to shareholders in the form of lower dividend payments. The report found that if the whole levy was passed through to shareholders it would cost an average superannuation account $7 per year.

If the bank levy was passed through to bank customers then those customers could shop around for a better deal on their banking services. As the levy is only paid by the 5 big banks, there are many banks that customers can turn to who are not subject to the levy. The paper found that even before the announcement of the levy customers with an average sized mortgage could save as much as $6,000 a year by switching from the average standard variable interest rate of the big 4 banks to the best rate.

The paper concludes that the bank levy will have minimal impact on the average Australians regardless of whom the levy is passed onto and if bank customers took this as an opportunity to shop around they could make substantial savings.

ADVERTISING BY BANKS IN FINANCIAL YEAR ENDING IN 2016

For comparison with the bank levy we show in table 1 the advertising expenditures of the various banks.

Table 1

	Advertising expenses
	$m
ANZ	261
CBA	491
Macquarie	85
NAB	196
WBC	156

Total	1,189

Source: Annual reports

Table 1 shows that banks spend roughly $1.2 billion on advertising which is comparable to the amount the levy will raise.

AUSTRALIA HAS SOME OF THE MOST PROFITABLE BANKS AND PAYS HEAVILY FOR THAT PRIVILEGE.

Our earlier submission on competition in banking contained a good deal of background information on the profitability of the banking sector. Since then The Banker has released its survey of the top 1000 banks in the world. In terms of pre-tax profit Australian banks ranked sixth highest in the world. That might not be too surprising given Australia is a reasonably large economy. Those figures are reproduced in Table 1.

Table 2

Rank		pre-tax profit (US$m)
1	China	307,993
2	US	206,431
3	Japan	57,280
4	France	41,394
5	Canada	35,767
6	Australia	35,077
7	UK	25,327
8	Spain	21,810
9	Netherlands	14,361
10	Sweden	12,634

A more meaningful measure is to calculate those profits as a share of GDP and when we do that Australia jumps to top of that list of countries. Those calculations are given in Table 2 which calculates bank profits in $US compared with IMF data for GDP expressed in $US. All data refer to 2015.

The figures in Table 2 show 2.9 per cent of everything spent in Australia ends up as bank pre-tax profit compared with the US and UK at 1.2 and 0.9 per cent respectively. Bank profits impose a large burden on the Australian people and economy.

Table 3

Rank		bank profit share of GDP %
1	Australia	2.9
2	China	2.8
3	Sweden	2.6
4	Canada	2.3
5	Netherlands	1.9
6	Spain	1.8
7	France	1.7
8	Japan	1.4
9	US	1.2
10	UK	0.9

OUR FINANCIAL INSTITUTIONS TRY TO DUPE US

The Treasurer has pointed out that the banks are not very well liked in Australia. While that may not be a very good basis for making tax policy we would like to reinforce the Treasurer's views by referring to TAI's submission to the Senate Economics References Committee on Consumer protection in the banking, insurance and financial sector which has now been released as a public document. That submission makes that point that private for-profit organisations face an environment in which there is a strong incentive to dupe customers who lack knowledge of complex financial matters and this provides the perfect opportunity for duping customers—selling something to people who don't understand it and would not have wanted it if they did.

The submission quotes Prof Luigi Zingales from Harvard University says 'if the most profitable line of business is to dupe investors with complex financial products, competitive pressure will induce financial firms to innovate along that dimension'. That fits Australian financial institutions to a T.

Duping includes the billion dollar plus advertising budget of the big four banks which is designed not to inform but to persuade. The insurance industry is incentivised to sell products to people who do not need them and may not even know they are buying them. And it is naïve to think that a claims manager will act fairly rather than maximise profit.

If a board wanted to clean up there is severe doubt it could monitor or even understand the performance of an institution with tens of thousands of employees dealing in complex financial markets selling complex products.

To combat the propensity to dupe there should be initiatives such as default funds that would be government-owned or not-for-profit institutions and would compete in the market by offering an honest alternative. That would restore some of the choice that consumers used to have.

Another solution in the insurance market is to address the conflict of interest when the company paying the claim also assesses the claim. There should be an independent claims assessor which might well be a government agency.

This submission takes the strong view that a lot of proposals to date are just tinkering with the system while proper structural reform would address the problems by altering the incentives faced by players in the banking, insurance and finance sectors.