



Brotherhood  
of St Laurence

Working for an Australia free of poverty

# Submission to Senate Economics Committee Inquiry into the Banking Amendment Bill 2010

Brotherhood of St Laurence

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# 1 Background into the Brotherhood of St Laurence's interest in the Inquiry

The Brotherhood of St Laurence is an independent non-government organisation with strong community links that has been working to reduce poverty in Australia since the 1930s. Based in Melbourne, but with a national profile, the Brotherhood continues to fight for an Australia free of poverty, guided by principles of advocacy, innovation and sustainability. Our work includes direct service provision to people in need, the development of social enterprises to address inequality, research to better understand the causes and effects of poverty in Australia, and the development of policy solutions at both national and local levels.

As part of our wider efforts to promote social inclusion, the Brotherhood is committed to developing and demonstrating effective programs for disadvantaged people to address financial exclusion. Financial exclusion involves being denied access to affordable, appropriate and fair financial products and services, with the result that people's abilities to participate fully in social and economic activities is reduced, financial hardship is increased, and poverty (measured by income, debt and assets) is exacerbated (Burkett and Sheehan 2009). In particular, financial exclusion means that Australians living on a low income may be forced into vulnerable situations, including:

- being forced to pay extremely high rates of interest to borrow from payday and other 'fringe' lenders in order to make ends meet
- going without important everyday items and services
- lacking even small savings or simple insurance, so that unexpected financial pressures are difficult, if not impossible, to manage
- not being able to access the impartial advice, particularly on debt problems and accessing rights and entitlements, that can help people avoid significant distress.

Addressing financial exclusion is not merely about service provision; it also includes capacity building and structural change.

To this end, the Brotherhood delivers the following financial inclusion programs:

- *Saver Plus*, Australia's largest matched savings and financial education program developed in conjunction with ANZ and delivered in partnership with a number of community agencies. During 2009 to 2011, with Federal Government support, Saver Plus will reach 7,600 participants in 60 communities nationally
- *Progress Loans*, a low repayment, affordable small loan program delivered in partnership with ANZ. During 2009 to 2011, this mainstream and fair loan product will be made available to 800 borrowers
- *MoneyMinded*, a financial literacy education program. The Brotherhood delivers this resource through a 'train the trainer' model and also through professional development for workers in community agencies
- *Financial Health Service*, a pilot one-on-one financial guidance and information service.

The Brotherhood welcomes further efforts by policy makers to address financial exclusion, including consideration of the proposals outlined in the Banking Amendment (Delivering Essential

Financial Services for the Community) Bill 2010 (the Bill). In particular, the Brotherhood agrees that improving access to simple and fair financial products and services, by providing incentives to banks and other financial service providers, can go some way in addressing financial exclusion.

For example, we are extremely supportive of the approach taken by the recent *Review of the Governance, Efficiency, Structure and Operation of Australia's Superannuation System* (the Cooper Review), which acknowledged that regulatory structures must contend with low consumer and financial literacy which is widespread among superannuation holders. In its final report, the Cooper Review states:

... realisations about financial literacy and engagement have led the Panel to propose the new 'choice architecture' framework for the Australian superannuation system .... This framework is an adaptation of contemporary thinking in the field of behavioural economics. ... The key tenet of this approach is the concept of 'libertarian paternalism' – the idea that the outcomes experienced by inert or disengaged consumers should have inbuilt settings that most closely suit those consumers' objective needs, as assessed by the expert providers of the product or service in question (Cooper Review 2010).

Such an approach could be applied for consumer benefit in a range of other financial and consumer markets, including banking. Some of the proposals in the Bill do propose improved access to simple products; however we have some concerns about the detail of the proposals in the Bill, which are outlined in this submission.

## **2 Detailed comments on proposals in the Bill**

The Bill proposes four amendments to the *Banking Act 1959* (Cth). Each of the amendments is commented on in turn.

### **Fee-free banking services**

The first amendment requires banks to offer basic transaction accounts that are free from account-keeping fees and penalty fees for the actions of third parties, and that limit other fees to a level sufficient to recover the cost to the bank of the penalised conduct.

The Brotherhood supports reduced fees on transaction accounts, which would be a move toward a more equitable outcome for consumers, especially low-income earners, who may feel the burden of bank fees more than others, and who may be more susceptible than others to incurring such fees.

A transaction account is an essential financial service since it is necessary in order to receive salaries via electronic payment, to receive Centrelink benefits, to withdraw cash via ATMs and to make electronic payments using EFTPOS facilities. The Brotherhood is very supportive of 'basic' transaction accounts that some banks presently choose to offer low income customers (generally those with a health care card or pensioner concession card). These accounts protect low-income earners from being charged exorbitant fees for their use of this essential financial service.

It is our experience that many low-income earners incur substantial penalty fees on their transactions accounts. Among clients of the Brotherhood monthly account keeping fees, transactions fees and penalty fees can take a sizable bite out of a monthly budget. For instance, a

Brotherhood client was recently charged several penalty fees because of a misunderstanding of the direct debit system. He said, '\$50 is food for a whole week for my kids. That little extra \$50 that they have charged, it's just shattered me. To someone on a disability pension, \$50 is a fortune'. While there may be some cost involved for a bank, the size of these fees seems to be a disproportionate penalty.

We acknowledge that many of the larger banks have taken steps to abolish or significantly reduce penalty fees, and welcome the initiatives undertaken. However, many of the smaller banks and credit unions still charge significant penalty fees. For example, Bendigo Bank charges \$27.50 on overdrawn accounts and \$40 for a direct-debit dishonour whereas the Commonwealth Bank charges a \$5 dishonour fee on overdrawn accounts. It is our view that these fees are unfair and that consumers should be protected from egregious penalty fees no matter what institution they bank with.

The Brotherhood does acknowledge that banks and financial service providers incur costs in offering transaction accounts. As such, we understand the need for banks to charge reasonable fees. That said, since transaction accounts are an essential service, we believe more should be done to encourage banks to provide 'basic' fee-free or fee-reduced transaction accounts to low-income earners. Further, where these accounts are offered, more effort should be taken to ensure those eligible for the accounts are accessing them. Estimates based on research conducted by the Brotherhood of St Laurence in 2009 (forthcoming) indicate that some 40 to 60 per cent of clients eligible for a basic bank account have not accessed one, and are instead incurring hefty fees on their transactions accounts.

We note that clause 14 of the Banking Code of Practice provides that banks must advise low-income consumers of account suitability. The clause states:

If you tell us that you are a low income earner or a disadvantaged person (regardless of whether you are an existing or prospective customer but not if you are a small business), we will provide you with details of accounts which may be suitable to your needs. We will also do this if you ask for this information or if, in the course of dealing personally with you, we become aware that you are in receipt of Centrelink or like benefits.

Despite this clause, it is our experience that banks do not regularly refer clients to basic or concession bank accounts where they have an existing account with an institution and do not make further inquiries about their transaction account.

**Recommendation:**

- **The Bill should provide appropriate incentives to all banks to offer 'basic' fee-free or reduced transaction accounts to low-income earners;**
- **Banks should identify customers who are eligible for such accounts and make them aware of the benefits in switching to such an account.**

## ATM fees

The second amendment to the Bill provides that transactions at a bank's own-branded ATMs are to be free of charge, and that charges for the use of a bank's ATMs by customers of another authorised deposit-taking institution (ADI) are to be capped at the cost of service provision.

The Brotherhood recognises that ATMs are a service which is highly valued by the users of such services. The Brotherhood recognises that banks and other providers of ATMs should not necessarily be prevented from charging their customers (and the customers of other institutions) some fee for the use of their ATMs. However the Brotherhood has some concerns on the matter, namely the potential exploitation of consumers using ATM services through exploitative pricing practises which do not consider how consumers actually use the service.

For example, many of our clients wish to use an ATM to check their account balance so that they do not overdraw the account. Many of these clients do not have access to internet banking or some other system to check balances. For some accounts, even checking the account balance via the ATM incurs a fee, making it difficult for consumers to then use their account in a way that minimises fees.

The Brotherhood is also concerned that providers of ATMs, in accordance with recent ATM reforms, may price their services differently according to time of day, or location. This could result in the exploitation of those wishing to access their funds at 'off-peak' times (e.g. higher fees for night-time use), or those who have limited ATM access (local monopoly could prevail). Depending on the extent of the price difference, and the characteristics (e.g. age, financial literacy level etc) of the market segment on which the higher fees could be felt, this practice could be considered exploitative.

We do note that the recent reforms requiring owners of ATMs to state the fee on a machine's screen before a transaction have resulted in more people using their own bank's ATMs, which generally do not incur a fee (RBA 2010). We support this increased transparency which allows consumers to more easily choose not to incur fees. Consideration should be given to whether such transparency can be applied to other payment mechanisms, such as EFTPOS. That said, we believe that regulators should be tasked with monitoring and ensuring ATM fees are not excessive or exploitative.

**Recommendation:**

- **That appropriate regulators be tasked with monitoring the level of ATM fees to ensure that they are not excessive, and empowered to regulate such fees should this be necessary.**
- **That reforms improving transparency of ATM charges be considered in relation to EFTPOS and other card services.**

## Fixed-interest gap mortgages

The third amendment requires ADIs to offer a mortgage product (a 'fixed interest gap mortgage') with an interest rate fixed at a negotiated margin above the institution's cost of funds.

The Brotherhood supports changes that make mortgages more accessible, especially to low income earners. The Brotherhood supports initiatives that reward savings in order to enter the mortgage market. An example of one such move toward improving accessibility was the introduction of the First Home Savers Account, which can improve access by incentivising savings for the purpose of purchasing a home. This policy (and indeed any others which incentivise savings) can allow people who would otherwise be unable to afford to enter the mortgage market to do so.

The Brotherhood also supports moves to increase transparency, particularly in regard to the sourcing of funds by banks, so as to drive competition. The Brotherhood acknowledges that banks must maintain a spread between the rate at which they source their funds and the rates at which they lend allowing them to cover costs (costs of funding<sup>1</sup>, admin costs etc) and to yield profits for shareholders. While not inhibiting banks' ability to profit from their mortgage products, a published rate indicating banks' 'average cost of funds' or similar would allow the market to see whether banks are pricing competitively.

**Recommendation:**

- **That further transparency be brought to the mortgage market through the Reserve Bank of Australia publishing the average cost of wholesale funding.**

### Mortgage exit fees

The fourth amendment stipulates that mortgage exit fees be capped at a level sufficient only to recover the cost to the lender of early termination, and that exit fees be mentioned in advertising and included in mortgage contracts in a uniform way to ensure customers are aware of them when deciding whether to sign the contract.

The Brotherhood supports such an amendment in principle, but acknowledges that the recently-enacted *National Consumer Credit Protection Act 2010* and the unfair contract term laws in the new *Australian Consumer Law* regulate early termination and other mortgage fees. Indeed, the Australian Securities and Investments Commission (ASIC) has recently released a consultation paper on its approach to regulating mortgage early exit fees under these laws (ASIC 2010). The approach taken by ASIC is preferable to regulating through the *Banking Act*, as it would regulate all mortgage providers, not just banks.

**Recommendation:**

- **That regulation of mortgage early exit fees be undertaken by ASIC under the new national consumer credit law and unfair contract terms law.**

## 3 Concluding remarks

The Brotherhood would like to see incentives for financial service providers to provide simple, appropriate and fair products designed for the needs of all. We would also like to see improved communications and engagement with those currently excluded from financial services.

The Brotherhood believes that the effective operation of a fair and inclusive market for financial services is a joint responsibility of the financial industry, government and civil society. However, we believe that there are opportunities through banking and financial service regulation to promote simple, appropriate and fair financial products and services. Such regulation should be guided by principles of actual consumer behaviour, particularly those living on lower incomes, who are more

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<sup>1</sup> The cost of funding is acknowledged to be higher than the RBA cash rate, as banks may have to seek funding at more expensive rates from beyond the Australian credit market.

susceptible to financial hardship arising from ill-informed decision-making and expensive or unfair products and services.

The Brotherhood would welcome the opportunity to provide further details and looks forward to the outcome of the Inquiry.

## 4 References

Australian Securities and Investments Commission (ASIC) 2010, *Mortgage early exit fees: unconscionable fees and unfair contract terms*, Consultation Paper 135, ASIC.

Burkett, I and Sheehan, G 2009, *From the margins to the mainstream: the challenges for microfinance in Australia*, Brotherhood of St Laurence and Foresters Community Finance, Fitzroy, Vic.

Reserve Bank of Australia (RBA) 2010, 'Reform of the ATM system – one year on', *Reserve Bank Bulletin*, June.

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