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Attn: John Hawkins, Senate Standing Committee on Economics

Submission to Senate Enquiry: 'Competition within the Australian Banking Sector'

Thanks for the opportunity to submit to this enquiry. We're glad to see some serious attention being paid to the issue and look forward to material, legislative outcomes.

Background

Accounts4Life is a start-up company which has '**attempted**' to bring a bank account portability solution to market over the last 18 months. I say 'attempted' as we have faced a number of barriers to entry given the existing nature of the payments systems. Our primary goal is the facilitation of customer movement and, consequently, increased competition. Given the pro-competition rhetoric espoused by nearly every banking sector participant, you'd think such an initiative would be welcomed with open arms: Clearly, there are bigger commercial forces at play. We believe we're in a unique position to offer comment, being neither a customer nor bank, but rather a stifled innovator. We have learnt to take nothing on face value and our investigations have uncovered a number of issues which we feel are relevant to this enquiry.

Following are many of the competition-related issues as we see them and recommendations for your consideration. We are happy to discuss any or all of them with the committee if requested.

Observations

1. **Does competition exist?** Clearly there is competition in the industry; the question is whether it effectively leads to consumer benefits. The Big 4 (i.e. ANZ, CBA, NAB, WBC) increased their market dominance after the GFC (partly through acquisitions and partly through the benefits of deposit guarantees) and now 'fight' with each other for business. If this 'fight' were effective, surely we'd see high levels of churn in the marketplace? While neither the RBA nor APRA claim to collect or provide churn data, they have estimated churn levels in Australia to be around **8%**¹. **We strongly believe that**

¹ Per Treasury minutes obtained by The Age (under FOI)



this is the single, most-damning indicator of a non-competitive market. How many other industries operate in such a static pool? A truly competitive market would surely see market share redistribution **away** from the Big 4 and **toward** small and mid-size players. (If not for significantly better deals, then at least as punishment to the Big 4.) One would also expect to see a tempering of profits as margins are continually trimmed to lower levels. None of this is apparent.

2. **Too many cooks.** We found it quite confusing trying to figure out who calls the shots in the banking industry. APRA are the regulator but seem only interested in the prudential health of the industry, not competition. The ACCC handle competition but will only act where a breach of the Trade Practices Act occurs; they do not proactively pursue a competitive banking environment. The Australian Payments Clearing Association (APCA) run the majority of payments systems and are effectively an industry collective making their own rules. The RBA espouse goals of decreased barriers to entry and increased competition (for the benefit of the Australian people) but seem limited in their ability to tangibly support new entrants. Treasury actually have a “Bank Competition Unit” but, while being supportive of new ideas, are limited by a need to remain neutral. Then there’s the ABA who valiantly espouse the benefits of competition² yet are unable to point to any active or past initiatives on the topic.
3. **Archaic Systems and Processes.** It was very surprising to learn that the industry does not have real-time settlement across the board and operates in a seemingly backwards, 20th century mode. Why would they not embrace technology? What would drive them to maintain ‘inefficient’ processes?
 - a. How is it possible that in 2011, the banks still manage to get away with overnight batch-processing of direct debits and credits? The overnight “float” is another creative revenue stream that the banks are loathe to lose. Perhaps there was once a valid argument to net out debits and credits between banks to reduce the transfer of physical assets: In a modern, digital age, this is conveniently lazy.
 - b. We do acknowledge APCA’s migration in BECS (the Bulk Electronic Clearing System for direct debits and credits) to a Virtual Private Network (VPN) or “cloud” from what was previously a bunch of direct links between all participants. Effectively, a new player can plug into the cloud and deal with all other participants rather than negotiate bilateral agreements with every other participant. This is a positive *technical* step but doesn’t help the *process* issue of not being able to get a seat at the table. (i.e. BSB number acquisition. See ‘Barriers to Entry’ below.)
 - c. **Barriers to entry.** APCA owns the BSB number range and will only release new numbers to Authorised Deposit-taking Institutions (ADIs). Accounts4Life has a business model that requires a BSB, yet does not constitute “banking business”³ and therefore does not need an ADI licence. Put simply, the APCA legislation does not consider the possibility of such a business model. As for attempting a policy change, any such proposal is reviewed and (proportionally) voted on by the members. As such, the Big 4 can squash any attempt to allow a new entrant to operate independently and increase competition.

² <http://www.bankers.asn.au/About-ABA/default.aspx>

³ As defined under the Banking Act 1959, as advised by APRA.



4. **Lack of independence.** As far as the payments system is concerned, how can APCA operate independently when it is funded by its members and allows voting by its member representatives? Is a CBA representative on an APCA panel ever going to vote for something that would damage the CBA? Will APCA fight for common sense with the hands that feed it? While the banks may have historically built and managed these systems, perhaps it's time to hand over control to a truly independent body.
5. **Lack of transparency** In dealing with APRA, it was not surprising to learn that they refuse to discuss their dealings with other Financial Institutions (FIs). What was surprising was their refusal to advise whether any discussions had ever taken place. Specifically we sought to understand how BPay (owned by the Big 4 through an entity called Cardlink Services Limited) managed to conduct "banking business" (specifically holding customer funds) without an ADI licence. APRA were unable/unwilling to advise whether BPay had: requested a ruling, been given an exemption or never even hit APRA's radar. We were left to conclude that having the Big 4 as shareholders was an excellent way to mitigate regulatory impediments.
6. **Honour first, check later ... then charge fees.** It was surprising to learn that the direct entry clearing system (BECS) operates on an "honour first, check later" principle. I.e. Transactions are honoured by the paying Financial Institution (FI) without checking the account balance. There is then a 24 hour window to check the transaction and initiate a reversal with a corresponding fee between FIs. It seems as though everyone is happier to ignore a simple 'lookup and on-the-spot rejection' for the chance to have a reversal fee. Fees are obviously a hot topic so we'll leave it for others to expand on this issue.
7. **Encouraged inefficient selection.** At the most basic level, a bank makes revenue from the interest differential on deposits and loans. Somehow, this concept has evolved to deliver numerous revenue streams through the creation of extensive product suites with complex pros and cons. The resulting consumer confusion allows the banks to harvest greater revenues through inefficient selection. While product diffusion can be argued for the purposes of meeting discrete customers' needs, we feel it has gone way too far and entered the realm of trickery and deceit.
 - a. **High interest teasers.** Why do almost all banks offer a "high interest" savings account BUT require you to operate out of a linked, zero interest account? Why must we continually monitor account balances to ensure there are sufficient funds in the low-interest account to avoid penalty fees? It appears a clear strategy to force inefficient selection, where the banks win either on "lazy" deposits with high gross margin OR fee revenue from customers who have the funds but not in the right account.
 - b. **Low interest credit card balance transfers.** These sound great until you read the fine print. Moving the balance is fine, as long as you're not tempted to make a purchase on the new card. Any minimum monthly payment is taken from the low interest debt first (the balance transfer) while the high interest debt is left to compound. Not paying the full balance at the end of the month (which INCLUDES the balance transfer amount) leads to a loss of the interest free period (on new purchases) and further compounding of the high interest debt. These are clearly designed to win the profitable customers. Yes, there is healthy competition, but it's to plunder those in a credit trap.



8. **The Power of Advertising.** If you believed what you were told, we'd be handing out awards to the banks for their unwavering concern for customers. With substantial advertising budgets, clever 'interpretation' of the truth and nobody able to afford to call them out, how can average customers distinguish fact from spin? This all creates a *perception* of high competition (and presumed customer benefit) when it's more a case of competition to gouge profits from the next 'clever' idea.
- a. **Fee-free accounts.** While fee removal is clearly a good thing, it seems a bit strange that we should applaud them for stopping a long-time rort. Furthermore, almost all fee-free accounts we researched offered 0.01% (or lower) interest. Many also had terms and conditions that required minimum balances and inflows to retain the fee-free status. There is no way that such a decision is made without a strong, financially-beneficial business case. We believe this was primarily just a clever way to attract free funds (and massive margins) with the added benefit of public kudos. Most interesting of the claims we researched was from NAB who proudly announced the removal of fees from 11 products ... 10 of which were no longer available!!⁴
 - b. **Customer (dis)satisfaction.** Commbank have spent plenty on a "hearts and minds" style campaign to have us believe how wonderful their service is. One catchphrase used is "*That's why Commbank has more satisfied customers than any other bank.*" This sounded unlikely given the Big 4 have consistently filled the bottom 4 positions in Choice Magazine's customer satisfaction surveys. Technically they are correct but it's only due to their superior *total* customer numbers. The corollary which they conveniently fail to mention is that they have "*more dissatisfied customers than any other bank*".
 - c. **NAB kills the asterisk.** In late 2010, NAB proudly claimed to have "killed the asterisk" that those other banks hide behind. No monthly account fees and no minimum deposits. Sounds great and certainly a better offer than some. So if they're into full disclosure, why not mention the disgraceful 0.01% interest rate? Again, they're just competing to gouge the less-informed customers.
9. **Self regulation doesn't work where money is involved.** While there is merit in the Government not taking an overly bureaucratic approach to regulation, the pendulum appears to have swayed too far in the banks' favour. How is it that mobile phone number portability occurred a decade ago and yet the banks can't (won't) make it happen in 2011? Indeed banking lobbies the world over seem to have successfully stifled material regulation. It appears that the industry has done very well at not only warding off serious regulatory reform but also pretending to be making their own changes for the good of the people.
- a. **Account Switching Service was a failure.** This was a much-lauded process (in fact a short 'pamphlet' or pdf) that told you how to switch banks ... in case you couldn't figure out the open new account / redirect traffic / close old account thing! (Try ringing your bank to see if they A) know about it or B) do anything more than tell you to look up your own account history.) And the special customer "hotline" was just ASICs existing freecall number! Plenty

⁴ http://www.nab.com.au/wps/wcm/connect/nab/nab/home/personal_finance/21/705/3



has been written about this including Treasury's own investigation into its miserable awareness and uptake. Of greater concern is how the industry managed to string out this project for around 12 months! Dare we say there's more effort put into managing appearances than problems?

- b. M@MBO drags on and on.** From what we've gleaned, project M@MBO is the industry's attempt at account portability. (I say 'industry' but it's really a BPay spin-off and therefore owned by the Big 4.) It's been on-again, off-again since (we believe) 2006 but effectively used as a beacon to stave off serious regulation. Naturally, the ABA (who strongly represent the views of the Big 4) claim it will solve the problem despite being very complex and expensive. The Treasurer's recent portability enquiry announcement will further stall M@MBO but hopefully call their bluff and result in a solution that is not controlled by those who stand to lose most from portability.



Recommendations

1. **Introduce some form of bank account portability.** We note the Treasurer's request (Dec 2010) for a 6 month enquiry into this issue, headed by Mr Bernie Fraser. This must result in legislated portability or an *industry-independent* solution since the industry can't be trusted to A) deliver a solution that works in the customers' best interests or B) deliver one in a timely fashion. Rather than broad-ranging regulation, just unshackle the customers and let churn drive market efficiencies.
2. **Identify a single point of accountability for banking competition issues.** We believe this should reside within either Treasury or the RBA to ensure independence. The entity would sit above the myriad of players and arbitrate on specific competition issues. It should have the power to effect fair and sensible policy change within the likes of APRA and APCA.
3. **Create and fund a Banking Awareness Unit.** Create an independent body responsible for "counter-spin" advertising, funded by a pro-rata levy on FIs' advertising spend. This unit would create advertising material (primarily TVCs) to expose the fine print and ulterior motives in whatever the latest hot product might be. This is not meant to be "anti-banks" but rather objective and transparent public education. (We note the existence of ASIC's FIDO website⁵ but believe in a more 'proportional response'.)
4. **Legislate for real-time settlement in all payments systems.** Eliminate the possibility for the 'float' and any customer-detrimental impacts from non-real-time, non-sequential transaction processing.
5. **Prevent further acquisitions by the Big 4.** Break the cycle of mid-tier banks growing (through differentiation) only to be swallowed by the Big 4.

Regards

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⁵ <http://www.fido.gov.au/fido/fido.nsf>