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The Parliament of the Commonwealth of Australia

# Competition in the banking and non-banking sectors

House of Representatives  
Standing Committee on Economics

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Canberra

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## Chair's foreword

Competition within the mortgage market has grown considerably since financial deregulation in the 1980s. In particular, the entry into the market of non-bank lenders and overseas financial institutions has resulted in greater competition, lower interest rates and margins, and an increase in mortgage products.

In August 2007, the collapse of the US sub-prime mortgage market disrupted wholesale funding markets around the globe making it extremely difficult for lenders to access funding, as well as undermining consumer confidence. During September 2008, the upheaval in financial markets escalated with large falls in equity prices and severe volatility across financial markets. As a consequence, a number of governments, most notably the US and the UK, implemented financial stability packages in an attempt to stabilise their financial systems.

During the past year there has been a noticeable increase in interest rates due to increases in the official cash rate but also increases in the cost of funding. Between January and September, Australia's four largest banks increased their interest rates by an average of 100 basis points, of which 50 to 60 basis points were raised independently of the Reserve Bank of Australia's (RBA) official cash rate. There has also been a reduction in the number of institutions offering home loan products.

Early in the year the rise in interest rates, combined with increasing petrol and grocery prices, put Australian households under financial pressure. Fortunately, the Reserve Bank of Australia, between September and November, reduced the official cash rate by 200 basis points to 5.25 per cent and the world price of oil is currently falling. The banks have passed on some of this rate cut but not all. For commercial rates to fall further the cost of funding needs to decrease and competitive pressures within the market place need to be more effective.

The non-banking sector, which has primarily used securitisation as the main source of funding, has found it particularly difficult to remain competitive in the current financial conditions. This has resulted in a decrease in competitive pressure within the banking and non-banking sectors.

The government is currently taking positive steps to increase liquidity both for the banking and non-banking sectors. There is still some uncertainty as to how long the recent downturn in the global financial market will last and the government should therefore continue to monitor the state of the market in light of any future developments.

The committee has also recommended that government examine a range of other proposals that could provide additional liquidity including expanding the RBA's repurchase agreements by extending their term to maturity even further and allowing Authorised Deposit-Taking Institutions to issue covered bonds.

In addressing matters relating to the state of competition, the committee received evidence on a range of other issues including: investigating and addressing issues of concern within the market; positive credit reporting; the government's account switching facilitation package; the regulation and entry and exit fees; and consumer protection for borrowers. The committee has recommended that:

- government review the current adequacy of the Trade Practices Act to extend the Australian Competition and Consumer Commission powers;
- government implement the findings of the Australian Law Reform Commission's report recommendations on reforming Australia's credit reporting system;
- government review the account switching package in 12 months time and that consideration be given to including card schemes in the package;
- government consider mechanisms for making entry and exit fees more transparent and for addressing unfair entry and exit fees;
- government consider the feasibility of regulating unsolicited credit card limit increases;
- the Australian Securities and Investments Commission includes a glossary of standardised financial terms and Treasury develop a standardised key facts document for mortgage products to help consumers to compare financial products; and
- government make it compulsory for all credit providers to be a member of an external dispute resolution scheme approved by ASIC.

On behalf of the committee I would like to thank all of the groups that participated in this inquiry.

Craig Thomson MP  
Chair



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## Membership of the Committee

**Chair** Mr Craig Thomson MP

**Deputy Chair** Hon Kevin Andrews MP  
(from 10/11/08)

**Members** Hon Julie Bishop MP (from 25/9/08) Mr Richard Marles MP  
Mr David Bradbury MP Ms Julie Owens MP  
Mr Steve Ciobo MP Hon Chris Pearce MP  
(from 28/8/08 to 10/11/08) (to 10/11/08)  
Hon Peter Dutton MP (to 25/9/08) Hon Tony Smith MP (from 25/9/08)  
Hon Joe Hockey MP (from 10/11/08) Hon Malcolm Turnbull MP (to 28/8/08)  
Ms Sharryn Jackson MP Mr Jim Turnour MP  
Mr Michael Keenan MP (to 25/9/08)

## Committee Secretariat

**Secretary** Mr Stephen Boyd

**Inquiry Secretary** Mr Paul Zinkel

**Research Officers** Ms Stephanie Mikac

Dr Cathryn Ollif

**Administrative Officers** Ms Natasha Petrovic

Ms Renee Van Der Hoek



## Terms of reference

On 3 June 2008, the Treasurer requested the Committee to conduct an inquiry with the following terms of reference:

*The Committee should examine competition in the retail banking and non-banking sectors in Australia. The inquiry will pay particular attention to home mortgage products and linked facilities frequently offered to consumers such as credit cards and savings accounts.*

1. *The Committee will undertake a stock take of the Australian retail banking and non-banking industries, focussing on:*
  - a) *recent developments in relation to products, providers and distribution channels;*
  - b) *the current state of the retail banking and non-banking industries;*
  - c) *the likely drivers of future change and innovation in the retail banking and non-banking sectors including the continuing impact of technological developments; and*
  - d) *comparisons with relevant international jurisdictions.*
2. *The Committee will also identify any barriers that may impact on competition in the retail banking and non-banking sectors, and policies to enhance further competition and product choice for consumers.*



## List of abbreviations

ABA	Australian Bankers' Association
Abacus	Association of Building Societies and Credit Unions
ACCC	Australian Competition and Consumer Commission
ALRC	Australian Law Reform Commission
AOFM	Australian Office of Financial Management
APCA	Australian Payments Clearing Association
APRA	Australian Prudential Regulation Authority
ARMs	Adjustable-Rate Mortgages
ASF	Australian Securitisation Forum
ASIC	Australian Securities and Investments Commission
ADI	Authorised Deposit-Taking Institution
BankWest	Bank of Western Australia
BECS	Bulk Electronic Clearing System
BSB	Bank State Branch
CALC	Consumer Action Law Centre
CCLC	Consumer Credit Legal Centre of New South Wales
CMHC	Canada Mortgage and Housing Corporation
COAG	Council of Australian Governments
CITE	Centre for Ideas and the Economy
CBA	Commonwealth Bank of Australia
DE Users	Direct Entry Users
EC	European Commission

Fannie Mae	Federal National Mortgage Association
FCS	Financial Claims Scheme
FHFA	Federal Housing Finance Agency
FIDO	Financial tips and safety checks
Freddie Mac	Federal Home Loan Mortgage Corporation
FSR	Financial Stability Review
FSRA	Financial Services Reform Act
HBOS	Halifax – Bank of Scotland
IMF	International Monetary Fund
Lloyds TSB	Lloyds Bank and the Trustee Savings Bank
ME Bank	Members Equity Bank
MFAA	Mortgage and Finance Association of Australia
NAB	National Australia Bank
OECD	Organisation for Economic Cooperation and Development
OFT	Office of Fair Trading
Repo	Repurchase agreement
RBA	Reserve Bank of Australia
RBS	Royal Bank of Scotland
RMBS	Residential Mortgage Backed Securities
SPV	Special Purpose Vehicles
UCCC	Uniform Consumer Credit Code
UK	United Kingdom
US	United States of America
WBC	Westpac Banking Corporation



# List of recommendations

## Options to increase competition

The committee believes that the 'AussieMac' proposal is not a suitable model for the Australian context.

The committee supports the move by the government to have the Australian Office of Financial Management (AOFM) allow both Authorised Deposit-Taking Institutions (ADIs) and non-ADIs to purchase \$8 billion in RMBS over the next 3 years.

The committee believes that the actions taken by the government are positive steps toward adding additional liquidity within the market.

Recent difficulties in the Residential Mortgage-Backed Securities (RMBS) market, as a consequence of the global financial crisis, have made it difficult for some mortgage providers to actively compete in the mortgage market. As a result, the committee welcomes the government's initiatives to invest \$8 billion of RMBS in order to support recovery in the RMBS market.

### *Recommendation 1*

*The committee recommends that the government continue to monitor the state of the Residential Mortgage-Backed Securities market and review the adequacy of the current level of investment in light of future market developments.*

## Reserve Bank of Australia's repurchase agreements

The committee supports the steps taken by the Reserve Bank of Australia (RBA) to widen the range of securities that it will accept as collateral and to lengthen the term to maturity.

The RBA repurchase agreements are an effective tool for adding short term liquidity to the market. However, there is still a concern that expanding the repurchase agreements by extending their term to maturity even further may place additional unnecessary risk on the RBA.

The committee believes that while there is merit in the proposal to make repos a long term funding option, further study on whether this will place additional risk on the RBA needs to be undertaken.

### ***Recommendation 2***

*The committee recommends that the Reserve Bank of Australia examine the appropriateness, feasibility and risks of expanding the repurchase agreements by extending their term to maturity even further and provide a public audit report within six months. The report must be made available to the committee for review.*

### **Covered Bonds**

The committee believes that further study on how covered bonds would be regulated needs to be undertaken.

### ***Recommendation 3***

*The committee recommends that the Treasury examine the appropriateness and feasibility of allowing Australian authorised deposit-taking institutions to issue covered bonds.*

### **Investigating and addressing issues of concern**

The *Trade Practices Act 1974* already contains a broad range of investigation and enforcement powers in relation to suspected breaches of the Act including, mechanisms to monitor competition in particular industries, and substantial penalties for breaches of the competition provisions. There are also a range of general consumer protection powers.

Some concerns were raised with the committee regarding whether the current mechanisms were adequate to monitor the state of competition within the banking and non-banking sectors.

### ***Recommendation 4***

*The committee recommends that the government review the current adequacy of the Trade Practices Act 1974 to provide the Australian Competition and Consumer Commission the powers to investigate and address issues of concern in markets and regulated sectors.*

### Positive credit reporting

The committee concurs with the Australian Law Reform Commission's (ALRC) recommendation that there should be some expansion of the categories of personal information that can be included in credit reporting information held by credit reporting agencies.

#### *Recommendation 5*

*The committee supports the findings of the Australian Law Reform Commission's report and urges the government to implement the report's recommendations on reforming Australia's credit reporting system.*

### The account switching facilitation package

#### Card scheme inclusion in the switching regime

The committee supports the combined effort of the government and the Australian Payments Clearing Association (APCA) to encourage card schemes to participate in the new switching regime.

The committee accepts that it is relatively easy for consumers to switch between card schemes. However, the committee notes that a consumer that holds a mortgage may also hold a credit card with the same mortgage provider and so may feel inhibited from switching between card schemes.

#### *Recommendation 6*

*The committee recommends that consideration be given to including card schemes in the Account Switching Package.*

#### Account number portability

The committee accepts evidence, which suggests that a central account registry could improve the efficiency of switching between financial institutions, but also understands that there may be significant costs in moving from a bilateral to a more centralised system.

The committee would like to see an examination of the costs and benefits of implementing a system, which could support a more centralised account switching process which would allow financial institutions to undertake this process on behalf of the consumer. The committee also believes that privacy considerations need to be taken into account under such a model.

The committee is aware that Australia's payments system operates differently to that of The Netherlands. However, the committee would also welcome a thorough investigation of the costs and benefits of implementing a switching system similar to that of The Netherlands.

***Recommendation 7***

*The committee recommends that after 12 months in operation, the Treasury review the Account Switching Package with consideration being given to any areas in which it may be enhanced, including consideration of the costs and benefits of a more centralised account switching system, such as those in operation in the UK and The Netherlands.*

**Regulation of entry and exit fees**

The committee acknowledges that there is community concern about the current level of entry and exit fees on some mortgage products.

***Recommendation 8***

*The committee recommends that, as part of the adoption of responsibility for the regulation of credit and the introduction of a national consumer policy framework, the government consider mechanisms for making entry and exit fees more transparent and for addressing unfair entry and exit fees.*

**Consumer protection for borrowers**

**Financial literacy**

The committee supports the goals and objectives of the Financial Literacy Foundation and encourages it to build on the work it has already done.

Furthermore, the committee believes it could be most useful to people who are trying to understand the products which are available if there were a glossary of standardised financial terms in very simple language. This glossary could be placed on both the Australian Securities and Investments Commission's (ASIC) consumer website and the Understanding Money website.

***Recommendation 9***

*The committee recommends that the Australian Securities and Investments Commission includes a glossary of standardised financial terms in simple language on its consumer website and also on the Financial Literacy Foundation's website.*



### **Predatory practices relating to credit cards**

The committee agrees that it is an undesirable practice for lenders to push people to increase their credit limits regardless as to whether or not those people are able to understand the implications of taking on more debt or if they will be able to repay the increased debt.

#### ***Recommendation 10***

*The committee recommends that, as part of its adoption of responsibility for the regulation of credit, the government consider the feasibility of regulating unsolicited credit card limit increases.*

### **Consumer information to compare products**

The committee believes that, in addition to the work Treasury is doing to improve product disclosure, there is a need in Australia for some sort of standardised 'key facts document', similar to the UK model, to help consumers to compare effectively mortgage products.

#### ***Recommendation 11***

*The committee recommends that the Treasury develop a standardised key facts document for mortgage products, based on the UK model, to help consumers to compare financial products. The standardised key facts document must be provided to the committee within twelve months.*

### **External dispute resolution**

The committee notes that there is currently no legal obligation for providers of credit or financial advice associated with credit, other than ADIs, to belong to an external dispute resolution scheme, although some non-ADIs voluntarily belong to such schemes.

In view of the concerns expressed by CHOICE and other stakeholders, the committee welcomes and supports the creation, as part of government reforms of the financial services regulatory regime, of an external dispute resolution body to which all licensed lenders must belong, to be introduced by mid-2009.

#### ***Recommendation 12***

*The committee recommends that, as part of its adoption of responsibility for the regulation of credit, the government make it compulsory for all credit providers to be a member of an external dispute resolution scheme approved by the Australian Securities and Investments Commission, as is currently the case for deposit-taking institutions.*