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Official Committee Hansard

SENATE

ECONOMICS LEGISLATION COMMITTEE

ESTIMATES

(Additional Estimates)

THURSDAY, 11 FEBRUARY 2010

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SENATE ECONOMICS
LEGISLATION COMMITTEE
Thursday, 11 February 2010

Members: Senator Hurley (*Chair*), Senator Eggleston (*Deputy Chair*), Senators Bushby, Cameron, Pratt and Xenophon

Participating members: Senators Abetz, Adams, Back, Barnett, Bernardi, Bilyk, Birmingham, Mark Bishop, Boswell, Boyce, Brandis, Bob Brown, Carol Brown, Bushby, Cash, Colbeck, Jacinta Collins, Coonan, Cormann, Crossin, Farrell, Feeney, Ferguson, Fielding, Fierravanti-Wells, Fifield, Fisher, Forshaw, Furner, Hanson-Young, Heffernan, Humphries, Hurley, Hutchins, Johnston, Joyce, Kroger, Ludlam, Lundy, Ian Macdonald, McEwen, McGauran, McLucas, Marshall, Mason, Milne, Minchin, Moore, Nash, O'Brien, Parry, Payne, Polley, Ronaldson, Ryan, Scullion, Siewert, Sterle, Troeth, Trood, Williams and Wortley

Senators in attendance: Senators Abetz, Boswell, Brandis, Bushby, Cameron, Colbeck, Coonan, Eggleston, Hurley, Joyce, Ian Macdonald, McGauran, Parry, Pratt, Ronaldson and Williams

Committee met at 9.01 am

RESOURCES, ENERGY AND TOURISM PORTFOLIO

In Attendance

Senator Wong, Minister for Climate Change and Water

Department of Resources, Energy and Tourism

Executive

Mr John Pierce, Secretary

Mr Drew Clarke, Deputy Secretary

Enabling Services

Ms Jo-Ann Rose, Chief Financial Officer, Enabling Services

Ms Nicola Morris, Chief Legal Counsel, Enabling Services

Mr Robert Towner, General Manager, Enabling Services

Resources and Energy Policy

Ms Tania Constable, Principal Adviser, Resources and Energy Policy

Resources Division

Mr John Hartwell, Head of Resources Division

Mr Chris Stamford, General Manager, Minerals Branch

Mr Martin Squire, Acting General Manager, Offshore Resources Branch

Mr Michael Sheldrick, General Manager, Fuels and Uranium Branch

Mr Peter Livingston, Manager, Offshore Petroleum Regulatory Reform Team

Ms Sue Kruse, General Manager, International, Resources Development and Taxation Branch

Mr Patrick Davoren, Manager, Radioactive Waste Section, Fuels and Uranium Branch

Ms Kristina Anastasi, Manager, Environment, Safety and Security Section, Offshore Resources Branch

Mr Mark Weaver, Manager, CCS Major Projects Section, Low Emissions Coal and CO2 Storage Branch

Ms Kathy Harman, Manager, International CCS Section, Low Emissions Coal and CO2 Storage Branch

Energy and Environment Division

Mr Brendan Morling, Head of Energy and Environment Division

Mr Bruce Wilson, General Manager, Environment Branch

Mr Oliver Story, Acting General Manager, National Energy Market Branch

Mr Geoff Whelan, Manager, Retail Policy, National Energy Market Branch

Ms Helen Bennet, Acting General Manager, Energy Futures Branch

Mr Paul Johnson, General Manager, Industrial Energy Efficiency Branch

Ms Louise Vickery, Manager, Energy Efficiency Opportunities, Industrial Energy Efficiency Branch

Ms Sarah Clough, Deputy CEO, Australian Centre for Renewable Energy

Mr Doug Cooke, Acting General Manager, Energy Security Branch

Mr Josh Cosgrave, Manager, Australian Energy Security, Energy Security Branch

Mr Peter Slobodian, Manager, Renewable Programs, Australian Centre for Renewable Energy

Mr Gino Grassia, Manager, Greenhouse Section, Environment Branch

Mr Rick Miles, Manager, APP Secretariat, Environment Branch

Mr Rick Belt, Acting General Manager, Environment Branch

Mr Gary James, Manager, Solar Flagships Projects

Tourism Division

Ms Jane Madden, Head of Tourism Division

Mr Wayne Calder, General Manager, National Tourism Policy Branch

Dr Peter Tucker, General Manager, Industry Development Branch

Mr Vic Dobos, General Manager, Tourism Research Australia

Ms Robyn Agnew, Acting General Manager, Market Competitiveness Branch

Geoscience Australia

Dr Chris Pigram, Acting Chief Executive Officer

Dr James Johnson, Chief, Onshore Energy and Minerals Division

Dr Clinton Foster, Chief Petroleum & Marine Division

Mr Gordon Cheyne, Acting General Manager, Corporate Branch

Mr Geoff McMurray, Chief Finance Officer

Tourism Australia

Mr Andrew McEvoy, Managing Director

Mr Grant Le Loux, Executive General Manager, Corporate

Ms Rachel Crowley, General Manager, Corporate Communications

CHAIR (Senator Hurley)—I declare open this public hearing of the Senate Economics Legislation Committee. The Senate has referred to the committee particulars of proposed expenditure for 2009-10 and related documents for the Innovation, Industry, Science and Research, the Resources, Energy and Tourism, and the Treasury portfolios. The committee has

set Thursday, 1 April 2010 as the date by which answers to questions on notice are to be returned. Under standing order 26, the committee must take all evidence in public session. This includes answers to questions on notice.

Officers and senators are familiar with the rules of the Senate governing estimates hearings. If assistance is needed, the secretariat has copies of the rules. I particularly draw the attention of witnesses to an order of the Senate of 13 May 2009 specifying the process by which a claim of public interest immunity should be raised, and which I now incorporate in *Hansard*.

The extract read as follows—

Public interest immunity claims

That the Senate—

- (a) notes that ministers and officers have continued to refuse to provide information to Senate committees without properly raising claims of public interest immunity as required by past resolutions of the Senate;
- (b) reaffirms the principles of past resolutions of the Senate by this order, to provide ministers and officers with guidance as to the proper process for raising public interest immunity claims and to consolidate those past resolutions of the Senate;
- (c) orders that the following operate as an order of continuing effect:
 - (1) If:
 - (a) a Senate committee, or a senator in the course of proceedings of a committee, requests information or a document from a Commonwealth department or agency; and
 - (b) an officer of the department or agency to whom the request is directed believes that it may not be in the public interest to disclose the information or document to the committee, the officer shall state to the committee the ground on which the officer believes that it may not be in the public interest to disclose the information or document to the committee, and specify the harm to the public interest that could result from the disclosure of the information or document.
 - (2) If, after receiving the officer's statement under paragraph (1), the committee or the senator requests the officer to refer the question of the disclosure of the information or document to a responsible minister, the officer shall refer that question to the minister.
 - (3) If a minister, on a reference by an officer under paragraph (2), concludes that it would not be in the public interest to disclose the information or document to the committee, the minister shall provide to the committee a statement of the ground for that conclusion, specifying the harm to the public interest that could result from the disclosure of the information or document.
 - (4) A minister, in a statement under paragraph (3), shall indicate whether the harm to the public interest that could result from the disclosure of the information or document to the committee could result only from the publication of the information or document by the committee, or could result, equally or in part, from the disclosure of the information or document to the committee as in camera evidence.
 - (5) If, after considering a statement by a minister provided under paragraph (3), the committee concludes that the statement does not sufficiently justify the withholding of the information or document from the committee, the committee shall report the matter to the Senate.
 - (6) A decision by a committee not to report a matter to the Senate under paragraph (5) does not prevent a senator from raising the matter in the Senate in accordance with other procedures of the Senate.

- (7) A statement that information or a document is not published, or is confidential, or consists of advice to, or internal deliberations of, government, in the absence of specification of the harm to the public interest that could result from the disclosure of the information or document, is not a statement that meets the requirements of paragraph (1) or (4).
- (8) If a minister concludes that a statement under paragraph (3) should more appropriately be made by the head of an agency, by reason of the independence of that agency from ministerial direction or control, the minister shall inform the committee of that conclusion and the reason for that conclusion, and shall refer the matter to the head of the agency, who shall then be required to provide a statement in accordance with paragraph (3).

(Extract, Senate Standing Orders, pp 124-125)

CHAIR—The committee will begin today's proceedings with the consideration of the Resources, Energy and Tourism portfolio with the tourism issues for the department, and will then follow the order as set out in the circulated program.

[9.02 am]

Department of Resources, Energy and Tourism

CHAIR—I welcome Minister Wong, representing the Minister for Tourism, and officers of the department. Minister or officers, would you like to make an opening statement?

Senator Wong—I do not.

Mr Pierce—No. We are happy to take questions.

Senator EGGLESTON—We are in two parts again this time, aren't we? We combined both parts last time, didn't we?

Mr Pierce—Yes. The way I read the timetable, the first half-hour is tourism within the department and the second half-hour is Tourism Australia.

Senator EGGLESTON—Is the department undertaking any additional research as a result of the Sustainable Tourism Cooperative Research Centre losing its funding? Have you found an alternative source of funds or an alternative body to do research into the industry?

Mr Pierce—You will recall from the last estimates that, with the transfer of Tourism Research Australia from TA to the department, a tourism research board was established with me, the chair of TA and representatives from the industry to establish a framework and to guide the research effort, not just of the department but also of other people who are undertaking research. We can give some guidance as to what sort of research would be the most productive to undertake.

In the context of doing an audit or a stocktake of the type of research that is done at the moment within the industry, universities and the public sector, the sort of work that TRA was doing is part of that review. The members of the board are trying through that process to leverage off their past work but also the expertise and the people who were involved and give them some guidance as to what things are worth while doing and to make sure that that expertise is not lost or dissipated into other areas.

That process is ongoing. The audit is being undertaken at the moment. The board is meeting again next week to receive a report on that. So, whilst I cannot say that all of that will be retained, I am certainly hopeful that a significant proportion of it will be. Perhaps, more

importantly, through the board we have a high degree of confidence that the sort of research that is being undertaken collectively around this sector is of the most value to the sector and has the highest utility.

Senator EGGLESTON—It is obviously very important that research goes on. I am very surprised that the Sustainable Tourism Cooperative Research Centre is no longer being funded. What kind of funding do you have for this new body that you have set up? What kind of budget do you have?

Mr Pierce—I will ask Jane to answer that specifically, but essentially the resources that were previously in TA have simply been transferred across to the department. There is not an increase in the aggregate amount that is available within the public sector, but what I am trying to do through this board is leverage off that with the universities, for instance. I will try to get a higher amount of research for the funding that comes through this department—obviously the universities are publicly funded—

Senator EGGLESTON—So these are universities with tourism as a course? They are the technical universities like Curtin in Perth?

Mr Pierce—Yes, and they have members of staff with an interest in this sector. I think it is important to indicate to them that that sort of work is still valued—

Senator EGGLESTON—Indeed.

Mr Pierce—not just by the government but by the industry, perhaps more importantly, and that their skills can be useful in that direction, so they do not start to get interested in other areas and wander off.

Senator EGGLESTON—Is the department producing or involved in the production of state tourism satellite accounts?

Mr Pierce—We fund the production of those accounts and the continuation of them was certainly the subject of conversation between us and the states.

Senator EGGLESTON—Were they friendly conversations?

Mr Pierce—Yes. Everyone sees the value of those satellite accounts and is looking at ways to be able to continue to produce them. Not just us but also the states are very keen to make sure that happens.

Senator EGGLESTON—That is very good.

Mr Pierce—If you were to rank different types of statistics and research in priority order, it would be fair to say that those satellite accounts would be fairly close to the top of the list of everyone who sits around that table.

Senator EGGLESTON—I would like to ask you about the provision of accurate, timely and effective policy advice to the minister and the government on tourism related issues. I refer to page 30 of the department's 2007-08 annual report, where it says:

The Department provided an evaluation regarding the impact of the Tourism White Paper in April 2008 to the Australian Government.

I understand that two requests have been made by the shadow minister for this evaluation to be made available to the shadow minister but neither have been responded to. Why is that so?

Mr Pierce—We will take that on notice, if you do not mind, so we can get to the bottom of it for you.

Senator EGGLESTON—Thank you. I understand there is also an audit on notice. Would you be able to table that as well?

Mr Pierce—An audit on notice?

Senator EGGLESTON—That is what I am advised.

Senator Wong—Are you able to give us some clarity around that. An audit document has been sought?

Senator EGGLESTON—With respect to the activities of the department, I would gather.

Senator Wong—It is a little hard for us to understand which document you are seeking with that sort of information.

Senator EGGLESTON—All right, I will put that on notice.

Senator Wong—Thank you.

Senator EGGLESTON—The development of the National Long-Term Tourism Strategy to provide a strategic framework for engagement with the tourist industry: can you tell us how much funding will be allocated for each recommendation in the Long-Term Tourism Strategy?

Ms Madden—You will recall the minister launched the National Long-Term Tourism Strategy in Western Australia, in Perth, on 15 December. I believe you were there, Senator.

Senator EGGLESTON—Yes, that is right.

Ms Madden—As part of that overarching framework, a number of key working groups were established to scope and put forward work programs to deliver the achieved outcomes. Those working groups have been meeting since the release of the strategy. All of them are scoping the required budget and resources, and meetings will be held in coming weeks to take that forward in 2010-11 budget context.

Senator EGGLESTON—So you cannot give me specific figures about how much money will be allocated for each of the recommendations?

Mr Pierce—No, not at this point. You would appreciate that a lot of the work that is going to be undertaken is not just being undertaken by the Commonwealth. It is a key part of the process to bind the states and the Commonwealth—

Ms Madden—And industry.

Mr Pierce—and industry, of course—so that they work together. There will be work that we will be undertaking, but we will be doing it in concert with the other two. The process that Jane referred to is reporting back to the Tourism Ministers' Council in April, and it is really from that point that decisions about how much funding—not only Commonwealth funding, but also resources from the states and in the industry—will sit behind each of those recommendations.

Senator EGGLESTON—I would now like to turn to the implementation of a national tourism accreditation framework working with relevant partners to improve the quality of

tourism products and services. I understand this has not been put into operation yet. Is that the case?

Ms Madden—That is the case. As you know there has been extensive discussion and some progress on this accreditation framework. It is a key deliverable under one of the work plans of the National Long-Term Tourism Strategy and will be the subject of discussion at that forthcoming tourism ministers' meeting, which the secretary referred to.

Senator EGGLESTON—That was an election commitment of the Rudd government and two years have now passed. Would the minister like to comment on the commitment of the government to this program? Two years is quite a while.

Senator Wong—I am sorry, Senator?

Senator EGGLESTON—I am surprised that two years has passed without it being implemented.

Mr Pierce—Good progress has been made, particularly in the last couple of months. The starting position was essentially a lot of different accreditation frameworks across the country and different parts of the sector that were inconsistent with one another. It took a bit of time to get acceptance of the need for a national accreditation framework. Having got that acceptance, the work that is going on at the moment is really down to the mechanics of what is going to be measured, how it is going to be judged. It is going to be voluntary, so we have to convince people that it is worth the while of each individual business that it is going to help them to be part of this process. It is really not something that you can sit there and—I suggest it would not be successfully implemented if you just try to dictate to the industry that this is what is going to happen. So the time up until now has been about bringing people along. I think that has been achieved. Now the discussions are around how to do it rather than whether to have it or not.

Senator Wong—Senator, in your more-than-a-decade in government, was there an accreditation framework under your government?

Senator EGGLESTON—Things move on, you see, Senator—

Senator Wong—Yes, we were elected and we are—

Senator EGGLESTON—and this is seen as a way of evaluating the industry. We ask the questions, as I understand it.

CHAIR—Well—

Senator Wong—Sorry, Chair.

CHAIR—Please go on, Senator.

Senator ABETZ—She does go on.

CHAIR—Senator Abetz, that is not helpful.

Senator Wong—The officers have provided an outline of the way in which work has been progressing in relation to this commitment.

Senator EGGLESTON—Yes, we accept that, and we do hope that it is put in place in a fairly short period of time. I would like to ask about improved access by overseas visitors to

Australian consumer protection. Will the department explain to the committee how access by overseas visitors to Australian consumer protection has improved over the last financial year?

Ms Madden—There have not been any significant changes to access by international visitors to consumer protection over the last year. However, I can note that the Treasury is currently conducting a review into access for consumer protection and we are actively involved in that.

Senator EGGLESTON—Is there a key performance indicator for this?

Ms Madden—The Treasury, as I said, is managing this. We have some supplementary initiatives that afford consumer protection. I think we have outlined those previously. These include an online complaint service, which is undertaken by Dr Tucker's area in the department. We are trying to afford, within the existing framework, the maximum access to consumer protection for international visitors. Indeed, the accreditation program, which the secretary outlined, is also part of this effort to lift quality in the industry and afford maximum protection to visitors, both international and domestic, in the tourism industry.

Senator EGGLESTON—Having an online complaint service is very good. Do you pass that through to the relevant bodies that are being complained about?

Dr Tucker—The complaints received through the online complaint form are passed through to the Office of Fair Trading in the relevant jurisdiction for their action. We, in collaboration with them, monitor the progress with particular complaints that might be made. The other information, the other resource we provide for tourists, is information about their consumer rights in Australia. Firstly, we publish material on the web and in hard copy for tourists so that they understand what their rights are. Secondly, we provide information to the tourism industry, the tourism operators, about their obligations under consumer protection laws.

Senator EGGLESTON—That is very good. Now I would like to ask you about the TQUAL Grants program and other tourism related programs, as required. For each of the grant recipients under the Australian Tourism Development Program and the TQUAL Grants program, will the department table a list of which grant recipients the minister visited from 1 January 2008 to 31 December 2009. Could you do that for us?

Ms Madden—Subject to the minister's agreement.

Mr Pierce—We will have to take that on notice.

Senator EGGLESTON—Yes, it has to be on notice because you need to do a little bit of research there. I would like to ask you about policy initiatives to support Indigenous tourism and engagement with relevant partners to support Indigenous tourism development in selected regions. Again, can the department table a list of what policy initiatives have been developed to support Indigenous tourism development?

Mr Pierce—We can certainly take that on notice. I note that one of the working groups under the National Long-Term Tourism Strategy has been given a brief to cover that area specifically. So it is an area of particular focus.

Senator EGGLESTON—Yes, it is a very important area because there is great scope for Indigenous tourism, especially in the north of Australia.

Mr Pierce—That is one of our differentiating factors of it, I would suggest.

Senator EGGLESTON—I understand that. I would now like to ask you about engagement with key stakeholders to ensure that tourism interests are taken into account in the broader context of government policy development and implementation, including in relation to labour and skills and regulatory issues that impact tourism. I have a copy of a letter from the Queensland Tourism Industry Council which expresses concern about the impact of the government's modern awards system on the tourism and hospitality industry. In the letter the council proposes that the process of rationalisation of existing tourism and hospitality awards does not recognise the diversity of the tourism and hospitality industry, will significantly increase labour costs and will also act as a disincentive for tourism and hospitality businesses to employ and retain staff. It raises concerns about how the modern awards will increase labour costs. It says that this could result in decreased visitor services because of staff shortages and that the loss of flexibility in working arrangements will not only threaten employers' capacity to create and retain jobs in the industry but will also disadvantage those workers who seek the currently flexible employment opportunities that the tourism and hospitality industry is able to offer. The council does point out that this is an industry which is grossing something like \$70 billion a year, which is 6.5 per cent of Australia's total GDP. It is an important industry. I wonder whether the minister would like to comment on the application of the awards to the tourism industry.

Senator Wong—I suspect that that should probably be a question directed to the department of employment, education and workplace relations or the Department of Education, Employment and Workplace Relations—I often get the two 'Es' mixed up. I realise that members of the opposition would still like to implement Work Choices and dislike the fact that the government has implemented its election commitment—Senator Abetz, I know, is particularly amongst those—but we have, and we will. If you have questions—

Senator Abetz interjecting—

CHAIR—Can we allow the minister to finish.

Senator ABETZ—It was a most gratuitous offence.

CHAIR—Minister.

Senator Wong—Thank you, Chair. If you have questions about the government's industrial relations framework, they should probably be addressed to the appropriate department, Senator.

Senator EGGLESTON—I take that point, but if this industrial relations system has a particular impact on this industry then I would have thought that the industry spokesman might have had some thoughts about it.

Senator Wong—The government's position on industrial relations is perfectly clear and was made very clear at the last election. If the officers have something to add about what engagement the portfolio has had with DEEWR on this issue, I am happy for them to do so.

Senator EGGLESTON—Thank you, Minister. If they would like to, that would be appreciated.

Ms Madden—As the senator noted, the employment standards in modern awards fall within the portfolio of DEEWR, but we do have a very active dialogue with that department. We are monitoring the effects of modern awards on the tourism sector. We have lot of contact with stakeholders, as you noted, such as industry groups, including the Queensland Tourism Industry Council. In fact, Senator, the labour and skills issues to which your question relates are also part of the working groups set up under the government's National Long Term Tourism Strategy. We can table the work program that is occurring under labour and skills in this public document, which is the work program supporting the National Long Term Tourism Strategy, which was released publicly by Minister Ferguson in December. That clearly outlines the types of issues that we are seeking to address that have been brought forward for the tourism sector by industry and other stakeholders that we are talking with DEEWR and others about.

Senator EGGLESTON—Thank you very much.

Senator PRATT—As I understand it, the tourism industry in Australia is worth about \$40 billion. Is that right?

Ms Madden—That is correct.

Mr Pierce—It is a bit over that, yes.

Senator PRATT—Can you tell me where tourism sits in relation to the service industry as a whole, in terms of its significance to Australia?

Ms Madden—Yes. According to the ABS 'tourism satellite', services in tourism account for over 10 per cent of Australia's services exports. They actually account for a 3.6 per cent share of the total economy. So it is a leading export industry and a leading part of the economy. We have other data that we can also provide in terms of employment, gross value-added figures and others statistics, if you wish.

Senator PRATT—Yes. As I understand it, tourism currently directly employs about half a million people. But I wanted to ask how our tourism workforce is going—what the key challenges and risks are going into the future and what the government is doing to address those.

Mr Pierce—I will let Jane talk about how we are addressing that through the National Long Term Tourism Strategy.

Ms Madden—You are correct, Senator, in saying that about half a million people are directly employed in the industry. The indirect impact of tourism on the employment market is even greater. Given that it is also a highly labour-intensive industry, we have been actively involved, as I mentioned earlier, in discussions with the Department of Education, Employment and Workplace Relations on the whole training and skills agenda. That is an important element of the government's National Long Term Tourism Strategy, with some key outcomes that we are required to report to ministers on over the next few years so that we can ensure that the needs of skilling and employing such a large proportion of the Australian population are effectively met.

Senator PRATT—And what are the key challenges in that task, as far as finding the workforce that the industry needs?

Ms Madden—Let me just outline a few.

Mr Pierce—I think it would be true to say, Senator, from the viewpoint of the industry one of the constant themes coming through to us goes to the skill levels within the industry. I think the industry has an image of having a low-skilled workforce. There are certainly forms of employment within the sector that are at the lower skill end, but the demand, if you like—what people are asking for, and where there is a sense of undersupply—is in that high-skilled part of the sector. Hence the focus of the working groups and some of the things that Jane has been involved in across other agencies.

Ms Madden—The industry skills council Service Skills Australia released last year a tourism and hospitality workforce development strategy and, as the secretary outlined, skills were one of the key challenges. Other challenges—and we are happy to table this report if you would like—included workforce planning. For example, what if there are gaps, particularly given that tourism is the major employer in rural and regional Australia. Recruitment and retention were also another challenge. So we have a range of initiatives and work underway in this national, long-term strategy working group to try and better address these challenges moving forward.

Senator PRATT—I would assume that different regions around Australia have slightly different needs as far as the kinds of skills they are looking for. How is the government balancing that out in its strategy?

Ms Madden—Your assumption is definitely correct. It is a work in progress, I think. But we would be happy, as I said, to table the report by the industry skills council, which is a key input, and that outlines some specific regional and subregional initiatives that will be important if we are to encompass all aspects of the challenges.

Senator PRATT—Okay. Thank you.

CHAIR—We have reached 9.30 am, but I understand Senator Abetz has a quick question.

Senator ABETZ—Yes, quite brief. There are two tourism grants that I have canvassed at previous estimates. The first one was to the Apex Club in Tasmania. I understand that has now been resolved to the satisfaction of both parties. Can you confirm that that is the case?

Mr Pierce—Yes, Senator.

Senator ABETZ—Thank you. Was it resolved with a financial contribution to the Apex Club?

Mr Pierce—In terms of the final settlement—is that what you are after?

Senator ABETZ—Yes.

Mr Pierce—When we settled it, the club returned an outstanding amount from a grant that was provided earlier which was a bit over \$13,000.

Senator ABETZ—Do you want to add to that, Ms Madden?

Ms Madden—I can just add that the club did return the majority of the grant funds and then, as you say, there were some negotiations regarding retaining a portion of the claimed project expenditure.

Senator ABETZ—Are you able to tell us how much they were allowed to retain?

Ms Madden—Yes. It was \$33,745 plus \$5,302.50 in relation to the administration of the project.

Senator ABETZ—It was the \$5,300 figure that was really the sticking point, wasn't it?

Ms Madden—It was the balance of funds that was—

Senator ABETZ—That's right; they were not repaying the balance of funds until there was some agreement in relation to a small or modest contribution for their activities.

Ms Madden—Yes, and that balance was \$33,745—

Senator ABETZ—That was the total—

Ms Madden—plus an additional \$5,000.

Senator ABETZ—Yes. Can you tell us the total legal costs that have been incurred in this matter?

Ms Madden—Yes, I can. The final legal cost—and the legal adviser is here—for the full recovery of grant funds was \$30,152.10, and that was—

Senator ABETZ—\$30,000 was spent arguing with a volunteer community organisation about whether they might be allowed to withhold a few thousand dollars in recognition of their volunteer activities?

Ms Madden—The amount outstanding, as noted, was a considerable proportion: \$250,000. We acted at all times in accordance with the Commonwealth legal guidelines. These were followed to the letter in relation to recovery of unspent funds.

Senator ABETZ—If not the spirit. How does that make sense? What commercial entity would have spent \$30,000 on action against a volunteer community organisation when the actual dispute, the real dispute, was only about how much money they would be allowed to retain for their volunteer activities? And it appears that that has been resolved at around the \$5,000 figure. So we spent six times that amount and we could have resolved it without causing pain to the organisation and the volunteers.

Ms Madden—As we have noted previously, we were keen to settle this matter as soon as possible, and both parties have reached an amicable settlement, so—

Senator ABETZ—We know all that.

Ms Madden—we are very happy that that has taken place.

Senator ABETZ—Yes, we know all that, but this settlement has cost the Australian taxpayer an extra \$30,000, whereas had a common sense approach been taken earlier one and recognition had been given to the club for its activities, the Australian taxpayer would have been better off and the matter would have been resolved earlier.

Senator Wong—You have managed to put a whole range of assertions on the *Hansard*. I am not sure whether officers want to add anything, but this was in relation to a funding commitment announced by the coalition in 2001. It was a quarter of a million dollars—

Senator ABETZ—Chair, with respect, we know all this. This has all been canvassed at previous estimates, and it is a winding down of the clock. It is irrelevant to the question.

CHAIR—Senator Abetz, you asked quite a long question that contained a number of aspects. I think the minister is entitled to answer.

Senator Wong—Through you, Chair, the senator made a range of assertions and I would like to place on record some of the facts. A quarter of a million dollars –

Senator ABETZ—On a point of order, Chair: I did not make any assertions about when the grant was made.

CHAIR—Senator Abetz, I am quite happy to continue this discussion for as long as possible, but I will point out that we are at the end of the time for the department and the minister is still to complete her answer. Then we can move on.

Senator Wong—I simply make the point that this concerns a coalition election commitment made in 2001 providing—

Senator ABETZ—Yes, we know that.

Senator Wong—Are you intending to interrupt me the entire morning, Senator?

Senator IAN MACDONALD—Oh, get on with it.

Senator ABETZ—It all depends how useless your answers are.

Senator WONG—Oh, Senator Macdonald is here, whose only contribution to estimates generally is to elevate the level of rudeness in the room.

Senator IAN MACDONALD—Minister, you are so pathetic—you should take a lesson from some other useless—

CHAIR—Order! Interjections will finish. We will continue with the minister's answer and then we will get onto the next part of the department of tourism. Minister, can you complete your answer. Discussion on either side of me will cease.

Senator Wong—This was a project announced by the coalition in 2001 for a quarter of a million dollars. It was in 2008 that the department advised the club of this decision to terminate the contract. This is a significant amount of money in terms of talking about taxpayers' funds. The majority of the funds were returned—\$225,743.22—and there was an issue as I understand it from the officers in relation to claimed project expenditure and administration which has now been resolved. The advice we have is that at all times the department acted in accordance with Commonwealth legal guidelines.

Senator ABETZ—That adds absolutely nothing more to what has already been provided.

CHAIR—Do you have a further question, Senator Abetz?

Senator ABETZ—I do. Can we be told how much money has been spent on legal costs in relation to Willow Court to date? I understand that matter has not been resolved.

Ms Madden—I am happy to advise that that one has also been resolved.

Senator ABETZ—Good. When was that resolved?

Ms Madden—Just in December.

Senator ABETZ—Do you have a date for that?

Ms Madden—It was just before Christmas—

Senator ABETZ—Take it on notice—nothing turns on it. How much were the legal costs?

Ms Madden—Total legal costs to the end of January did total \$70,576.77. That was with regard to the recovery of remaining grant funds of \$475,000. There have been extensive negotiations, as you know, and we have reached a settlement of mutual agreement.

Senator ABETZ—And that was with the Derwent Valley Council?

Ms Madden—That is correct.

Senator ABETZ—Is Valley Vision involving that at all, or just the Derwent Valley Council? They were the auspicing organisation or whatever it is called?

Ms Madden—The funding was to the Derwent Valley Council, that is correct, for the Willow Court project.

CHAIR—Thank you to the Tourism section of the Department of Resources, Energy and Tourism. I now ask Tourism Australia to come to the table.

[9.39 am]

Tourism Australia

Senator EGGLESTON—Will Tourism Australia or the minister at the table, even on notice, explain the circumstances around why the deputy chair, Mr Andrew Burns, left the board, and did he leave voluntarily?

Mr Pierce—So you have asked for that on notice, Senator?

Senator EGGLESTON—No, I would rather have an answer now. If you could provide us with an answer now I would appreciate it.

Mr Pierce—I am not in a position to answer that, I am afraid, at the moment. I am perfectly happy to take it on notice and provide it to you.

Senator EGGLESTON—This question is about the recruitment and training of travel agents through the Aussie Specialist Program. How many travel agents have been recruited under this program?

Mr McEvoy—We have around 25,000 Aussie specialists globally.

Senator EGGLESTON—That is a lot.

Mr McEvoy—It is.

Senator EGGLESTON—How many have completed training under this program?

Mr McEvoy—I think that is the number of people who have completed training. It is an ongoing program; they do various modules and get better and better. It is a great program.

Senator EGGLESTON—It sounds like it, if you have 25,000 graduates from it. Regarding the rephasing of the \$9 million Tourism Australia funding from the 2009-10 to 2010-11 budget, what will this funding be used for in 2009-10? Will it be for a domestic campaign, an international campaign or both?

Mr McEvoy—It is mainly focused on short- to medium-haul markets. The \$9 million brought forward by the government has been added to by \$11 million of industry money, so there is a total of \$20 million. There are about 62 campaigns, predominantly into what we could call short-haul markets, like New Zealand and Asia—China, India, Singapore, Indonesia et cetera. So it is terrific stuff. The industry has really come to the party. It is like pouring some water on what they are calling the green shoots of recovery. It is about tactical marketing to get people to travel from shorter haul markets in the shorter term.

Senator EGGLESTON—Regarding the rephasing of the \$9 million Tourism Australia funding from 2010-11 to 2009-10, what will Tourism Australia not do in 2010-11 that it would have ordinarily done with that money? In other words, where have the cuts been?

Mr McEvoy—What the money has done is brought forward activity. As I said, with \$11 million from the private sector, it has been a good time to invest the money. We think we will also get some gains in terms of foreign exchange next year and perhaps be able to buy a little bit better also, so we will manage that through our normal process. But it was a good example of how the private sector is willing to work with us, so we are quite confident we will run a normal range of programs in 2010-11.

Senator EGGLESTON—Thank you. What is Tourism Australia's total annual domestic spending?

Mr McEvoy—It is \$8.4 million. Just to add to that, there are a lot of programs we run nationally and globally that would add value to that, but that is the specific domestic spend.

Senator EGGLESTON—Can you confirm that, as a result of the rephasing of the 2010-11 government appropriation, this will be the lowest appropriation since the Australian government tourism white paper of 2003—the smallest amount since 2003?

Senator Wong—Senator, to which appropriation are you referring? Is this given the bring-forward—is that the assertion?

Mr McEvoy—I beg your pardon?

Senator Wong—Are you relating this to the bring-forward? I was not clear from your question.

Senator EGGLESTON—I do not know that I am, necessarily, but I am talking about a total government appropriation to the industry, which is apparently the lowest since the government's tourism white paper in 2003. So it would seem the total amount going to tourism under this government is the lowest since 2003. Is that something you can confirm?

Mr Pierce—Senator, I am happy to take on notice the actual numbers back to 2003. Prior to this bring-forward, at least in the last couple of years, I suppose the impression I had was that the total amount of funding going to TA was being held relatively constant. As to how that relates to the situation in 2003, I would have to dig out some numbers for you.

Senator EGGLESTON—Perhaps you could provide all the figures for us on notice so that we can really see what the status of funding for tourism—

Senator Wong—Which figures?

Senator EGGLESTON—The bring-forward and the total appropriation for tourism.

Senator Wong—Well, that is all in the budget papers, but I am sure we can do that.

Senator EGGLESTON—If you would be kind enough.

Senator Wong—We will see what we can do, Senator.

Senator EGGLESTON—Thank you. International tourism seems to have dropped somewhat, I am told. I wonder if you could tell us how the figures from China, Japan and India are going.

Mr McEvoy—The figures from China and India certainly grew again last year. Japan has been a difficult market for us. They have had a fairly flat economy. The yen has not been so strong against our dollar, and we had the added problem last year of H1N1. Our Japanese market is a great market for Australia but, when those things come up, they tend to stay at home a bit more and not travel. So it was a tough year in terms of Japan, but the figures for both India and China grew last year. The ABS numbers just came out to December last year, and Australia was reasonably flat overall, which was actually regarded by the industry as a fairly good effort. The global forecasts were for a four per cent decline in tourism movement around the world, and Australia held its own and had no decline at all. So our inbound numbers—while we would all like to see growth, and we believe we will see growth in 2010—have held up quite well. Interesting, to give you the specific numbers, overall growth was eight per cent last year, delivering some 124,000 passengers.

In fact, in the month of December, the figures from India grew by 15 per cent. So we know there are some issues there, but so far the people are still travelling, which is terrific. The figures for China grew last year by three per cent to over 356,000 visitors—certainly not the higher levels of growth we had in previous years but still terrific growth in a tough year. Japan, as you said, had a very difficult year; the figures had dropped about six per cent in December. But, overall, the value of the money spent by the Japanese has remained fairly level—there was a drop of one per cent—so they are still terrific, high-spending, high-yielding visitors for our country.

Senator EGGLESTON—Tell me your numbers for outgoing internationals. Can we identify outgoing holidaymakers as against business travellers and so on?

Mr McEvoy—Are you talking about Australians going out?

Senator EGGLESTON—Yes.

Mr McEvoy—There has definitely been growth in Australians travelling overseas, with our strong dollar and a lot of low-cost carriage in new airlines. I would have to take on notice the specifics about the leisure element of that. I believe outbound growth is eight per cent year on year, generally, but that would include all sectors: employment, education, business et cetera. If you wanted me to give you the specific leisure number, we could get that.

Senator EGGLESTON—If you could do it on notice I would be grateful. Thank you.

Senator IAN MACDONALD—Mr McEvoy, I found out from environment estimates that the environment management charge which funds GBRMPA and is taken from tourist travel to the Great Barrier Reef, the Whitsundays and Cairns, is about steady with this time last year—last year it was disastrously low but it has not got worse. I appreciate there is concern at government level—as there certainly is in Cairns and to a lesser extent in the

Whitsundays—about the huge fall-off in tourism traffic. Can I ask—and I apologise for my parochialism—what are Tourism Australia specifically doing to encourage people into Cairns and Port Douglas, which as you know, are very dependent on tourism.

Mr McEvoy—It is a good question, Senator. Tourism Australia promote the whole country but North Queensland is definition a very important part of our tourism offering, with two World Heritage listed environments up there that are phenomenally popular with visitors. We have worked really hard with the people of North Queensland and also Tourism Queensland. For example, with the \$9 million brought forward, matched by \$11 million of industry money, a lot of effort is going into North Queensland, including a lot of charter services out of China. So there is a lot more stimulation of direct services out of China through charters, through the Chinese New Year period.

I will give you some numbers, if you like. About 870,000 of the \$9 million that was brought forward has been specifically allocated for consumer marketing for tropical North Queensland. Of course, the industry is matching that. About \$280,000 of that was invested in support for those charters. There are probably going to be about 18 charters out of China alone, which will bring an extra 5,300 seats out of China. So there is a lot of short-term tactical effort. Talking to the operators up there, to Rob Jason, who runs Tourism North Queensland, the domestic market has been pretty good for them. They believe the inbound business is coming back. If you want me to go on, there are a lot of other programs that we have done.

Senator IAN MACDONALD—Because time is short, would you mind just dropping me a brief note on the other programs.

Mr McEvoy—Sure.

Senator IAN MACDONALD—You mentioned some figures coming in from China. I forget what period you said that was for. Could you just give me some statistics on what is coming in from China.

Mr McEvoy—Sure. For North Queensland generally?

Senator IAN MACDONALD—Yes. The Whitsundays and Cairns.

Senator Wong—Can I just check something, Senator. I assume dropping a brief note means providing the answer on notice?

Senator IAN MACDONALD—Yes, but just dot points on the figures. Just give me the bare facts. There are just two other quick matters. Singapore is a significant market with a very wealthy population looking to travel. Can you, either now or on notice, tell me what emphasis there is on it and what details are going into the Singapore market?

Mr McEvoy—I will take that now, if that is okay. Singapore is an essential market for Australia. It has been a terrific performer for Australia in recent times. In the year ending December—that is, the last calendar year—we had five per cent growth out of Singapore. In the month ending December we had seven per cent growth, so it is going well. Really importantly, going to your point about the high spending, the value of the market grew also. So it is a terrific market. It generates just under \$1 billion worth of tourism expenditure for Australia. We have a great office up there. You have perhaps met Brent Anderson, our guy up

there. The other big part of Singapore is our strategic relationship with Singapore Airlines. That is one of the great many carriers that come into our country. So we would concur that there is a lot of activity up there. We have seen terrific growth in the last year.

Senator IAN MACDONALD—Is much of that going to the Whitsundays or Far North Queensland, bearing in mind that Singapore, whilst a lovely country, does not have much in the way of beaches, coral reefs and rainforest—although there are a few across the strait.

Mr McEvoy—Yes. The Singaporeans know Australia well. A lot of them have been often before. There is a good repeat visitation rate. They are what we call mono-destination travellers; they go to places they really enjoy. I would have to check the amount that are heading to the Whitsundays and to North Queensland. But they do love our country, disperse reasonably well in our country and come back again and again. So they are good visitors.

Senator IAN MACDONALD—Finally from me, there is a road that goes, effectively, from Cairns and Townsville to Perth—from Winton to Laverton—called the Outback Way. It goes right across the centre of Australia. I have been told that the outback highway council have done one of those very detailed maps and have combined with Hertz or Avis to do a program, marketed mainly into Germany, where you hire a car in Perth and drive across to Cairns and stop on the way at any number of magnificent natural sites. It is a two-week thing, I understand. Are you aware of that? Are you helping with that? Do you have any stats on that or any projected spending assistance for that program?

Mr McEvoy—I am not specifically aware of it, but I would agree that the German travellers and Europeans generally love our open spaces and our outback. I know that a lot of work is done particularly in Germany but also in Switzerland, Austria and Scandinavia on that type of trip. I know that South Australia and the Northern Territory have one called the Explorer's Way, up through the middle from Adelaide to Darwin, or from Kangaroo Island to the Tiwi Islands. Our marketers in those markets would work with the wholesalers to put self-drive itineraries together for those people. But I do not have the specifics in front of me.

Senator IAN MACDONALD—On notice again, could I just alert you to that. Could you get your people to look at it to see if you are involved and, if you are not, if you could be and how you might be able to help in what is a very significant market, not just for tourism but for a lot of the Indigenous communities on the way. It is likely to be their lifeblood into the future.

Mr McEvoy—Absolutely.

Senator EGGLESTON—Could I ask that the audit of research that the department referred to be tabled or provided on notice.

Mr Pierce—I cannot see why not, but let me check. Of course you understand that the audit has not been completed as yet and it would be our intention, as I said, to do so through this research board when we have done that. The purpose is to identify where there are research gaps and what we should be doing going forward. As for the audit going to the board, with the way I am chairing this board I would expect that members of the industry who are on that board would share that information with the organisations that they represent, hence I cannot see a reason why it should not be tabled because it will be out there in the

industry. Allow me to qualify that by saying I would obviously need to check with the minister, but I cannot see a reason why it would not be.

Senator EGGLESTON—I understand that, but if you can that would be appreciated. The last thing I would say is there is another road from Alice Springs to the Kimberley, called the Tanami Road. I think the Tanami Road should be upgraded. It is a major tourist connection.

Senator Abetz interjecting—

Mr Pierce—The quality of the road is part of the adventure.

Senator IAN MACDONALD—Senator Abetz wants to add the Launceston to Hobart road as an outback way.

Senator ABETZ—We could make it a dual carriageway.

Senator EGGLESTON—You could call it the Cheese Highway.

CHAIR—While we are being parochial I will ask this of Mr McEvoy, who understands South Australia very well. There is a perception in South Australia that the state misses out on a lot of the international visitations. I just want to check if that is so and if there is anything being done to address that.

Mr McEvoy—South Australia gets just under eight per cent of total inbound visitations. It does very well out of the UK and Europe. Almost one in four Germans visit South Australia. The French are a big market, so are the Italians. There are places like Kangaroo Island and the Flinders Ranges. This was all set up to do a sell job on South Australia! No, it is a terrific place. Probably the issue for South Australia is really the number of nights in the yield. It could do better. It is getting about eight per cent of the business but probably under five per cent of the actual nights and dollars. That is really the thing, and that is probably a longer term infrastructure thing for the state. But they are really investing in a lot of new infrastructure—places like Southern Ocean Lodge on Kangaroo Island, the new Port Lincoln Hotel. Yes, I do know South Australia well. It is a terrific part of the great Australian journey.

CHAIR—In terms of improving infrastructure, are there any state or federal government programs to specifically address that?

Mr Pierce—Firstly, the infrastructure part of the stimulus package included an infrastructure component that I think is seen as supporting the tourism sector. The specifics of that in relation to South Australia I do not have here, I am afraid. We could look at that.

CHAIR—I am happy for you to take that on notice, if you would like.

Senator IAN MACDONALD—Mr Pierce, could you extend that to where all of the stimulus package money on tourism has been spent, not just South Australia but across Australia?

Mr Pierce—It is about infrastructure which we are saying has a relationship with tourism—and people referred to roads before, for instance. We are quite happy to see what we can find, but I think it is more appropriate for that to be a question to the infrastructure department, who will have the total amount available. But I can go and look for it.

Senator IAN MACDONALD—All I am saying is what you are doing for South Australia you can do for other states as well.

Mr Pierce—We will see what we can do for you.

Senator IAN MACDONALD—Thank you very much.

Senator RONALDSON—Madam Chair, I will have some questions on notice which I will put to Mr McEvoy.

CHAIR—As there is nothing further, I would like to thank the Department of Resources, Energy and Tourism and, in particular for this morning's evidence, its tourism section. Thank you for coming in. I thank the minister too. We will now move on to the Treasury portfolio.

[10.00 am]

TREASURY PORTFOLIO

In Attendance

Senator the Hon. Nick Sherry, Assistant Treasurer

Department of the Treasury

Dr Ken Henry, Secretary

Outcome 1: Sound Macroeconomic Environment

Output Group 1.1: Macroeconomic Group

Dr David Gruen, Executive Director

Mr Tony McDonald, General Manager, Macroeconomic Policy Division

Dr Steve Morling, General Manager, Domestic Economy Division

Mr Adam McKissack, Principal Adviser, Forecasting, Domestic Economy Division

Mr Paul Flanagan, General Manager, International Finance Division

Mr Bill Brummitt, General Manager, International Economy Division

Mr Damien Dunn, General Manager, Macroeconomic Modelling Division

Mr Robert Ewing, Manager, Macroeconomic Modelling Division

Outcome 2: Effective Government Spending Arrangements

Output Group 2.1: Fiscal Group

Mr Nigel Ray, Executive Director

Ms Peta Furnell, General Manager, Social Policy Division

Mr Peter Robinson, Principal Adviser, Social Policy Division

Mr Steve French, General Manager, Industry, Environment and Defence Division

Mr Russ Campbell, Principal Adviser, Industry, Environment and Defence Division

Ms Natalie Horvat, Manager, Industry, Environment and Defence Division

Ms Kirsty Laurie, Senior Adviser, Industry, Environment and Defence Division

Mr Scott Rogers, Senior Adviser, Industry, Environment and Defence Division

Mr Kurt Hockey, Manager, Industry, Environment and Defence Division

Ms Penny Sirault, Manager, Industry, Environment and Defence Division

Ms Jan Harris, General Manager, Budget Policy Division

Ms Luise McCulloch, Principal Adviser, Budget Policy Division

Mr Jason Allford, Principal Adviser, Budget Policy Division

Ms Sue Vroombout, General Manager, Commonwealth-State Relations Division

Ms Deidre Gerathy, General Manager, Corporate Services Group

Mr Robert Donnelly, Chief Financial Officer, Corporate Services Group

Outcome 3: Effective taxation and retirement income arrangements

Output Group 3.1: Revenue Group

Mr David Parker, Executive Director

Ms Maryanne Mrakovcic, General Manager, Tax Analysis Division

Mr Phil Gallagher, Manager, Tax Analysis Division

Mr Colin Brown, Manager, Tax Analysis Division

Mr Damien White, Manager, Tax Analysis Division

Mr Marty Robinson, Manager, Tax Analysis Division

Mr Paul McCullough, General Manager, Business Tax Division
Mr Michael Willcock, General Manager, Personal and Retirement Income Division
Ms Christine Barron, Secretary, Board of Taxation and General Manager, Indirect Tax Division
Mr David Hazlehurst, General Manager, Tax System Division

Outcome 4: Well Functioning Markets

Output Group 4.1: Markets Group

Mr Jim Murphy, Executive Director
Mr Richard Murray, Executive Director, Policy Coordination and Governance
Mr Geoff Miller, General Manager, Corporations and Financial Services Division
Ms Vicki Wilkinson, Principal Adviser, Corporations and Financial Services Division
Ms Marian Kljakovic, Manager, Corporations and Financial Services Division
Mr Bede Fraser, Manager, Corporations and Financial Services Division
Mr Mark Sewell, Manager, Corporations and Financial Services Division
Ms Alix Gallo, Manager, Corporations and Financial Services Division
Ms Kate Preston, Manager, Corporations and Financial Services Division
Mr Patrick Colmer, General Manager, Foreign Investment and Trade Policy Division
Mr Frank Di Giorgio, Principal Adviser, Foreign Investment and Trade Policy Division
Mr John Lonsdale, General Manager, Financial System Division
Ms Jacky Rowbotham, Manager, Financial System Division
Mr Justin Douglas, Manager, Financial System Division
Ms Kanwaljit Kaur, Manager, Financial System Division
Mr Roger Brake, Manager, Financial System Division
Dr Steven Kennedy, General Manager, Infrastructure, Competition and Consumer Division
Mr Brad Archer, Manager, Infrastructure, Competition and Consumer Division
Mr Bruce Paine, Principal Adviser, Infrastructure, Competition and Consumer Division
Mr Andrew Deitz, Infrastructure, Competition and Consumer Division
Mr Paul McBride, Principal Adviser, Cities and Housing, Infrastructure, Competition and Consumer Division
Mr Paul Madden, Program Director, Standard Business Reporting Management Group
Mr Greg Divall, Program Manager, Standard Business Reporting Management Group
Ms Megan Bonny, General Manager, Stakeholder Management, Standard Business Reporting Management Group
Ms Helen Austin, General Manager, Chief Solutions Architect, Standard Business Reporting Management Group
Mr Geoffrey Turner, General Manager, Core Services Team, Standard Business Reporting Management Group
Mr Peter Martin, General Manager, Australian Government Actuary
Mr Michael Burt, Senior Adviser, Australian Government Actuary
Ms Susan Antcliff, Senior Adviser, Australian Government Actuary
Mr Simon Writer, Manager, Infrastructure, Competition and Consumer Division

Australian Bureau of Statistics

Mr Brian Pink, Australian Statistician

Mr Peter Harper, Deputy Australian Statistician, Population, Labour, Industry and Environment Statistics Group

Mr Trevor Sutton, Deputy Australian Statistician, Social Statistics Group

Ms Gillian Nicoll, Assistant Statistician, Office of the Statistician

Mr Paul Lowe, Assistant Statistician, Population Census Branch

Mr Michael Belcher, Chief Financial Officer

Ms Janet Murphy, First Assistant Statistician, Corporate Services Division

Mr Ian Ewing, Deputy Australian Statistician, Macroeconomics and Integration Division

Australian Competition and Consumer Commission

Mr Graeme Samuel, Chairman

Mr Brian Cassidy, Chief Executive Officer

Mr Nigel Ridgway, General Manager, Compliance, Research, Outreach and Product Safety

Mr Marcus Bezzi, Executive General Manager, Enforcement and Compliance Division

Mr Mark Pearson, Executive General Manager, Regulatory Affairs Division

Mr Tim Grimwade, Executive General Manager, Mergers and Acquisitions Group

Ms Helen Lu, General Manager, Corporate Branch

Mr Adrian Brocklehurst, Chief Financial Officer

Mr Richard Chadwick, General Manager, Adjudication Branch

Mr Bob Weymouth, Acting General Manager, Enforcement Operations

Mr Michael Cosgrave, General Manager, Communications

Ms Michelle Groves, Chief Executive Officer, Australian Energy Regulator

Mr Sebastian Roberts, General Manager, Water

Australian Office of Financial Management

Mr Neil Hyden, Chief Executive Officer

Mr Michael Bath, Director, Financial Risk

Mr Gerald Dodgson, Head of Treasury Services

Mr Andrew Johnson, Head of Compliance and Reporting

Mr Pat Raccosta, Chief Finance Officer

Australian Prudential Regulation Authority

Dr John Laker, Chairman

Mr Ross Jones, Deputy Chairman

Mr John Trowbridge, Member

Mr Keith Chapman, Executive General Manager, Supervisory Support

Mr Senthamangalam Venkatramani, General Manager, Central Region

Australian Taxation Office

Mr Michael D'Ascenzo, Commissioner of Taxation

Mr David Butler, Second Commissioner

Mr Bruce Quigley, Second Commissioner

Ms Jennie Granger, Second Commissioner

Mr Mark Konza, Deputy Commissioner - Small and Medium Enterprises

Ms Raelene Vivian, Chief Operating Officer

Mr Neil Olesen, Deputy Commissioner, Superannuation

Mr Robert Ravanello, Chief Finance Officer

Australian Securities and Investment Commission

Mr Tony D'Aloisio, Chairman
Mr Greg Medcraft, Commissioner
Mr Michael Dwyer, Commissioner
Mr Justin Owen, Manager, Government Relations
Ms Kate Harvey, Senior Executive Specialist, Communications
Mr Barton Hoyle, Research Adviser to the Commissioner

Productivity Commission

Mr Gary Bank AO, Chairman
Mr Bernie Wonder, Head of Office
Ms Lisa Gropp, Principal Adviser, Research
Mr Terry O'Brien, First Assistant Commissioner

CHAIR—I declare open this consideration of the Treasury portfolio by this public hearing of the Senate Economics Legislation Committee. The Senate has referred to the committee particulars of proposed expenditure for 2009-10 and related documents for the Innovation, Industry, Science and Research, the Resources, Energy and Tourism, and the Treasury portfolios. The committee has set Thursday, 1 April 2010 as the date by which answers to questions on notice are to be returned. Under standing order 26, the committee must take all evidence in public session. This includes answers to questions on notice.

Officers and senators are familiar with the rules of the Senate governing estimates hearings. If assistance is needed, the secretariat has copies of the rules. I particularly draw the attention of witnesses to an order of the Senate of 13 May 2009 specifying the process by which a claim of public interest immunity should be raised, and which I now again incorporate in *Hansard*.

The extract read as follows—

Public interest immunity claims

That the Senate—

- (a) notes that ministers and officers have continued to refuse to provide information to Senate committees without properly raising claims of public interest immunity as required by past resolutions of the Senate;
- (b) reaffirms the principles of past resolutions of the Senate by this order, to provide ministers and officers with guidance as to the proper process for raising public interest immunity claims and to consolidate those past resolutions of the Senate;
- (c) orders that the following operate as an order of continuing effect:
 - (1) If:
 - (a) a Senate committee, or a senator in the course of proceedings of a committee, requests information or a document from a Commonwealth department or agency; and
 - (b) an officer of the department or agency to whom the request is directed believes that it may not be in the public interest to disclose the information or document to the committee, the officer shall state to the committee the ground on which the officer believes that it may not be in the public interest to disclose the information or document to the committee, and specify the harm to the public interest that could result from the disclosure of the information or document.

- (2) If, after receiving the officer's statement under paragraph (1), the committee or the senator requests the officer to refer the question of the disclosure of the information or document to a responsible minister, the officer shall refer that question to the minister.
- (3) If a minister, on a reference by an officer under paragraph (2), concludes that it would not be in the public interest to disclose the information or document to the committee, the minister shall provide to the committee a statement of the ground for that conclusion, specifying the harm to the public interest that could result from the disclosure of the information or document.
- (4) A minister, in a statement under paragraph (3), shall indicate whether the harm to the public interest that could result from the disclosure of the information or document to the committee could result only from the publication of the information or document by the committee, or could result, equally or in part, from the disclosure of the information or document to the committee as in camera evidence.
- (5) If, after considering a statement by a minister provided under paragraph (3), the committee concludes that the statement does not sufficiently justify the withholding of the information or document from the committee, the committee shall report the matter to the Senate.
- (6) A decision by a committee not to report a matter to the Senate under paragraph (5) does not prevent a senator from raising the matter in the Senate in accordance with other procedures of the Senate.
- (7) A statement that information or a document is not published, or is confidential, or consists of advice to, or internal deliberations of, government, in the absence of specification of the harm to the public interest that could result from the disclosure of the information or document, is not a statement that meets the requirements of paragraph (1) or (4).
- (8) If a minister concludes that a statement under paragraph (3) should more appropriately be made by the head of an agency, by reason of the independence of that agency from ministerial direction or control, the minister shall inform the committee of that conclusion and the reason for that conclusion, and shall refer the matter to the head of the agency, who shall then be required to provide a statement in accordance with paragraph (3).

(Extract, Senate Standing Orders, pp 124-125)

CHAIR—The committee will begin consideration of the Treasury portfolio with the Macroeconomic Group of the department and will then follow the order as set out in the circulated program. Treasury has requested that questions about the *Intergenerational report*, which covers several groups, be asked during the Fiscal Group evidence, which is on later today.

[10.04 am]

CHAIR—I welcome Senator Sherry, representing the Treasurer, and officers of the department. Minister or officers, would you like to make an opening statement?

Senator Sherry—I do not, Chair.

CHAIR—Dr Henry?

Dr Henry—No, Chair.

CHAIR—We will go straight to questions. I believe Senator Joyce has some.

Senator JOYCE—You would be aware of the comments the other day by Glenn Stevens from the RBA talking about the trade-off between spending and interest rates?

Dr Henry—Yes, indeed. I was there.

Senator JOYCE—Mr Swan stated that these comments were directed at other countries and not ours. Do you think that is the case?

Dr Henry—I am aware of a sentence in the speech that is a caution really from the governor to readers and listeners that the content of the speech is not to be taken as reflecting in any way on current circumstances in Australia.

Senator JOYCE—Would you say the general summary of the speech is that, if you keep spending and racking up debt, you are going to put upward pressure on interest rates?

Dr Henry—The speech covers 50 years of learnings from monetary policy and there are quite a number of messages in the speech. I would not have thought that the material that relates to the interaction between monetary and fiscal policy is among the most significant messages in the speech. But my understanding of what the governor was saying in that part of the speech is that, in the quite recent circumstances globally in several parts of the world, fiscal policy and monetary policy were acting together to achieve a common objective, and that the fiscal stimulus in various countries will be withdrawn at different rates in different countries. In some countries fiscal policy might be withdrawn at a quite rapid rate and in those countries that could have negative consequences for growth. I think he then says in the speech that in those circumstances, were growth to slow, monetary policy would be more accommodative than it otherwise would be. That is what I took from the speech in respect of the connection between fiscal policy settings and monetary policy settings.

Senator JOYCE—Is it a fair statement that, if we keep borrowing money and our debt keeps getting larger, we would be putting upward pressure on interest rates?

Dr Henry—No disrespect, Senator, but that is a gross oversimplification of economic understanding of these matters. To illustrate, you will recall that during the early years of this decade, as debt was being repaid, interest rates were steadily climbing. So I think we should be careful not to rush into simplistic relationships between levels of debt and interest rates. In Australia since the early to mid-1990s—it is not necessarily true in other countries—it has been the case that, as government debt has been repaid, interest rates have increased, not fallen. That is not altogether surprising because governments have an enhanced ability to repay debt as their fiscal positions improve, which is fairly obvious, and their fiscal circumstances improve as the economy strengthens, which is also fairly obvious. As the economy strengthens, other things being equal, there is increasing upward pressure on prices and monetary policy responds to that. So it is not terribly surprising that we should see, as you would see if you were to have a look at the data, that since the early to mid-1990s the repayment of debt has actually been associated with increasing interest rates.

Senator JOYCE—What do you predict the current deficit to be? I know that there have been statements about it being reduced. What do you think it is going to be reduced by?

Dr Henry—The most recent publicly available figures are of course set out in the Mid-Year Economic and Fiscal Outlook—

Senator JOYCE—\$57.7 billion

Dr Henry—As I understand it, the government has no intention to publish revised forecasts in advance of the May budget.

Senator JOYCE—So that deficit figure remains current and is the latest and most appropriate figure which has been put forward?

Dr Henry—Certainly it is the most current figure publicly available.

Senator JOYCE—Are there any other figures?

Dr Henry—We are, of course, as advisers to the government, advising the government on a frequent basis about the emerging economic and fiscal position. This is something we do as a matter of course particularly intensively between mid-year economic and fiscal outlooks, usually around the end of each calendar year and the budget these days is usually brought down in the second week of May.

Senator JOYCE—Do you have any information before you which says that the deficit will be lower?

Dr Henry—I have no information that I able to share publicly on the matter.

Senator JOYCE—But there is information in the public arena to suggest that it is. Where would that information have come from?

Dr Henry—As I understand it, the information to which you are referring is backward-looking information. It relates to revenue collections and, more particularly, outlays in the present budget year to date. Much of the commentary I have read in recent times speculating on what the budget might look like in the present year and in future years is just that—speculation. It seems to be based on those backward-looking collections numbers with respect to revenue and backward-looking numbers with respect to outlays.

Senator JOYCE—When we look backward through previous MYEFO documents, which I have been trawling through, in year 2007-08 the forward projections for 2009-10 were an underlying cash balance positive surplus of \$17.7 billion. I realise that that was not taking into account the full extent of the global financial crisis, but the next year the underlying cash balance for the same year—it looks as though it was 2009-10—a \$3.6 billion surplus. What is the figure we are actually heading towards, a \$57.7 billion deficit?

Dr Henry—I believe that is the MYEFO figure, yes.

Senator JOYCE—Two years ago you could not have put much reliance on that figure, could you?

Dr Henry—I am sorry?

Senator JOYCE—Two years ago, we could not have relied too much on MYEFO for exactly where we would be, could we? In fact, one year ago we could not have relied too much on the MYEFO for exactly where we would be.

Dr Henry—Two years ago you are talking about pre the GFC.

Senator JOYCE—And through it—in fact every one. The position we are currently in is a record. \$57.7 billion deficit in dollar terms, is it not?

Dr Henry—In nominal dollar terms I expect it would be.

Senator JOYCE—What do you envisage the peak gross debt position to be of our nation?

Dr Henry—That is the question probably better taken when Fiscal Group is before you. It may be that one of my colleagues has the number in front of me.

Senator JOYCE—Peak gross debt.

Dr Henry—17.3, I guess. I refer you to a media release of 8 December last year in which the Treasurer said:

Net debt is now expected to peak at 9.6 per cent of GDP in 2013-14 ... Government securities on issue—

I guess that is what you are referring to—

Senator JOYCE—Yes.

Dr Henry—It continues—

are now expected to peak as a share of GDP in 2011-12 at 17.3 per cent, compared to 18 per cent of GDP under the previous standards.

Senator JOYCE—So what is that in dollar terms?

Dr Henry—Does somebody have that number off the top of their head?

Dr Gruen—We can get back to you on that.

Dr Henry—It is a rather simple calculation, of course.

Dr Gruen—We need to know what GDP is projected to be in that year.

Senator JOYCE—Less than \$200 billion?

Dr Gruen—Could we ask you to ask that question of Fiscal Group, Senator.

Senator JOYCE—You have a \$1.2 trillion economy—two lots of 17 is 34—so you are looking at about \$180 billion or \$190 billion.

Dr Henry—About \$245 billion.

Dr Gruen—That's gross debt.

Dr Henry—That's gross; yes. And net of \$121 billion.

Senator JOYCE—Did you say that it was \$245 billion?

Dr Henry—Government securities on issue.

Senator JOYCE—Have we got the legislation and power to borrow to that level?

Dr Henry—I think these questions are better directed to the Fiscal Group people when they get here.

CHAIR—Can I interrupt you, for a moment Senator Joyce. I need to ask the permission of the committee about the filming of the hearing. Unless there is any objection I will agree but I remind people to adhere to that rules about filming—not filming behind the desk and so on.

Senator JOYCE—Dr Henry, is that the end of the answer?

Dr Henry—I think we have to be rather careful that we answer these questions very precisely, as I am sure you would understand. Mr Ray, when he appears before the committee later, I am assured, will have all of the details at his fingertips.

Senator JOYCE—To your knowledge is there only that \$200 billion appropriation that we have allowed borrowing levels to? Is that correct?

Dr Henry—Again, I would not want to mislead the committee. I think it would be better if you were to await Mr Ray. Alternatively we could have a short pause and I could make a phone call.

Senator JOYCE—We will ask Mr Ray.

Senator RONALDSON—You are the secretary of the department. Did you come in prepared for this, or not?

CHAIR—Did you have questions or will I let Senator Joyce continue?

Senator PRATT—Questions belong in the appropriate outcomes.

Senator McGAURAN—I would like to go back to one of the questions. It is a question on interest rates.

Senator JOYCE—We are currently at \$122.01 billion gross government securities outstanding. In the last two months we have borrowed a further \$7 billion extension. Is there any point where you envisage that the borrowing, or the rate at which are you are borrowing, will become excessive?

Dr Henry—Not in our forecasts or our projections.

Senator JOYCE—What is the debt of the states? The last time that you gave evidence of the debt of the states it was about \$170 billion. Do you know what the gross debt of the states is at the moment?

Dr Henry—I do not have a current number for the gross debt of the states; no.

Senator JOYCE—You might have it now, from your colleagues.

Dr Henry—We can get those numbers but I do not have the gross debt numbers with me for the states, this morning.

Senator Sherry—Interestingly, Senator Joyce, gross debt of the Commonwealth at the end of 2007 was approximately \$58 billion. That does seem to draw some consternation from some of your colleagues occasionally when it is pointed out that we inherited a gross debt of \$58 billion—not a net debt at a gross debt; there is an important difference.

Senator JOYCE—You are somewhere between doubling and tripling it at the moment. Is that a recommendation of good management?

Senator Sherry—No. I think it is important to understand that gross debt, which is the figure that you are asking about, when you left office was \$58 billion. We actually had a debt of \$58 billion when you lost office.

Senator EGGLESTON—It is seven times that already, isn't it?

Senator Sherry—Gross debt? No. You are not right. Gross debt is what is being asked about.

Senator JOYCE—I have heard you run this through the parliament before.

CHAIR—Excuse me. Are we now moving to Senator McGauran for questions?

Senator JOYCE—According to—

CHAIR—Senator Joyce, I want to clarify whether we are moving to Senator McGauran for questions.

Senator McGAURAN—No, we are still with Senator Joyce. But I am provoked. The minister at the table provokes.

CHAIR—Senator McGauran, I ask you to cease interjecting because if you are asking questions I have to assume that you are taking the questioning.

Senator JOYCE—According to the Australian Bureau of Statistics, what is our foreign debt at the moment?

Dr Henry—I presume you are not asking about the government's foreign debt?

Senator JOYCE—No.

Dr Henry—You are asking about the national foreign debt?

Senator JOYCE—Yes.

Dr Gruen—Australia's net foreign debt—

Senator JOYCE—No, gross.

Dr Gruen—You want gross?

Senator JOYCE—Give me both.

Dr Gruen—Gross debt liabilities are \$1.2 trillion.

Senator JOYCE—Gross debt is \$1.2 trillion?

Dr Gruen—Yes, but that is obviously offset by debt assets.

Senator JOYCE—And the net?

Dr Gruen—The net is \$638 billion as of September 2009.

Senator JOYCE—\$637.5 billion or something?

Dr Gruen—It could be. I have only got it to the nearest billion.

Senator JOYCE—And what percentage is that of GDP?

Dr Gruen—It is 51 per cent.

Senator JOYCE—It is 51 per cent?

Dr Gruen—At least, yes, according to this.

Senator JOYCE—Compared to other nations, where does that put us?

Dr Gruen—On net foreign debt?

Senator JOYCE—Yes.

Dr Gruen—I think we have one of the higher ratios to GDP of net foreign debt of many countries. It is lower than some. New Zealand is significantly higher than we are. There are a few other countries that are. But it is relatively high.

Senator JOYCE—So there are a few other countries that are higher than ours?

Dr Gruen—Yes.

Senator JOYCE—Who is lower than us on net foreign debt? Is the United States lower than us?

Dr Gruen—Yes.

Senator JOYCE—Is Japan lower than us?

Dr Gruen—Yes. They are a surplus country in terms of net foreign assets.

Senator JOYCE—Is Singapore lower than us?

Dr Gruen—I think so, yes.

Senator JOYCE—Apart from New Zealand being higher than us, who else is higher?

Dr Gruen—We can find that out. There are a few OECD countries that are higher than us.

Senator JOYCE—Such as?

Dr Gruen—As I said, we can find that out for you.

Senator JOYCE—The United Kingdom?

Dr Gruen—No. I think they are a net creditor.

Senator JOYCE—So they are lower than us as well?

Dr Gruen—On the national net foreign debt, yes.

Senator JOYCE—Is it a concern that we are one of the highest holders of net foreign debt in the world?

Dr Gruen—What the net foreign debt and net foreign liabilities demonstrate is that for a very long time Australia has tapped foreign savings to boost our domestic investment. Australia as a country saves about the average of the OECD. We are not a low-saving country. We have higher savings than many of the countries that you mentioned, like the US and the UK. But we have an extremely high level of investment. That has been true for 25 years. Australia's level of investment has exceeded our level of savings by about 4½ per cent of GDP since the mid-1980s and, as consequence of that, our stock of net foreign liabilities has been rising as a share GDP over that time.

This borrowing, which is almost completely done by the private sector, has enabled Australia to invest more than it would have otherwise been able to. Recently, a large part of that has been funding a big mining boom. To the extent that it is funding profitable investment, particularly in the traded sector, I think it is something that will expand Australia's productive capacity over time and I do not think it is a worry. It certainly means that it is imperative for Australia to keep the confidence of international capital markets—that is absolutely true. And it is certainly the case that the global financial crisis was a stress test for the global financial system and it is also very clear that Australia retained the confidence of the global financial markets at a time when other countries were coming under severe strain. I think it is something that we need to keep our eye on, but I also think that it is to a considerable extent a sign of the rest of the world's confidence in investing in Australia.

Senator JOYCE—What I am saying is: shouldn't the government now do the prudent thing and address some of those pressures by reducing the Australian government's requirements on borrowing, otherwise we will have the government also putting further pressure on it?

Dr Gruen—The forecasts that are in MYEFO have the government reducing its deficit at about the rate that it was reduced coming out of the early nineties recession. So it is quite a rapid fiscal consolidation that is forecast in the numbers. We have the deficit coming down by either a per cent or more than a per cent of GDP in each year of the next three years. That is a pretty rapid fiscal consolidation. The projections in MYEFO are doing precisely that—namely, the government significantly reducing its call on savings.

Senator JOYCE—I do not for one moment hold you responsible for changes in figures; it is the nature of economics that things change.

Dr Gruen—Yes.

Senator JOYCE—They are completely beyond your control. But I do point to the fact that in 2007-08 we were looking at a surplus of \$17.7 billion and now we are looking at a deficit of \$57.7 billion. If nothing more, that is an indicator of the uncertainty. So the idea that we can hold as a complete and utter truth what is two years away is a very tenuous promise, is it not?

Dr Gruen—Senator, these are forecasts. All forecasts have a margin of error. They are our best professional judgement. If you look at the last two years, I think most commentators would agree that this has been an extraordinary period. We have had one of the biggest falls in tax revenue that we have seen in our lifetimes as a consequence of the global financial crisis. If the Australian economy is hit by an enormous shock, our growth numbers will change and our fiscal aggregates will change. I think the last two years have been extremely unusual, and I am certainly hoping—and I suspect you are too—that the next two years do not look like the last two—

Senator JOYCE—We are all hoping that.

Dr Gruen—So you are completely correct that the estimated fiscal balance the 2009-10 had moved by a large amount over that time—no question about it. I think this has been an extraordinary episode and I think we understand why it is that the fiscal position has moved by as much as it has.

Senator JOYCE—To rely on your capacity to finance the debt and finance deficit, are you anticipating that your revenue stream will increase by a certain amount? What amount?

Dr Gruen—Again, this is really a question for Revenue Group. But, just to give you a quick, broad answer, the government's fiscal strategy is, as you know, to hold real spending to two per cent or less and to allow revenue to recover as the economy recovers. So the projections of what will happen to revenue as a share of GDP, I think, are in MYEFO, and I can draw your attention to that if you wish.

Senator JOYCE—Does that take into account any prospective changes from the Henry tax review?

Dr Henry—I can answer that question: certainly not, Senator.

Senator JOYCE—The large hole that you say was there in revenue—what was the predominant cause of that? What sector of the economy did that revenue stream—

Dr Henry—There were two principal contributors. We were thinking that a third would also turn out to be quite significant, but it did not turn out to be. The first two contributors were capital gains tax receipts—that is, a very big reduction in capital gains tax receipts—and company tax receipts. We were not so long ago forecasting that the unemployment rate would rise a good deal higher and that would have consequences for withholding tax receipts from individuals, but that effect has not been as large as we had at one time thought it would be. So the two largest components would be capital gains tax and company tax.

Senator JOYCE—Have you factored into your budget the current blow-outs that are becoming apparent in the stimulus programs?

Dr Henry—The most recent publicly available figures, as I said earlier, published in MYEFO. They take full account of all known information as of the date of publication of MYEFO—back in December, obviously enough—and, as I indicated earlier, we and the department of finance are monitoring outlays in revenue collections continuously and, on a very frequent basis, providing updated forecasts, estimates, to the government.

Senator JOYCE—For instance, the \$850 million blow-out in the ceiling insulation and solar panels appropriation—has that been factored in?

Dr Henry—As I said, whatever is happening on the outlay side of the budget is being factored in terms of our frequent updating of the government on the fiscal position.

Senator JOYCE—Has the \$1.5 billion blow-out in school halls been factored in?

Dr Henry—I have nothing to add. I have said the same thing three times, now, I think.

Senator JOYCE—Do you think that the global financial crisis is still with us or that it has passed?

Dr Henry—What people have called the global financial crisis, that has passed, I think it is safe to say, but that is not to say that there will not be further adverse shocks for financial markets down the track. Some of those shocks for financial markets could be of some significance for individual countries. I do not imagine shocks of the sort that would be globally significant, and I do not think it would be helpful for anybody, really, to speculate on those possibilities. But since I do not see it as something significant I certainly will not be speculating on those sorts of possibilities. The global financial crisis itself, that is, a period in which it was extremely difficult to encourage financial institutions to lend to one another, far less lend to businesses and households—that period, I think, is now behind us.

CHAIR—I am sorry, Senator Joyce, if I can interrupt for a second, the committee and witnesses would notice a number of photographers and cameramen. If anyone objects at any stage please let me know, and I just remind the people who have just come in to adhere to the rules set by the parliament. Senator Joyce.

Senator JOYCE—The cameras are here so I think it is a good time for Bossie to speak.

Senator BOSWELL—Can I talk about Treasury modelling of the outcomes on climate change. Has Treasury modelled other scenarios than those which have been made public?

Dr Henry—Sorry, Senator, that is a question that should be directed to our people from Fiscal Group. I know you have asked a lot of questions on this topic in other Senate estimates hearings and we have always made sure that we would have the technical experts here in order to answer those questions because, as you know, it is quite technical.

Senator BOSWELL—I will not continue then; I will hand back to Senator Joyce. What time are those other people coming in?

CHAIR—Fiscal Group will be here at 2 pm.

Senator BOSWELL—I will defer to Senator Joyce.

Senator JOYCE—And I will defer to Senator Bushby.

Senator Sherry—Isn't it the chair who actually decides who is next?

CHAIR—Yes, I am afraid so.

Senator CAMERON—I think their party room is chaos again!

CHAIR—Senator Pratt, who is next on my list, has just walked out the door so I will go to Senator Bushby.

Senator BUSHBY—Thank you to the officers of the Treasury for coming along today. In the budget papers you provide, at page 4-8 of Budget Paper No 1, a chart which demonstrates the estimated impact of the fiscal stimulus on real GDP. It also shows a pre-stimulus estimate of what would, presumably, have occurred without the stimulus. This shows a fall in GDP from the September 2008 index of 100 to about 9.5. In MYEFO the corresponding chart, at page 13, shows a fall from the same index without the stimulus to just 98. Most of the commentary from the government on our current position claims the credit due to the decisive action they took—which placed Australians and our children in debt for generations—that is, the massive stimulus package. But it appears that, even on those figures that do change a bit, around 2.5 per cent of the improvement between the two publications was due to factors other than the fiscal stimulus. Is that a correct assumption?

Dr Gruen—Senator, I think this traverses ground that we have discussed earlier, but I am happy to traverse it again.

Senator BUSHBY—We did not have access to MYEFO the last time you were here—

Dr Gruen—Right; I am sorry.

Senator BUSHBY—and I am referring to the difference between the MYEFO chart and the corresponding chart that was in Budget Paper No. 1.

Dr Gruen—Okay. We have I think on a few occasions laid out the approach we used in estimating the effect of the fiscal stimulus on GDP growth. That was to use what we regarded as reasonable estimates of the fiscal multiplier for the cash transfers to households and then for other spending, and we assumed a smaller multiplier for the cash transfers than for the direct investment spending, and we applied those multipliers to the profile through time of the fiscal stimulus. That was the way that we estimated the effect of the fiscal stimulus.

At budget, we used those estimates along with our estimate of how we thought the economy would track through time to back out an estimate of how the economy would have

performed without the fiscal stimulus. So it gave the two lines—the line which was our forecast line and then the line which was our estimate of what would have happened without the stimulus. As events turned out, the outcomes on GDP, and unemployment as well, have turned out to be much more favourable than we anticipated at budget. We were therefore faced with the possibility of going back to our estimates of the multipliers and applying larger multipliers and redoing the calculation. I think it would be fair to say that there is a significant margin of error in the economics profession's level of knowledge of the exact value of these multipliers. We have chosen multipliers that we think are at the conservative end of the sort of numbers that the IMF and the OECD have come up with.

Senator BUSHBY—The multipliers, if I understand your explanation correctly, apply to the impact that the fiscal measures have had?

Dr Gruen—Yes.

Senator BUSHBY—I will get to questions that touch on those sorts of things in a minute, but my initial question is that the charts in MYEFO and Budget Paper No. 1 for the position without a stimulus has improved by some 2 1/2 per cent?

Dr Gruen—Yes

Senator BUSHBY—And multipliers would not come into that?

Dr Henry—Before you go on, what Dr Gruen is getting to is that we make an estimate before the event, a forecast, of the impact of fiscal policy on GDP.

Senator BUSHBY—So that is the chart line we see in Budget Paper No. 1?

Dr Henry—Yes, you saw that in the budget. If we then discover that outcomes are stronger than what was implied by those forecasts, we then have to ask ourselves the question: is that stronger outcome due to stronger underlying activity or is it due to the fact that the multipliers were in fact quite a lot stronger than we had earlier thought. What Dr Gruen is getting to is that the judgement that we made in presenting the numbers in MYEFO—

Senator BUSHBY—But the judgement you made, though, is that you have changed the line which shows what would have happened if there had been no stimulus—and improved it by 2½ per cent.

Dr Henry—Right. The judgement we made was to stick with the original estimates that we had for the multiplier. That gives us the same profile of the gap.

The **Senator BUSHBY**—Above the no stimulus line?

Dr Henry—Exactly. So to the extent that the outcome is looking better, the two lines shift up and the gap remains the same. As I was saying, it would be nice to be in a position to make precise statements about what those multipliers are. We have, as I have said, chosen multipliers that are at the conservative end of the range that international institutions have come up with for Australia. We do have reason to believe, and I am going to come to that, that the stimulus may well have been more effective than we initially estimated.

Senator BUSHBY—That is not how you presented it in MYEFO.

Senator CAMERON—It has been more effective.

Dr Gruen—Yes, more effective. I think we said in MYEFO—I can check—that our estimates were conservative. I think we did make that statement—

Senator BUSHBY—But the chart itself shows a conservative line—

Dr Gruen—We did not change our qualitative estimates, because there is not sufficient precision. We thought the most reasonable thing to do was to keep the previous estimates that we had derived for the effect of the fiscal stimulus but to make the point that we thought that those estimates were conservative.

Let me make one other point which I think is important. One of the things that has occurred—we drew attention to it in the MYEFO—was that both business and consumer confidence bounced back much more strongly than it did in other OECD countries, and much more strongly than we had anticipated that it would. Our interpretation—and I think it is the interpretation of most commentators—is that the macroeconomic stimulus, both fiscal and monetary policy, was sufficiently quick and sufficiently big that it convinced the community that things were not going to turn out that badly. That was extremely important because it meant that businesses went on with their normal activities. They did not hunker down and cut staff; they found ways to cut hours rather than cutting staff.

CHAIR—The committee will adjourn for 15 minutes.

Proceedings suspended from 10.45 am to 10.59 am

CHAIR—The committee will now resume. We will continue with the Treasury macroeconomic group. Senator Bushby is continuing his questions.

Senator BUSHBY—Before our break, we were discussing the reasons why, between MYEFO and the budget papers, Treasury's prediction in an equivalent chart of how the economy would have fared without the fiscal stimulus had improved by roughly 2½ per cent. You were talking about how you had made some assumptions about the multipliers and that you had not changed those. They were conservative. I think you may have even said to the delight of Senator Cameron that the impact of the fiscal stimulus may have been greater than what was shown in those predictions. That was a 'may'. You are not sure of that. That is correct?

Dr Gruen—As I said, there is a margin of error around these estimates but the estimates that we used for the fiscal multipliers are at the conservative range that the IMF and the OECD suggest are appropriate for Australia. That was the first point. There is a margin of error but we think it is more likely that we have underestimated it than overestimated it.

Senator BUSHBY—But, on balance, you chose to indicate a net impact of the fiscal stimulus in those two charts that has not changed.

Dr Gruen—That is right. We thought it was the prudent thing to do to simply stick with the methodology that we had used at budget, but other aspects of the economic environment led us to think that, if anything, the fiscal stimulus might have been more effective. We actually make that point at the beginning of part 2 of the document. I will read it to you. On page 9 of the MYEFO, we say:

The fiscal and monetary stimulus appears to have been more effective than expected at Budget, not only directly supporting spending, but also boosting business and consumer confidence to a larger than expected degree ...

I guess we did not want to quantify the extent to which it had been more effective. That is our professional judgement but we thought the prudent thing to do was to stick with the quantitative estimates that we had presented at budget rather than raising them by some particular amount.

Senator BUSHBY—If you had been sure that it had been more effective, would you have shown that in your papers?

Dr Gruen—If we were sure, yes.

Senator BUSHBY—Okay. You also mentioned that the combination of both fiscal and monetary measures resulted largely in the confidence boost that was greater than expected.

Dr Gruen—Yes.

Senator BUSHBY—Did the combination also result in the actual improvement in the figures to an extent that was greater than was originally predicted? Was it just the fiscal stimulus?

Dr Gruen—Let me give you an example, which I think is quite important. With the release of the March quarter national accounts, most commentators were expecting that to show declining real GDP—and that would have been two quarters in a row. The December quarter had a fall and, had the March quarter also shown a fall, that would have been two quarters of negative growth.

Personally, I do not hold a huge amount of store in that measure of a recession—the measure of two consecutive quarters of negative growth. But it is a measure that generates headlines, and there was a lot of talk by commentators in the media before the release of the national accounts that this national accounts was going to confirm that Australia was in recession. The March quarter national accounts were released in June and they showed a rise in GDP rather than a fall. Consumer confidence rose in the immediate aftermath of that by an enormous amount. In fact, in the four months following that release, consumer confidence rose by the biggest amount it has ever risen in the history of the series.

Senator BUSHBY—That was following a great fall, though, wasn't it?

Dr Gruen—Yes, absolutely.

Senator BUSHBY—It was coming from a low base.

Dr Gruen—That is certainly true. Our estimates are that, without the fiscal stimulus, the March quarter would have been negative. In fact, our estimates for the effect on growth of the fiscal stimulus—which, as I say, are conservative—imply that without the fiscal stimulus we would have had four quarters of negative growth in a row—December 2008; March, June and September 2009. They would have all been negative.

As it turned out, we have had one quarter of negative growth in those four and, as I said, I think our estimates of the effect of fiscal stimulus are conservative. So the conclusion that we drew from that, was that the fiscal stimulus and the monetary stimulus helped to convince

consumers that things were going to turn out not as badly as they thought. We did not quantify the effect of that but we are reasonably confident that it helped the economy do better than it would otherwise have done.

Senator BUSHBY—We are going in a little bit with that answer; I do not really want to go into the fiscal stimulus. We have done that in this committee and in other things, over and over. I was particularly interested in the impact of the monetary changes as well as the fiscal stimulus. Some of your answers earlier indicated that they were working in concert—

Dr Gruen—Yes.

Senator BUSHBY—I am just trying to work out whether there is any way of identifying the relative impact of both. That was the point of my question. Even though I do not want to go over it again, with regard to the fiscal stimulus I note your comments that without the stimulus your assessment is that we would not have had positive growth in that second quarter you referred to.

Dr Gruen—The March quarter of 2009.

Senator BUSHBY—Is it the case that only the stimulus package as put forward by the government could have delivered that outcome or could an alternative fiscal stimulus—with a different spend, a different makeup and maybe even a different quantum—have delivered the same result? Can you rule that out?

Dr Gruen—I think our assessment was that, given the multipliers that we think are reasonable to apply, you would have needed to have spent something similar to have had a similar effect.

Senator BUSHBY—But you could have spent it differently?

Dr Gruen—In principle. One of the critical things was to get the spending done quickly. Provided an alternative package was able to get that much spending into the economy as quickly then that would have been fine, but that was one of the important constraints.

Senator BUSHBY—But a government making different decisions as to how to spend it, but within the parameters that you outlined, could still have delivered a similar benefit by choosing different areas to spend in.

Dr Gruen—Provided it was as quick.

Senator BUSHBY—I will move on from there. Recent statistics indicate that the impact on the unemployment rate of the global financial crisis may have peaked and is beginning to fall. We could argue all day about the reason Australia has fared relatively well—and we have done that in this committee before—but I am interested in the potential impact of a tightening labour market. What risks does Australia face in terms of skill and productive capacity shortages impacting on wages and other prices as the unemployment rate continues to go down?

Dr Gruen—I am loath to answer this question at five past 11 on the grounds that we are going to get another number at half past 11.

Senator Sherry—Do you want to come back to that?

Senator BUSHBY—I am not asking specifically about what it is, other than about the trends that we have seen recently. We may well come back to it at 11.30 if something strangely unexpected happens.

Senator Sherry—As long as you do not then, at 25 to 12, quote back the witness's comments at 5 past 11 if things are very different.

Senator BUSHBY—You mentioned earlier the prediction that we, as a nation, will grow at similar rates to when we were coming out of the recession in the early 1990s. But at that time we had a far greater degree of spare capacity to tap into to feed that growth—

Dr Gruen—That is right.

Senator BUSHBY—than we do now, because we are starting the recovery from a much lower position in terms of unemployment and probably other necessary resources.

Dr Gruen—I will make a couple of points on this. From the budget to MYEFO we reduced our estimate of the growth rate in the projection period.

Senator BUSHBY—From 4½ per cent down to four per cent.

Dr Gruen—Yes, and for a shorter period of time, for precisely the reason that you—

Senator BUSHBY—You are saying that is because there is less spare capacity to absorb during the recovery.

Dr Gruen—Precisely. The other point worth making is that this has been a remarkable episode. We do not yet know whether the unemployment rate has peaked, but it is remarkable to be where we are now, in early 2010, with the highest unemployment rate having been a number with a five in front of it. Although US unemployment is slightly below 10, it has been to 10 per cent and it is probably going to stay there for an extended period. European unemployment is at 10 per cent.

Senator BUSHBY—Despite large fiscal packages in those countries.

Dr Gruen—Indeed, and monetary easing down to close to zero.

Senator BUSHBY—Exactly. As I said, I do not want to go into the reasons why we are different today because we have discussed that in the past.

Dr Gruen—The point I was going to make is that it has been a very good outcome that firms have been able to—

Senator BUSHBY—I do not argue with that. It is a fantastic outcome.

Dr Gruen—cut hours rather than workers, but the relevance of that point is that the unemployment rate gives you—the fact that the unemployment rate is as low as it is means that there is more spare capacity in the economy than the unemployment rate would lead you to think—

Senator BUSHBY—Through underemployment.

Dr Gruen—because hours have come down so far. It is unusual to have an extended period in which the number of hours worked in the economy is falling. We had an extended period from about mid-2008 to mid-2009 in which hours worked were actually declining. This is in an economy in which workforce growth is quite rapid. So actual declines in hours worked are

opening up quite a big amount of spare capacity. The point I am making is that an unemployment rate of 5½ gives you an overly optimistic idea of how close we are to full employment.

Senator BUSHBY—So essentially 5½ per cent is not a true indicator of our labour capacity—**Dr Gruen**—That is right.

Senator BUSHBY—because it masks—

Dr Gruen—Weakness in hours worked.

Senator BUSHBY—hours worked. So a lot of people are not working as much as they would choose to if they could.

Dr Gruen—And in the recovery it will be possible for those people to pick up their average hours.

Senator COLBECK—Is there any doubt on the quantum of that?

Dr Gruen—Yes, there is. The ABS publishes monthly employment trends. It was falling at an annualised rate of nearly four per cent at its peak. That monthly data is available and it is now the case that hours worked are growing, yes.

Senator Sherry—If you want to, we can take it on notice.

Dr Gruen—We can give you that data.

Senator BUSHBY—Despite that spare capacity which is masked by what one could term as—but I doubt you would—an artificially low unemployment rate, the fact is there is not as much spare capacity as we have had at other times and not as much as you predicted as that the budget.

Dr Gruen—That is right.

Senator BUSHBY—That is why you have wound back the future growth prediction for GDP.

Dr Gruen—Yes. I would make the point that GDP growth in the latest year has been half a per cent. So on the latest data over the last year the economy has grown by half a per cent compared to its trend growth which is a bit above three per cent. The unemployment rate has been a standout. Everybody should be extremely pleased that the unemployment rate has gone up as little as it has but the economy actually has been growing pretty sluggishly. It grew by 0.2 in the September quarter and by half a per cent over the most recent year.

Senator BUSHBY—So we have only just escape recession, is really what you are saying.

Dr Gruen—Yes. We had a serious slowdown—no question about it—but my point is that over the last year the amount of spare capacity in the economy has still been rising but less than we had anticipated.

Senator BUSHBY—Yes, less than you had anticipated and the net impact is that it is sufficiently germane to limit the amount of growth of the Australian economy which you are predicting in the coming years.

Dr Gruen—There is less of the gap to get us back to full employment than we had anticipated.

Senator BUSHBY—Exactly, but the net effect of the smaller amount of spare capacity is that it will impact on the ability of the economy to grow at the rate that it might otherwise have grown.

Dr Gruen—Yes.

Senator BUSHBY—What impact has the change from 4½ down to four had on one estimated government revenue and the ability of the government to repay debt?

Dr Gruen—Again, if we are going to go into this in detail it is probably best to ask Revenue Group, but I will make this point. A crucial number that is relevant for how the economy is performing—it is relevant to the revenue collection—is the dollar value of GDP, rather than the growth rate. The dollar value of GDP is higher than we thought because the downturn has been less severe so, despite the fact that we have lowered the growth rate from 4½ to four, the actual level of nominal GDP in those years is higher than we previously thought—so the growth rate is less.

Senator BUSHBY—I understand what you are saying. You are saying that the money will be there regardless of that fact.

Dr Gruen—Yes.

Senator BUSHBY—So you are saying that that will not have any impact on the forecast ability of the government to repay its debt?

Dr Gruen—We gave them our updated estimates in the MYEFO, of nominal GDP being higher than we previously projected and forecast, and we updated the tax collection numbers accordingly.

Senator BUSHBY—Just to remind me, if the tax collection numbers are higher, and taking the funds available to government to repay debt, will they have more under this lower growth scenario than they would have had under the earlier higher growth scenario?

Dr Gruen—I think the answer to that is yes, but we will make sure.

Senator BUSHBY—Coming back to the lack of spare capacity, given that your own predictions indicate that at some point the availability of spare capacity will effectively act as a brake on the ability of the economy to grow as much as it might otherwise, that suggests that, particularly in the labour market, you actually are going to run out of employees spare and available for employers to take up. What will that mean for wage pressures?

Dr Gruen—The point you are making is that, because the downturn has been less serious, you should expect that you would not have above-trend growth for as long as we previously thought, and we have built that into our forecasts. So there will come a time when the economy returns to full employment with hours worked being back to their normal level and we have provided an estimate in the MYEFO of the year in which that will be.

Senator BUSHBY—Which is sooner than was otherwise predicted?

Dr Gruen—Sooner than previously, and someone here can tell me what year it is, but it is certainly a couple of years in the future. I can give the definitive answer to the previous question. If we update the estimates of revenue from budget to MYEFO, there is a small rise in our estimates in both 2009-10 and 2010-11.

Senator BUSHBY—And that is total revenue, gross revenue?

Dr Gruen—Total revenue in dollars in both of those years.

Senator BUSHBY—Thank you. Will an increasingly tight labour market lead to wage rise pressures?

Dr Gruen—Eventually it will but we do not anticipate that it is going to lead to those pressures for some time.

Senator BUSHBY—When you say ‘some time’ what do you mean?

Dr Gruen—I can refer you to the forecasts that we have got in the MYEFO, which are the most recent publicly available forecasts, so let me just flip to those. We are anticipating growth in wages through the year to the middle of 2011 of 3½ per cent. That is a slight pick-up from the previous year so we are anticipating growth in wages of 3¼ per cent.

Senator BUSHBY—How does that compare with the growth in wages over the last decade?

Dr Gruen—This would be the wage price index and that averages a number in the high 3s or 4s, I think, so it is a bit softer. A number around four is its average. On the consumer price index, our forecasts are for growth in the consumer price index through both of those years to be slightly below the midpoint of the RBA’s target range.

Senator BUSHBY—Those forecasts would assume normal actions being taken by the RBA?

Dr Gruen—Yes. These are predicated on—

Senator BUSHBY—The RBA taking action to try and keep CPI within the target range and so forth.

Dr Gruen—Just the market profile—the profile that the market was predicting for the cash rate at the time we put the forecasts together.

Senator BUSHBY—I think we have gone over before that you do not actually do it on a static basis; you actually do build in profiles.

Dr Gruen—Both we and the RBA do that.

Senator BUSHBY—Those wage price predictions would not include the increasing trend that we are seeing currently towards unsustainable wage claims without corresponding productivity gains, like the actions with the Pluto facility in WA.

Senator Sherry—Does that indicate a trend? Do you have any statistical analysis? You have got one case that you have referred to involving 50 workers I think, but does that indicate the statistical trend that you have implied? If you have got a statistical trend, show us the data, because I have not seen a statistical trend.

Senator BUSHBY—I do not have statistical data for it, but I think that anecdotally you can see that there is a lot more industrial action occurring around the country as unions in particular take advantage of the new laws that they are working under, the industrial relations regime.

Senator Sherry—That is an argument, but I have not seen statistical data from the ABS indicating this trend you claim.

Senator BUSHBY—I am sure we will see that in due course.

Dr Gruen—I can provide the latest data. The average annualised wage increase per employee for agreements certified in the latest quarter for which data is available, which is the September quarter of last year, was 3½ per cent, down from 3.9 per cent in the previous quarter. But that is not this year; that is just the latest.

Senator BUSHBY—That is pre the IR laws taking effect.

Dr Gruen—Yes, that is the latest data.

Senator BUSHBY—I will ask more questions about that as the trend emerges and continues to emerge.

Senator Sherry—As the trend you claim is shown not to be correct on any data that has been published!

Senator BUSHBY—I think it is already emerging, but as we actually get statistical evidence to back it up.

Senator JOYCE—The Fair Pay Commission is already in negotiations.

Senator BUSHBY—That is right.

Senator Sherry—I think the saying is: one swallow does not make a summer. You can have one claim that some people would argue is excessive involving a small group of workers; it does not mean it is going to sweep through the entire economy.

Senator BUSHBY—It does under collective bargaining.

Senator COLBECK—Let's hope it doesn't.

Senator BUSHBY—Exactly. We will move on from there then. At the last estimates I asked Treasury questions regarding Treasury's predictions that they formed at the beginning of the financial shock, including whether Treasury would have recommended the same fiscal response that was actually employed, given what they knew in October of last year.

Dr Gruen—Do you mean in October 2008?

Senator BUSHBY—No, in October estimates last year I asked you whether Treasury would have recommended the same fiscal package given what you knew then and given that the circumstances as they transpired and as we have discussed today have turned out to be quite different to what you originally predicted. I think Dr Henry indicated that we will never know the answer to whether retaining flexibility in the government's response would have been appropriate, but Dr Gruen made the statement that, with the benefit of knowledge of actual outcomes such as those then to be delivered in MYEFO, Treasury would be better informed as to what the appropriate response would be looking forward from there. We now have MYEFO. Does the information it contains better inform Treasury as to what action was required given that by Treasury's own assessment it demonstrated the actual impact of the global financial crisis without the fiscal stimulus was probably not as bad as originally thought?

Dr Henry—In your conversation with Dr Gruen earlier he was making the point that we really do not know how much of the added strength that we have seen in the economy is due to the fiscal stimulus being more effective than we thought it may have been, to monetary policy being more effective than we thought it may have been or to other factors, including what happened to the exchange rate in late 2008.

Senator BUSHBY—Or China's resilience?

Dr Henry—Exactly. There was China's fiscal stimulus package and so on. We have not attempted an exercise that isolates all of these things. Without undertaking that exercise your question is rather difficult to answer. If it were the case that all of the additional strength could be attributed to the fiscal response then the answer to your question would be no, and we would recommend precisely what we recommended in October 2008. That would be obvious. But the less confident you are of that being the case the less confident one can be that, hypothetically, putting ourselves back in October 2008 with different facts at our fingertips, we would recommend precisely the same package. So I cannot really answer the question.

Senator BUSHBY—That is what I think you basically indicated in October, which is why I outlined that. But Dr Gruen suggested that, with MYEFO, you might be able to add something.

Dr Henry—The point is, though, that Dr Gruen did not actually do that piece of work that would be required in order for us to answer that question.

Senator BUSHBY—Whereas Dr Henry did.

Dr Henry—No, he did not. The work has not been done and quite sensibly so because, as Dr Gruen indicated, we have in both the budget and the MYEFO used the best available figures on the size of fiscal multipliers. We thought it prudent to continue to use those same figures in MYEFO, even though it is arguable that we had understated those fiscal multipliers in the May budget.

Senator BUSHBY—You have just stated that it is not possible to unpick what the factors were that led to Australia coming through in the shape that it has come through.

Dr Henry—Precisely. We have some confidence that the fiscal policy was quite significantly important and we have some confidence that the monetary response was also important. We have some confidence that the exchange rate would have been important and we have some confidence that China, in particular, was important.

Senator BUSHBY—So you are confident that all those factors would have contributed but you cannot unpick to the extent to say that the fiscal package resulted in this percentage of GDP and the monetary resulted in that? You cannot tell us in that sort of detail?

Dr Henry—That is right.

Senator BUSHBY—Yet the government, and I think Senator Sherry in the Senate in answer to a number of questions on a number of occasions, has claimed that the fiscal package has saved—I think he actually quantified it—200,000 jobs. Are you able to say, given what you have just said about the lack of certainty, what factors actually led, in particular, to how many jobs saved by any one of those four factors that you have mentioned?

Dr Henry—Dr Gruen will correct me if I am wrong, but my understanding is that the figure of 200,000 jobs saved comes from a comparison between those two lines we were talking about earlier. So it relates to the conservative estimate of the impact of the fiscal stimulus and it relates to the conservative fiscal multipliers that have been used. As was noted earlier, in moving from budget to MYEFO we have not changed that gap between those two lines—that is, what GDP would have been without the fiscal stimulus and what GDP we now think will look like.

Senator BUSHBY—I have a question to clarify that.

Dr Henry—So, the 200,000 jobs—

Senator BUSHBY—I understand what you are saying: you are saying it is the gap.

Dr Henry—Yes.

Senator BUSHBY—But does the GDP line without fiscal stimulus take into account the monetary policy changes?

Dr Henry—Yes.

Senator BUSHBY—So the assumption is that, without any fiscal stimulus at all, that is where it would be?

Dr Henry—Yes.

Senator BUSHBY—You are saying that, without the other three factors, more than 200,000 jobs would have been lost?

Dr Henry—Yes, that is right.

Senator JOYCE—Can I add a query on that point? As we have stated earlier, there is a massive inflow of funds into Australia by reason of us having one of the highest—

Dr Henry—Investment rates.

Senator JOYCE—debt levels as a nation in the world. In the actual extra stimulus that the government puts in, does that have comparative effect to the stimulus that was already there from this vast amount of foreign borrowing that is also coming in and also the stimulus, as you have just stated, from China and its involvement and its demand for our resources? How many billions do you need to spend in Australia before it has an effect?

Dr Henry—Any amount will have an effect. What is important in undertaking this work is to compare one year with another. You cannot conduct this exercise simply by looking at absolute levels. What you have to look at is how the level of government spending in this year compares with the level of government spending last year, for example, or how the strength of exports in this year compares with the strength of exports in the preceding year. It is the same with private investment and with household consumption. In that way you can figure out the contribution that each is making to GDP growth and figure out the contribution that each is making to what is happening to unemployment and so on. That is how this exercise would be undertaken. When you say that the Australian economy has a large stock of foreign debt, that in and of itself does not tell us much about the contributions being made to GDP growth from the things that foreign borrowing is financing. We need to know what is happening to the things that that foreign debt is financing. We need to know what is happening to household

consumption expenditure: is it higher this year than last year? What is happening to private investment expenditure: is higher this year than last year? Is government expenditure higher this year than last year and so on?

Senator JOYCE—It is about a \$52 billion package all up. Wouldn't it conversely be true that, if our debt peaks at \$245 billion gross, whatever that is, \$157 billion.

Senator Sherry—This is government debt because you are talking about government and national debt at various times.

Senator JOYCE—Everybody knows what I am talking about now.

Senator Sherry—There might be some people who are not quite sure what you mean.

Senator JOYCE—When we have to start repaying those funds—and seeing as how we are going to be paying back vastly more than was actually part of the stimulus package with interest and the implied oppressing effect that will have on the economy—conversely, in the future, are you going to basically have a negative stimulus campaign? This negative stimulus campaign can go on for—

Dr Henry—We already have it actually. Right through this year the fiscal policy is making a negative contribution to GDP growth.

Senator BUSHBY—We have had a discussion about that.

Dr Henry—We have discussed this previously, yes. There is an inevitable negative fiscal stimulus effect, so you are quite right, Senator, and we are already experiencing that.

Senator BUSHBY—If the stimulus package were withdrawn completely tomorrow, what impact would that have on GDP? Is it positive or negative?

Dr Henry—It is negative.

Senator BUSHBY—Exactly. We went through the explanation in October and I understand why but, despite what you are saying, it continues to support, as Dr Gruen said in October, growth even though the fact that it is not being maintained at its highest level forever means that in an economic sense it detracts from the GDP as the size of the package declines.

Dr Henry—Sure. So a negative number can be made larger—a larger negative; a larger and absolute number.

Senator BUSHBY—Despite the fact that in a technical sense it actually detracts from growth this year it is still—

Dr Henry—I would detract more if the stimulus package were to be—

Senator BUSHBY—supporting the GDP.

Dr Henry—Correct. That is right. It is actually supporting the level but it is attracting—

Senator BUSHBY—And that is the fact because it is not being maintained at its highest level.

Dr Henry—That is correct.

Senator BUSHBY—Thank you. Coming back quickly to that gap in those charts that we were talking about: you have mentioned on a number of occasions that you have maintained

that gap. It is hard to tell from looking at the charts because they are not exactly the same scale, but it appears that the gap has actually shrunk slightly from looking at the chart. You do not give the number, so it is hard to see.

Dr Gruen—Let me be as precise as I can be. In the budget and in the MYEFO we used exactly the same multipliers. We got updated information about the timing of the spending and therefore the gap as you see it will not be exactly the same.

Senator BUSHBY—It has shrunk by what looks like about one per cent, but it is hard to tell.

Dr Gruen—I would be surprised if it is as much as that.

Senator BUSHBY—It is not a graph that you can actually measure accurately against.

Dr Gruen—No. We got updated information about the timing of the spending and we also did further analysis on how rapidly we thought households had spent the cash transfers. So we used that updated information to update our estimates of the profile, but we used exactly the same multipliers.

Senator BUSHBY—So, in effect, using the updated information of what you knew about how people were really reacting to things, the actual impact at any point in time has got a little bit smaller than what it was.

Dr Gruen—I am not sure that it has got smaller, but we can certainly get back to you on that.

Senator BUSHBY—I would appreciate it if you could take that on notice.

Dr Gruen—I think it is timing. In other words: the total area between the two lines has stayed the same.

Senator BUSHBY—The area is the same but it may be just a little bit longer, rather than doing it up front as quickly as it might otherwise have been. So the impact at any one point in time has probably got smaller, on the assumption that that is what this shows, but over time you might still get the benefit. At any one point in time the impact in terms of growth, assuming that it is smaller, is smaller.

Dr Gruen—Yes.

Senator BUSHBY—Finally, this is just a general question. How are the recommendations from the various reviews—such as the Henry, Harmer, retirement, Cooper and PJC inquiries—going to be integrated into coherent and consistent policy, noting that most are being conducted by different committees and different sections of Treasury and yet many issues overlap or are in common?

Senator CAMERON—That is what governments do.

Senator BUSHBY—Of course they do. I want to know how they are actually going to apply the findings when they have actually finished.

Senator Sherry—I think that is a matter for a government policy announcement in response to the various reviews that have been completed or are partway through completion.

Senator BUSHBY—Okay. Thank you.

Senator PRATT—There have been assertions made that Australia's economy has performed about the same way as the New Zealand economy. I wanted to ask if this comparison is fair, particularly when you look at issues such as growth versus contraction?

Dr Gruen—We do not have a New Zealand comparison with us, but we can get one. It is the case that their latest unemployment rate came out just in the last week or so and I think New Zealand unemployment is sitting at 7.3 per cent. New Zealand's unemployment coming into the global financial crisis was below Australia's unemployment and had been for several years. So it is certainly the case in terms of the labour market that the labour market in New Zealand has deteriorated by significantly more than Australia.

Senator PRATT—I suppose the argument that was put out in the public arena was that New Zealand has done just as well and they did it with less stimulus. But clearly, when you look at it, that is not actually the case, is it?

Dr Gruen—It is also the case that they have had several quarters of falling real GDP, rather than just one. We can find out the exact numbers for you, but my memory is that they have had at least three consecutive quarters of falling real GDP.

Senator PRATT—Can I ask about what our current inflation rate says about the capacity of our economy and which consumer goods have been putting upward pressure on inflation and which ones are putting downward pressure?

Dr Gruen—As you would be aware, the headline CPI is not always a good measure of underlying price pressures, so the Reserve Bank and ourselves tend to focus more on a range of underlying measures. If you look at those underlying measures, underlying inflation has been coming down for several quarters in a row. In through the year terms I think underlying inflation has come down from a number with a four in front of it to a number more like 3.4—I think that is the latest through the year estimate to the December quarter. So there have been, over the last year or so, declining inflationary pressures in the Australian economy, which is what you would imagine in a situation where you have got considerable excess capacity in the Australian economy.

Senator JOYCE—That is the inflation—

Dr Gruen—That was an average of the two measures that the RBA uses of underlying inflation. Headline inflation tends to jump around for a whole lot of other reasons. Headline inflation through the year to the December quarter is 2.1. The average of the underlying measures is 3.4 through the year to the December quarter.

Senator PRATT—I want to ask what we are doing to ensure strong growth but low inflation into the future and what the approach is to getting that balance right, given the current economic circumstances.

Dr Gruen—Sorry, what we are doing?

Senator PRATT—Our monetary and fiscal balances. The government has to have an approach to how we think those issues are going to play out.

Mr McDonald—I suspect that part of the points you are getting at there is that, beyond the current period where growth is supported and demand in particular is being supported by

macroeconomic policy, over the medium to longer term we know that effectively growth is driven by the three Ps: population, productivity and participation. Would that be correct?

Senator PRATT—Yes, that is right, and infrastructure and all that kind of thing. I want to ask about an update on Australia's current unemployment. We have had significant increases that are now starting to stabilise. Can you give us an overview of those statistics?

Dr Gruen—I can give you a summary of the numbers that came out at 11.30. The seasonally adjusted unemployment rate has fallen to 5.3 from 5.5 in December. There was growth in both part-time and full-time employment, with full-time employment growing by nearly 16,000 and part-time employment by nearly 37,000. So it is a strong labour force result.

Senator PRATT—Over what period of time is that 37,000 improvement?

Dr Gruen—This is from the previous month. This is the result for January and it is from the December result.

Senator PRATT—Thank you very much.

Senator JOYCE—Time to stop the stimulus.

Senator COONAN—Just picking up on a particular aspect of participation, on 30 November last year Goldman Sachs JB Were released research on gender participation and productivity called *Australia's hidden resource: the economic case for increasing female participation*. According to the report, estimates show that closing the gap in employment rates in Australia would boost GDP by 11 per cent. The report argues that, while raising participation is obviously critical, bridging the gulf between historic male and female productivity rates has the potential to boost the level of economic activity by as much as 20 per cent. I think I have fairly summarised the findings of that report. With estimates of this magnitude and the recent comments, I think they were Australia Day comments, from the Prime Minister about lifting productivity growth to two per cent per year, has Treasury conducted any research into this gender based gap within the Australian workforce?

Mr McDonald—We have gone through the report to some degree. I think is fair to say that the broad issue of both participation and productivity is something that we have been doing work on over a number of years now. Many of those are common between genders but there are some issues that are different for female and male participation. I am not sure precisely that I could outline all of the pieces of work we have done, but I think that is an area we have looked at. One point to make just as a qualification, without wishing to take away from the broad thrust of what this report is saying, is that there is a need to be careful and aware of the limitations of GDP as a measure of output and particularly wellbeing, so some of the things we know about GDP and its limitations include that it does not take into account work undertaken in the home, for example. Another thing that we know, and I think the Secretary outlined this in a speech made last year, is that productivity and output is measured better in the market sector than it is in the non-market sector. I think this particularly goes to the point made in this report about a gender productivity gap. To some degree the report refers to sectors such as the health and I think the education sectors as being sectors that are low productivity. It might be better to describe those as sectors that we do not measure productivity well in. That could then affect your analysis.

Senator COONAN—Given that, can you point me to any analysis which actually measures the impact of these factors that were identified in the report on the economy?

Mr Henry—In the Intergenerational Reports, I think in the first and certainly in the second and in the most recent one, there is some sensitivity analysis. It asks the question: what would be the impact on GDP and GDP per capita of lifting rates of participation of various cohorts? That work attempts to quantify what would happen to gross domestic product and gross domestic product per capita if, for example, rates of female participation were to increase by certain amounts. There is some sensitivity analysis there.

Senator COONAN—I appreciate how difficult this may be to quantify, but has there been any measurement of the potential flow-on effects of the gender-based gap on overall female workforce participation? The World Economic Forum Global Gender Gap Report scored Australia at something in the order of 50 per cent. Has there been any measurement of what flow-on effect there might be if this gap is right on overall female workforce participation?

Mr Henry—I understand—you are asking the question: if Australia were to lift its rates of female participation to, say, the best performing in terms of female workforce participation, what would that do to the level of GDP and the GDP per capita?

Mr McDonald—I think we might have to take that on notice to see what analysis we have. There may well have been some that we have done and there may be some that it is in broader cross-country studies.

Senator COONAN—I realise that is just a scale. I am just interested in whether there has been any measurement.

Mr McDonald—We are happy to take that on notice and see what we can provide.

Senator COONAN—Has Treasury performed any specific analysis on the gap between historic male and female productivity rates? That is the productivity question, not the participation question.

Mr McDonald—Not as far as I am aware. I just looked at this paper fairly recently. I guess there is the point I have already made which is that you would expect the extent that data shows such a gap that it would, at least to some degree, be reflecting differences in the quality of the measurement of productivity that are well known. I think that is certainly an interesting area to look at further, and I expect it is something we would do further work on. The potential qualification on that is that productivity data is often best looked at in aggregate and overrun of years. As you seek to disaggregate it, which is natural to do to try and work out the performance over different periods and in different industries, the quality of data necessarily declines as you do that. That is also a factor to take into account in the analysis. We will have a look at that as well and see what we can provide.

Senator COONAN—This is probably a flipside of the same question, but, what work has been done on improving the gender based gap in workforce participation within the economy? Is that the flipside of that question in that you would be looking at it or is there anything that you can point to?

Mr McDonald—I think these questions are now getting to work that colleagues in fiscal group may well be better placed to answer.

Dr Gruen—I can answer, I think, from the Intergenerational report. The Intergenerational report does provide estimates of Australia's participation rate compared to other countries for both males and females. One of the interesting things is that participation rates for females of prime working age in Australia is actually higher than the OECD average and it has been rising faster than the OECD average, whereas with males the opposite is the case. For both prime age and older women Australia's participation rate has been rising more rapidly than the OECD average, whereas for men in prime age Australia's participation rate is significantly lower than the OECD average, which is at least of some interest.

Senator COONAN—Does Treasury have any analysis which supports the inference—and I call it an inference because I just do not know what the data is—that increased female participation in senior positions within the Australian workforce will lead to an overall increase in female participation?

Dr Gruen—I do not think we have any specific evidence on that but it sounds plausible.

Senator COONAN—I did not have any data so I was asking that question in that way. Representation of women on boards and in executive management of corporate Australia remains, as I think we all agree, stubbornly and disproportionately low. In fact we are going backwards according to the latest data. There has been a steady stream of calls from regulatory agencies, peak representative bodies and business leaders for voluntary and early action to address the gender gap. There is certainly some momentum. Is Treasury monitoring, or at least aware of, policies to address this being implemented in Spain, Norway and France which address the gender gap in terms of female participation in leadership positions in the workforce?

Dr Henry—We are certainly generally aware of what is happening in those other countries. But as to the implications for corporate Australia, it may be that somebody from markets group would be able to provide some detail. Given that you have asked the question now, it may be that some of them are presently scurrying around looking for some of that detail. We will see. But I do not have anything at my fingertips. I understand the question and the significance of it, but I am not aware of any work that we are doing in that area.

Senator COONAN—Perhaps it is a question for the minister, then. Is the government content to leave it to the private sector to address the gender gap that currently exists within the top echelons of business in terms of female participation in leadership positions? Is the government concerned enough to formalise what appear to be voluntary actions taken by the Australian Stock Exchange and other bodies?

Senator Sherry—In a previous ministerial capacity—corporate law—I can recall that this matter was discussed at the ministerial council on at least two occasions. The rough figures as I understand were 12 per cent declining to less than 10 per cent—that is very approximate. It was a cause of concern. There were a range of responses discussed. Since that time, I am aware that the ASX and the Australian Institute of Company Directors have announced some initiatives. I know that they are on the public record. Whether the government would go beyond what has been announced so far would be a matter for my colleague Minister Chris Bowen. I would have to take on notice whether it would be his intention—and obviously a collective decision of government—to proceed beyond that. I said on a number of occasions

at the ministerial council and publicly that the decline in female participation at board level was a cause for concern and needed to be addressed.

Senator COONAN—Thank you for that, Minister. When taking this on notice, could you ask Minister Bowen whether the government considers that imposing a timeframe or at least monitoring a timeframe with particular targets is what the government is encouraging.

Senator Sherry—I will take that on notice.

Senator COLBECK—I want to ask some quick questions about the bank deposits guarantee. I understand that the government made an announcement in respect to the wholesale funding guarantee, which has been withdrawn. What is the timeframe for the removal of the bank deposits guarantee? What is its ongoing effect on those funds that are frozen? Are there any moves to modify what is currently happening in that respect?

Dr Henry—No, there are not. At the time that the guarantee was announced—which, if my memory serves me correctly, was 12 October 2008—the government said that the deposit guarantee, which was for deposits up to \$1 million, would remain in place for a period of three years and would then be reviewed.

Senator COLBECK—What about the contributing effects of that on particularly those accounts that remain frozen because of the fear of flight from those funds? How do we manage to get around that particular circumstance and the impacts that that is having at quite a personal level in some circumstances?

Dr Henry—As for those funds that you are referring to, we have been monitoring developments in those funds. We were monitoring developments in those funds actually before the guarantees were announced and we have continued to monitor developments in those funds subsequently. Whilst it is true that a significant number of the funds remain frozen to redemptions, except in cases of hardship and some other cases where redemptions are being made, I think the general story is that the industry has continued to manage the liquidity of those funds very well. That is the general story. Where individuals with investments in those funds are experiencing difficulty there are arrangements in place, which ASIC in particular is monitoring, to allow access to the funds. Our colleagues from Markets Group would be able to add further detail.

Senator COLBECK—So there is a formal process in place for access in hardship conditions to funds that are currently held?

Dr Henry—Yes, there are specific conditions which if satisfied would allow access. The precise details I can get for you and I am quite happy to take that on notice or, alternatively, a question could be put to one of the Markets Group people here.

Senator COLBECK—I would certainly be interested. I have some constituents of retiring age whom I would consider to be doing it fairly tough, particularly one of the partners. The other is of pension age, living in fairly meagre circumstances in a camper van in a caravan park and wanting to buy a house but has funds frozen in one of these accounts and would like to get access to them. His request to me, and he has asked the Prime Minister this, is how he goes about it. I think I have probably gone one better in having a chat to you, with you being in the suit that you are in. But if there were hardship provisions that we could point him to

that would perhaps be a response. From my perspective, this puts a real-life perspective on the situation that exists with a lot of people out there having these accounts. I am not sure as to your perspective on the need for continuation of the guarantee. I would be interested in that. Certainly that is the real-life impact of what is going on in some circumstances.

Senator Sherry—That is understood but I would certainly not accept that the guarantee of itself was the only issue around the freezing of funds. What I found interesting was that a significant number of funds of that type actually collapsed before the financial crisis even hit the world. It has been well canvassed over a period of some years at ASIC estimates that Fincorp and others actually fell to pieces. So I think there were some regulatory issues as well and that, further to that, there may well be some matters as to how the level of risk in some of these funds is disclosed, the extent to which the risk is readable and understandable, so there are a number of issues here that extend beyond the guarantee itself.

Senator COLBECK—I understand the government's perspective on this but I can say to you, Senator Sherry, that this is this couple's reality. Their fund is telling them they cannot get hold of this money because of the deposit guarantee. They would like to know when it is going to be released so that they can do that. Once they have got access to their funds they can actually buy themselves a home. That is the practical bottom line reality that they are facing right now; that is what they are being told. Their fund is saying to them that because of the guarantee they cannot get their money. So that is their reality and if the government has a perspective on it I understand that.

Senator Sherry—I well understand the reality of people who are not able to access moneys or who in fact cannot get money because funds have collapsed.

Senator COLBECK—Knowing the detail of it and not putting all that on the record here I do not think that is the issue. I have all the detail.

Senator Sherry—There are certainly plenty of people who are in those circumstances—that is, collapse of funds, redemption of funds, access to funds which have not collapsed. There is quite a mixture.

Senator McGAURAN—250,000—

Senator Sherry—Yes, there is quite a mixture—

Senator McGAURAN—have had their funds frozen.

Senator COLBECK—If it were in a fund that I thought was in a dubious situation I would not have put the situation on the table here today.

Senator Sherry—But it would be wrong to say that the bank guarantee in and of itself has been the only factor in that mix of issues. As to the figure of 250,000, Senator McGauran, I do not know what the latest figure is. I understand that was the figure at some point in time. ASIC or the Markets Group Treasury I am sure could give us an accurate update. Whatever the personal circumstances of the individuals whom Senator Colbeck has raised, I understand that a number of funds have come back online. The number that have come back online, so to speak, I am not aware of, but Markets Group or ASIC may be aware and can give us the latest figures.

Senator COLBECK—Dr Henry, on the flip side of that, what would be the impact of the removal of the guarantee prior to the date that the government put in place initially? Can you give us some sense of that?

Dr Henry—No, I am sorry, Senator. I do not want to speculate on the possibility of an early removal of the deposit guarantee. At the that time the government announced the deposit guarantee it made it quite clear, and for good reason, that the deposit guarantee would remain in place for a substantial period of time—namely, for three years. I do not think it would be helpful, and it certainly would not be appropriate, for an official to speculate on the early removal of it.

Senator COLBECK—Okay.

Senator CAMERON—Dr Gruen, you said earlier that it was your professional judgment that the stimulus has been more effective than you had thought it would be. Has anything you have heard this morning in the questioning from the coalition members of the committee given you any cause to rethink your professional judgment?

Dr Gruen—Let me restate what I think I said. We used the same multipliers in the MYEFO as we did in the budget, and my professional judgment is that those are conservative estimates of the effect of the fiscal stimulus. There is a margin of error around our estimates, but I think it is more likely that we have underestimated the effect of the stimulus on growth rather than that we have overestimated it. But I also made the point that we are not certain about this. There are margins of error about these things, but we have assumed estimates for the multiplier and, therefore, for the effect on growth we think they are prudent and conservative.

Senator CAMERON—Thank you. I want to try to put this into a bit of context and come back to the issues. We were facing a global financial crisis that was one of the greatest economic challenges governments have faced since the Great Depression. Is that correct?

Dr Gruen—Certainly this was a huge shock to the global economy, particularly to advanced economies.

Senator CAMERON—And the Australian economy has come out of that challenge quite effectively in terms of employment and growth; is that correct?

Dr Gruen—It is certainly the case that we have had a very mild downturn and that the unemployment consequences of this shock have been significantly less than most people, including us, thought was likely.

Senator CAMERON—It has been stated in the financial press that Australia is the envy of the rest of the world because of our handling and outcomes of the global financial crisis. Would that be a fair statement?

Dr Gruen—I am not really in a position to comment on commentators. I think I would leave it to others to make judgments about the effectiveness of the response, but it is certainly the case that the Australian economy has performed very well through this period.

Senator CAMERON—It has been continually put here that debt is the big problem. Has the borrowing been responsible and necessary, in your estimate?

Dr Gruen—A consequence of running a fiscal stimulus in a situation in which your tax revenues have fallen is that you do have to borrow the money, so there is no question that a consequence of providing the fiscal support to the Australian economy has been the need for the government to borrow. It is also true that the forecast rise in Australia's federal government net debt, which I think is the appropriate measure to look at, in the updated MYEFO numbers, is set to peak at, I think, 9.6 per cent of GDP. If we compare that to most advanced economies, that is a very low number. The projection for most of the major economies of the world are that net government debt will reach a number like 90 per cent. So, by the standards of most countries, we have extremely low levels of government net debt.

Senator CAMERON—Can I take you to the argument that has been put up continually through this whole debate on the stimulus package—that the government spending would create more problems than it would solve. I am having a look at the stimulus package results in retail trade, on page 11 of MYEFO, and it shows a huge jump in retail trade in Australia compared with the G7. Is that a significant part of providing the confidence in the economy and providing a direct stimulus to maintaining that confidence?

Dr Gruen—The first cash payments to households were received in the first weeks of December 2008, and retail trade in the month of December rose by four per cent, in seasonally adjusted terms, compared with November. It is certainly the case that, over subsequent months, it stayed high. So our estimate is that a significant proportion of the cash transfers were spent by households, partly on retail trade and partly on other things. So I think the logic of those cash transfers was that they could provide rapid support to demand in the Australian economy, and I think the evidence does support the argument that those transfer payments were successful in doing that.

Senator CAMERON—So, on the cash-transfer debate against the tax-cut debate, because of the speed and because of the outcome, your judgment is that the cash transfer did the job that it was designed for?

Dr Gruen—I think the outcomes support the sorts of estimates that we used. I think the estimate we used was that something like 70 per cent of the cash transfers would be spent over our forecast horizon. The evidence we have seen from the performance of retail trade, and also consumption, in the national accounts, has not led us to change that estimate. So it is certainly the case that the cash transfers seem to have done roughly what we expected them to do.

Senator CAMERON—The estimate is that the stimulus package has saved 210,000 jobs. If those 210,000 jobs had disappeared and no stimulus had been undertaken, has any debate or analysis taken place as to what effects that would have had on the economy?

Dr Gruen—I think that estimate is an estimate of the peak effect of the stimulus. So, at its peak, I think our estimate was that employment is 210,000 higher than it would otherwise have been, or that many jobs were saved. There are a range of benefits from that. Some of those people would have been unemployed for an extended period of time and people who are unemployed for an extended period of time suffer atrophy to their skills and general dissatisfaction with society, so I think there are considerable benefits, both economic and non-

economic, to not having the unemployment rate rise by as much as it would have if this action had not been taken.

Senator CAMERON—Thanks.

Senator EGGLESTON—I would just like to ask some questions about the level of foreign investment in Australia in recent times. Have the patterns of countries from which foreign investment is coming into Australia changed relatively, and has the purpose or the intention of such investment changed?

Senator Sherry—I think that would be best put to the Foreign Investment Review Board markets group because they would have data and statistics.

Senator EGGLESTON—Okay. That is fine. There have been a number of articles about our recovery from the global financial crisis and the fact that we did not go into technical recession, but in that second quarter there was quite a lot of activity from the Chinese in terms of purchases of mineral resources and so on. Would it be a fair comment—and I am just asking for an opinion—that China played an important role in preventing us going into a technical recession? Had the Chinese stimulus package not led them to keep on building infrastructure, would we perhaps have gone into recession?

Dr Henry—As I was indicating to Senator Bushby earlier, we have not undertaken an analysis that allows us to break up the various contributors to the stronger than anticipated GDP outcomes that we have had. I cannot say for sure that, in the absence of Chinese strength, the economy would definitely have recorded at least two consecutive quarters of negative GDP growth. I can say with somewhat greater confidence that, as Dr Gruen said earlier, without the fiscal stimulus package we would have, on our figures, recorded four consecutive quarters of negative GDP growth. But your question is, as I understand it: supposing that we had had the same fiscal stimulus package but China had not had its fiscal stimulus package, would the Australian economy have recorded two consecutive quarters of negative GDP growth? I do not know that for a fact. It is certainly possible.

Senator EGGLESTON—One can only speculate of course. I noticed Australia has come to a loan arrangement with Indonesia for the equivalent of US\$1 billion, and I just wondered if you could be good enough to enlighten us about the purpose of that and its terms and conditions? Is it likely to be called upon?

Mr Playford—The loan with Indonesia was entered into at the end of 2009. Economic conditions in Indonesia have improved significantly since the intention to enter the loan was first established. We are not expecting at this stage that the Indonesian government will draw upon the loan. The loan is a standby facility if it is unable to finance its budget deficit. At this stage the Indonesian government has already year to date financed 15 per cent of its borrowing requirements. We would anticipate that the Indonesian government will continue to be able to finance the activity.

Senator EGGLESTON—I see here that it says that the nature of the loan agreement was to help mitigate the effects of the global financial crisis as it impacted on Indonesia. I suppose we have not heard a lot about what happened to the Indonesian economy, and I was just interested in the fact that Australia felt able to provide this credit line, I suppose, of a billion

dollars to assist Indonesia. I wondered about the creditworthiness of Indonesia, but you have answered that question in part.

Mr Playford—The standby facility which Australia entered in conjunction with the Asian Development Bank and the World Bank helped provide a level of confidence for the international financial markets around Indonesia. Certainly the Indonesian government believes that has helped support their ability to access financial markets over the last 12 months.

Senator EGGLESTON—In other words, we were in effect guaranteeing the credit worthiness of Indonesia or suggesting that they were worthy of receiving credit?

Mr Henry—We were not quite guaranteeing, but I think we were giving some confidence to global financial markets that Indonesia's fiscal financing task would be supported and we were prepared to offer some support ourselves. I think that contributed to confidence globally that Indonesia would be able to finance its budget.

Senator Sherry—I was at the Asian Development Bank meeting in Indonesia last year. There was a general sense that Indonesia had done comparatively well in the circumstances. The advice here indicates that its largely domestically oriented economy continued to grow at more than four per cent annually, so despite the economic and financial difficulties Indonesia, comparatively, has done well.

Senator EGGLESTON—I went to a forum on Australia-Indonesian relationships last year where their trade minister, I think, said they had fundamentally followed the advice of the IMF regarding the management of the global financial crisis, but they were not sure what their degree of growth was. So thank you for that, Minister.

Senator JOYCE—Are we currently capping spending growth at two per cent?

Mr Henry—That condition of the medium-term fiscal stabilisation strategy becomes effective when growth has returned to normal levels. Growth is presently below trend and therefore that particular leg of the fiscal strategy is not applicable right at the moment.

Senator JOYCE—What is our growth at the moment?

Mr Henry—Growth through the year to the latest data, to September, is half a per cent. Our forecast is that growth will be below trend this financial year, 2009-10.

Senator JOYCE—And what is trend?

Dr Gruen—Trend is three to 3¼.

Dr Henry—Senator, I can add to that. Real GDP growth—and I am relying on MYEFO figuring here—09-10 is 1½ per cent; 10-11, 2¾ per cent. Then we have got growth at above trend in 11-12, 12-13, 13-14 and 14-15—those are the four per cent figures. Over that period with those four per cent real growth figures the commitment to hold real spending growth to two per cent applies. In the MYEFO figures the real spending growth is actually below two per cent in those two years, which are within the forward estimates period.

Senator JOYCE—So in 10-11 and 11-12—

Dr Henry—11-12 and 12-13.

Senator JOYCE—In 11-12 and 12-13 the spending growth does not have to stay below—

Dr Henry—No, I am sorry, I misunderstood where you were going. In 09-10 and 10-11 it does not have to be below two per cent real because the economy is growing below trend in those two years.

Senator JOYCE—What is spending growth at the moment?

Dr Henry—In 09-10 real growth in spending is 5.1 per cent and then in 10-11 it is minus 1.3 per cent. That is because of what we were discussing earlier, that the fiscal stimulus is unwinding through that period.

Senator JOYCE—That is just by reason of the parabola, the curve—

Dr Henry—Correct.

Senator JOYCE—and we are coming down the other side.

Dr Henry—Yes.

Senator JOYCE—So if you look at it in a comparative analysis with the year before it is less, but if you look at it in a lineal relationship over a number of years it is actually still higher.

Dr Henry—Correct.

Senator JOYCE—If we take it back to a lineal relationship rather than a parabolic relationship, what is the average spending of the government over the last three years, as a percentage? You are having one of those moments that I have, where there is an answer there but you just don't know whether you should say it!

Dr Henry—No, it is not that. I can see multiple answers. I am just not sure which is going to be more helpful to you.

Senator Sherry—Give them all to him and then he will pick them out.

Dr Henry—I will give you some answers. Let us consider government spending as a proportion of GDP. Obviously that is going to be affected by the cycle because government spending is going to go up, so the numerator goes up, and GDP is going to be lower than it otherwise would have been because of weakness in economic growth. So for those two reasons that ratio is going to go up. That is certainly what we see happening. In 2009-10, which is where the peak of the fiscal stimulus occurs, the payments to GDP ratio is 26.7.

If we go back some years, that was tracking on average around 24. In fact it came down to a low of 23 in 2007-08, but a normal level would have been a bit over 24 per cent of GDP. So that goes up to 26.7. We then have it on the projections coming back to 24.4 per cent of GDP by the end of the projection period, 2012-13. So that is one way of looking at it.

Senator JOYCE—Just to provide a comparative analysis, what is the spending to GDP ratio of the United States?

Dr Henry—It is certainly higher than ours—a good deal higher than Australia's spending to GDP ratio. Because we are both federal systems, a meaningful comparison would take the federal government here—

Senator JOYCE—And add the states.

Dr Henry—and add to it the states, and do the same in the United States. When you do that, I have seen OECD figures that show that the total with respect to the United States public sector is significantly higher than here. I know their tax to GDP ratio is broadly similar, but they have a budget deficit of about 11 per cent of GDP—so their spending to GDP must be much higher than ours.

Senator JOYCE—While you are looking for that—

Dr Henry—I may have to take it on notice. I am not sure whether we have that here.

Senator JOYCE—We have gone through and we have said that, when growth goes back to trend, we will cap spending at no more than two per cent. I understand it is currently at the top of the curve, at 5.1 per cent. But the other mechanisms indicate that we are getting a clash between monetary and fiscal policy. The Reserve Bank is pushing interest rates up. If the Reserve Bank is pushing interest rates up, wouldn't it make sense, in any way, shape or form, to take away further stimulus into the economy at this point in time? On top of that, acknowledging that really the greatest mechanism of stimulus to the Australian economy is its connection to the Asian economies, what effect are our progressive stimulus payments going to have on them?

Dr Henry—Our fiscal stimulus would not have a lot of impact on GDP growth rates in our trading partners. It probably does have a bit of an impact on New Zealand, and that is a significant growth trading partner. But, putting New Zealand aside, it would not have much of a spill-over impact globally. So I can answer that part of the question.

As to the trade-off between fiscal policy and monetary policy, it is usually the case that a tighter fiscal stance, other things being equal, would provide the scope for less restrictive monetary policy. That is usually the case. But it is also the case, as I indicated earlier, that these two things—the stance of fiscal policy and the stance of monetary policy—are overwhelmingly affected by the state of the business cycle. So, as I indicated earlier, it is quite often—it is usually the case, actually—that, as fiscal policy is tightening, so too is monetary policy tightening. So it is very difficult to draw a simple conclusion about a link between the size of a budget deficit and the stance of monetary policy.

Senator JOYCE—Let's work on the premise that the correlation between the two events is not apparent. Shouldn't that be yet another argument to say that, in that case, we need to pull back on fiscal stimulus anyhow, because its correlation to effect is not present and we should just save ourselves the debt that we will have to repay?

Dr Henry—No, because the reason the correlation is not there is that the underlying strength of the economy tends to drive both. It is the underlying strength of the economy that is going to determine the future course of interest rates—generally, that is what the history suggests.

The underlying strength of the economy also has an impact on the budget deficit. As the economy is strengthening, is history is any guide, one should expect to see the budget position improve and one should also expect that over time interest rates would move up. When they would move up and how much they would move up are obviously matters that I would not want to speculate on, and I will not. But generally that is the pattern that history reveals.

Senator JOYCE—Because of the wonders of a range of things, including such things as APAC, there are people watching this. We hear statements about the 210,000 jobs saved and we hear about the fact that the transfer payments—the \$900 cheques—were part and parcel of that. But a \$900 cheque is predominantly a mechanism by which people buy consumables not necessarily a mechanism that increases the aggregate size of the economy, because the economy has the capacity to deal with it as it is. If someone buys an electronic consumable, a new retail store does not have to open up to sell it to them. At best, they open up a new checkout to sell it to them or they get it out of storage to sell it to them or they import a new container. The economy has the capacity to handle it. It does not inspire aggregate growth in the economy. That is the premise that I put forward. You would have a different view. What is your view about how these cheques worked? If 210,000 were saved, where are they? What is the theory behind how these jobs were created?

Dr Henry—Let us take your example. This is not the whole story, but it is part of the story. What we would say is that without the fiscal stimulus package some of those people working in retail stores would have lost their jobs, and that would be part of the 210,000.

Senator JOYCE—Wouldn't it just be the case that these people, if there is flexibility in wage arrangements, would get more overtime or moved from a different section?

Dr Henry—We have seen that, too. As Dr Gruen was saying earlier, we have seen average hours worked fall quite considerably. Presumably, some of those people serving in retail stores would be working fewer hours—and they are working fewer hours notwithstanding the fiscal stimulus package. But without the fiscal stimulus package some of them would have not only worked fewer hours but would have worked no hours; they would have lost their jobs.

Senator Sherry—Senator Joyce, your colleague the shadow Treasurer, Mr Hockey—and he was not the only one, I have to say; there were some economists and other critics at this time last year in the run up to the budget and after the budget—was claiming that Australia would see one million unemployed. That was the claim being made by some people last year, including your colleague. Clearly, we are nowhere near one million unemployed and fortunately we are not going to get anywhere near one million unemployed. I have referred to this on a number of occasions. You cannot have it both ways. Here you are criticising the government of the day for its stimulus package—

Senator JOYCE—Minister, with all due respect—

Senator Sherry—but you were highlighting what you believed would occur without a stimulus package and claiming that we would see one million unemployed. You cannot have it both ways.

Senator JOYCE—With all due respect, your assertion is bringing a whole new section to the debate that was not even part of the discussion. I suppose you are welcome to make it. I do not know whether that is a question to me or a statement by you that you wished to make.

Senator Sherry—It was a response to your question.

Senator JOYCE—Tell me what my question was, then.

Senator CAMERON—Have you forgotten?

Senator JOYCE—No. It was a response to my question, so I want to know what the minister thought that my question was.

Senator CAMERON—This is not about tricks; this is about serious economic issues. Try and be a serious player.

Senator JOYCE—What was the question, Minister?

Senator CAMERON—Try and be a serious player.

Senator Sherry—You were asking about a range of—

Senator JOYCE—If he needs you to defend him, then he really is struggling.

Senator CAMERON—You are not a serious player.

Senator Sherry—You were asking about a range of reasons or factors as to why unemployment did not go up to the extent that was believed this time last year.

Senator JOYCE—No, the question was about the effect of the—

Senator Sherry—and then the Treasury secretary responded. You specifically refer to \$900 payments and how that saved jobs. The Treasury secretary referred to people not being put off in the retail sector, for example. You then came back with a couple of other examples. That was the tenor of the questions and the general discussion.

Senator JOYCE—It was a discussion about the mechanism of effect, and your answer had absolutely nothing to do with the question.

CHAIR—Minister, have you finished?

Senator Sherry—I have.

Senator JOYCE—When we discuss the federal net debt position obviously we are taking into account what is owed to us by states and territories. Dr Gruen, when you look at the net debt position of the Commonwealth you take into account the money owed to the Commonwealth by states and territories. Is that correct?

Dr Gruen—Certainly the net debt is the gross debt minus all the debt-like assets held by the Commonwealth, a large part of which would be in the Future Fund—but, yes.

Senator JOYCE—It is cash and other deposits, and moneys owed by states and territories. How much is actually owed by states and territories?

Dr Gruen—I think it would be probably be best to address those questions to the fiscal group if you want detail about that.

Senator JOYCE—So in the net debt position we also have the money in the Future Fund.

Dr Gruen—Not equities but the debt-like assets.

Senator JOYCE—The assets in the Future Fund?

Dr Gruen—Yes, financial assets.

Senator JOYCE—Assets in the Future Fund at this time are what—about \$65 billion?

Dr Gruen—You want just their debt-like assets, not their equities, because that does not subtract from net debt.

Senator Sherry—I think from the evidence we had from the Future Fund—I do not know whether you were there, Senator Joyce; I cannot recall—the \$65 million—

Senator JOYCE—Billion.

Senator Sherry—Sorry, \$65 billion. There are a range of additional assets in the other funds that are administered by the Future Fund—the infrastructure and the health. So I think for the sake of accuracy the \$65 billion may just relate to the Future Fund for the public sector superannuation liabilities.

Senator JOYCE—The amounts in the Future Fund are there to deal with superannuation liabilities. Are the superannuation liabilities included in your net debt position?

Dr Gruen—Senator, if you want to have a detailed discussion about this I think it is best to do it with the fiscal group.

Senator Sherry—What is included in net debt has not changed under this government from what was included under your government. That is the bottom line, Senator Joyce. You cannot argue that you exclude assets from net debt because there is a Labor government in power when you did not exclude them when you were in power. They are treated in exactly the same way.

Senator JOYCE—We are just giving an explanation. You talk about net debt, but that really takes into account that you call what is owed to you by states and territories and asset, and some of them are lumbered with debt. You take into account items in the Future Fund. That money is actually put aside to deal with superannuation liabilities. You bring into account things such as HECS debt. Good luck collecting that—wandering around the countryside finding students to see if they ever want to pay you back! You take into account things such as IMF subscriptions.

Senator Sherry—If you are criticising that approach, and you appear to be doing so, why didn't you criticise your own colleagues when they were in government for taking exactly the same approach? Why didn't you come to Senate estimates and say to Senator Minchin when he was finance minister and sitting where I am, 'It's not reasonable to include these sorts of assets in net debt'? My response to you is that you are inconsistent in your critique. If you criticise us for including those assets as part of net debt why didn't you criticise your own colleagues at the same time?

Senator JOYCE—That is a very good question and I will take that question, Senator Sherry.

Senator Sherry—I am not asking you a question. I am answering your question.

Senator JOYCE—I will answer the question now. There is a very good reason. When Senator Nick Minchin was finance minister, we were not heading towards \$245 billion—

Senator CAMERON—You did not have a global financial crisis either, did you?

Senator JOYCE—in gross debt. That is probably a very good reason.

Senator Sherry—My answer to that would be—

Senator JOYCE—And when Senator Minchin was there we did not have to do appropriations to allow you to go to \$200 billion in debt; we actually had a surplus in place.

We had \$6 billion put away in the tertiary endowment fund, we had \$2 billion put away in a medical fund, we had money put away in the Future Fund and we had a budget in surplus. That is why I never asked those questions of Senator Nick Minchin. There is absolutely no consistency whatsoever between your management and what was managed under the coalition government.

Senator Sherry—As I pointed out twice earlier today, which you and your colleagues do not like being pointed out, if you want to use the figure of gross debt, when we came into government you had a gross debt figure, which is the one you like to refer to most regularly, of some \$58 billion. You cannot have it both ways.

Senator JOYCE—And you were claiming it is a critique for your management that you were going to have four times that.

Senator Sherry—Chair, I am happy to take questions and have debate but—

CHAIR—Yes, I should point out that—

Senator JOYCE—I will let someone else ask a question.

CHAIR—I think that is the cue for Senator Abetz to begin.

Senator ABETZ—I have got a few questions generally on that, but it will not surprise that I also have a question or two on OzCar. So whoever that official is, can they come forward. Can I ask in relation to the overall budgetary position: is it agreed that a critical next step to sustainable growth for the government is to articulate a convincing plan to put the budget back into surplus quickly through—I dare say you would assert that you have got a plan to put the budget back into surplus quickly, and I do not want to get into that debate about whether it is quick or slow or whatever—expenditure control and not through higher taxation?

Senator Sherry—I think we would be repeating the discussion we had earlier. Dr Henry referred to the parameters that the government has announced in terms of restraining expenditure to two per cent as trend growth resumes. There has been a fair discussion about that. I know you were not here, and I am not criticising you for that because I understand the—

Senator ABETZ—I was half listening in as well.

Senator Sherry—I think we are going back over ground that has been canvassed.

Senator ABETZ—Yes, but are we putting greater emphasis on the expenditure control or getting more money in for the repayments? What is going to be the focus?

Senator Sherry—There has been ongoing focus on expenditure. I can assure you of that because I sit on the Expenditure Review Committee, for example, and there has been significant restraint on expenditure in a range of measures that have been well detailed in budgets—

Senator ABETZ—Schools, pink bats.

Senator Sherry—A range of expenditure reductions have been announced. I do not have the list here in front of me today. I actually did have it in the finance estimates because that deals with expenditure and expenditure reductions, but there have been a range of significant

reductions and that work is always ongoing. That is part and parcel of the work of the Expenditure Review Committee and that will continue.

Senator ABETZ—All right. So we have had significant reductions on the one hand but a stimulus package on the other. Can I simply ask then: in the two years to June 2010, are we agreed that Commonwealth spending as a percentage of Australia's gross domestic product will have risen from 24 per cent to approximately 27.8 per cent?

Senator Sherry—Again, Dr Henry can check the figures, but I think they were the same figures that he gave earlier and he gave an explanation for them as well. We have traversed this.

Senator ABETZ—I just want to make sure that those figures that I am quoting are accepted.

Dr Henry—I indicated earlier in response to a question from Senator Joyce that the 2009-10 figure, which is the peak figure, is 26.7 per cent.

Senator ABETZ—All right.

Dr Henry—The figures have been rebased because of the new national accounts figures released in early December. I presume you are reading from the budget papers, and in the MYEFO the figure was 27.8—

Senator ABETZ—Yes.

Dr Henry—but because of the—

Senator ABETZ—And is that updated now?

Dr Henry—Yes.

Senator ABETZ—To?

Dr Henry—To 26.7.

Senator ABETZ—Thank you for that. Was that publicly announced before today?

Dr Gruen—Certainly.

Senator ABETZ—When was that?

Dr Gruen—The data was updated on the website and there was a media release.

Dr Henry—There was a media release on 8 December last year.

Senator ABETZ—Eight December? Chances are the coalition was undertaking other matters at that time, so that is why it may have escaped my attention.

Senator Sherry—Well, you will get distracted!

Senator ABETZ—Thank you for that clarification; I do appreciate that. As a general concept, do we agree that it is not only how quickly a country goes into deficit that matters, but also how quickly it comes back out of deficit for its long-term economic wellbeing? Is that a proposition that we agree with?

Senator CAMERON—In what context?

Senator ABETZ—We have gone into debt to very quickly, into deficit very quickly, there is no doubt about that. I think people agree to that. Even a distinguished head of Treasury I think said ‘Go early, go big and go domestic.’

Senator Sherry—He was not referring to going into debt though! Dr Henry was referring to the stimulus package.

Senator ABETZ—Sorry, and how did we fund the stimulus package?

Senator Sherry—Government expenditure.

Senator ABETZ—And how was that raised? Via debt, Minister?

Senator SHERRY—Yes.

Senator ABETZ—Thank you. So we got into debt to stimulate the economy, which was seen as being important, and I want to draw a line under that and make no comment about that. What I am now asking is—

Senator Sherry—I had not finished my answer. We traversed most of this ground, if not all of it, earlier in the discussion with Senator Joyce this morning. As was pointed out, the financial and economic crisis led to a very significant reduction in revenue. We had a significant discussion about that earlier.

Senator Abetz—I accept all that, but what I now want to move on to is the importance of moving our country—or economy, same diff, in layman’s terms, to me—as quickly as possible out of debt, that there is an imperative that we do that as expeditiously as possible, just as a general principle. There is nothing untoward about that proposition, is there?

Dr Henry—One has to be careful.

Senator ABETZ—We always have to nuance everything, don’t we?

Dr Henry—I am afraid we do, and this might be more than a nuance.

Senator ABETZ—All right.

Dr Henry—The appropriate stance of fiscal policy, as you obviously understand very well, has implications for the profile of net debt. The appropriate stance for fiscal policy depends upon the underlying macroeconomic circumstances. When you say that it would be sensible to move to zero net debt as expeditiously as possible, my word of caution is you might want to consider the impact on the macro economy of the fiscal action that would be required to achieve that.

Senator PRATT—Put the GST up like New Zealand has?

Senator Bushby interjecting—

CHAIR—There is a lot of conversation across the table now, and I am sure it is very distracting for witnesses.

Senator ABETZ—I think the presses have been stopped for that.

CHAIR—Senator Abetz, Dr Henry has not—

Senator JOYCE—Is he going to put the GST up?

CHAIR—I am prepared to adjourn early if you want to just have a discussion—

Senator PRATT—Sorry; I beg your pardon, Chair; I should not have interjected.

CHAIR—but we were listening to the answer from Dr Henry.

Senator JOYCE—Did you say ‘put the GST up’?

Senator PRATT—No, that New Zealand has.

CHAIR—Well—

Senator PRATT—Sorry. I beg your pardon, Chair. I apologise.

CHAIR—Conversations across the table means I cannot hear what is going on and it is distracting for the witnesses. I think sometimes it has been distracting for the questioners. Could we let Dr Henry finish in the five minutes we have before we go to a break.

Dr Henry—No, I had finished.

Senator ABETZ—What I was wanting to do was contextualise my proposition that persistent deficits, would you agree, lead to slower employment growth and slower new investment as government borrowing expands to fund a growing national debt as a general concept? That was going to be the follow-up question, so I will give it to you all at once so you can answer in one and then I will move on.

Dr Henry—As a general proposition, once the economy has got back to full capacity utilisation then, as a general proposition, a government contributing to aggregate demand through running a budget deficit, for example, could be expected to crowd out private sector activity. In the intervening period, that is before the economy gets back to a position of full capacity utilisation, the extent to which government activity crowds out private sector activity is considerably more ambiguous. Certainly when the economy was weakening, and weakening rapidly as we perceived that it was back in late 2008, we did not see much risk of a fiscal expansion crowding out private sector activity at that time. Obviously now that the economy is in recovery at some point this will become a consideration but, as Dr Gruen said earlier in response to questions from your colleagues, the Australian economy is right now some distance from full capacity. The reason for that is we are in our second year of well below trend growth. We have opened up an outward gap, in economists language, whilst the unemployment rate is as of today sitting at around 5.3 per cent and that is not a particularly high unemployment rate, nevertheless average hours were underperforming considerably so we think there is substantial spare capacity in the economy at this point. We would not think that there is a lot of crowding out of private sector activity at the moment. You are right to draw attention to it.

Senator ABETZ—For the future.

Dr Henry—Sure.

Senator ABETZ—That is what I am talking about because with ill-disciplined governments, and I do not want to put a party political label on that, but there is,—oppositions do not control budgets, usually—deficits have a tendency to persist if a government is ill-disciplined. If you allow the deficit to persist then it would have the impact of slowing employment growth and slowing new investment.

Senator Sherry—I think Dr Henry well answered your question. I would not accept your summation of Dr Henry's answer, put it that way.

Dr Henry—That is right, Minister, because that is not quite what I said. You say 'slowing employment growth.' I was saying that the issues to which you referred become important once unemployment has got to a pretty low level; a level that we refer to as the NROU, or the natural rate of unemployment, at which level employment growth is going to be slower anyway. We have had this discussion before as well, and I am sure we have used in this committee previously the line that it is probably about half or one percentage point lower than the current rate when you already think you are close to it. That is to say that we are not quite sure, although in the Intergenerational report in our projections we use a figure of five per cent. As Dr Gruen said earlier, you have to be very careful with that number because average hours worked is also rather important and, if five per cent is the number, that would be on the basis of a cyclically high level of average hours worked. We are presently at a cyclically low level of average hours worked. If you wanted to translate our unemployment rate into what it would be if we had cyclically high average hours worked at the moment, you could probably add a couple of percentage points to it. That is instead of talking about 5.3 per cent you might be talking about 7.3 per cent unemployment rate, which would suggest that we are still some way away from that tight labour market condition in which crowding out might apply.

CHAIR—Thank you to the Treasury macroeconomic group for coming in this morning.

Senator ABETZ—Chair, can I at least put my questions on notice?

CHAIR—Certainly, any of the senators can put questions on notice. You are quite welcome to. The committee is now adjourned until two o'clock.

Proceedings suspended from 1.00 pm to 2.01 pm

Senator BOSWELL—Who do I address questions on modelling to?

Mr Ewing—It would probably depend on the exact nature of the question as to whether it was myself or Marty Robinson to my right.

Senator BOSWELL—Okay. Did the Copenhagen conference outcome match the assumptions made by Treasury in its modelling of a globally coordinated approach?

Mr Ewing—That is a slightly difficult question, because the assumptions we made in the Treasury modelling extend far beyond the horizon of the Copenhagen outcomes. So, to some extent, there are some things over the horizon we have assumed about action that are not in there. That said, my advice is that the kinds of commitments that we have seen from countries such as the United States, the European Union, Japan and China are broadly consistent with the assumptions that we made in our CPRS 'minus five' scenario.

Senator BOSWELL—Have you modelled a scenario in which the rest of the world does not participate in an ETS?

Mr Ewing—We have not, but there is a scenario along those lines which was included in the modelling for the Garnaut review.

Senator BOSWELL—I am not sure that is correct. I have information here on Treasury, which says:

... Treasury modelling assumes the main policy intervention modelled is the cap-and-trade emissions trading scheme ... The scheme is assumed to apply globally—

This is at annexe B. So what you are saying there is that you have assumed that everyone is going in to a global scheme. That is how you modelled it. There is some more information here that says that some of the modelling assumes that annexe B countries will have an ETS up and running—this is your modelling—from 2010, including Australia, Canada, the EU, the former Soviet Union and Japan, with China and higher income developing countries from 2015 and India and middle-income countries from 2020, with full global coverage from 2025. That is what you are basing your modelling on. That is what you have said your modelling is on.

Mr Ewing—Yes, that is the description of what we fed into the models. I would like to note another part of our report, page 85, where we note that our technical modelling assumption of a national emissions target and an emissions trading scheme is a simplified proxy for the range of policies and measures that constitute a national climate change response.

Senator BOSWELL—Hang on a moment. You have either based your modelling on that or not, and you have told us that is what your modelling is on. In the section on annexe B Treasury climate change policy and design features, table 2.3, the summary of policy assumptions, says that developed countries set targets and participate in international emissions trading from 2010 and that scheme participants have equivalent emission trading scheme policy settings to Australia. Then it says that the main policy intervention model is a cap and trade emissions trading scheme. This scheme is assumed to apply globally. Features of the scheme differ across the CPRS. That is what you have told us that you modelled. That is what your model was about.

Mr Ewing—Yes. To clarify my point, you have read out the description from our report of exactly what we fed into our modelling and into the computer programs that run these models. I was just quoting another of the report that says that while that technically is what the models are doing it can be considered in economic terms a proxy for a broader range of measures than simply an international emission trading regime.

Senator BOSWELL—Hang on. You cannot have it both ways. If that is what you put into your model, you cannot assume that the model can change to accept that China is going to plant a couple of million trees. That is not modelling at all. I am sure that you would agree with that and I am sure that you would not associate Treasury with that loose—

Senator Sherry—Senator Boswell, I think that the witness can speak for himself. You are asking him a question.

Senator BOSWELL—All right. If he wants it to go on record that the modelling that you told us that you were performing and the assumptions that you have based it on are correct, that will stand on the record. I do not think that they are.

Mr Ewing—Economic models are necessarily simplified representations of the economy. You could never capture the whole economy in an economic model. There are simply too many variables. When we model these things, sometimes it is necessary for us to use proxy measures in the modelling.

Senator BOSWELL—I assume—

Mr Ewing—We build the models with assumptions that are slightly different to the exact policy that is measured because that is the models are capable of delivering and doing.

Senator BOSWELL—I suggest that Copenhagen was not slightly different to your modelling.

Senator Sherry—Senator Boswell, the witness had not finished. He should get a fair go to give his answer to give his answer in a comprehensive way before you come in with what is essentially an argument.

Senator BOSWELL—No, it is not an argument; it is fact. If you can suggest that Copenhagen was a roaring success—

Senator Sherry—Please let him finish his answer.

Mr Ewing—In this instance, while what the models have is an emission trading scheme, to some extent that can be thought of as a proxy for a broader range of measures. Obviously, it is not a perfect proxy or representation. But that is part of the necessary simplifications that are required when dealing with the complexity of the economic models that we have.

Senator BOSWELL—So what you are telling me is that you modelled on the assumption that everyone was going to be in this—you told us that; that was in your papers—but, having arrived at Copenhagen, where it all turned to custard and no-one signed up on world emissions—China said it would not be in it, India said it would not be in it, the US signed up on a vague assumption that it would keep temperature change under two degrees—you are now saying that fits your modelling, as I understand it.

Mr Ewing—I believe that my words were that it was ‘broadly consistent’. What matters here is that there is an international price on carbon, which there clearly is; we can see that there are working markets with an international price on carbon. The exact nature and depth of that market are certainly somewhat different to the technical assumptions that we made in our modelling.

Senator BOSWELL—Has Treasury modelled scenarios other than those which have been made public?

Mr Ewing—Could you clarify that.

Senator BOSWELL—Yes. You have put down your modelling and your assumptions. That turned to custard. Now has Treasury modelled any scenarios other than those which have been made public, which were in the white paper or before the white paper?

Mr Ewing—Well—

Senator BOSWELL—Yes or no?

Mr Ewing—Unfortunately, it is not a question I can give a yes or no answer to. When we do the modelling we have to run the models many, many times so the scenarios evolve in the process of developing the models and feeding into the models the assumptions that we make and so on, so they develop over time. You could argue that there are scenarios not published in that they were draft scenarios we had along the way. We have not done a scenario, I believe, along the lines that you are suggesting, which is taking outcomes from Copenhagen

and trying to put those exactly into a model. We have not done that. I would argue that in my—

Senator BOSWELL—No, that is not what I said. What I said—listen to me—is this. Has Treasury modelled scenarios other than those which have been made public? I did not say anything about Copenhagen. Is there any other modelling there on other scenarios—yes or no? It is a simple question.

Mr Ewing—There are no separate scenarios. There are individual—

Senator BOSWELL—No. Have you modelled—

CHAIR—Senator Boswell, again can you let Mr Ewing finish. You are assuming, without letting him say more than a few words, that he is not answering your question.

Senator BOSWELL—All right; okay.

Mr Ewing—Sorry, I have got myself distracted and slightly lost the question there.

Senator BOSWELL—I will ask the question again. Has Treasury modelled scenarios other than those which have been made public? Have you got any other modelling that you have not made public?

Mr Ewing—You have asked two different questions there.

Senator BOSWELL—I have asked one question.

Mr Ewing—Not in my interpretation, I am afraid, Senator, because ‘scenario’ and ‘modelling’ mean very different things. Now in terms of—

Senator BOSWELL—All right, have you done any other modelling?

Mr Ewing—Have we done any other modelling? Yes, we have done other modelling beyond what is there because that is the process of modelling. The process of modelling requires us to run these models many, many times. What we have published in the report is a synthesis of the four main scenarios that are published and the many sensitivity scenarios that we have published.

Senator BOSWELL—So you have done other modelling on different scenarios.

Mr Ewing—No, I did not say that we did modelling on other scenarios. Those four scenarios and the sensitivity analyses are the ones that we have done. We have done other modelling within those scenarios in the process of arriving at the final—

Senator BOSWELL—When are they going to be made public?

Mr Ewing—It is not common practice to release drafts of modelling as you go along. We have released the final versions of that modelling.

Senator BOSWELL—In particular has Treasury modelled a scenario in which the rest of the world does not participate in an ETS?

Mr Ewing—As I mentioned, and I believe I have answered this question already, the answer was no, Treasury has not. There was modelling along those lines contained in the Garnaut review.

Senator BOSWELL—So you have not?

Mr Ewing—We have not.

Senator BOSWELL—Why didn't it do this given the significance of the assumptions?

Mr Ewing—Because it does not seem to me it is a very relevant scenario to be modelling. We are not in a world where Australia is going it alone. It does not seem that it is very relevant to model that.

Senator BOSWELL—With due respect, the EU has got an ETS of a sort which exempts all its people. I do not know who else has got one. New Zealand is supposed to have one. My inquiries found: 'We're so integrated with the Australian community we're not going to fire ours off if you don't.' India, China, America, Russia and Brazil are not going down the ETS path. These are the big emitters. So do not then say to me that the rest of the world is—

Senator Sherry—Senator, it is not a debate.

Senator BOSWELL—I know it is not a debate.

Senator Sherry—You are arguing with the witness and expecting an argument back. That is not the witness's role. I am not keen to intervene and I do want the questions answered, but a question, please, not an argument and not an invite to argue with the witness.

Senator BOSWELL—I will ask the question again. Why didn't Treasury remodel given the assumptions all fell over?

Mr Ewing—I would say that, as it is not Treasury's view that the assumptions have all fallen over, we do not see a need to remodel.

Senator BOSWELL—That is okay. As Senator Sherry suggests, and I take him on his word, I cannot argue with you, but I think this will be revisited on your answers as long as you are prepared to stand by them. Copenhagen has turned to custard, as I have said, and that has reduced the likelihood of an international agreement to participate in an ETS. Does Treasury intend modelling a realistic scenario of Australia proceeding with an ETS in the absence of an international agreement?

Mr Ewing—The modelling that Treasury does is at the direction of the government so Treasury intends nothing. It is entirely at the government's direction what we will model in the future.

Senator BOSWELL—Then I will direct my question to Senator Sherry.

CHAIR—You might want to repeat your question, Senator Boswell.

Senator BOSWELL—Sure. The modelling assumptions were based on the rest of the world going into an ETS. That is clear and I have read your assumptions out as it was all explained to me. Now I am asking that, since it is well established that the major emitters—India, China, the US and Brazil—are not going ahead with an ETS, are you prepared to do remodelling on the assumptions and put in the assumptions that these people are not going in?

Senator Sherry—What I will do, Senator, is I will take that on notice. I have to take that on notice. I am sure the Treasurer would want to consult with Senator Wong, so I will have to take that on notice.

Senator BOSWELL—All right; thank you for that. I will ask this question again. Did the Copenhagen conference outcome match the assumptions made by Treasury in its modelling of a global coordinated approach?

Mr Ewing—I believe that with some of the targets that have been announced the targets that the countries are pursuing are broadly consistent with the targets that we modelled in the modelling for the CPRS minus five scenario. I would also say that the long-term environmental goals that have been signed up to in Copenhagen are consistent with the modelling. Certainly some of the details of sequencing of action and exact policy do not match our modelling, but it is hardly a surprise. It would be very convenient if the real world would match our assumptions more often but, sadly, it is not the case.

Senator BOSWELL—I go back to this information that was given to all of us at estimates. We assume what Treasury gives to us is right. What it said was:

... Treasury modelling assumes the main policy intervention modelled is the cap-and-trade emissions ... scheme ... The scheme is assumed to apply globally—

Then it is said that some of the modelling assumes that annex B countries will have an ETS up and running in 2010 including Australia, Canada, the EU, the former Soviet Union, Japan and the US—but none of those countries is going to do it!—with China and high-income developing countries from 2015 and India and the middle income countries from 2020. Clearly, that has not happened and will not happen. You are saying basically that everyone has conformed. Do you see how silly that appears?

Mr Ewing—I do not believe that is what I said.

Senator BOSWELL—Well, tell me what you said.

Senator McGAURAN—It is modelled on a global CPRS.

Senator Sherry—Senator McGauran, you are now starting to run interference.

Senator BOSWELL—Yes, let the guy have a go.

Senator Sherry—Please let the witness finish the answer.

Mr Ewing—What I believe I said was that the targets that countries have committed to were broadly consistent with the targets that are included in our modelling and that some of the policy mechanisms that countries are using to achieve those targets do differ somewhat from our assumptions, yes.

Senator BOSWELL—But then how can your modelling be right? The assumptions you fed into it were that all these people were going to be included, and now they are not included.

Mr Ewing—The question really is: how material is the deviation? Also, in the nature of the long-term climate policy, as I mentioned earlier, it is not simply a question of the short-run assumptions that we make in the modelling but the long-run assumptions that we make in the modelling. The long-run assumptions are in many ways more critical to the modelling and to the results that we get. I believe that the Copenhagen conference probably increased the certainty on our long-run assumptions rather than reduced it.

Senator BOSWELL—You must be the only one in the world that does so. But, all right, that is an opinion.

Senator JOYCE—Can I just ask one question.

Senator McGAURAN—It is an excuse, not an opinion.

Senator Sherry—Senator McGauran, all you do is interject from the sidelines and you don't ask a decent real question.

Senator JOYCE—Mr Ewing, was your modelling process a formal modelling process?

Mr Ewing—I am sorry, I am not entirely sure what it is about our modelling process you are referring to.

Senator JOYCE—Was your modelling process peer reviewed?

Mr Ewing—We engaged a range of consultants with our modelling, including some of the foremost experts in this sort of modelling in Australia, and they reviewed many aspects of our modelling, yes.

Senator JOYCE—Was it holistically peer reviewed, across all facets of it?

Mr Ewing—I believe that every substantive facet of the modelling was peer reviewed, yes.

Senator JOYCE—Every substantive facet, but not all of it?

Mr Ewing—I would have to take that on notice. There were a lot of aspects of our modelling—

Senator JOYCE—There were a lot of aspects that were not formally modelled?

Mr Ewing—No, I am saying that there were a lot of aspects which go into assembling our formal modelling and I would have to take on notice the extent to which all of those aspects were peer reviewed. As you may be aware, we used a suite of models, there were different consultants and experts involved in each stage of the process, so I would need to take on notice the exact status of every single piece of the modelling.

Senator BOSWELL—In modelling, Treasury assumed that the US would have an emissions trading scheme operating by 2010. Is that likely to happen?

Mr Ewing—It is not my place to make an assessment of that.

Senator BOSWELL—What does the Treasury modelling say about the number of jobs will be lost in the current reality where Australia goes it alone without a global coordinated approach? Has that modelling been done?

Mr Ewing—As I have said, we have not modelled a scenario where Australia goes it alone.

Senator BOSWELL—But you have done other modelling?

Mr Ewing—We have done a range of modelling in the process of producing the final modelling that was published in that report, yes.

Senator BOSWELL—But after Copenhagen have you done other modelling?

Mr Ewing—I would have to take on notice exactly what everybody in the unit is doing, but if I could just give a broad answer to that one, with the specifics on detail, I do not believe so, no.

Senator BOSWELL—That stands on the record as no. Do you want to correct that?

CHAIR—Mr Ewing said that he would take that on notice. He was trying to assist you by giving you a general answer.

Senator BOSWELL—No, he has given the answer is no.

CHAIR—No, Senator Boswell.

Mr Ewing—I will take the question on notice.

Senator BOSWELL—I think that is a safer way to go.

Senator CAMERON—No wonder you're laughing!

Senator BOSWELL—You should be doing this. You should be standing up for your constituents. You know you should.

Senator CAMERON—Don't you lecture me about standing up for workers, with your Work Choices!

Senator BOSWELL—What does Treasury modelling say about the impact on pensioners if Australia goes it alone on an ETS without a global coordinated approach?

Mr Ewing—I might pass to my colleague to answer specifically on the impacts on pensioners but, as I have mentioned, we have not modelled that scenario.

Mr M Robinson—The modelling that we have undertaken in terms of the impact on the household sector, in particular on different types of households, feeds off the main more global economic scenarios run by Mr Ewing's area. So the latest analysis that we have undertaken, which is suggesting an overall CPI impact of about 1.1 per cent with an impact for pensioner households, for example, of about 1.5 per cent, would be based on the underlying scenarios that Mr Ewing's area has done.

Senator BOSWELL—Have you done any modelling on this after Copenhagen?

Mr M Robinson—As I said before, the scenarios that we work off are the main scenarios from Mr Ewing's area. So we have not undertaken any further modelling or scenarios.

Senator BOSWELL—So you have no modelling that you have done after Copenhagen?

Mr M Robinson—No.

Senator BOSWELL—What industries will be made less competitive by having a carbon cost when their international competitors do not have a carbon cost?

CHAIR—I think that might be more a question for the Department of Climate Change than Treasury, but if any of the Treasury—

Senator BOSWELL—No, because they would have modelled this.

CHAIR—If any of the Treasury officials would like to answer it, I will open it up.

Senator BOSWELL—These should have been modelled.

Mr Ewing—As we have not modelled that scenario, I have no way of giving an answer on that question.

Senator BOSWELL—Has Treasury updated its modelling to take into account the lack of a coordinated global approach? Has it done any work, for example, using revised assumptions on international action following the failure of Copenhagen?

Mr Ewing—No.

Senator BOSWELL—Why not?

Mr Ewing—As I mentioned earlier, the modelling that we do is at the direction of the government.

Senator BOSWELL—As the assumptions of global coordinated approach have proved totally wrong, surely that would significantly affect Treasury's modelling outcomes since our trade competitors would have cost advantages. Has the Australian government done any work at all on the impacts of a CPRS where the US does not start an ETS this year?

Mr Ewing—I will just make a general note first that the Carbon Pollution Reduction Scheme policy design does include shielding for emissions-intensive trade-exposed industries, which is intended to help them deal with a situation where there is not yet coordinated global action and the potential for competitive effects.

Senator BOSWELL—I understand shielding very well and I have been involved in that process, but there is still a very severe penalty on our heavy industries even with shielding granted. I cannot believe you have not done it, but anyhow I will take your word. Has the Australian government done any work on any of this modelling with the US or any of the other countries being part of it?

Mr Ewing—We have done no modelling. As to any work, you would probably have to ask the Department of Climate Change on that one. They may have—

Senator BOSWELL—No, they do not do that; you do the modelling.

Mr Ewing—We do the modelling, but you asked about any work, which would presumably encompass more than formal modelling.

Senator BOSWELL—I am asking about the modelling, not the work. Could you answer that please.

Mr Ewing—No, we have not modelled that.

Senator BOSWELL—So there is no modelling done on the current international situation?

Mr Ewing—There is no modelling done that directly replicates the fine detail of the current international situation.

Senator BOSWELL—Did anyone in Treasury go to Copenhagen?

Mr Campbell—There was one individual, Damien Dunn, from the London post that attended.

Senator BOSWELL—After Copenhagen, was there any analysis on how poor outcome would affect the relevance of Treasury modelling that was based on a global approach to emission reduction?

Senator CAMERON—That does not make sense.

Senator BOSWELL—It makes sense to me. I will read it again for Senator Cameron.

Senator CAMERON—That would be good.

Senator BOSWELL—After Copenhagen, was there any analysis on how the poor outcome would affect the relevance of Treasury modelling that was based on a global approach to emissions reductions?

Mr Ewing—We had internal discussions following Copenhagen about the targets, how those targets lined up with our modelling and how the overall international situation compared to our modelling. Our conclusion was that there would be little value added by additional modelling as it would not change the fundamental conclusions of our modelling.

Senator BOSWELL—Let me finish by asking the question again, because I think this will go further: has Treasury modelled scenarios other than those which have been made public?

Mr Ewing—I believe I have answered that question already.

Senator BOSWELL—What was the answer? No?

Mr Ewing—The answer was that we have done a range of modelling in developing scenarios that are presented in Australia's low-pollution future but we have not done modelling on scenarios beyond those of the type presented there.

Senator BOSWELL—Thank you.

CHAIR—Before we have further questions, I point out that another three senators have indicated they have questions related to the ETS modelling. Do we want to set any kind of time on that before we get onto other fiscal group questions?

Senator JOYCE—I most definitely have questions for the fiscal group, away from the ETS. Senator Boswell is doing an admirable job so I will not go back into that territory. I think we will need at least 45 minutes on things that are not related to the ETS.

CHAIR—Okay.

Senator BUSHBY—In the course of its modelling or analysis has Treasury made any specific consideration of the impact of the CPRS on small business?

Mr Ewing—We have not given specific consideration to the impact on small business beyond the general economic impacts and the price impacts that we considered. We did not feel there was much that we could add to that analysis specifically for small business.

Senator BUSHBY—So there has been no specific examination of what the impact of the CPRS might be on direct energy costs or accumulated supply chain input costs for small business?

Mr Ewing—There has been no direct consideration of that in relation to small business. However, we did consider the impacts on households, and our results for that would contain a lot of information for the position of small businesses.

Senator BUSHBY—That is an interesting comment because compensation will be provided to a large proportion of households under the CPRS. I am curious to know whether any analysis has been done which justifies the exclusion of the vast bulk of small businesses from CPRS compensation arrangements.

Mr Ewing—The assumption was made in our modelling, and I can only speak to the modelling—as to compensation arrangements, you would have to speak to Mr Campbell—that, when considering the price impacts, small businesses would be able to fully pass on the impacts of the price rises they receive in higher prices for the products and services that they sell, hence their margins would remain unchanged. From that you could conclude that no compensation would be required. But Mr Campbell may like to add to that.

Senator BUSHBY—It is a very easy assumption to make from the perspective of Treasury, but it is not necessarily as easy an action to put into place for most small businesses.

Mr Ewing—It is an assumption that is standard in this kind of analysis and is well backed up by the historical evidence, such as the experience of the GST and the modelling that Treasury did for the price impacts there.

Senator BUSHBY—The GST is easily quantifiable. Everyone knows that there 10 per cent is put on top of the price. As a small businesses owner it is very hard to justify the cumulative supply chain input costs as justifying the price increases. No doubt there would be some small businesses, less scrupulous than others, who would actually try to pass on more than they should. On the whole, small businesses operate in a competitive environment and it is not always as easy to pass on input costs, whether they are government created or otherwise, as your modelling suggests.

Mr Ewing—On that, I note that in a competitive environment all domestic businesses will be facing the same increases in costs and so will have the same pressures to increase their prices.

Senator BUSHBY—But some may have more scope than others to absorb, due to different factors. I just think that it is interesting that there is no analysis on how it will actually impact which informs the decision that you have made.

Mr Campbell—We should clarify, though, that what Mr Ewing is talking about is specific economic modelling undertaken by Treasury with the GE models. That is not to suggest that the Department of Climate Change, in putting forward the policy package, did not actually look through some of these issues as part of its analysis.

Senator BUSHBY—I was interested in what Treasury had done. I am sure the question has been asked of the Department of Climate Change at some point. Similarly, no analysis has been done that looks across different sectors of small business either, given your previous comments?

Mr Ewing—No, there has not been.

Senator BUSHBY—That is fine. Thank you.

Senator BRANDIS—I just had one question arising from Senator Boswell's questions, Mr Ewing, about the modelling. I am not going to get into the question of what, if anything, was done after the Copenhagen climate change conference failed but, did I understand you to say that there was modelling also done in the Department of Climate Change?

Mr Ewing—No, Senator. What I intended to say was that Senator Boswell's question as I heard it went to any work which could encompass a wide range of analysis and were economic or otherwise outside of formal modelling.

Senator BRANDIS—What I want to direct my questions to is the relationship, if any, between Treasury and the Department of Climate Change. When you prepare your modelling do you do that on the basis of your own initiative or at the request of the Treasurer ultimately, I suppose, or do you do it at the request or with the participation of the Department of Climate Change?

Mr Ewing—Ultimately we are answerable to the Treasurer, and his work program is ultimately set by the Treasurer. When we are working in the climate change space we work very closely with the Department of Climate Change on assumptions and other inputs. We had a seconded officer from the Department of Climate Change working with us for most of the period of producing our major modelling report. We have very frequent contact with them.

Senator BRANDIS—That is exactly where I was going, thank you, Mr Ewing. When you are to use your phrase ‘working in the climate change space’ is Treasury made aware of what work relevant to your modelling the Department of Climate Change is doing? In particular, given that the worth of all these models depends upon the assumptions and the methodology, does your work and the work of the Department of Climate Change in relation to these issues proceed on the basis of the same assumptions and the same methodology?

Mr Ewing—I cannot speak to all the work that is done at the Department of Climate Change.

Senator BRANDIS—Just pausing there, Mr Ewing, of course I am only asking you about the work that department is doing of which you or other officers in the room are aware. Where I am going with this is that it would be alarming if we had one specialist economic department, the Treasury, doing modelling on a topic and one specialist department, the Department of Climate Change, also doing modelling on a topic and the assumptions and the methodology were not common to them. Coming back to my earlier question to the extent to which you are aware of what the climate change department does in the climate change space, is there an agreed set of assumptions between you? Is there an agreed methodology between you?

Mr Ewing—There is not any sort of formal set of agreed assumptions or agreed methodologies. What there is instead is a process of conversation where, when we have processes and so forth that require us to develop these assumptions on methodologies, there is a conversation between the Department of Climate Change and Treasury to ensure that we have a consistent approach. We have assumptions which are for an economic modelling purpose which I do not think are always going to be appropriate for every other purpose the Department of Climate Change would necessarily have.

Senator BRANDIS—I understand that, Mr Ewing. That sounds perfectly sensible to me. Let’s cut to the chase here. Ultimately the question is: what the concentration of carbon in the atmosphere is likely to be on certain projected future dates given certain assumptions as to the output of various industries and various other activities. There are a lot of assumptions built into that which must be built into your model. Given, one assumes, the Department of Climate Change has topic-specific expertise in the field of climate change, and given you have expertise in economic modelling, I want to be reassured that those various assumptions on the basis of which one projects the range of carbon concentration against certain future dates

depending on how different policy outcomes will operate, that you and the Department of Climate Change approach this question on the basis of shared assumptions and shared methodologies.

Mr Ewing—I believe that we do do that to the maximum—

Senator BRANDIS—How do you do that?

Mr Ewing—We simply do that by, when we have the occasion to develop such assumptions, inviting the specialists from the Department of Climate Change to come over and review them. In that area, as the expertise on particularly the climate science side of things is much more in the Department of Climate Change than with us, we have relatively little role in reviewing their assumptions and work.

Senator BRANDIS—I understand that, Mr Ewing, but doesn't it follow from that, given that they have the expertise about the science, that the accuracy and reliability of your modelling really does then depend on the assumptions about the science in particular that the Department of Climate Change gives you?

Mr Ewing—It is certainly a very important assumption in our modelling, yes.

Senator BRANDIS—So you are really the methodological people, aren't you? I mean you take their assumptions and you put them into your model and, according to various variables, those assumptions produce a range of alternative projections against certain specified future years. Is that the way it works?

Mr Ewing—Yes, although we normally work in the space of emissions in terms of tonnes of carbon dioxide equivalent or in terms of carbon dioxide equivalent. We do not really follow that into the temperature translation.

Senator BRANDIS—Other than the Department of Climate Change, what are the other inputs in terms of the assumptions that you make for the purposes of operating your model? For example, does the Bureau of Meteorology or the CSIRO or any other department or agency of the Commonwealth with specialist expertise in climate feed into your assumptions for the purpose of creating your model?

Mr Ewing—Certainly in our previous modelling exercise, the CSIRO was involved. I do not believe the Bureau of Meteorology was involved at any point. There is a range of other agencies, including ABARE and the Bureau of Transport and Regional Economics, that were also involved in the process and, to some certain extent, they would both have some expertise in these areas.

Senator BRANDIS—Given that what this is ultimately about is future projections about climate, why wasn't the Bureau of Meteorology involved? Is that because they are only short-term forecasters, or is there another reason for that?

Mr Ewing—I do not think I would completely agree with your characterisation that it is about long-term projections of climate. What we have modelled is a scenario of what happens if we do nothing and then scenarios of four core scenarios of a certain level of emission reductions. That level of emission reductions was informed by the science, but fundamentally what we are modelling is the economic impact of policy measures to reduce emissions by that amount worldwide.

Senator BRANDIS—But you do not critically review the science, do you? You assume—and I dare say from your point of view it is a fair assumption—that the scientific assumptions provided to you by in particular the Department of Climate Change are sufficiently reliable assumptions that you can just proceed and build a model on the basis of them. Is that right?

Mr Ewing—We certainly have no independent expertise in this area, although in the process of developing our understanding of climate policy and climate policy issues, we have obviously read a lot and understood things. If we had seen something from the Department of Climate Change that was vastly different to our understanding, that would have been something that would have triggered alarm bells and we would have followed it up.

Senator BRANDIS—But that did not happen.

Mr Ewing—That did not happen, no.

Senator BRANDIS—So basically it sounds to me that the take-out of this is that you do not second-guess, in building your model, the scientific assumptions that in particular the Department of Climate Change provides you with?

Mr Ewing—No.

Senator BRANDIS—Thank you.

Mr Ewing—Although I should clarify: it is very much a collaborative process between the Department of Climate Change and Treasury in settling at the climate scenarios because it is a combination of the economics and the science.

Senator BRANDIS—At the risk of over generalising, would it be broadly right to say that you provide the economics, they provide the science?

Mr Ewing—Broadly correct, yes.

Senator BRANDIS—Somebody stop me if this question has already been asked in my absence, and if you have to take it on notice, perhaps you could just tell us from the table: what was roughly the date on which you were first instructed to prepare this model? When were you first given this task?

Mr Ewing—Senator, if you would be happy with a half of the month, I can do it without taking it on notice.

Senator BRANDIS—That will do, yes.

Mr Ewing—Treasury was first instructed to begin doing this modelling I believe in the second half of April 2007.

Senator BRANDIS—And when was the first iteration, the first draft as it were, of your model and its conclusions finalised?

Mr Ewing—That is a much more difficult question to answer. I was explaining to Senator Boswell earlier it is very much a process, and so it is very hard to really draw a line in the sand and say, ‘This is now a draft.’

Senator BRANDIS—I understand that it would be an iterative process, but there must have been a date at which what was recognisably the first draft of your document was

published and distributed to those officers in your department and other departments who were the key participants.

Mr Ewing—If you needed an exact date for when the first draft was—

Senator BRANDIS—No, a rough date.

Mr Ewing—As is relatively common with this sort of document, the first draft of the actual write-up would not have been ready until around mid-October 2008.

Senator BRANDIS—Mid-October 2008. And what was the last date, prior to the Copenhagen climate change conference, on which the most mature draft of the same document was published?

Mr Ewing—I believe the final draft of the modelling was published on 30 October 2008. The final draft of that would have been—

Senator BRANDIS—2008! Not 2009?

Mr Ewing—2008, yes. This is referring to this modelling report here that that report was published in 2008.

Senator BRANDIS—Okay. So there was no further iteration or edition of this report in the year-and-a-bit from 30 October 2008 and the Copenhagen climate change conference in the middle of December 2009. Is that right?

Mr Ewing—That is correct.

Senator BRANDIS—The science had moved on rather. I do not want to get into this controversy about whether or not the science is bodgey, but even among those who are not called sceptics, the climate change scientists who seem to represent that the body of the scientific establishment in this area, even among them the science had moved on quite a bit hadn't it between October 2008 and December 2009?

Mr Ewing—As I mentioned, I am not an expert in the science and so I could not really comment on to what extent the science, as it relates to the concentration targets and the emission reduction targets that we included our modelling, would have changed.

Senator BRANDIS—All right. And I think you told Senator Boswell that there has been no new edition of the modelling since the Copenhagen climate change conference, so may we conclude that the Australian government's thinking in relation to this, here in the middle of February 2010, has not progressed, at least in terms of the modelling, since 30 October 2008?

Mr Ewing—The modelling that we released on 30 October 2008 certainly stands as the best conclusion that we have on this material publicly released.

Senator CAMERON—Mr Ewing, I just want to take you through some of these issues on modelling, so bear with me because there are a lot of issues that I want to raise with you. On the issue of the science, Dr David Gruen gave a speech to the CEDA National Forum in November 2008 where he said:

I agree with Professor Garnaut that the relevant yardstick with which to assess the scientific evidence on climate change is not what we know for sure, but what we know on the balance of probabilities. And, on the balance of probabilities, continued growth in greenhouse gas concentrations would generate high and rising risks of dangerous and potentially irreversible climate change.

Do you agree with that view of Dr Gruen?

Senator BUSHBY—He said he is not an expert on climate change.

Senator CAMERON—I am not asking him for his expert opinion.

Senator BOSWELL—I am calling a point of order on Senator Cameron. The people before us are from Treasury—they are not climate scientists and have no expertise, as I understand, in climate science. They are number crunchers.

CHAIR—What is your point of order, Senator Boswell?

Senator BOSWELL—Senator Cameron is not addressing his question to the right committee. These people are number crunchers, not experts in science.

CHAIR—I think the minister and the officers can deal with that.

Senator CAMERON—I took the balance of probabilities as put forward by the executive director of the macroeconomics group. He spoke about dealing with this on the balance of probabilities. Is that a fair and reasonable way to deal with it in terms of the models?

Mr Ewing—I personally would agree with Dr Gruen's characterisation there.

Senator CAMERON—Thank you. I now go back to the model itself as there has been some criticism of the model. As I understand, the modelling is the most comprehensive ever done in Australia in terms of modelling any issue. Is that correct?

Mr Ewing—I believe it to be correct. I have not done an exhaustive survey of all modelling exercises ever done in Australia. I certainly believe it to be so.

Senator CAMERON—In his speech to CEDA, Dr Gruen said that it took 18 months to develop the model. A climate change modelling team was built with a strength of 18 dedicated to staff. Is that your understanding?

Mr Ewing—Yes, that is correct.

Senator CAMERON—That dedicated staff then drew on resources from across the public sector, including the Productivity Commission, ABARE, the Reserve Bank and the Department of Climate Change. Is that correct?

Mr Ewing—Yes.

Senator CAMERON—Much of the work was done in partnership with the Garnaut Climate Change Review, with expert input from Professor Garnaut. Is that your understanding?

Mr Ewing—Professor Garnaut and also the many members of his secretariat and other consultants who provided some very valuable inputs.

Senator CAMERON—And eight consultants contributed to the modelling, including national and international experts in economic modelling and modelling of climate change policy, such as Professor Warwick McKibbin and Professor Philip Adams. Is that your understanding?

Mr Ewing—That is correct.

Senator CAMERON—And the Treasury also received invaluable input from industry and environmental groups.

Mr Ewing—Yes.

Senator CAMERON—And the team consulted with and received support from international experts, including the OECD, the International Energy Agency and IMF. Is that your understanding?

Senator BUSHBY—What is the question?

Senator JOYCE—You can send an email to Senator Wong.

Mr Ewing—Yes.

Senator CAMERON—We have the best economic minds in Australia and international experts, so this is the most comprehensive modelling ever done.

Senator EGGLESTON—And they got it wrong. They changed the assumptions.

Senator CAMERON—I know you lot get a bit testy about this, saying it is pure nonsense. Senator Joyce, try and behave like a shadow minister. You have the brightest economic minds—

CHAIR—Order! Can we have the end of the conversation across the table.

Senator CAMERON—Is it correct that this is the most comprehensive modelling ever done?

Mr Ewing—As a member of the team, I would prefer not to comment on the ‘brightest economic minds’ comment, but beyond that I would agree.

Senator CAMERON—It is good that we have that approach. Was the methodology comprehensive and robust? Can we say that?

Mr Ewing—That is my professional view, yes.

Senator CAMERON—Part of that modelling says that the economic costs of moving early to deal with climate change—and the balance of probability is that it is going to happen—are 15 per cent lower, while the cost for late movers is 20 per cent higher. Can you explain that?

Mr Ewing—So that is—

Senator JOYCE—Where is it going through? It is not going to go through the Senate.

Senator BOSWELL—The whole thing has changed after Copenhagen.

Senator CAMERON—I did not raise the modelling; you guys did. I just want to make sure people understand it. You raised it.

Senator BOSWELL—You are before Copenhagen. You are on the white paper.

CHAIR—Mr Ewing, are you ready to answer? Senator Boswell, can we let Mr Ewing answer.

Mr Ewing—Senator, I believe you were referring to box 5.4 of our report, which is on page 104. It is a comparison between a scenario where some countries act earlier than others

and a scenario where there is coordinated world action. What we found in that scenario was that the GDP costs were 15 per cent lower for those countries that acted in 2010 rather than in 2013—and those are the GDP costs by 2050, the long-run costs.

Senator CAMERON—And through the long-run costs economic growth through to 2050 is described as ‘robust’. Economic growth for the economy will continue to be robust. Is that correct?

Mr Ewing—That is correct. The modelling showed that the various scenarios would slow GNP per capita growth by 0.1 per cent per annum.

Senator CAMERON—I understand one of the other findings is that even ambitious emissions reduction goals would have limited impact on national and global economic growth.

Mr Ewing—Yes. The scenario with the largest emission reduction targets still found strong, robust continued growth.

Senator CAMERON—I am not arguing for unilateral action, because we have 36 countries around the world dealing with climate change now. But in 2006 ABARE, who were part of this report, also argued that deep cuts to emissions were consistent with strong economic growth. Are you aware of that study?

Mr Ewing—I believe that I am aware of that study. ABARE has done a number of them. I have read them all and I am familiar with that conclusion they reached.

Senator CAMERON—Even if we took unilateral action—which we are not arguing for—they modelled that growth between 2010 and 2050 would be 2.25 per cent compared to 2.5 per cent without taking any steps on global warming. Is that correct?

Mr Ewing—I would have to take the exact numbers on notice if you wanted that, but when you were going it alone they still found only a slowing in growth rather than negative growth. That is the finding that I am familiar with.

Senator CAMERON—Are you aware of modelling numbers done on behalf of the Minerals Council of Australia on employment in the minerals industry and the coal industry?

Mr Ewing—I recall seeing that modelling but I do not have all its details memorised.

Senator CAMERON—Even though you are not aware of the details, are you aware of any problems with that modelling?

Mr Ewing—Without the report in front of me I would have to take that on notice.

Senator CAMERON—Could you take that on notice and could you provide me with the details of any problems that were detected in relation to the Minerals Council modelling?

Mr Ewing—Just for the assistance of my officers when they prepare it, could you give me a date or a title for the Minerals Council’s report?

Senator CAMERON—I can get you that information. I thought it was well known.

Mr Ewing—I believe I know the one, but on the off-chance that there are two it would be helpful to make sure.

Senator CAMERON—It was controversial modelling.

Mr Ewing—I believe you are referring to modelling that was prepared on their behalf by Concept Economics.

Senator CAMERON—I think it was Concept Economics. They are the mob that went bankrupt. Do you know them?

Mr Ewing—I understand that Concept Economics is no longer in business, yes.

Senator CAMERON—They went bankrupt.

Senator Sherry—Chair, just one thing—and I am not being overly sensitive. Senator Boswell has gone. Treasury officials are more than simply number-crunchers. They have a lot more diverse talents and skills than in the simplistic description of them as ‘number-crunchers’.

Senator CAMERON—It was the National Party. What do you expect?

Senator Sherry—I think that description was a bit rough.

Senator McGAURAN—It was a term of affection.

Senator Sherry—The trouble was that the affection was not embracing enough. It should have been broad.

Senator McGAURAN—Let’s call Senator Boswell back into the room.

CHAIR—No. Let’s not.

Senator Sherry—I know that Senator Boswell was, in his descriptive way, being kind and generous. I understand that.

Senator BOSWELL—I meant no offence when I said ‘number-cruncher’. I think it is an honourable profession.

Senator Sherry—But they are more than number-crunchers. I think it is a bit narrow.

CHAIR—Now we need to deal with the question.

Senator EGGLESTON—I have a question, again, on ETS modelling. I presume the basis upon which you did your modelling was that there would be an emissions trading scheme, trading with other countries. Is that the case?

Mr Ewing—That was certainly the technical assumption that we made in the modelling, yes.

Senator EGGLESTON—Did you model carbon tax on the same basis—or didn’t you model the carbon tax?

Mr Ewing—When you are dealing with these economic models, there really is very little difference between a carbon tax and an emissions trading scheme. Fundamentally, as the models work, a carbon tax plus some international transfers is an emissions trading scheme. So, while we did not directly model a carbon tax, you could certainly draw a lot of the conclusions for a unified world carbon tax from the GDP results in our report. The GNP results would then reflect on top of that the impact of the trading of permits between countries.

Senator EGGLESTON—Was any modelling done on the actual situation we now face in that there are no other countries for Australia to engage with in carbon trading? If not, why not? Was it not an accepted possibility that the Copenhagen conference would fail? Why, if it was not done, was there no modelling of the actual situation in which Australia would be going it alone in setting up the CPRS or ETS without countries to trade with, especially in our region?

Mr Ewing—One of the reasons we did not model that scenario was that we felt that the Garnaut review's modelling of that scenario had already covered the important questions and modelling by Treasury would add little to that.

Senator EGGLESTON—When did Garnaut model it? I was not aware of that.

Mr Ewing—Professor Garnaut included modelling of that in his supplementary draft report of September 2008.

Senator EGGLESTON—Nevertheless Garnaut was Garnaut and you are the Treasury and you are responsible for planning for the economic impact on Australia. Therefore I remain surprised that you did not actually model a scenario on which there would be no other countries to trade with.

Mr Ewing—My understanding is that that is not the situation we are in, because there are other countries to trade with.

Senator EGGLESTON—There is only New Zealand and the European Union—none of our major trading partners in the region and not the United States—so effectively there is no-one to trade with. I am just curious as to why that scenario was not modelled, because it was so predictable.

Senator CAMERON—ABARE modelled both alone and said there was no problem.

Senator EGGLESTON—I am not interested in your comments.

Senator CAMERON—And we are not interested in the—

CHAIR—Then I will ask you not to respond, Senator Eggleston.

Senator CAMERON—You cannot stand the truth.

Senator EGGLESTON—I would be grateful if the Treasury would explain why they did not model that situation.

Mr Ewing—As I mentioned, we felt that existing modelling covered that question quite adequately, and we did not feel that our modelling would have anything particularly useful to add, given that we had modelling of scenarios where we did feel that our analysis had some important contributions to make.

Senator EGGLESTON—Given that the Australian economy depended—so many decisions depended on your modelling, I find that an extraordinary answer, but thank you.

Mr Campbell—We are undertaking the scenarios that were put in the modelling reports under the direction of the government. Future assessments about the success or otherwise of the Copenhagen accord and how various economies have responded to that with the various pledges that have already been made will continue to be assessed by the Department of

Climate Change. As Mr Ewing said before, we work very closely with the Department of Climate Change in checking, validating and considering those assumptions against developments, and we will continue to do so.

CHAIR—We will move off the ETS modelling.

Senator JOYCE—What is the current gross level of state debt?

Mr Ray—The latest number I have, the actual, would be the end of 2008-09, and that is \$127.6 billion.

Senator JOYCE—What date was that?

Mr Ray—The end of 2008-09—so, 30 June 2009.

Senator JOYCE—There are no other figures later than that?

Mr Ray—I do not have any.

Senator JOYCE—You see, Mr Ray—I might even have it here on the *Hansard* record—the last time I asked you that question I think it was more than that, and I know it has not gone down. You do not have any other figure?

Mr Ray—Not an actual number. You asked for an actual number; that is the most recent actual number.

Senator Sherry—The figure given last time on—

Senator JOYCE—One hundred and seventy billion.

Senator Sherry—was an estimate. I think the officials may be able to give you an estimate but it is not the actual figure.

Senator JOYCE—Okay. So who gave the estimate last time?

Mr Ray—I think you gave us a number and we agreed with it, or something like that.

Senator JOYCE—So, \$127 billion—what is the predicted peak debt, then, of the states?

Mr Ray—I do not think we have predicted peak debt. So we published in MYEFO estimates of their future debt levels, out to the end of our forward estimates period.

Senator JOYCE—So what are the future debt levels of the states?

Mr Ray—The number I have for 2009-10 is \$143.7 billion.

Senator JOYCE—Sorry, Mr Ray—I can't quite hear you because Senator Cameron is speaking.

Senator Sherry—Oh, fair cop—I mean, Senator Boswell was speaking as well.

Senator JOYCE—Well, just speak into the microphone, Mr Ray.

Mr Ray—Sorry; I am trying to read my numbers. The numbers that I have are \$143.7 billion for 2009-10, \$171.8 billion for 2010-11, \$190.9 billion for 2011-12 and \$204.2 billion for 2012-13.

Senator JOYCE—Where will they predominantly get that debt from?

Mr Ray—The market.

Senator JOYCE—Will the Commonwealth be the buyers of any of that debt?

Mr Ray—Over that period, I would not expect us to hold state debt for any period. The AOFM issued a notice in December last year saying that it was going to hold some state paper for short-term cash management reasons, but I would not expect us to be holding large volumes of state debt.

Senator JOYCE—What is the yield that the states are offering?

Mr Ray—I do not have market state yields with me, but they are a margin above ours.

Senator JOYCE—So what is yours?

Mr Ray—These numbers are available on the Reserve Bank's website. On 9 February, the yield on an 11-year bond was 5½ and a one-month note was 3.77. So they range in that range.

Senator JOYCE—Where is federal debt predominantly held, between 10-year bonds and one-month notes—what is the mean average?

Mr Ray—What is the mean duration?

Senator JOYCE—Yes.

Mr Ray—I do not know that we have that. We have about \$10 billion of notes and \$100 billion of bonds, roughly.

Senator JOYCE—And you must have something else, because you have \$122 billion.

Mr Ray—And then we have indexed bonds, but the bonds range across the yield curve. If you want to know what the average duration is—

Senator JOYCE—Yes.

Mr Ray—the AOFM are coming tonight and they would know.

Senator JOYCE—Do you take into account the debt owned by government-owned or government-controlled entities?

Mr Ray—When we talk about net debt, we are talking about the general government sector.

Senator JOYCE—So do you concern yourself with the debt held by a government owned entity such as Ergon?

Mr Ray—They are state entities.

Senator JOYCE—They are state government entities, sorry.

Mr Ray—We would need to check. But I suspect that they are outside their GGS.

Senator JOYCE—In your movement of bonds and notes, who is purchasing them? How much is being purchased domestically and how much is being purchased overseas, and where overseas?

Mr Ray—This is a vexed question in the sense that the data is not easy to obtain. The latest estimate that we have is that as at the end of September about 59.3 per cent of the stock of debt was held by non-residents.

Senator JOYCE—So 59.3 per cent. So about 60 per cent is held by non-residents.

Mr Ray—It does fluctuate a bit.

Senator JOYCE—Around about there, give or take.

Senator Sherry—Just looking back to about 2005, it has fluctuated up and down between 50 per cent and 60 per cent.

Senator JOYCE—Of the non-residents, the predominant country holding debt would be China. That is a fair statement, isn't it?

Mr Ray—Most of this is held through nominee companies.

Senator JOYCE—We have gone through this conversation.

Senator Sherry—We have been through it. There is a difficulty in going through the offshore countries and identifying the actual owner. But even if you could, I would be surprised, frankly, if it was China.

Senator JOYCE—I think about a third of it is held by China. You would be aware that 60 per cent of US bonds will be turned over by 2014. If 60 per cent of their bonds are maturing by 2014, do you see that as putting upward pressure on the yield curve in Australia?

Mr Ray—I do not know what the refinancing need of the US Treasury is. But let us assume that you right. It is not clear to me that that is going to put upward pressure on the yield curve. The reason for that is that the market would know already what that refinancing need is and that would already be built into the US yield curve.

Senator JOYCE—So generally you are seeing that there is upward pressure on the yield curve?

Mr Ray—I do not think so. Our yield curve, certainly at the long end of the market, has been pretty stable for the last few months.

Senator JOYCE—And the short end?

Mr Ray—The short end moves because of actions taken by the Reserve Bank.

Senator JOYCE—In light of international factors, especially what is happening in Portugal, Italy and Greece, there are new elements coming onto the agenda every day in that domain.

Mr Ray—Sure.

Senator JOYCE—Are they having effects on price sensitivity in the market?

Mr Ray—In the market for their paper or for all paper?

Senator JOYCE—For all paper.

Mr Ray—The experts on their paper were here this morning, the international economy division, which is in macro group. You would expect, though, that those sorts of market developments would have some effect on their markets. They are obviously having an effect on CDS spreads and those sorts of things. In terms of our own paper, as I said, our yield cover at the long end has been pretty stable for some time.

Senator JOYCE—Talking about CDS spreads, what is the CDS spread on Australian—

Mr Ray—I do not know. We can take that on notice.

Senator JOYCE—You do not want to hazard a guess? It is 68 basis points, isn't it?

Mr Ray—It is not something that we watch.

Senator JOYCE—You do not watch it?

Mr Ray—Our colleagues in macro group may watch it, but we do not watch it.

Senator JOYCE—Is there any form of quantitative easing going on in Treasury at the moment?

Mr Ray—No, Senator.

Senator JOYCE—You do not know?

Mr Ray—I said no, Senator.

Senator JOYCE—Are you in fiscal group at all concerned or involved in any way, shape or form with the pressures that the requirement for the purchase of US bonds in the international environment places on the price for Australia, which is sourcing 60 per cent of its funds from overseas?

Mr Ray—Coverage ratios for our issuance remain very solid. As I said, we have not seen much movement in yields at the long end of the curve over the last few months. I think we have answered this question several times over the past year or so. The demand for our paper remains very strong.

Senator JOYCE—We were discussing this morning the actual net debt of Australia as opposed to the net sovereign debt of Australia and we heard evidence that Australia has one of the highest. Do you know exactly where we rate in that?

Mr Ray—No. The people who know that were here this morning. I think they may have taken that on notice.

Senator JOYCE—We found out that New Zealand is worse than us.

Mr Ray—My recollection is that Dr Gruen said that they would take it on notice and check.

Senator JOYCE—We got more than that. We found out that we were certainly higher than United States, certainly higher than England, certainly higher than Japan and basically higher than everybody. We found out the only one we are not higher than is New Zealand.

Senator Sherry—The one identified was New Zealand. There may have been others. We will take it on notice if it was not taken on notice this morning. We will get you a comprehensive list.

Senator JOYCE—In the global representation of that, is there a decision by the market that looks at the whole picture of Australia rather than just the government's issuance?

Mr Ray—Certainly. Are you talking about whether it would affect our sovereign bond yields?

Senator JOYCE—Yes.

Mr Ray—Views on the general state of the macro economy would affect our sovereign yields.

Senator JOYCE—So if there is a large borrowing throughout the nation, does that affect the price that the government has to pay?

Mr Ray—I think what I said was, ‘The aggregate view of the market on Australia would affect our yields, yes.’

Senator JOYCE—That would suggest that if the government becomes more and more of a player in the market then that would affect the price everyone else has to pay?

Mr Ray—No, that is going to crowding out. I think you had a long discussion about that this morning with Dr Henry. At this stage, given the state of the economy, you are right to raise it as a general issue but we are well short of that point.

Senator JOYCE—But we are heading to a peak debt position of \$245 billion. Will it start affecting the price everybody pays when it gets to that level?

Mr Ray—I think what matters is our net debt rather than our gross debt.

Senator JOYCE—In that case, we need to go back to discussing what the debts of the states are.

Mr Ray—Our net debt is expected to peak, from the Treasurer’s press release of 8 December, at 9.6 per cent of GDP in 2013-14.

Senator JOYCE—In discussing the net debt, did he tell you what the debt securities the government owns from the state and territory governments are? Is that amount in there?

Mr Ray—To the extent that we did own any, they would be included in that.

Senator JOYCE—How much are they in that net debt position?

Mr Ray—I would need to take that on notice because I do not know, for example, what the Future Fund holds.

Senator JOYCE—What about the HELP loans? How much of them are in there?

Senator Sherry—Sorry, which fund was that?

Senator JOYCE—HELP.

Mr Ray—In MYEFO the estimates for HELP were \$12.2 billion in 2009-10, \$12.9 billion in 2010-11, \$13.3 billion in 2011-12 and \$13.4 billion in 2012-13.

Senator JOYCE—While you have that there, what are the cash assets in that net debt position? What is your cash component of your peak net debt position?

Mr Ray—No, we have only got to the end of the forward estimates, which is 2012-13.

Senator JOYCE—How much do we have at—

Mr Ray—\$2.1 billion.

Senator JOYCE—So we have \$2.1 billion in cash, \$245 billion gross and your net debt position was about \$150 to \$160 billion. Is that correct?

Mr Ray—Yes, \$153 billion.

Senator JOYCE—If we start working backwards through that, we have \$153 billion net debt, and then you have \$2 billion in cash, so we have to try to get up to \$245 billion. So it is

\$153 or \$155—say \$156 billion. And all the rest that we are netting it out against, since our total reliance on the net debt position, are amounts that the state governments owe to the federal government; things such as the HECS debt—we are going to have some interesting times collecting that—and IMF capital subscriptions. Don't you think that, even if it is not about the stringency but the capacity, the ability to clearly collect that money if you need it in a hurry is not really there?

Mr Ray—I am not quite sure I understand where you are going, Senator. The standard accounting treatment of this is that there is debt on the liability side, and then debt and debt-like assets, setting off against one another. That gives you the net debt.

Senator JOYCE—I know. So you have \$245 billion in a gross debt position—that is, real money owed to real people who really want it back—at your peak debt position. Then when you are netting it off, you are netting it off against a whole range of other items, which gets you down to \$153 billion; but in amongst those things you netted it off against, there is only about \$2 billion in actual cash.

Mr Ray—True, but there will be debt-like instruments like the Future Fund's holding of paper—

Senator JOYCE—Okay, let us go to the Future Fund. The Future Fund is earmarked to cover the liability of superannuation—in fact, the superannuation liability of public servants is in excess of the \$65 billion we have in the Future Fund.

Mr Ray—That is correct.

Senator JOYCE—So there is a difference—

Senator Sherry—But not all public servants are retiring on the one day, Senator—it occurs over time. The money in the Future Fund, which I think is about \$65 billion, is not being touched until the interest earned that accrues—which is interest on interest—equals the level of Public Service liabilities, and we will start to draw down on it over time.

Senator JOYCE—So there is difference between the \$65 billion and whatever the Public Service superannuation is—I imagine it is around \$120 billion. Is that noted in the \$245 billion peak debt position?

Mr Ray—No, superannuation liability is in net financial worth, which is also reported—

Senator JOYCE—Okay. So the other \$55 billion, being the difference between the \$65 billion and \$120 billion, is not noted in the \$245 peak debt position, is it?

Mr Ray—The gross debt that you are talking about is a projection of the gross amount of Commonwealth government securities on issue. That is one thing. Then there is a calculation of net debt—

Senator JOYCE—It is quite obviously not part of it. It is stating the bleeding obvious.

Mr Ray—And the superannuation liability is not in the calculation of net debt; it is in the calculation of net financial worth.

Senator JOYCE—Because it is not part of the Australian government securities outstanding in notes and bonds, you do not think there is a little bit of a peculiarity that you are netting the \$65 billion off to get down to your net position?

Mr Ray—It is standard accounting treatment. It is consistent with the accounting standards.

Senator JOYCE—So it is in for one but it is not in for the other?

Mr Ray—I beg your pardon?

Senator JOYCE—The liability is not in, which makes absolute sense. The difference between the \$65 billion and \$120 billion being \$55 billion, not being in, makes absolute sense because it is not part of the government securities outstanding; but finding the net debt position you do include the \$65 billion in the Future Fund.

Mr Ray—This is exactly why the government, in its fiscal strategy, looks at net financial worth, not net debt.

Senator JOYCE—But can the return from the Future Fund be put towards paying off the gross debt?

Mr Ray—The return to the Future Fund is held in the Future Fund.

Senator JOYCE—That is right. So you cannot actually put it towards paying back the money we owe overseas and domestically, can you?

Mr Ray—Net debt is a calculation of the government's net asset position, or net liability position. It does not go to the questions of capacity to pay. If you are looking at capacity to pay, interest costs are low by historical standards.

Senator JOYCE—The main thing is: when we need to pay back that \$245 billion, we cannot use the money from the Future Fund, nor can we use the returns from the Future Fund.

Mr Ray—Correct, Senator. The way that the debt will be paid back is by the government running surpluses.

Senator JOYCE—Okay. How many years of surpluses and by what amount would you need to run to pay back \$245 billion?

Mr Ray—The projections that were done at MYEFO were, I think, that net debt is returned to zero in 2021-22. The first surplus was in 2015-16.

Senator JOYCE—What sort of surplus do you need to run? About \$17 billion or something, isn't it?

Mr Ray—We can take the question on notice, but I do not think we have published anything that can help you calculate that.

Senator JOYCE—When would the first surplus have to be? In what year?

Mr Ray—It is not when it has to be, Senator. Under the projections—

Senator JOYCE—When under your projections is it?

Mr Ray—2015-16.

Senator JOYCE—So you have got 2015-16, 2016-17, 2017-18, 2018-19, 2019-20, 2021-22—seven years of consecutive surpluses.

Mr Ray—Correct.

Senator JOYCE—We are not going to have any more recessions, are we?

Senator CAMERON—Why do you keep talking the economy down? How about responsibility for once in your life?

Mr Ray—Senator, the projections are built—as all of these long-term projections are—with the economy growing. Once the output gap is closed the economy grows at trend.

Senator JOYCE—But don't you think it is a bit fanciful to have a prediction that you will go along seven years—and I think the surplus amounts are going to have to be huge to pay off the debt. It just does not happen like that.

Mr Ray—In Australia's history it has happened before.

Senator JOYCE—When?

Mr Ray—In the 1990s.

Senator JOYCE—What was the largest surplus we have ever had?

Senator CAMERON—I'd stop asking those questions.

Senator JOYCE—Madam Chair, if you do not want to control him then we are quite happy to talk all the way through yours, okay?

CHAIR—Except that we do not really have many questions, but I do take your point. Please ignore the interjections.

Mr Ray—I have only got data back to 1970-71, so if you want me to go further back I would need to take it on notice. The largest surplus back to then was in 1970-71 and it was 2.2 per cent of GDP.

Senator JOYCE—And what proportion are these surpluses going to be, from 2015-16 on? What sort of surpluses are we looking at there?

Mr Ray—If you look on page 34 of MYEFO, chart 3.1, you will see how the surpluses run out to 2019-20. As you will see, the 1920 one, which is the highest one, is somewhat below two per cent.

Senator JOYCE—What we are asking for is a consecutive run of surpluses which are equal or greater than any surplus we have ever had before.

Mr Ray—I do not think that is correct, Senator. None of those is anywhere near the highest surpluses we have had in history.

Senator JOYCE—So we are relying on consecutive surpluses from 2015-16 to—

Mr Ray—2021-22.

Senator JOYCE—And is our projected position right now inferior or superior to what was projected a year ago?

Mr Ray—Our projected position in the future at MYEFO—

Senator JOYCE—If we go back to the midyear economic forecast, the midyear fiscal outlooks for 2008-09, where we are right now are we ahead or behind?

Mr Ray—That is a question that you discussed this morning around the passage of forecasts. I think a better way to think about this is our projections of net debt at budget compared with MYEFO, and the MYEFO projections are lower than at budget.

Senator JOYCE—Is the position projected in 2008-09 of where we are right now better or worse than where we are? I have got it right here in front of me.

Mr Ray—On the budget deficit?

Senator JOYCE—Yes. Underlying cash surplus, \$3.6 billion surplus. That was what was projected in 2008-09.

Mr Ray—You discussed this morning that that projection was done before the global financial crisis.

Senator JOYCE—So when do you say the global financial crisis started and finished?

Mr Ray—I think we usually mark the major event as September 2008. There had been disruptions in financial markets before that, but September 2008—

Senator JOYCE—When was the midyear economic fiscal outlook put out in 2008-09?

Mr Ray—Sorry, you are going from MYEFO. My recollection is October. We think actually it was the first week of November.

Senator JOYCE—And this was put out in November. You said the global financial crisis started in 2008. This predicted a \$3.6 billion surplus. In the latest one your predicting a \$57.7 billion deficit. That is quite a turnaround considering that the global financial crisis was actually at foot when this document was written, yet we have got to somehow believe that we are going to have seven miraculous surpluses in a row after 2015-16 to pay off a peak gross debt of \$245 billion.

Mr Ray—I think you are talking about two different things. You are talking about forecasting in an extremely uncertain environment, so those forecasts were changed. For example, the IMF was constantly revising down its forecast, as wrongly, through that period. We published revised outlook for the budget in February of 2009 which showed deficits. Then the budget in May showed deficits and the 2009-10 deficit did not change much between budget 2009-10 and MYEFO compared with projections, which are a rather different beast.

Senator Sherry—Senator, when the financial crisis I think became apparent in September of 2008, as Mr Ray has mentioned, it was not sunshine one day and doom and gloom the next. It evolved; it gradually got worse and worse and worse over quite a long period of time.

Senator JOYCE—My point being that what is real is the actual numbers; what is real is the numbers you actually owe. What is speculative is the belief that things will happen that will allow you to have seven surpluses in a row. You just cannot predict that sort of certainty to bring yourself to being able to pay off the debt in 2022, especially when you look at the current financial environment where you have got the uncertainties of sovereign debt risk in Portugal, Italy, Spain, Greece and the stresses that are on United States and the stresses that are on the United Kingdom. These stresses are evident to any person who has a look on the internet and sees the evidence. To come up with this idea that we will continue to march ourselves into greater and greater debt—

Senator Sherry—To summarise, I was at the IMF World Bank meeting for Australia last year—I had the privilege of attending last year. I have to say that I met a huge range of people, not just from the government sector but also from the financial sector, from ratings agencies and right across the economic and financial world. There was a unanimous view: they viewed Australia very favourably because of the strength of our economy, our regulatory system, our financial regulatory system and our robust governance. Compared to other advanced economies they viewed Australia very favourably. They viewed favourably the purchase of Australian bonds and investment in Australia. There was no other advanced economy that was comparable. That remains the situation today.

Senator JOYCE—I am not actually arguing with you on that point, to be precise; I am asking why we would continue to go down the path of borrowing more money when we do not have to put ourselves in a position of greater stress considering the possibilities and turmoils that are out there in the marketplace—not necessarily domestically but surrounding us globally. Why wouldn't it be a prudent thing to start withdrawing the stimulus and pulling back from what seems to be our insane desire to walk ourselves out to a \$245 billion gross peak debt position?

Senator Cameron interjecting—

Senator JOYCE—Everything about your approach, Senator Cameron, shows that you just think the whole thing is a joke. You just do not take it seriously. The Labor Party does not take it seriously. All we have heard from you today is a buffoon in the corner barking out. That is the approach that you have taken.

CHAIR—Senators, if you do not want to discuss this issue then please go outside because I know there are other senators who do.

Senator JOYCE—Madam Chair, you cannot control him. Why can't you control your colleague?

CHAIR—Senator Joyce, you are responding to the interjection and continuing the conversation. I am merely saying that if you continue to do that then I will pass the question to your colleagues who are happy to ask questions.

Senator JOYCE—Why can't you control Senator Cameron?

CHAIR—Senator Joyce, do you have further questions?

Senator JOYCE—Why can't you control Senator Cameron?

CHAIR—I am very happy to go to one of your colleagues.

Senator JOYCE—I will cede to Senator Bushby.

Senator BUSHBY—I only have a few questions. In answer to a question on notice that I received from APRA they provided a graph showing a depiction of bond lines and the yields from July 2007 up until October 2009. It shows a consistent increase in the yield being paid, since about December 2008 or January 2009. It basically consists of an upward line. You have mentioned a couple of times today that in recent months, and I acknowledge that graph only goes to last October, you have not seen any trend or change. I will be asking APRA about this later this afternoon but is the general upward trend of the last 12 or 13 months still apparent?

Mr Ray—Someone will correct me if I get this wrong. MYEFO was published in November and the 10-year bond today is roughly the same yield as last November so that is what I mean by recent months. What you are talking about is that on bond markets as a result of the global financial crisis bond yields were unusually low.

Senator BUSHBY—Exactly, they dropped once the GFC started and they have been steadily building back up—

Mr Ray—Yes, that is right.

Senator BUSHBY—over the last 12 to 14 months or so. That obviously impacts on the cost of borrowing to the government—

Mr Ray—Yes.

Senator BUSHBY—in a negative way; negative in a qualitative sense. It adds to the overall cost of borrowings for the Australian government.

Mr Ray—Yes, and I think we probably discussed this in the past. When we did the calculations that the government published in the budget the average cost of funds was let's call it X—I cannot remember—and at MYEFO it was higher as a result of market movements between budget and MYEFO.

Senator BUSHBY—I am going to explore that a little more with AOFM later on about where it is currently heading. I get updates from AOFM on a regular basis and I have seen some coming in very close to the six per cent, depending on the line, in recent times. I do not know if I have seen any over six—I may be wrong but it is certainly getting to six. I am curious as to what impact that has on the Treasury's predictions for the interest payable in the coming years. What assumptions have been built into the modelling or the forecasts for the actual rates?

Mr Ray—As we have discussed before, when we do the estimates for the budget or MYEFO we take our estimate of the interest rate off the existing yield curve. For new issuance—

Senator BUSHBY—The dynamic thing? What the market has built in for expectation?

Mr Ray—Obviously for the stock we know what the cost of those funds are and then it is for new issuance which may be for refinancing or for—

Senator BUSHBY—At this stage, though, we are adding—

Mr Ray—Incremental additions to the debt.

Senator BUSHBY—Yes.

Mr Ray—That is based across the forward estimates off the yield curve just before whenever the document is finalised.

Senator BUSHBY—Looking forward in terms of the debt that we have not yet filled or, alternatively, debt that is being rolled over, the actual interest or yield that ends up on those bond loans is actually higher than the estimates that you put in place. That will actually result in higher levels of interest having to be paid in absolute terms, certainly on that section of debt.

Mr Ray—That is correct.

Senator BUSHBY—What amount in dollar terms is the most recently forecast to be payable for servicing government debt in this and each of the forward years, as far you have actually made those estimates?

Mr Ray—For 2009-10?

Senator BUSHBY—For this year and then as far as you have done the forecast.

Mr Ray—This is in the historical tables. The net interest payments are \$1.95 billion in 2009-10, which is about 0.2 per cent of GDP; \$4.974 billion in 2010-11, which is 0.4 per cent of GDP; \$6.949 billion in 2011-12 and \$8.206 billion in 2012-13, and they are about half a per cent of GDP.

Senator BUSHBY—And that is as far you have gone in calculating that?

Mr Ray—That is as far as we go in the forward estimates. With the budget there will be an additional year.

Senator BUSHBY—Presumably, on that forecast that the debt will not be paid off until about 2021-22, or was it 2020-21? There is a plan by the Treasurer to pay off or retire debt in its entirety by the early 2020s.

Mr Ray—The government has a fiscal strategy. The way we do our medium-term projections is that we take the forward estimates and then we build off that. So they are seamless, if that answers your question.

Senator BUSHBY—In your medium-term projections do you have any assessment of what the cost of servicing debt will be? I am interested in whether, on the basis of your forecasts, it is possible to quantify how much it will cost to service the debt having, I think, gone back into net debt in this year through to the point where the government's fiscal strategy indicates that it will be paid off?

Mr Ray—Let me take that on notice.

CHAIR—That concludes the session. Thank you to the fiscal group of Treasury for your attendance this afternoon.

Proceedings suspended from 3.45 pm to 4.05 pm

CHAIR—The committee will resume. I welcome the Treasury Markets Group for outcome 1. Mr Murphy, there is no opening statement?

Mr Murphy—No.

CHAIR—I will start off with a question about the withdrawal of the large-deposit and wholesale-funding guarantee and perhaps just an initial question about the implications of that for the banks' wholesale fundraising activities and competition between banks.

Mr Murphy—Madam Chair, the minister will be joining us, I assume.

CHAIR—I assume so. If we need to refer questions to him, we will.

Mr Murphy—Okay. The Treasurer's announcement on the withdrawal of the wholesale funding guarantee has, I think, been widely discussed post the announcement, and actually

there was a lot of discussion prior to the announcement as to whether the guarantee needed to continue and also, I suppose, about the effectiveness of the guarantee in meeting its objectives. It has been reported—so I will not go into all that information—that it proved a highly effective measure to enable the Australian banks to continue funding Australian businesses and the Australian community. It demonstrated that the banks could retain their position as leading financial institutions.

In terms of the impact on competition, I think what you saw was a concentration in the Australian financial system largely caused by the global financial crisis. There has been a diminution in market share of the nonbanks and some of the regional banks, but that was not unexpected given the stresses and strains financial systems were withstanding. I would expect that competition, to the extent that is optimal for the Australian market, will return over time.

CHAIR—What about its effect, if any, on mortgage funds? I am thinking particularly of those that are frozen at the moment.

Mr Murphy—I think some comments were made by the secretary this morning about that. Yes, a consequence has been the freezing of certain mortgage funds. Mortgage funds were having difficulties with their redemptions prior to the GFC and in the early stages of the GFC. The facility of freezing the mortgage funds is a response to that, which the funds have the capability of implementing. It is disappointing that people cannot withdraw their funds as they wish, but I think the bottom line on that at the moment is that no-one has lost any money in a mortgage fund. Yes, their funds have been frozen. Hardship provisions have been introduced whereby people can withdraw their funds. A number of the funds are making periodic distributions. ASIC has set up a task force to see what further measures can be taken. Again, the bottom line is that it is a consequence of the global financial crisis that mortgage funds are in a more vulnerable position than bank deposits—but, that said, no-one has lost any funds so far, and one would hope that over time the funds, which have managed the liquidity issue quite well, can continue to manage it and that, over time, funds become unfrozen and people can make their decisions as to whether they wish to reinvest with the mortgage fund or invest elsewhere.

CHAIR—That phrase that the mortgage funds ‘have managed their liquidity quite well’ interests me. A large number apparently are frozen, and it is my understanding that those that are releasing funds are releasing them only in very small quantities—something like five per cent annually, I understand. They might be still liquid, but I am wondering if there is any real incentive for those funds to release the funds to their investors any more easily than they appear to be at the moment.

Mr Murphy—I do not think there is any incentive there to hold onto funds other than for ensuring the stability and the financial viability of the fund. That is why the funds have frozen their assets. It would seem that, over time, they will make larger distributions as markets return to normality.

CHAIR—I will follow that through later with APRA and ASIC.

Senator EGGLESTON—I understand that during the 2007 election the Labor Party promised that it would establish a superannuation clearing house by 1 July 2009 and that the clearing house concept was to allow small businesses to pay their superannuation

contributions electronically to a single location. The clearing house would then distribute the contributions to the relevant superannuation fund as selected by the employer. I understand that Medicare has been appointed as the clearing house. Is that correct?

Senator Sherry—That is correct. That is a matter for Revenue Group. I do not think it falls into Markets Group.

Senator EGGLESTON—The secretary advised me that it is Markets Group.

Mr Murphy—Sorry.

Senator EGGLESTON—These are important questions.

Senator Sherry—It is a mistake, but we will do our best.

Senator EGGLESTON—I appreciate that, but I was advised that this is where it was. What advice did the Treasury give to the minister regarding the decision to award the superannuation clearing house contract?

Senator Sherry—That is policy advice.

Senator EGGLESTON—Okay. Have there been alternative business proposals for the superannuation clearing house put forward to the government?

Mr Murphy—We cannot answer that.

Mr Brake—I am sorry, Senator; I do not know the answer to that.

Senator EGGLESTON—On the grounds that it is policy?

Mr Brake—That would be a matter for Revenue Group, but we can take it on notice.

Senator Sherry—We will take the question on notice.

Senator EGGLESTON—Given that the original Superannuation Clearing House discussion paper promised a tender to the private sector, was a draft tender document prepared by Treasury in 2009?

Mr Brake—We will also take that on notice; it is revenue group.

Senator EGGLESTON—You cannot answer any subsequent questions on that, but there are two which will be put on notice. Effective and ASIC fully licensed commercial clearing house alternatives exist which could be implemented in less time than the Medicare proposal and could be delivered under your allocated budget. Given that alternatives exist in the private sector, why has the government opted to spend significant taxpayer dollars attempting to reinvent a technology from scratch with a provider who is not providing this service now?

Senator Sherry—We would have to take that on notice.

Senator EGGLESTON—I have a feeling that a lot of these will be like that.

Senator Sherry—I recall reading Minister Bowen's press release on this which would deal with some of the matters, but I do not have it with me. The officials that handled it are not here. I think, and it is unfortunate, that you should put the questions on notice. I will try to expedite a response as quickly as we can, given the circumstances.

Senator EGGLESTON—I have other questions which might be appropriate. These questions relate to the retirement savings gap. Is that issue relevant to you?

Senator Sherry—No.

Mr Brake—Not really.

Senator Sherry—The claimed ‘retirement savings gap’, and that is a matter of dispute, is a retirement income issue, frankly. Our master modeller, Mr Gallagher, is not here. He was here for most of the day and I think he would deeply regret the fact that you were not able to pose those questions earlier. I know Mr Gallagher is always very willing to discuss those sorts of issues.

Senator EGGLESTON—I was advised that this was the appropriate group. Do you want me to quickly go through these questions and see whether they can be answered?

Senator Sherry—I doubt that they can.

Senator EGGLESTON—Alright, thank you. We will put them on notice.

Senator Sherry—Frankly, without Mr Gallagher’s expertise it would be very difficult if not possible.

Senator EGGLESTON—I accept your advice gracefully.

Senator Sherry—Again, I will try to expedite the answers for you.

Senator EGGLESTON—I have another question which might be in the Markets Group area. I understand that a rebate on television licences was provided; is that within your area?

Mr Archer—That is a policy matter that falls within the realm of the Department of Broadband, Communications and the Digital Economy.

Senator EGGLESTON—So what are you saying?

Mr Archer—I am saying that policy responsibility rests with another portfolio.

Senator Sherry—If you look at the media coverage—I have glanced at it—you will see that Senator Conroy is the responsible minister not the Treasury minister.

Senator EGGLESTON—It is a communications issue, but it does involve money.

Senator Sherry—Everything involves money and, on that basis, you could ask about anything.

CHAIR—Not everything.

Senator Sherry—Well, almost everything. You could be here asking us questions in any policy area. The responsible minister is Senator Conroy. It is his portfolio.

Senator EGGLESTON—Again, I was advised that it was a Markets Group issue, so I will put both of those questions on notice.

Senator BUSHBY—Did Treasury have any involvement?

Senator McGAURAN—My question is in relation to the Foreign Investment Review Board. A decision was made in 2008, or around that period, to lower the threshold for foreign investors buying residential property. Firstly, would you inform us when that decision was made and what the threshold is? Moreover, what has the effect been in regard to volume, value terms and unit terms?

Mr Colmer—In December 2008, Minister Bowen announced changes to the arrangements for residential real estate. Basically those arrangements were administrative changes rather than changes to eligibility. Those arrangements were implemented, I think, from 1 April 2009. Essentially those arrangements streamlined the administration. They did that by exempting people with temporary residence visas from coming to formally seek approval for foreign investment. The eligibility was not actually changed. A person who is a temporary resident may buy a house for use as their principal place of residence or may buy a vacant land to develop a dwelling, but that was the situation prior to the change. So what we actually did was remove the requirement for them to formally notify.

In terms of nonresidents, the rules have not changed but we have moved from a formal screening arrangement to a simple notification arrangement. The rules restrict nonresidents from buying new property in the vast majority of cases. The only real exception to that is that in some circumstances a nonresident may buy an existing property. If they are going to develop that property by demolition and rebuilding—

Senator McGAURAN—That is a commercial property?

Mr Colmer—No, that is a residential property. There are not many cases of that, but there are some.

Senator McGAURAN—That was not clear. The rule is that nonresidents can purchase new residential property.

Mr Colmer—That is right.

Senator McGAURAN—What is ‘new’?

Mr Colmer—‘New’ is new, obviously, but it includes—

Senator McGAURAN—Never occupied.

Mr Colmer—No. It used to include ‘never occupied’. That used to be a blanket rule, but we have extended the definition of ‘new’ to include properties that have not been sold and have not been occupied for more than a year. That was in response to some problems that were arising with developers finding it difficult to sell new properties.

Senator McGAURAN—Are you able to gauge the effect of those changes which are in a sense lowering the threshold or streamlining the system? Have you been able to gauge the effect?

Mr Colmer—The immediate effect has been that we are no longer dealing with 8,000 applications a year. It is a bit too early to tell what the actual impact is because as part of those changes we no longer get notifications of temporary residence purchases. For nonresidents it does not look as though there has been any significant change in the overall numbers but it is a little bit too early to tell at this stage.

Senator McGAURAN—I am surprised. Mr Murphy, in response to the chair’s question about bank competition pre and post the guarantee, you said that you believed that we would return to the optimal competitive state, or something like that. What is that? What is the optimal state?

Mr Murphy—That is a good question. I was talking about whatever is optimal for the Australian market. We would say that in the circumstances prior to the GFC we had a reasonably competitive mortgage market and funding for small business. It seems that over a period of time mortgage rates had become more competitive and access to finance had become more competitive, including for small business. So we are looking to ensure that we are in a position whereby any distortions or impediments to the flows of funds through the Australian economy are removed and there is true competition between the various market players.

Senator McGAURAN—It is something you know when you see it or feel it, is it?

Mr Murphy—Well, you have the ACCC and ourselves doing an analysis as to what we think would be the benchmark upon which we could compare what we have at the present time and what we should have.

Senator McGAURAN—Can we safely say we will never return to the optimal competitive situation we were in before the global financial crisis because we have lost a few along the way?

Mr Murphy—No, I do not think so.

Senator McGAURAN—Aussie Home Loans, for example.

Mr Murphy—No, I think you will find that the market is returning to a more normal state and, as in any competitive market, there will be new players emerging and old players will lose market share because of inefficiencies or because they will be less competitive. Even now—and Yellow Brick Road, which is tied in with a credit union, is one example—they are starting to emerge. You may have foreign players come into the Australian market. The thing about the Australian market for financial services is it is a very good and profitable market. So I think that, more likely than not, we will have much more competition coming back.

Senator McGAURAN—Are you at liberty to answer why you think the bank guarantee has been lifted? The Treasurer himself has said why it has been lifted—and I dare say why it was ever introduced. He said:

... we've seen from the date that's been published that their interest rate margins—
that is, the banks'—

... are back to pre crisis levels. That means that they are as profitable in terms of their rate margins now as they were ... the global financial crisis.

Is that why it was introduced, to support the banks' profit margins?

Mr Murphy—No.

Senator McGAURAN—Well, that is what the Treasurer—

Mr Murphy—No, it was not. I think that it is out of context. That is a paper's report.

Senator McGAURAN—8 February.

Mr Murphy—The Treasurer made a fulsome statement when he announced the withdrawal of the guarantee. That comment there I think is alluding to the fact that the banks

are now in a position whereby they can successfully raise wholesale funding to finance their books without the need for government support. That is what the Treasurer is on about.

Senator McGAURAN—It was all about getting them back to their profit margins.

Mr Murphy—No, it is not about getting them back to profit margins. It is enabling the Australian financial system to operate successfully. The four major banks are key elements or key pillars of the Australian financial system. If our four main banks were unprofitable or in a parlous financial state, the Australian financial system would be in a difficult position. But we are not. What we have got is a competitive financial system which could be enhanced with the introduction or the comeback of some of the other fringe players which were there prior to the GFC.

Senator McGAURAN—I must admit that I agree with you, that was why we did introduce it so that we could get a more fluid credit market.

Senator Sherry—The Treasurer said that time and time again. The guarantee has been vital to support the flow of credit into our economy. In fact, during that period \$160 billion was raised. Can you imagine the consequences if that money had not been raised for businesses and consumers? It would have been catastrophic.

Senator McGAURAN—That is what we all understood. So I do not know what he is talking about here.

Senator Sherry—The Treasurer has always maintained that, and said it very frequently in a whole range of public forums.

Senator McGAURAN—Well, explain his comment that I just quoted before.

Senator Sherry—Senator, you come in here, as you usually do, with press clippings—is that a press clipping you've got there?

Senator McGAURAN—Yes.

Mr Murphy—It is in the *Fin Review*. It is out of context.

Senator Sherry—It is a press clipping, Senator McGauran.

Senator McGAURAN—And?

Senator Sherry—It is a press clipping.

Senator McGAURAN—Don't believe everything you read in the newspapers?

Senator Sherry—I am not going to tell you how to put your questions together at estimates. I notice you come in with lots of press clippings, but there is a bit more research required than collections of press clippings.

Senator McGAURAN—Back to the competition question and the bank guarantee. As you know, there are two different fee structures for the banks. The big four have a lesser fee to pay than those outside that orbit. That seemingly, certainly the Bank of Queensland would tell you, had a severe effect on competition, did it not? An ability to access the bank guarantee did more to diminish competition.

Mr Murphy—The Bank of Queensland has expressed those views. I do not agree, a lot of people do not agree with the Bank of Queensland's views. Access to the government's

wholesale guarantee was priced to represent the risk to the Commonwealth of underwriting or supporting the fundraising by a financial institution. There is a three-tier pricing level, not two. The majors, who are AA, were paying 70 basis points; the A banks, such as Macquarie and Suncorp, were paying 100 basis points; and the BBB rated banks, such as the Bank of Queensland or the Adelaide and Bendigo Bank, were paying 150 basis points.

Largely, banks such as the Bank of Queensland do not raise significant wholesale funding; they raise some, but largely they rely on the securitisation market which, yes, has been severely affected by the global financial crisis. The policy response to that by the government has been to step in and issue two different tranches of \$8 billion by the AOFM to support the securitisation market to enable people like the Bank of Queensland and others to obtain funding to continue on their businesses. So I think that, all things considered, the government's response in going forward with a wholesale guarantee plus the government's response in trying to support the securitisation market to benefit the smaller players has been a very timely and successful two-pronged attack on the problem that had emerged.

When the wholesale funding guarantee was introduced, one of the key factors was that other countries had guaranteed their banks in terms of their funding. If the government had not moved there, Australian banks would have been discriminated against. So, largely, the guarantee for the Australian major banks was to just bring them back to an even keel with banks from other countries. And what we have seen is that the four major banks are now in the top 12 banks in the world because they have been able to compete and have not been discriminated against because they have not got a government guarantee.

The Treasurer has made the decision on the advice of the Council of Financial Regulators that now is the time to give notice that the government guarantee for wholesale borrowings will be withdrawn because largely the market has returned to normality, and that was the criterion which the Prime Minister announced. He said that the wholesale funding guarantee would remain in place until markets normalised. One of the key factors for saying there is normality is the fact that largely the four major banks have stopped using the guarantee and can now borrow or raise funds internationally without the guarantee. Non-guaranteed issuance is largely priced more favourably than guaranteed issuance, given that they have to pay a fee to the Commonwealth.

Senator McGAURAN—This question is to Senator Sherry. It is still on the bank guarantee and on the Bank of Queensland. Do you object if I quote something from the newspaper? The newspaper reports that the Chief Executive Officer, David Liddy, was very upset that he was not consulted prior to the announcement of the abolition of the bank guarantee. Is that so? If so, why not? More so, I come back again to this obsession the government had with the big four and putting everyone else aside. Obviously there was huge consultation with Westpac, because prior to the announcement—

Senator Sherry—Why do you say there was consultation with Westpac? What evidence do you have?

Senator McGAURAN—Let me ask you the question: was there? Prior to the announcement there was an enormous surge by Westpac—

Senator Sherry—Of what?

Senator McGAURAN—of borrowing to take advantage of the final days of the guarantee and yet the Bank of Queensland were left out of that.

Senator Sherry—Senator, I can indicate to you that I am advised that there was no consultation with anyone—

Mr Murphy—from the department

Senator Sherry—As far as the department goes, it did not consult with anyone; nor did I. I can take the question on notice for the Treasurer. The surge you referred to—

Senator McGAURAN—It was \$9 billion, I think

Senator SHERRY—It was a surge in what, sorry?

Mr Murphy—They raised funds. Westpac raised funds in December. The other major players had announced that they had no wish to continue to raise funds through the guarantee. Westpac's decision was a commercial decision.

Senator McGAURAN—But if you knew the announcement—

Mr Murphy—These banks raise funds all the time. That was their decision.

Senator McGAURAN—If you knew the announcement was coming, you would take advantage of it in its last, dying days.

Senator Sherry—But that was December last year. The announcement was made, I think, last Sunday, whatever date that was. So what is the issue, Senator?

Senator McGAURAN—Were the major banks consulted about the abolition of the guarantee?

Mr Murphy—No.

Senator Sherry—As far as the department, my office and I are concerned, the answer is no and I will take the question on notice for the Treasurer.

Senator BUSHBY—I might as well start with banking since we are talking about that at the moment. We have been over this in the inquiry that was held, Mr Murphy, but in your explanation about the impact on competition you rejected Senator McGauran's assertion that the wholesale guarantee had imposed any competitive disadvantage on anyone other than the top four banks. You then went on to explain the reason why the government put it in, which was fine, but you stated that the reason why there was a differential charging system was based on risk from the government's perspective—basically to protect the taxpayer. Therefore, it was not based on maintaining the competitive position of banks relative to each other. The fact is that, if you were not a top-rated bank, you had to pay more for the guarantee. Therefore, if you had no choice but to get your funds with the government guarantee, it did put you at a competitive disadvantage compared to the banks that had to pay less.

Mr Murphy—I am sorry. I am not clear about the question.

Senator BUSHBY—It imposes a higher cost of funds.

Senator Sherry—You are stating a fact.

Senator BUSHBY—That is right, but Mr Murphy said that he did not concede that it put smaller banks at any competitive disadvantage when, to access the same funds, they had to pay more. I understand that the reason for that is the government chose to price according to risk, but, in doing so, I cannot see how you can not concede that it did put the banks who could not get it at the cheapest rate at a competitive disadvantage to those who could.

Mr Murphy—Realistically, the fee schedule was derived from the ratings of the banks.

Senator BUSHBY—I understand that.

Mr Murphy—The ratings of the banks are the market's ratings.

Senator BUSHBY—I understand that too, but the government could have made a decision to price it based on something other than risk. I understand that is the choice it made and there may have been very good reasons for doing that, but nonetheless the consequence must be that it makes it harder for those who cannot access at the cheapest rate to access funds at the same competitive level as those who can.

Mr Murphy—A consequence could have been that, without the guarantee, no-one would have accessed new funds.

Senator BUSHBY—I am not arguing with the need for the guarantee. I am not arguing with any of that. But I am saying that I do not see how you can not concede that the differential rating, regardless of all the reasons, as justified as they are or otherwise, did have that consequence.

Mr Murphy—If you do not have a differential fee, you are basically giving an advantage to the lower rated banks by having a flat fee for the guarantee.

Senator BUSHBY—You may well be, but—

Mr Murphy—The fee is trying to represent imposition of the guarantee to put the banks into the same position they should be in without the guarantee. In other words, you are not trying to give the Bank of Queensland a free kick—

Senator BUSHBY—But if you are trying to maintain the status quo of the banks prior to the GFC, and the government is intervening to try to maintain the system and to shore it up and make sure it does not suffer any of the consequences we saw elsewhere, why did we end up through the course of that—and this information came from the answer to a question on notice SBT 54—with the major banks' share of housing loans increasing from 53 per cent in June 2007 to 56 per cent in June 2008 and 70 per cent in June 2009? Similarly, household deposits went from 68 per cent in June 2007 to 69 per cent in June 2008 and 82 per cent in 2009. I cannot see that a status quo is being maintained there. Part of the reason that change has happened is confidence issues.

Mr Murphy—That is true.

Senator BUSHBY—Adding to that would be the issue of costs and competitiveness. If you were looking to maintain the status quo, maybe giving some of those smaller banks a bit of an advantage might have actually assisted.

Mr Murphy—I think we did give the banks an advantage with the securitisation issue.

Senator BUSHBY—I am coming back to your particular answer where you said that if you had priced at the same level then you would have given them an advantage. Surely that could have been a good thing to try to avoid that drift towards a much higher concentration.

Mr Murphy—Yes, but for a lot of the banks—if you are looking at the regional banks and you are looking at, say, credit unions—the other big support governments give is through the deposit guarantee. They have benefited significantly through the deposit guarantee.

Senator BUSHBY—I am sure they have. Nonetheless, household deposits in the majors have gone from 68 per cent in June 2007 to 82 per cent in August 2009.

Mr Murphy—Yes.

Senator BUSHBY—I am sure they have all benefited from the guarantee. You still had a concentration—

Mr Murphy—You can take one figure and you can take it out of context. For example, take the earlier question on frozen funds. That is linked to deposits. We can compare the price of the wholesale funding of the smaller banks' debt with the majors. You have to put this in terms of the fact that the major banks live and fall by the fact that they need wholesale funding. That is the business.

Senator BUSHBY—And traditionally the smaller banks have got their money through other methods?

Mr Murphy—Elsewhere, yes.

Senator BUSHBY—Securitisation being a large part of that.

Mr Murphy—I know Mr Liddy has some very strong arguments, but what I am saying is that I think they are exaggerated. Mr Liddy is a very good banker; there is no issue about that. I think he is pushing a position. I think you have to look at these things in perspective. Yes, it is not to be unexpected that you are going to have a change in market shares coming out of the GFC.

Senator BUSHBY—I agree with that. You were the one who said you were trying to maintain the status quo and not actually introduce any—

Mr Murphy—Any intervention in any market is going to have certain implications.

Senator BUSHBY—Absolutely; I agree with that.

Senator Sherry—I am sure that description of the status quo did not mean that the financial system as existed on the day prior to the guarantee being introduced would continue unchanged in terms of credit being raised, interest rates, bank share of the markets and building society share of the markets. There was no way you were going to be able to continue the status quo—just continue on as though nothing had changed in the world—given the circumstances, even with a bank guarantee.

Senator BUSHBY—I would be very surprised if that is what he meant. Nonetheless, what was concerning me was the fact that he would not concede one of the consequences—which I think is obvious to a lot of financial commentators—of the differential in the thing. That said, we will move on. You have made your point; I have made my mine.

Mr Murphy—Yes, but I think—

Senator BUSHBY—I will leave it up to the people who read the *Hansard* to draw their own conclusions.

Mr Murphy—All right. But it is—

Senator BUSHBY—Can we move on, please. I will stick to banking for the moment. Can Treasury provide updated figures for the market share of each of the four big banks? Do you have any updated figures that can give us their share of those things since June of last year?

Mr Lonsdale—In terms of housing loans, the current share of the major four banks is 82.4 per cent as at September.

Senator BUSHBY—So in three months it has gone up by 12 per cent?

Mr Lonsdale—As at September 2009.

Senator BUSHBY—In June 2009 it was 70 per cent.

Mr Lonsdale—In June 2009, 81.3 per cent.

Senator BUSHBY—Those are not the figures that you provided in answer to the question on notice.

Mr Lonsdale—These are for housing loans stock.

Senator BUSHBY—I have got here—well, this is transcribed onto my notes so there may have been an error in that, but the answer mentioned shows that the major banks' share of housing loans increased from 53 per cent in June 2007 to 56 per cent in June 2008 to 70 per cent in June 2009.

Mr Lonsdale—Sorry; I am reading from the wrong line.

Senator BUSHBY—Are you reading household deposits?

Mr Lonsdale—In September 2009, 71.2—

Senator BUSHBY—71.2—that is more like it.

Mr Lonsdale—which was 70.4.

Senator BUSHBY—What about household deposits? That might have been the line you were reading from.

Mr Lonsdale—Yes. So, for household deposits for the major four banks: 82.1 in December 2009.

Senator BUSHBY—What about business loans?

Mr Lonsdale—Business loans to non-financial corporations for the major four banks, as at December 2009: 70.7.

Senator BUSHBY—So that is basically unchanged from June 2009?

Mr Lonsdale—Yes, it was 70.5 in June 2009.

Senator BUSHBY—I note in the answer to that question on notice that you have no published data on loans to small business.

Mr Lonsdale—I think that is correct.

Senator BUSHBY—Is that something that you think would be useful to the work that you do?

Mr Lonsdale—All data is useful to the work we do; it can be very difficult to get it sometimes.

Senator BUSHBY—Is this data ultimately sourced through the ABS?

Mr Lonsdale—I believe so.

Senator BUSHBY—The ABS does do surveys of small businesses for various purposes, and they are required by law to respond—is that not so?

Mr Lonsdale—Yes.

Senator BUSHBY—I am just querying the fact that you do not have data on that; I would have thought that, given the importance of small business to the Australian economy, more small business data would be useful, particularly in terms of recent problems that small business has had in terms of accessing finance. Can you outline the extent to which the wholesale banking guarantee has been utilised over each of the past 12 months?

Senator Sherry—Do you want a figure for every month for the last 12 months?

Senator BUSHBY—Yes, but I am happy for that to be taken on notice.

Mr Lonsdale—We have that data.

Senator BUSHBY—What level of usage was made by other than the big four banks over the time that it was available in terms of a percentage of the moneys guaranteed?

Mr Lonsdale—I can give you some of that information now if that is useful.

Senator BUSHBY—Yes.

Mr Lonsdale—In the first quarter of 2009, as to the amount of guaranteed funding used: 99 per cent of funding derived was guaranteed funding; only one per cent was non-guaranteed. I am going down now: for the second quarter, 62 per cent in 2009 was guaranteed and 38 per cent was not guaranteed; it was 54 per cent in the third quarter of 2009 and 46 per cent was non-guaranteed; in the fourth quarter of 2009, 30 per cent was guaranteed and 70 per cent was non-guaranteed; and, in the first quarter of 2010, so far, three per cent was guaranteed and 97 per cent was non-guaranteed.

Senator BUSHBY—Which is why the Treasurer has decided that the time has come; it was always discussed that the market would sort itself out eventually.

Mr Lonsdale—Yes, so this follows on from Mr Murphy's comments. If you compare the first quarter in 2009, where almost all the funding raised was guaranteed—

Senator BUSHBY—Because it was the only way they could get funding at that time. At this point, they can get funds without having to pay the fee to the government.

Mr Lonsdale—Yes, that is right.

Senator BUSHBY—So it is a cheaper, more competitive offer.

Mr Lonsdale—Correct.

Senator BUSHBY—I understand all of that. What about non—

Mr Lonsdale—This was the total usage of the facility.

Senator BUSHBY—What about usage other than by the four big banks?

Mr Lonsdale—I would have to come back on that point.

Senator BUSHBY—That is fine. If you take that on notice, that would be appreciated. An analysis of RBA research by the *Daily Telegraph* late last year showed that the big banks had collectively raised some \$1.8 million—sorry, \$1.8 billion; I have a typo here—

Senator PARRY—It is contagious!

Senator BUSHBY—Yes. Of course, I am sitting next to everybody!

Senator Sherry—It is contagious. I made the mistake at one point too.

Senator BUSHBY—They raised some \$1.8 billion more through wider margins than they would have earned had they maintained margins at their pre-global financial crisis levels. Have you looked at that analysis conducted by the *Daily Telegraph* at all?

Mr Lonsdale—No, I am advised.

Senator BUSHBY—Without having the benefit of having analysed their conclusions, do you think that their conclusions sound as if they could be plausible?

Mr Lonsdale—I think, with respect, that before commenting on it it would be useful for us to read the press article.

Senator BUSHBY—Could you take that on notice, then, please.

Mr Lonsdale—Yes.

Senator BUSHBY—In general, is it your opinion that the major banks have been able to widen the margin spread since the start of the global financial crisis?

Mr Lonsdale—Which margin in particular?

Senator BUSHBY—The margin between cost of borrowing and what they are lending it out at.

Mr Lonsdale—I am not sure we can conclude that.

Senator BUSHBY—You are not sure that you can conclude that because you think otherwise or because you are not sure?

Mr Lonsdale—That would be something that we would want to have a close look at the data on.

Senator BUSHBY—So you would like to look into it further before you comment?

Mr Lonsdale—Yes.

Senator BUSHBY—That is fine; I just wanted to clarify what you meant. As we have just outlined, the trend appears to have continued into the last quarter of last year. Over the last 18 months, the banking market has become far more concentrated, with large sectors of the loans market not operating, like Aussie Home Loans, which was mentioned earlier. It is far more

concentrated with the four big banks. To what extent has this lessening of competition affected the major banks' ability to set margins?

Mr Lonsdale—I think part of the answer goes back to what Mr Murphy was talking about before in terms of what you mean by competition. It is true that it has become more concentrated. Whether that has fed into rates and other indicators around competition would need to be defined, if that is what you are talking about.

Senator BUSHBY—Mr Murphy, you also mentioned that there were discussions with the ACCC regarding ongoing competition issues and where it should be—doing things that the government should do, looking at a market like the banking market to ensure that competition in future returns to normal levels. That is happening?

Mr Lonsdale—That is something that we are very interested in.

Senator BUSHBY—Is that a formal process that is happening or is it more ad hoc?

Mr Lonsdale—A formal process with the ACCC?

Senator BUSHBY—Yes, this examination of competition issues. I am not saying, 'Is it a formal review?' Is it something that has just happened as an aside or is it something that—

Mr Murphy—I suppose you could use this as a signal that, with the impact of the global financial crisis on the Australian financial system, we have got to a certain stage. I think there are still financial problems out there in international markets, but we have now got to the stage where, with the lifting of the wholesale guarantee, a key policy issue for the government is competition in the financial services industry.

Senator BUSHBY—I do not recall the exact details, and I am not sure whether it was Treasury or APRA who provided the evidence, but during the banking guarantee inquiry there was evidence provided that suggested—I do not argue with this—that during the midst of the crisis the most important factors were stability and solvency.

Mr Murphy—Yes.

Senator BUSHBY—And competition came a distant third, in a sense, because if you did not have those first two factors then competition was irrelevant.

Mr Murphy—Exactly.

Senator BUSHBY—But, coming out the other side, you are saying that the focus is returning to competition. Is that a correct conclusion?

Mr Murphy—We will always have stability and solvency.

Senator BUSHBY—Absolutely, that is right. But that is less of a concern; therefore the focus can return to competition.

Mr Murphy—Yes, in effect to enhance the wellbeing of the community. The government's objective is to ensure that the community has access to funding for its own purposes at the cheapest possible cost. That is the policy goal. In terms of competition, it is not just a focus on current players; it is a focus as to whether there are new players and whether existing players can expand their market share. It is a dynamic system.

Senator BUSHBY—It is, but there are a number of decisions that government can make that can affect how those dynamics play out. To some extent, that is subject to discussions you will be having with the ACCC and ultimately recommendations to government. I might add that I expect nothing other than that.

Mr Murphy—Yes. It is a worldwide problem. There is a major conference on at the OECD next week to which people from here are going which is all about the stability and competition in financial markets. It is not only in Australia where there has been a greater concentration in financial systems due to the impact of the GFC. It is a concern to governments worldwide.

Senator BUSHBY—We have had discussions before about the potential risk to the Australian financial system of adopting solutions to problems that occurred elsewhere that have not occurred in Australia.

Mr Murphy—This is on competition. I think you are alluding to the capital requirements coming out of the FSB and the liquidity requirements.

Senator BUSHBY—I would be interested to hear at next estimates how this conference goes.

Mr Murphy—I think these issues are very important.

Senator Sherry—There is a similar and related issue in wealth management superannuation, if it can be described as that, that has emerged. There were some questions yesterday. The ACCC issued a discussion paper yesterday afternoon.

Senator BUSHBY—I have a few questions about that market I will ask in a minute. Has Treasury been asked to provide any advice in relation to the concept of delivering banking services or similar services through any government owned body such as Australia Post?

Mr Murphy—Not to my knowledge.

Senator BUSHBY—Did the Markets Group assist in the development of the financial sector legislation amendment prudential regulation and other measures bill 2010?

Mr Murphy—Yes.

Senator BUSHBY—That has been released for consultation?

Mr Murphy—Yes.

Senator BUSHBY—How will this bill, if passed, add to better prudential regulation of the ADI sector in Australia?

Mr Lonsdale—My understanding is that there are a significant number of proposals in that bill put to us by APRA that would assist many objectives of the financial system—stability being a key one. A number of them are contingent, but they have largely been put to us by APRA.

Senator BUSHBY—I will ask APRA about that later.

Mr Murphy—A number of those measures come out of lessons regulators and policymakers got out of the global financial crisis. In certain areas there seems to be a need to ensure that APRA has sufficient powers to enable it to get the information it needs and to be

able to intervene at an appropriate time. You have to acknowledge what happens overseas. A number of the overseas regulators were found to have deficiencies in their powers and APRA did the analysis there and came to the government and said, 'We need to have enhanced powers in certain areas.'

Senator BUSHBY—Although the reality is that the prudential system we had stood us in good stead.

Mr Murphy—Very good stead.

Senator BUSHBY—Dr Henry and others have acknowledged that before. That is not to say we cannot improve things.

Mr Murphy—You learn from other people's experiences.

Senator BUSHBY—Is this the section of Treasury that put out the corporate whistleblowers paper?

Mr Murphy—Yes.

Senator BUSHBY—I understand in October last year, you released a discussion paper looking at improving the conditions. Can you outline where that process is currently at?

Mr Fraser—As you would be aware, the government issued an options paper in October 2009. Submissions on that paper closed on 23 December. We received 21 submissions.

Senator BUSHBY—Not all praising it, from what I understand.

Mr Fraser—There were certainly a wide range of views. It was an options paper which presented a range of views on a number of different matters. As I said, we got around 21 submissions—we have put them on the Treasury website—canvassing a wide range of views. Our next step is to have some roundtables with those respondents.

Senator BUSHBY—When do you think that will be occurring?

Mr Fraser—Hopefully around March.

Senator BUSHBY—And then after that you will be—

Mr Fraser—Providing some advice to the minister.

Senator BUSHBY—That is fine. I will move on to financial services. What is the government's view of the PJC's recommendation to consider a last-resort compensation scheme. Has Treasury provided any comment on that?

Mr Murphy—This is in the Ripoll report.

Senator BUSHBY—Yes.

Mr Murphy—Those matters are being considered by the minister at the present time. Treasury is working on those.

Senator BUSHBY—Are you assisting the minister with those issues though?

Mr Murphy—Yes.

Senator BUSHBY—I am aware that there are some others who want to ask some questions, so I might put the rest of these on notice. I imagine you would just tell me that they

are all with government anyway and not answer my questions. I will go back to where I was going to start, which is with the update as to where the taking over of the ASX responsibilities by ASIC is at.

Mr Murphy—A bill is being introduced into the parliament. It is still to be debated in the House of Representatives.

Senator BUSHBY—I have not had a look at that bill, so forgive me for not knowing what it actually says at this point. I have been busy this week. I have not had a chance. I was talking to ASIC at estimates in October and I asked them about how they were going to deal with the trading rules and how they would interact with the corporations law. Their answer to me indicated that that was a matter they were in consultation with Treasury on. Has any decision been made on that? Does the bill actually deal with that?

Mr Murphy—Yes. In the bill there is a power for ASIC to be able to make market rules. They will be able to make their own rules to administer and supervise the market players.

Senator BUSHBY—Will that be separate to the corporations law and regulations?

Mr Murphy—Yes. That is quite a significant step—to give ASIC the power to make rules applicable to the market.

Senator BUSHBY—In the meantime, will the current trading rules apply?

Mr Murphy—Yes.

Senator BUSHBY—And the new market rules by ASIC will replace them over time?

Mr Murphy—Yes.

Senator BUSHBY—I will move on from there as well then. Also at estimates last year I asked the Fiscal Group a question regarding comments made by Dr Henry regarding the need to ensure that all government spending is cost effective. I will quote him. He said:

Government spending that does not pass an appropriately defined cost-benefit test necessarily detracts from Australia's wellbeing.

He went on a bit to justify that. I asked the Fiscal Group whether Treasury properly conducted cost benefit analyses on the NBN. The response was, 'This is a question for our markets group colleagues.' So I am putting that to you now.

Mr Murphy—Mr Murray will deal with the NBN.

Mr Murray—The issues around cost benefit analysis were raised with us at the Senate inquiry into the NBN.

Senator BUSHBY—I am particularly asking in the context of Dr Henry's comments, which he made on 3 September last year before the Australian Research Alliance for Children and Youth.

Mr Murray—These were comments around the need for cost benefit analysis?

Senator BUSHBY—Basically he said that there is need to ensure that any activity is cost effective and that:

Government spending that does not pass an appropriately defined cost-benefit test necessarily detracts from Australia's wellbeing.

Mr Murray—Yes. Certainly we would see that as a first, best principal, and I outlined that at the Senate inquiry. In relation to NBN, we certainly did not undertake a cost benefit analysis, and without a very significant resource input we would have been able to do that. As far as I am aware, the government did not ask us to do any of that sort of modelling. However, I can at least make some comments about what our attitude was in terms of the costs and benefits.

Senator BUSHBY—I am sure you have done that before in the—

Mr Murray—I have. I have outlined that in quite some detail to the Senate inquiry.

Senator BUSHBY—I will not ask you to repeat yourself here, given that that is already on the public record. I just wanted, in the context of Dr Henry's statement, to confirm in my own mind that Treasury was not asked to do a cost benefit analysis.

Mr Murray—We and our secretary have not moved from the position that he set out.

Senator BUSHBY—That is fine. I understand that we have someone here specifically to answer questions on Auscar SPV. Senator Abetz has asked me to ask a couple of questions on his behalf. They are seeking an update on where it is currently at. What is the current size of the funding and how much has been guaranteed under it?

Mr Brake—There is \$170 million at present.

Senator BUSHBY—How many participants are there in that?

Mr Brake—In terms of financiers or dealers, Senator? The car dealers themselves?

Senator BUSHBY—No, both, actually.

Mr Brake—Currently, there is just the one financier.

Senator BUSHBY—Just Ford Credit, still?

Mr Brake—Yes.

Senator BUSHBY—How many dealers are there?

Mr Brake—There are approximately 120.

Senator BUSHBY—What is the critical mass in terms of the size of the spend before taxpayers have to start subsidising it?

Mr Brake—I am not sure if we have a precise calculation of that figure.

Senator BUSHBY—Are you able to take that on notice and see whether you can give an indication?

Mr Brake—There may be a number of variables such as fluctuations in interest rates and so on.

Senator BUSHBY—If you can take it on notice and outline what those variables may be and answer it as best you can, that would be much appreciated.

Mr Brake—All right.

Senator BUSHBY—My final set of questions is on the securitisation market. What is the current state of play regarding APRA's proposed APS 210? I will ask APRA about that as well.

Mr Murphy—APRA? It says they are—

Senator BUSHBY—Presumably, they liaise with you on changes they make that affect the securitisation market?

Mr Murphy—Yes, we talk to APRA about their prudential standards and whatever. Do you want to comment, John, or will we just—

Senator BUSHBY—No, I will get an update from APRA when they are up with that.

Mr Lonsdale—That is the best route, I think, Senator.

Senator BUSHBY—Has Treasury done any work since October on the potential impacts of requiring all ADIs to invest in sovereign bonds and the potential for domestic liquidity to meet that requirement?

Mr Murphy—It is a significant policy issue—and I think it is largely to do not with the Australian market—that, because of problems in international markets, there are proposals being discussed for trying to ensure that there is higher-quality assets capital within financial institutions. That could have a significant impact on Australia, given the size and the depth of our bond market and the interplay between Australian financial institutions—the interlending between the banks. I think APRA are aware of that; we are aware of that and, internationally, these things are still being resolved. They have put out this paper, and I think that is a key—

Senator BUSHBY—Apparently, it has caused some ripples—

Mr Murphy—Oh yes.

Senator BUSHBY—in terms of some of the ADIs, considering how they actually approach the liquidity challenges and concern about what it might mean for them down the track.

Mr Murphy—Yes. But these things still have a fair way to go in terms of policy development, consultation and discussion not only in Australia but internationally.

Senator BUSHBY—Could you advise on the current status of the plan announced by the government on 11 October last year for further support for RMBS of up to \$8 billion?

Mr Murphy—Yes. That has been quite a successful program. Would you like us to talk to it or do you want us to table some data?

Senator BUSHBY—This is in respect of the additional \$8 billion announced in October last year?

Mr Murphy—Yes.

Senator BUSHBY—When we spoke in October, at last estimates, there were a number of questions that still needed to be consulted on, but obviously you have worked through those and it is all up and running?

Mr Murphy—Yes.

Senator BUSHBY—How much of the \$8 billion—

Mr Murphy—Has gone?

Senator BUSHBY—Yes.

Mr Murphy—Jacky Rowbotham will give you the numbers.

Ms Rowbotham—The investment under the extended program commenced in January, with AOFM supporting the first RMBS deal of the year, undertaken by AMP. The AOFM invested \$36 million in a \$1 billion deal. They have also allocated a further \$3.4 billion to a serial investment program. It will be extended over 2010.

Senator BUSHBY—As I understood this program in October—I have not seen anything about its current activities—it was not so much about buying them themselves but to act, in a way, as a buyer of last resort. Is that correct? That is how it was explained in October last year?

Ms Rowbotham—Essentially, yes.

Mr Murphy—Yes.

Senator BUSHBY—Have we actually expended this money or have we just guaranteed to buy these if there is not a buyer? Have we had to buy them because there were no other buyers?

Ms Rowbotham—There has been strong private sector interest but, in some instances, AOFM has offered some money with respect to this extended program. For example, with the AMP deal, which is the only one that has occurred this year, of the \$1 billion the AOFM provided only \$36 million. But the rest of it was private sector participation.

Senator BUSHBY—And, presumably, that \$36 million enabled the \$1 billion deal to go ahead—

Ms Rowbotham—Absolutely.

Senator BUSHBY—It provided the—

Ms Rowbotham—Support.

Senator BUSHBY—Thank you.

Senator PRATT—The committee is well up to speed with progress so far on consumer credit reform. We are about to move into our next phase. I understand that recently there have been consultations that have put forward some further changes and enhancements and that we are consulting on those changes. One of those is regulations to accommodate difference practices in the way interest may be calculated or charged by lenders in respect of the provision of credit for residential investments. Is this the way we currently regulate interest in relation to residential investments or is it new? And what is the significance of that particular change?

Mr Murphy—I think it would be best if—

Ms Rowbotham—I put that one on notice?

Mr Murphy—Yes. The Consumer Credit Code is being picked up from the states. Gradually, we are working our way through to try to improve consumer credit regulation and the second tranche, the second phase, is addressing that.

Senator PRATT—Another issue that came up—and you are also welcome to take this notice—was the consideration that pre-existing contracts should perhaps also be subject to responsible lending provisions. How is it proposed that that will work? Has it come up in response to a perceived flaw in the original reform and, if so, is there any reason why old contracts should necessarily be any different to new contracts in respect of that?

Mr Murphy—I am not sure.

Senator PRATT—Further, with respect to consumer issues, I note that in December we finally announced movement towards an Australian consumer law. The Productivity Commission has said that it is an important thing to pursue. Can I ask about progress on the Australian consumer law and what are its perceived benefits?

Mr Writer—Two bills implement the Australian consumer law. The first of those is currently before the Senate and is awaiting a slot for debate. That bill covers unfair contract terms and the new enforcement powers, penalties and remedies and was the subject of a Senate Economics Legislation Committee inquiry last year. There is a second bill in the process of preparation which will cover the remainder of the issues that were agreed by the ministerial council in early December. That is to be introduced early this year. That is really all I can say in terms of timing.

Senator PRATT—Before I conclude on this issue, what is the significance of this reform?

Mr Writer—I am not sure if that is a policy question. It will involve the implementation of a single national consumer law which covers generic consumer protections. It will fold in all of the existing state and territory laws and the current national law.

Senator PRATT—I would envisage that there would be significant savings to the national economy based on—

Mr Writer—The Productivity Commission estimated in its report, which was published in May 2008, that there would be benefits to the community of between \$1.5 billion and \$4.5 billion.

Senator PRATT—I think that answers that particular question. Finally, I want to ask about financial services in Australia. Clearly, Australians have played a very active role internationally throughout the global financial crisis in terms of campaigning for strong regulation and promoting the kinds of reforms that Australia believes underpin a responsible financial services sector. What is the implication for our domestic financial services sector in terms of not only growth and promotion of the services that we provide here but growth of our own financial services sector because of that perceived strength and credible underpinning?

Mr Murphy—Australia has always been well regarded in terms of the standard of the financial services industry and the standard of its regulation. Australia is seen to have best practice in terms of regulation and operation of a financial system. Yes, there are some wrinkles around the place but, overall, it is a pretty good system. Recently a review was

undertaken in terms of financial services. The government published the Johnson report, which looks at financial services. That review reported very favourably. It recommended some changes and that is now being worked on and examined by the government. In terms of international practice we are well regarded, but I suppose you have to be vigilant to ensure that you have a strong, vibrant financial system.

Senator PRATT—Thank you.

Senator JOYCE—Now that the guarantee has concluded, what is the residual effect of where we are? I was listening to the chair of Bendigo Bank on the weekend talking about the \$140 billion. Do you want to throw some light on that statement? What is the exposure that the government currently has by reason of a guarantee?

Mr Murphy—The guarantee runs on to 2015 at the maximum because of the issuance—\$166 billion has been raised.

Senator JOYCE—So we still have a contingent exposure for \$166 billion? Is that correct?

Mr Lonsdale—Yes.

Senator JOYCE—Thank you.

Mr Murphy—The large majority of that is AA rated banks, that is the two-edged sword. You can criticise them but they are going to be able to pay their debts. The other side is that probably around \$5 billion in fees to the government will come through for the use of the guarantee. It is not costless—the banks have to pay. They are the major facts and figures about the guarantee.

Senator JOYCE—How does the peel-off of the \$166 billion work? Is it just going to guillotine at 2015?

Mr Murphy—No, over time.

Senator JOYCE—It will run down?

Mr Murphy—Yes.

Mr Lonsdale—It is a mixture of different instruments, short- and long-term.

Senator JOYCE—What was the general term of the instrument that was issued under the guarantee?

Mr Lonsdale—I think we have figures on the amount of short and long. Of the \$166 billion, the amount of long-term debt is \$133 billion and about \$19 billion is short term and \$13 billion is in large deposits.

Senator JOYCE—What did we earn out of the guarantee whilst we had it there? You say you still have another \$5 billion to wash through, to pick up. What has been the revenue stream from the issue?

Mr Murphy—Up to now, about \$1.5 billion.

Senator JOYCE—So \$1.5 billion plus the \$5 billion to come.

Mr Murphy—No, in total it will be \$5 billion but \$1.5 billion has come through so far and that is an estimate.

Senator JOYCE—Can we get a break-up of who the predominant bank is in the \$166 billion?

Mr Murphy—We have the figures. CBA and Westpac raised the most.

Mr Lonsdale—So currently the big four banks would hold 76 per cent. The others would hold the residual, a much smaller amount.

Senator JOYCE—On the deposit side, I notice people still have coverage for deposits under \$1 million. Is that right?

Mr Lonsdale—Under the financial claims. That is a separate guarantee and that will remain.

Senator JOYCE—How much is in that at the moment?

Mr Lonsdale—Do you mean total deposits?

Ms Rowbotham—The total coverage of deposits under the Financial Claims Scheme was estimated on 30 June at \$660 billion.

Senator JOYCE—So that contingent liability stays in place? There is \$660 billion for deposits under \$1 million which the government is still underwriting?

Mr Lonsdale—Correct, there is that guarantee.

Senator JOYCE—Who is the predominant holder of that \$660 billion for deposits that the government has underwritten? Through which institutions are these being put?

Mr Murphy—It would be the major banks.

Senator JOYCE—So 76 per cent through the major four again?

Mr Lonsdale—I do not have that information, Senator. If you like, we can see if that exists.

Mr Murphy—Every mum and dad in Australia holds that money.

Senator JOYCE—Yes, I know. Obviously the facilitating body does not take the deposits. They are not held by you.

Mr Murphy—They are held by the institutions.

Senator JOYCE—Every part?

Mr Murphy—I do not know. We will try to get that information for you.

Mr Lonsdale—Mr Murphy is right. The bulk of deposits lie with the major banks.

Senator JOYCE—To the same proportion—about 76 per cent?

Mr Lonsdale—Seventy-six per cent is quite a precise number.

Senator JOYCE—Well, 75 per cent.

Mr Lonsdale—I think it would be better if we had a look and were sure before we gave you a number.

Senator JOYCE—With regard to the market aspect of it, were concerns conveyed to you by the regional banks about the effect of the guarantee?

Mr Lonsdale—When? Do you mean during the life of the guarantee?

Senator JOYCE—Yes, during the life of it.

Mr Lonsdale—My understanding is that the banks have raised issues about the pricing. But against that, as Mr Murphy outlined before, the fact that the guarantee was brought into play supported all the ADIs that were able to access that.

Mr Murphy—The deposit guarantee underpinned all the ADIs at a time when there was quite a lot of concern in the community about the safety of bank deposits. That is why it was a very important measure.

Senator JOYCE—This guarantee is basically being peeled back around the globe, though, isn't it?

Mr Murphy—The wholesale guarantee?

Senator JOYCE—Yes.

Mr Murphy—Yes.

Senator JOYCE—Are we in train with where the rest of the world is regarding cessation in 2015, or are they stopping at a different time?

Mr Murphy—It is consistent with overseas practices.

Senator JOYCE—With who? Is it consistent with America and Europe? Is their desire to bring the thing to a conclusion in 2015? Obviously, what I am looking for is whether there is going to be a period that creates arbitrage, differential or capacity for the movement of funds.

Mr Murphy—No, I do not think so. That is what the government decided when it made a decision to withdraw. It was looking at overseas developments. We have the list of countries and the dates when they will withdraw their guarantees.

Senator JOYCE—When is America withdrawing its guarantee?

Ms Rowbotham—The US closed their scheme on 31 October 2009.

Senator JOYCE—It has already gone?

Ms Rowbotham—Yes.

Senator JOYCE—What about the UK?

Ms Rowbotham—The UK will close their scheme on 28 February 2010.

Senator JOYCE—That is getting close. What schemes are open to 2015?

Ms Rowbotham—The majority of schemes, pretty much all of them, will have closed by 30 June 2010. Our scheme will close on 31 March. The figure that you are referring to, the 2015 date, is the term of the securities. Our scheme is open to five-year securities. You can issue five-year debt.

Senator JOYCE—Could you get five-year securities for the US scheme? What was their term?

Ms Rowbotham—All the international schemes have different arrangements, but the majority have shorter terms, in the vicinity of about three years.

Senator JOYCE—With the current uncertainty that is certainly surrounding sovereign debt issues in Europe and issues of debt in the United States, is there a capacity to get the guarantee up and running again if you need to?

Mr Murphy—If the government decided it was necessary. It would be necessary not so much for Australian markets; it would be looking at international markets. We do not expect that that will happen, but who knows?

Senator JOYCE—You went overseas for a coordinated forum to discuss this. Is that correct?

Mr Murphy—No. Sorry for the confusion. I was referring to a discussion that is going to occur next week on competition and concentration in banking markets. The decision on the guarantee was made through the government consulting very closely with the Governor of the Reserve Bank; the Chairman of APRA, John Laker; and the Secretary, Dr Henry. I think it is fair to say that the governor was very much tapped in to overseas markets and what was happening through his overseas colleagues.

Senator JOYCE—I just want to quickly go to FIRB. Can you discuss FIRB?

Mr Murphy—Yes.

Senator JOYCE—What is the value of deals that are currently before FIRB?

Mr Colmer—I do not have a figure for current deals before FIRB. I would say, as a general observation, that we are picking up again after the Christmas break, but I do not actually have a number. There would probably be something in the order of 20 or 30 active cases. I can get that number for you, though.

Senator JOYCE—In those cases, what is the source predominantly? Where are they coming from?

Mr Colmer—I would have to check, if you want the current cases.

Mr Murphy—I think we can give you some figures. I think there is some concern about the spread of foreign investment cases, where the companies are largely coming from.

Senator Sherry—I have five-year, year-on-year data, up to the end of calendar year 2008.

Senator JOYCE—2008? Can we get something that is current right now?

Mr Colmer—What exactly is your interest, Senator?

Senator JOYCE—My interest is in how many of these deals are coming from China, how many of them are coming from the United States, how many of them are coming from Japan and how many of them are coming from Europe.

Senator Sherry—Number of deals or value of deals?

Senator JOYCE—Value is more my interest.

Mr Colmer—We are just about to finalise the annual report for 2008-09. That will show that China, in value terms, was the No. 2 source of investment in that financial year. In the previous year it was No. 6.

Senator JOYCE—What would they be now—No. 1?

Mr Colmer—It is hard to say. I suspect they will be in the top five for the current financial year. It is important to realise that in 2008-09 the value of Chinese investment was \$28 billion but something in the order of \$19 billion of that was for the first stage of the Chinalco-Rio deal. So, while there is undoubtedly ongoing interest from China in Australia, it will bounce around, I think, in the top five and it will change year by year.

Senator JOYCE—How much of that is due to state owned entities?

Mr Colmer—Most of it. I have not looked at that recently—not since September—but at September there had been roughly 90 projects, of which 12 were non-government. We are currently up to a figure of about 140 Chinese proposals under the current government. I suspect that that proportion is roughly the same, so there are probably something in the order of 15 to 20 that are private rather than government.

Senator JOYCE—In your discussions, how do you ascertain issues such as vertical integration? I know we have had this discussion before, so maybe I should rephrase the question. I have noticed that lately there have been changes to the Foreign Investment Review Board's guidelines, because I remember going through an oversight of them. How do they affect your assessment process?

Mr Colmer—The question really is not so much about vertical integration; it is about pricing and marketing arrangements.

Senator JOYCE—Transfer pricing?

Mr Colmer—Well, transfer pricing is a particular form of pricing. We look much more generally at the way commodities will be marketed. We look for arms-length arrangements and we look for market based pricing. If you are talking about the resources industry, the transfer-pricing arrangement is managed by the tax office, from the income-tax perspective, and by state revenue offices for the royalty arrangements.

Senator JOYCE—For a little bit longer.

Mr Colmer—There is a variety of mechanisms, I think. But I think the general arrangement is that, if there is evidence that a non-market price is not being paid for the commodities then the effective price for the calculation of tax liabilities can be adjusted.

Senator JOYCE—With these new changes to the laws, what is the significant difference between what you had and what you have now?

Mr Colmer—Are you referring to the recent bill that went through the Senate?

Senator JOYCE—Yes.

Mr Colmer—That does not have any impact on transfer pricing as such. That change related to the fact that the original legislation dated back to 1975 and based the calculation of a 'substantial interest' on issued shares. That was 1975 terminology. Essentially, the bill that went through the Senate broadened that to take into account a variety of preferences, options, convertible notes and so forth, so that when we are calculating the proportion of the stake that an investor is taking in a company, we can look through just the issued shares and into the longer term convertible options as well.

Senator JOYCE—Can debt give you influence?

Mr Colmer—Debt can give you influence, but the bill did not go to debt as such. Certainly, we look at control. The legislation is really based around two main concepts. One is ownership and what proportion of a company might be owned, and the other one is potential for control. Debt in itself does not normally give control, in the terms of the legislation. But there may be occasions when debt is accompanied by other, more overt, arrangements, which can go to the issue of control.

Senator JOYCE—Covenants within the debt instrument?

Is one **Mr Colmer**—Covenants certainly tend to put restrictions on what companies can and cannot do. Covenants would not be caught under the legislation though.

Senator JOYCE—What if the person is issued debt and the foreign entity takes some form of security to underpin its debt? Is that something that comes under the auspices of FIRB?

Mr Colmer—It can do. There is a general exemption for security if the person providing it is doing it as part of a business in providing finance. So it is a question really about whether or not the person providing the debt is some sort of financial institution or some sort of investor. We certainly look at that and try and get as good an understanding as we can, and sometimes that is not a simple matter.

Senator JOYCE—I want to talk about the water market. I do not know whether you can help me here. Do you have any oversight or any involvement with that?

Mr Murphy—Not really.

Senator JOYCE—We will steer away from it then. With the NBN, have you been involved in any way, shape or form with any public documentation regarding competition issues or market effects of the NBN?

Mr Murphy—I think Brad might be able to comment.

Mr Archer—I am not sure we can provide—

Senator JOYCE—I do not want to know about policy discussions or advice from the minister. Is there anything on the public record?

Mr Archer—The minister for broadband did release a discussion paper at the time of the announcement of the NBN policy, which I think was in April, which canvassed proposed regulatory reforms that have subsequently led to the bill that I believe is in the parliament currently. Some of those issues around regulatory reforms certainly go to competition issues in the telecommunications market. That document—its province—lies with the Department of Broadband, Communications and the Digital Economy.

Senator JOYCE—With your knowledge of the market, what views are held by you about the capacity of the development of competition within the current telecommunications structure?

Mr Archer—I think the current structure reflects reforms that have been progressively implemented from a decade or more ago. We share the concerns that the Australian Competition and Consumer Commission has made known—that, while the regulatory arrangements have promoted growth in terms of the market and we have seen more telecommunications companies emerge to provide services over time, the regulatory

arrangements embodied in the Trade Practices Act under part 11C have led to a lot of disputation, a lot of timely and costly administrative and legal action and have, arguably, hindered the development of competition in the market as a consequence. That is one of the government's stated rationales for the content of the bill—and was an issue canvassed in that discussion paper. We are certainly of the view that there is scope to improve the regulatory arrangements that are in place.

Senator JOYCE—With your knowledge of the telecommunications industry, do you have a sincere belief that another provider would develop the infrastructure, especially in regional areas, that is comparable to what is there at the moment through the major carrier?

Mr Archer—I am not sure under what circumstances—

Senator JOYCE—By reason that basically Telstra was Telecom—it was the PMG—do you think that in a changed environment, other telecommunication providers would go out into regional areas and set up exchanges with all the capital that is there at the moment, or do you believe that that sort of infrastructure that was invested in was only invested because it was paid for by the taxpayer and no commercial entity is going to bother going out there and duplicating what is there nor is there return out there to warrant them going out there?

Mr Murray—I think that you can approach this in a fundamental way about how you might drive competition in a market that is a whole continent—the land mass is a whole continent—but the population is very low and very concentrated. It is concentrated in six or seven major cities. If you look at the United States, you see that they have a land mass which is a bit bigger than ours and 300 million people—and geographically they spread over a lot of that area. How did competition develop there, particularly for broadband and the rollout of fibre and, in some areas, excellent service and a certain degree of competition—even into some of the regional areas?

It was the intervention of cable TV companies that decided they could provide a certain level of broadband, so clear competition with the telecommunications companies was developed. You would have, for instance, comcasting and significant competition with Verizon, which then prompted Verizon to have to meet that challenge and for it to compete with coaxial and fibre cable with their own fibre network. That has rolled out to certain parts of the market and, because of the size of the market, you can have that sort of what we economists would call 'facilities competition' and you would have a certain cross-subsidisation within those competitors into the regional and rural areas.

In Australia it is far more difficult. Here you would probably think more of a model where you might want to roll out some of the network as a natural monopoly but keep it at a wholesale level. That is certainly the model where the government has moved to for an open access model at the wholesale level for NBN Co. Does that mean it would reach every nook and cranny of the country? The intention is that it will, but we will have to wait for the implementation study to see how that would be done, what the level of cost would be, and therefore price, in all of the different segments of the market and whether there may be some need for some cross-subsidisation of that or some universal service obligation. Telstra has been subject to universal service obligations in voice, and the government would need to

make some policy judgments about what that means for broadband and for a high-speed fibre network across the whole nation.

Senator JOYCE—What I am drilling down to is that what you are saying there, Mr Murray, is that in regional areas you are going to have to have a different type of marketing arrangement and legislative framework than what you are going to have to have in urban areas to keep the services going out.

Mr Murray—No, you would not necessarily have to have a different regulatory regime, but you certainly may deliver it in a different way and on different platforms, so you may certainly deliver by wireless and by satellite into various regions. If you think about what coverage there is at the moment from the 3G wireless networks, you have got Telstra, which covers about 97 per cent of the country with its network by population, and you have got the other two, Hutchison and Optus, covering about 95 to 96 per cent of the country in the existing mobile industry.

Senator JOYCE—In a changing market condition are you going to get other telecommunications companies actually putting in backhaul optic fibre, going out into regional areas, or basically is it the fact that the infrastructure that is there at the moment, which was paid for fully by the taxpayer, is the only infrastructure that is ever going to be there, away from wireless?

Mr Murray—From our point of view, I do not know. The copper network—some of it, anyhow—as you say, went in under the PMG regime, so there were different parameters, and was it a government business enterprise as we would think of a government business enterprise today? Of course it was not; it was very much driven by the engineers, rather than the accountants or the economists. So it is difficult to tell. However, the development of satellite and the development of wireless are bringing a certain level of revolution to how you might service these particular markets. Without going into too much detail, because I am not an expert in this, you can have a satellite that services the rural areas of Australia, for instance, and it can service parts of Asia as well. So, with the new and latest satellites that are under development, you can actually spread your costs quite a lot. You do not have to have the satellite necessarily. You might lease access to a transponder or whatever just to cover the Australian market, where the rest of the satellite might cover a different market. Asia is a huge market.

Senator JOYCE—Just going to the markets division—has there been any further discussions about interest rates and banks' mechanisms for interest rates and margins? Have there been any people involved in that?

Mr Murray—Just in general terms?

Senator JOYCE—Yes, just like there has been a study of the NBN; has anybody done any study into the centralisation of the marketplace and banking and the effects on interest rates? Has that come across the markets division in any way, shape or form, seeing it is a market?

Mr Lonsdale—I am not sure we have done any direct work on that. Certainly, the issues of interest rates—margins around those—bank funding costs and how they translate are very important to the work that we do. We are closely monitoring those; we talk to the banks all the time. But in terms of that precise piece of work, I have to check.

Senator JOYCE—Costs of funds are fundamental in every section of the market, and you would be aware of the banks now moving interest rates in excess of RBA movement—

Mr Murphy—Yes.

Senator JOYCE—It is an issue of public discussion. Do you think that is a reflection of an effective market, or do you think that starts to become a reflection of super normal profits?

Mr Murphy—That is a matter of judgment. You have to try to analyse the current margin between the RBA's rate and, say, the mortgage rate that the banks charge. There has been analysis done in the RBA, which they have spoken about. The deputy governor gave a speech late last year in which he looked at the interest rates, mortgage rates and rates for lending to small business. To some extent it seems that the rates to small business are the ones who may be carrying a burden at the present time, given there has been an extra risk premium added into the rates that have been lending to small business.

Senator JOYCE—Do you feel there could be a concern that, with a greater centralisation of the marketplace, the role of the Reserve Bank will start to be overshadowed and have less of an effect?

Mr Murphy—No. The cash rate that the RBA sets provides the base. That is not the true indicator of—

Senator JOYCE—The cost of funds?

Mr Murphy—No. There are various rates which the banks have for mortgages, for lending to small business and for other commercial lending, and what the government wants, of course, are the lowest rates possible across the board which reflect a profitable business for the banking institution—to make sure that it remains a profitable business—but at the lowest cost to the consumer.

Senator JOYCE—Is the correlation between the Reserve Bank's base rate and the rates in the Australian marketplace as tight as it has been, or is it starting to become more dispersed? Is it becoming less of a relationship between the Reserve Bank base rate and the rates in the marketplace than it was in the past?

Mr Murphy—That is hard to say. We would have to look back and give you some analysis on that. As a matter of perception, when everyone focuses on the monetary policy committee's decision every second Tuesday of the month that seems to cascade through to movement or pressure on rates set by the majors. Whether that has just become a matter of course or whether there is a deliberate nexus is another issue. We would have to look at it, I think—we would have to examine that.

Senator JOYCE—As the market and the finance market become more and more reliant on access to international finance and international events and circumstances do the banks have a right to say, 'Well, the role of the RBA is kind of superfluous because it does not reflect our cost of funds.'

Mr Murphy—No, it provides the foundation stone for business for the cost of funds in Australia. That is what the cash rate does. And then you build off that really. No, I think it is still the basic barometer for cost of funds in Australia and then you take it from there. It is still a monetary policy to them.

Senator JOYCE—To the same extent it was in the past?

Mr Murphy—You would have to examine that.

Senator CAMERON—Mr Murphy, I just want to ask a brief question in relation to Treasury analysis of government policy. I want to take you back to July 2007. Back in July 2007 Senator Joyce had not had his wings clipped and he was a free spirit and he was at war with the then Prime Minister over the Murray-Darling water scheme. It was reported that that scheme was developed on the back of an envelope by the then Prime Minister. It did not go to cabinet and did not go to Treasury. I do not want you to comment on any of the other issues, except: did the Murray-Darling \$10 billion scheme go to Treasury? Or is it a bit of hypocrisy from the other side of politics here on these issues at the moment?

Senator JOYCE—Madam Chair, this is a reflection on you.

Senator Sherry—I do think—

Senator BUSHBY—Asking Treasury officials about decisions made by the last government is not actually—

Senator Sherry—That is a particularly argumentative and loaded question, which reminds me of quite a number of others we have been asked at these estimates. I do not think it would be appropriate for Mr Murphy to respond.

Senator CAMERON—Okay, I am happy to let matters move on.

Senator JOYCE—I was waiting for a dissertation on John Stanley Bruce and what he might have done.

Senator CAMERON—Bring back the old Barnaby, that is what I say!

Senator SHERRY—If we run out of questions, I am sure the officials and I would appreciate dinner 15 minutes earlier.

CHAIR—Wouldn't we all, but Senator Eggleston has questions.

Senator EGGLESTON—Earlier this afternoon we talked about the superannuation clearing house proposal. It was said that it belonged in the Revenue Group. Since then a little bit of research has been done and on Thursday, 22 October 2009, when Senator Bushby raised some questions about superannuation, it was said by Senator Sherry:

It is an operational systems matter, so it would be the Markets Group.

Later—

Senator Sherry—Sorry, what date was that?

Senator EGGLESTON—Thursday, 22 October 2009. We have also looked in the annual report and on page 88 it says that the 'governance, efficiency, structure and operation of superannuation system is the Markets Group'. This is structure and function; it is nothing to do with money.

Mr Murphy—Just by way of explanation—there is no trying to avoid the question—responsibility for superannuation falls between two groups: Revenue Group and Markets Group. In terms of policy advice it is between Markets Group and Revenue Group. That

project, which was a key initiative of the minister at the table, was undertaken and ran from out of the Revenue Group.

Senator EGGLESTON—The rules are the rules, I would have thought. I would like to get these into the record and to have them answered.

Mr Murphy—We will make sure that we get answers to those questions.

Senator EGGLESTON—Do you wish me to go through the questions?

Mr Murphy—If you just want to table them, we are happy to get the answers. I do not think anyone—

Senator Sherry—I think we would struggle to get answers tonight.

Senator EGGLESTON—I will go through each question, and if you can answer something then do, otherwise I will put them all on notice.

Mr Murphy—Yes, sure.

Senator EGGLESTON—Thank you very much for your indulgence, I appreciate it. Question 1: is the government in receipt of alternative business proposals for the superannuation clearing house?

Mr Murphy—We do not have a—

Senator EGGLESTON—Question 2: given that the original superannuation clearing house discussion paper promised a tender to the private sector, was there a draft tender document prepared by Treasury in 2009?

Mr Murphy—I am not aware of that.

Senator EGGLESTON—Question 2, part (a) is: if so, why was the tender not released by the department so that Medicare could be formally compared to the alternative providers?

Mr Murphy—No, I am not aware of that. Sorry.

Senator EGGLESTON—Part (b) is: can the government confirm that confidential intellectual property provided by the private sector in response to its discussion paper has not been provided to Medicare in any way, and can Treasury produce either its own written report or an independent expert's report justifying why deciding to appoint Medicare was a superior solution over tendering to the private sector? Can you answer that now?

Mr Murphy—No.

Senator EGGLESTON—Question 3: effective and fully ASIC licensed commercial clearing house alternatives exist which could be implemented in less time and could be delivered under the allocated budget. Given that the alternatives exist in the private sector, why has the government opted to spend significant taxpayer dollars on attempting to reinvent a technology platform from scratch? Can you answer that one now?

Mr Murphy—No.

Senator EGGLESTON—Question 4: can the department provide a fully costed budget for the Medicare clearing house project, including all costs for both internal government resources and external consultants, planning costs, software development costs, all costs of

engagement with industry, a comprehensive operating budget for three years, all costs of handling payments in and out of the clearing house, the costs of supporting employers who use the clearing house and the cost of ensuring take-up of the clearing house by the small business sector? Can you answer that?

Mr Murphy—No.

Senator EGGLESTON—Question 5: can the government confirm that in issuing the contract to operate the clearing house to Medicare it is fully in compliance with the letter and spirit of the Trade Practices Act, and (a) in particular, does the nomination of the Medicare clearing house as the only approved clearing house in the proposed legislation create an unfair competitive advantage for Medicare over existing commercial clearing house operators and (b) does the government intend to compensate commercial clearing house operators if Medicare is found to have breached the Trade Practices Act?

Question 6: what are the success criteria for the clearing house project, and (a) how many employers does the government think will use the system in each of the three years of its operation and (b) how will this take-up of employers be achieved if there is no budget for promoting the service to small business?

Question 7: how will the solution meet the objective of reducing employer red tape if by the project's own admission—see the minutes of 15 January—the scope of the functionality for employers has been reduced even before the development has commenced, and (a) can the government guarantee that the solution will not damage existing market confidence because the proposed Medicare model descopes critical validation criteria that are widely available in the private sector, (b) can the government guarantee the scope of functionality will not be further reduced given there is only four months available for developing the service, and (c) has the cost of further development to finish the development of a fully effective clearing house solution been costed and will this require further expenditure beyond what has been budgeted?

Senator Sherry—I hate to interrupt, but is there much more? This is an extraordinarily well written set of questions.

Senator EGGLESTON—It is, isn't it? You have no idea how hard we worked on producing such fine and well-balanced questions.

Senator Sherry—I am very impressed. It is outstanding compared to some of the other questions we have been getting at these estimates.

Senator EGGLESTON—Absolutely, but—

Senator Sherry—But wouldn't it be better to just put them on notice?

Senator EGGLESTON—I can quickly read the last one: which public health projects have been impacted by the redeployment of Medicare resources to the clearing house project and (a) if none then how long have excess resources been available within Medicare and why has Medicare not sought to reduce its operating costs and return excess budgets to reduce the government's operating deficit; and (b) what improvements on public hospitals could be made with these resources rather than diverting critical resources away from core Medicare business into the superannuation industry?

There is, I am afraid, one more over the page, question 9. It has taken effective commercial clearing house operators many years and a combined estimate of \$50 million to \$80 million to develop effective clearing house solutions that are fully integrated with many hundreds of superannuation providers' back office systems. How can the government justify the overall cost to the industry, given that there are no defined success criteria for employer usage of the clearing house? If the government cannot achieve an equivalent solution to that which is commercially available with the extremely limited budget and very short time frame available, will the government consider utilising a commercial solution which meets the project objectives and does not require rebuilding of interfaces to superannuation providers? Thank you for your indulgence. I will also table this.

CHAIR—Thank you. We will all look forward to the answers to those questions coming in on notice.

Proceedings suspended from 6.06 pm to 7.16 pm

Australian Prudential Regulation Authority

CHAIR—I welcome the Australian Prudential Regulation Authority. Do you have an opening statement, Dr Laker?

Dr Laker—I will read an opening statement, thank you. When we last appeared before this committee in late October, I noted that the view was clearly firming that the worst of the global financial crisis was behind us. Since then the portents have been largely positive—the global economy has begun to rebound, commodity prices have risen significantly and conditions in global funding markets have continued to improve. These developments and a lift in consumer and business confidence will contribute to what the Reserve Bank of Australia has forecast as 'reasonably strong' overall growth in the Australian economy in 2010 and 2011. The improved global funding conditions are the backdrop, as well, to the government's announcement earlier this week of the withdrawal of the guarantee scheme for large deposits and wholesale funding on 31 March this year.

Nonetheless, uncertainties continue to cloud the global economic outlook. Recovery in most advanced economies—as the IMF has recently noted—is expected to be weak by historical standards, the unwinding of substantial public interventions is presenting serious challenges abroad and banking systems in a number of economies are still 'ground under repair'. The pressure on the sovereign debt of some European issuers lately is also a harsh reminder that the global economy and global financial markets remain vulnerable to aftershocks.

Since we last met, APRA's 2009 annual report has been tabled. Sometimes the narratives in such reports can become quickly dated, but in our case the themes remain highly relevant. Most importantly, the annual report confirms APRA's view that Australia's unrivalled performance during the global financial crisis has been supported by, and has in turn reinforced, the fundamentally sound condition of APRA regulated institutions, notwithstanding two years in dangerous seas. At the same time, as I noted in my chairman's remarks:

Although it may now seem a case of 'steady as she goes', the operating environment for financial institutions supervised by APRA will remain testing for some time to come. ... Boards and management

will need to be particularly careful not to drop their guard on risk if relief at surviving the most challenging circumstances in many decades gives way, as it may, to excessive confidence that their institutions are now invulnerable.

In other words, this is not the time for 'hats in the air' by Australian financial institutions. Certainly, APRA is not ready to dial down the level of its supervisory intensity.

Since we last met, reforms to regulatory arrangements globally and in Australia have begun to take firmer shape. To remind the committee, the main aspects of the G20 global reform initiatives in which APRA is actively involved are remuneration incentives, the level and quality of capital held by banking institutions and the management of liquidity risk.

In late November, APRA released its prudential requirements on remuneration for authorised deposit-taking institutions, ADIs, and general and life insurance companies. As it always does, APRA consulted extensively before finalising its requirements, and there was broad recognition that poorly structured remuneration practices may result in excessive risk-taking by individuals and can undermine risk-management systems. APRA's principles based approach focuses on the structure of remuneration arrangements. It is not our role to intrude into the market and shareholder disciplines involved in determining absolute levels of remuneration. Our requirements come into effect on 1 April 2010, but APRA regulated institutions should already be taking steps to meet them.

In mid-December the Basel Committee on Banking Supervision, the global standard-setting body for banking institutions, released its long-awaited proposals to strengthen global bank capital requirements. The proposals aim to raise the quality, consistency and transparency of the capital base; promote the build-up of capital buffers in good times that can be drawn down in periods of stress; and strengthen capital requirements for certain counterparty credit risk exposures. The proposals also introduce a leverage ratio as a supplementary measure to the risk based Basel II framework.

At the same time the Basel Committee released a set of proposals to strengthen the management of liquidity risk. They include a global minimum liquidity standard aimed at ensuring that internationally active banks have sufficient high-quality liquid resources to survive acute stress, lasting for a month. APRA's proposals on liquidity risk management, released a few months earlier, largely anticipated the Basel Committee's approach, and our timetable in this area will now dovetail with that of the Basel Committee.

Finally, later in December APRA released a consultation package on strengthening the capital requirements of ADIs for market risks arising from complex trading activities, securitisations and exposures to off-balance-sheet vehicles. This consultation package responds to an earlier set of proposals by the Basel Committee—not those in December—and is not expected to have a significant impact on ADIs, which largely avoided higher risk activities.

The next stage in the reform process, over the first half of 2010, is a global quantitative impact study to assess the impact of the Basel Committee's reform proposals and to ensure that they are calibrated appropriately. This is important work. While the need for global reform is unquestioned, prudential regulators do not wish to introduce measures that impose an overall burden, greater than the sum of the parts, that would thwart global recovery efforts

or would have unintended consequences. APRA are participating actively in this study, and we will be feeding in relevant information from a number of ADIs to ensure that we understand fully the implications of the reform proposals for Australia.

The Basel Committee's reforms are intended to be finalised by the end of 2010 and to be phased in, when economic recovery globally is assured, by the end of 2012. We in APRA therefore have a considerable amount of policy work ahead of us this year. I can assure this committee that no decisions on implementing the final Basel reforms in Australia, or on our other reform initiatives in general and life insurance, will be taken without extensive consultation. We are now happy to take the committee's questions. Thank you, Madam Chair.

CHAIR—Thank you, Dr Laker. I will take the opportunity to ask a question myself. I think you rightly sound a note of caution. We are only just out of a very difficult period and we cannot take anything for granted. I think Australia is rightly proud of the supervision of our banking sector, which was one of the reasons that enabled us to come through this period relatively well—but, of course, with the signs of recovery, people are becoming quite impatient.

You did address in your opening statement the issue of liquidity and the management of liquidity. I am quite interested in what is happening with mortgage funds that have been frozen. I think a number of members of parliament are continuing to get representation from people who are unable to withdraw funds. They do see signs of a recovery. The news has come of the government lifting the government guarantee on wholesale funds. People are asking why they cannot withdraw their funds from one of these mortgage funds. Most recently, I have had a constituent come to me who is able to withdraw only five per cent of his funds. He is an 80-year-old man and is very keen to withdraw his funds. Obviously I do not want to deal with my constituent issue in detail, but I wonder if you can explore a bit more deeply for me these types of funds that I have been told by Treasury are managing their liquidity well. I am just wondering if there is any hope for, perhaps, a faster redemption for some of these people.

Dr Laker—I do not think we can give you a direct answer to that because we do not supervise mortgage funds. Our knowledge and exposure to them really come through our oversight of the superannuation funds which have money invested in those mortgage funds. I do not know whether we can say much from the perspective of supervision of superannuation, but we do not have any direct involvement with mortgage funds.

Mr Jones—From the point of view of the superannuation industry, so far we have seen no-one freezing funds and, in fact, we track on a regular basis those superannuation funds who apply to us for exemption from the portability rules. At the moment all those funds that were frozen in 2009 have requested extensions through to 2010. So at the moment we have not seen any change in superannuation. We have not seen any increase, but at the moment we are not seeing any decrease.

CHAIR—I suppose my understanding may have been at fault, but I thought superannuation funds were quite a major component of this sector.

Mr Jones—Yes, but a number of funds have been frozen and so pensions coming out of superannuation have not increased but have not decreased either.

Mr Chapman—The mortgage funds are an ASIC issue, so you might like to talk to ASIC about the underlying funds.

CHAIR—I will.

Mr Chapman—On top of that, we have seen that a number of super funds have offered them as investment options for their members. We went through an extensive process last year to allow those funds to suspend portability, which is really the technical issue from our perspective. The rationale is that they could not strike a decent unit price. If they had to strike a unit price based on an illiquid underlying investment, members would have got very little in the dollar. As Mr Jones has just said, we gave them a 12-month freeze only, in order to make sure the trustees kept track of what was actually happening. Coming back through, we will be giving them another 12 months. In the interim, however, a lot of them have managed to get some liquidity because some of the underlying trusts now have windows where people can withdraw funds. It is largely a question of whether people can get their 100c in the dollar as opposed to whether they can get something. Your constituents are clearly getting something but, until those underlying trusts and the mortgages actually run off and mature, those funds will have to stay frozen because there is no cashflow.

CHAIR—My questions are really to get a feel for how wide the problem is. Are you saying, then, that until they are matured the customers do not have any hope of being able to redeem—

Mr Chapman—They effectively became a closed fund. The way the mortgage trusts operated in normal times was that you and I would put \$100 in and when you wanted \$50 back that might be the time that Mr Jones put his \$100 in. So they did not actually have to redeem the underlying mortgages.

CHAIR—No.

Mr Chapman—That worked well until the deposits froze up. We are not closely involved with the underlying trusts, although we do talk to ASIC about what they are seeing. We are not aware of any widespread losses. It is not like the estates mortgage situation back in the 1980s. They are good mortgages. They are three- or five-year mortgages. People will get their money back over time or will get their money back when these funds manage to get liquidity again.

Mr Jones—In terms of the extent of the problem, we are talking about 23 trustees and around 50 funds.

Mr Chapman—Just to clarify that, 51 funds are affected but that does not mean that 51 funds are frozen, because there are various options within the funds. There will be options frozen within the 51 funds, but the majority of the rest will still be open. In the analysis that we did—and some of the trustees have done a lot more than others—while I do not know the exact numbers, if 100 members are affected, 95 of them have a spread in investments anyway, so they might not have put all of their money into that particular investment option. We have not seen and we are not aware of a lot of superannuation fund members who have all of their money in one of these options. Probably the issue that we have been chasing up the most with the trustees is the importance of making sure that pensioners continue to get their pension streams. If it is a choice between me as an accumulation member getting money and a

pensioner getting their pension then, subject to the no danger of default and loss of capital principle, our view is that we should be looking at the pensioners first.

CHAIR—It seems to me in looking at this issue that the liquidity depends on people continuing to invest. Yet there seems to be a tension here. The longer the funds stay frozen, the less chance there is of investors wanting to invest in that particular form of investment.

Mr Chapman—That is very true. When I talked about liquidity earlier, that is liquidity in normal terms. In normal terms, they are writing a mortgage today, a mortgage tomorrow and a mortgage the day after. But do not forget that liquidity is also being generated by mortgages being repaid. If you had a fund full of five-year mortgages, that would gradually become liquid over the five years rather than it having to wait until the last day before it became liquid. Some of them have reopened. Liquidity will be also generated by the process of mortgages being repaid.

Mr Venkatramani—The long-term reprieve will come when the market reverts to the normal state where in addition to ongoing contributions the underlying assets and their valuations revert to normal levels. The servicing of these mortgages on property depends on market sentiment. As the market recovers, these things will happen. But in the meantime what we have said directly to the super funds that invest in these mortgages is that in formulating investment choice menus trustees need to be careful to offer a diversified rather than a concentrated option. As Mr Chapman pointed out, if somebody had invested all of their super in mortgages then in the current situation they would find things very difficult. But if they only put in five per cent then only part of five per cent might be frozen. The message that we have been giving during the last 18 to 24 months has been that trustees, even in a choice environment, have an obligation to set their choice menus responsibly.

CHAIR—I suppose what really annoyed me about the position for this person was that he is getting an income of \$592 a month, with \$421 being paid out in expenses, some of which are from administration fees of \$81.44 a month and adviser review fees of \$58.49. The advisers and administrators are continuing to draw their income quite happily every month, whereas this constituent cannot. I appreciate that you are not responsible for that.

Mr Chapman—There is another element of this, too. If there is genuine hardship, ASIC have given the underlying managers relief from their normal obligations under the Corporations Law. So I am not sure what your constituent—

CHAIR—That was my next question. The APRA guidelines for constituent hardship are the same as those, as I understand, for those people seeking early release of their superannuation funds.

Mr Chapman—Our guidelines are the same.

CHAIR—Yes. Is there any scope for you to have a look at that? Those guidelines are very tight.

Mr Chapman—I do not think that having them the same is illegitimate. There is scope for us to have a look is the short answer to your question. If someone is under hardship we have two things here: one is the release from the super system, which are the APRA hardship rules, and the other is the release from the underlying investment, which are the ASIC Corporations

Law rules. I am not aware of any cases under the APRA guidelines where someone who has been assessed as being in a position of hardship, so they would be allowed to get their money from super, and someone not being assessed as eligible under the ASIC requirements for the underlying mortgage trust to release the money. We have not gone through a detailed analysis of that but I am not aware of that having come up as an issue at all across the board.

Mr Venkatramani—The underlying issue is somewhat different here. You have got the responsible entity managing your mortgage fund. If the cashflows within that fund are insufficient to pay the benefits, even if APRA is able or minded to provide relief, that trustee will have to find the cash to pay those benefits. What is happening here is that the cashflow is not sufficient to service the requirements.

CHAIR—I do understand that. I am not asking for an overall loosening of the guidelines, but here we have an 80-year-old man who is a part pensioner. I can understand the tightness of those guidelines for someone who is 40 or 45 to withdraw their super as a very serious matter. But we have an 80-year-old man on a part pension who, it seems to me, might have some priority over other members of that particular mortgage scheme who apparently cannot under the guidelines argue for that.

Mr Venkatramani—Again, as you said, in relation to the normal APRA relief provisions they operate separately. Here the problem arises because of liquidity. However, our assessment from our regulated institutions is that most of those institutions do apply a more considerate yardstick in relation to people such as the one you described and to old people and people on pensions.

CHAIR—That is your experience, is it, because that was not mine when I rang to inquire. That is very interesting, thank you.

Senator JOYCE—You are developing new capital requirements with the RBA and ASIC? Is that correct?

Dr Laker—Capital requirements for banks?

Senator JOYCE—Led by finalising new capital requirements for the banks and other deposit-taking financial groups.

Dr Laker—We are developing those but it is not an RBA/ASIC joint endeavour. To put it precisely the Basel Committee, which is a global committee, has put out proposals to strengthen what is called the Basel II framework, which is a set of global rules. We are on that committee and the Reserve Bank is represented on that committee. As and when these proposals in whatever form are finally introduced in Australia, they will be introduced by APRA through APRA's prudential standards.

Senator JOYCE—What is the time frame for their introduction?

Dr Laker—As I mentioned, there is a very large study of the numbers going on right now, not just in Australia but globally, of all the major internationally active banks. That work will be completed in the first half of this year. It will then be provided to the Basel committee and the Basel committee's intention is to reach a decision on capital requirements by the end of 2010; so it is this year. What follows in the normal course is that we would then look at how these particular proposals would be implemented specifically in our rules, so they have to be

translated from a global document to an APRA prudential standard. We do that by putting out our proposals to industry and consulting with them about how it would work in Australia, and that process could take some months into 2011. We are waiting to see how the Basel committee timetable is determined before we finalise ours.

Senator JOYCE—Is it envisaged that the capital requirements will be comparable across the globe for the members of Basel?

Dr Laker—Yes, very, very much so. They are already consistent across the globe, but not fully, and they have been since 1988. At the beginning of last year we introduced the updated or more comprehensive version, the Basel II framework, which is the global set of rules. But one of the clear lessons from the global financial crisis was that the amount of capital overall in the banking system was not adequate to cope with the losses and also that different jurisdictions applying the framework were defining capital differently. The Basel committee is very determined, as is the G20, to make sure that the word ‘capital’ means the same in whatever jurisdiction it is applied.

Senator JOYCE—What is your preferred definition of capital?

Dr Laker—APRA applies the Basel framework, which has tiers of capital in it. But the highest quality form of capital is common equity. What the Basel proposals seek to do—and they are proposals at this stage—is to give greater prominence to common equity as the core of the capital base.

Senator JOYCE—And what proportion of that do you foresee being the requirement?

Dr Laker—I could tell you the technical answer. In the paper put out by the Basel committee, the formula is X, Y and Z. In other words, they have not worked it out yet. We will fill in the X, Y and Z but we have got to do this impact study and to do it thoroughly, because, as I said in my opening remarks, the danger is overachieving in this area and tightening up the definition of capital and increasing the requirements but in a way that puts a substantial impost on the financial system. That is why this work, as I say, is very important, but it is in the early stages of being worked through.

Senator JOYCE—You are aware of the profit CBA made the other day. I heard discussions about their concerns about the influence of capital requirements. Are you getting much feedback from local banks about this?

Dr Laker—There is certainly substantial public comment about these proposals, but the way we work is we leave aside the public comment, we sit down with industry and we work through the proposals. At this stage, it is too early to get submissions in from industry on the capital requirements, but on the liquidity requirements, which are a separate set of proposals, we had already begun talking to industry and working with a working group of representatives of deposit-taking institutions some months ago. We are working our way through our proposals and now the Basel proposals. There will always be commentary when we put proposals out, but we work productively with industry and we have for a long period of time.

Senator JOYCE—Would the tightening of capital requirements have an effect in the short term on the capacity of dividend payments?

Dr Laker—I think we need to clarify what the tightening might actually involve. We might globally toughen up the definition but we in Australia already impose a pretty tough definition. So it is not obvious that tightening around the globe means tightening in Australia. That is something which we need to clarify when we have done the hard numbers. Australia starts the reform process with well-capitalised banks, so it is not as pressing an issue. It is an important issue but it is not one that requires immediate remediation in Australia. Our banks have chosen to increase their capital. They have had very good investor support and the listed companies have been able to raise capital very successfully. They have already, in a sense, positioned themselves for the new world. In the process, they have reviewed their dividend payout ratios. I have said publicly that that was a prudent thing to do and that dividend payout ratios in very good times are not necessarily the appropriate payout ratios when things get tougher. That is all part of the mix for a bank in choosing how to, if it has to, get more capital.

Senator JOYCE—What about liquidity requirements? Has there been any effect on them by your update of the Basel negotiations?

Dr Laker—There is again considerable commentary about how the liquidity proposals might work in Australia for one particular reason. The proposals globally want banks to hold more high-quality liquid assets to deal with stress, rather than run skinny on liquid assets and go straight to the central bank to get help when funding pressures emerge. The Basel Committee has now put out a definition of high-quality liquid assets and within that one of the core elements is high-quality sovereign debt.

Senator JOYCE—Tell me about quality sovereign debt. What's that?

Dr Laker—Can I just give you the rest of my answer so that you can follow with the question. In Australia, for virtuous reasons, we do not have a very large sovereign debt market. We do not have a large CGS market. We have said publicly on a number of occasions we can do the maths and we know we have a particular set of circumstances in Australia where, for the best of reasons, we do not have a large pool of their high-quality liquid assets that banks can hold. So we have to work cleverly on this one to come up with a framework in Australia that meets the high-level principles that Basel is seeking to achieve, which we support, and make it operational in Australia. I do not know how that will come out yet because we are still doing the work.

Senator JOYCE—So a high-quality liquid asset includes sovereign issued debt. What would be the best forms of it in Australia, just notes and bonds I suppose?

Dr Laker—What the Basel Committee is looking for is an asset that you can sell in a reliable market in hard times. The experience across the globe has been that high-quality sovereign debt, government paper, has traded through the crisis. Paper that is issued by other banks did not trade through the worst of the crisis. So what the Basel Committee is looking at is paper that is in a sense separate to the pressures on the banking system at the time. At this stage we have not ruled in or out on the definition but what we have said very clearly is that Commonwealth government debt is a prime high-quality asset and that would meet the definition. The issue of state government debt would be, likewise, a high-quality asset for which you could expect there would be a good market even when the going gets tough.

Senator JOYCE—What about other governments' sovereign debt? Would that be a prime asset?

Dr Laker—As I have said, we have not ruled a definition in yet. What you need to look at is what is the performance of these assets in good times and in hard times, and that is what is being analysed in the Basel framework at the moment.

Senator JOYCE—I imagine government debt from Greece would not at this point in time be a good asset to hold, nor might it be from Spain or Portugal.

Dr Laker—We are really talking here about Australian banks having access to Australian dollars to meet an emergency stress. So you need to be satisfied that, if you are holding the debt of another government in another currency, you will be able to swap that into Australian dollars quickly, so most of the focus is really on assets that are issued in Australian dollars at this point in our discussions.

Senator JOYCE—In the Basel agreement was there laid down any sort of determination of when a sovereign debt becomes prime and not prime or secondary or whatever term you give to something that is not a premier asset?

Dr Laker—The framework is not that specific at this point. It is a set of proposals which say that in principle sovereign debt would meet the criteria. Now it may lose its value, as the spread has widened, but the question is: is it liquid and can you sell it? Can you sell it in a reasonably reliable market without suffering a major drop in value in the process? In the course of these discussions, which are out for public discussion around the globe—they only went out on 17 December—feedback will be coming in from all sources about how this definition could work in a practical sense. Those are the sorts of questions that the Basel Committee needs to address. I cannot give you an answer yet.

Senator JOYCE—I imagine that you would also be doing it with the back-up of derivatives such as credit default swaps and things like that.

Dr Laker—Under the current definition we would not be thinking of including those as liquid assets. At the moment with the framework for Basel the definition of high-quality liquid assets includes those which are readily available to be converted into cash and they have opened the possibility of considering two other types of assets depending on how they have performed in bad times. One is corporate bonds and one is covered bonds. Only covered bonds are issued by banks. The other paper is paper not issued by banks. What the committee is trying to do is get away from having a system where you rely on your liquidity by holding claims on other banks. What went wrong in the middle of the worst months of September and October in 2008 was that banks were not prepared to hold each other's paper, so that the market in a sense almost froze. So we are trying to look through these periods of acute stress to assets which you can be highly confident you can get liquidity from when you need it.

Senator JOYCE—Do you have any discussions with the Bank for International Settlements? Are they part of the Basel negotiations?

Dr Laker—No. The Basel Committee meets at the Bank for International Settlements and the BIS, as we know it, provides support to it. But the Basel Committee itself is a separate

stand-alone committee. I think we have said in the past it is supported by but it is not a BIS committee as such. It is a broader committee.

Senator JOYCE—I remember bringing up a couple of years ago a statement by the then chair of the Bank for International Settlements talking about his concerns around the globe. It was fortuitous because obviously it was correct. I would be very interested to know what the Bank for International Settlements has to say about the current economic position especially with sovereign debt risk in Europe. Was any discussion held there?

Dr Laker—APRA is not a shareholder in the BIS. APRA does not go to the BIS meetings as such. That is an RBA involvement. But the general manager of the BIS, as he is known there—or you could call him a chief executive—did speak on—

Senator JOYCE—Who is that now?

Dr Laker—Jaime Caruana, a former governor of the Bank of Spain. He spoke at the Reserve Bank of Australia symposium on Tuesday and he has a paper looking at the global financial crisis which he has published. We could give you the reference to it. It is on the BIS website. He spoke only generally about the importance of reform. I not think that even then he touched on the issues. But these are not issues for APRA; this is about RBA involvement in the BIS.

Senator JOYCE—Going into more mundane things at home, you would be aware of the government moves for the consolidation of government super funds into one super fund including the Defence super funds. Concerns are currently held by obviously those predominantly in Defence wanting to remain unique. Is there any reason why Defence or anyone else should be outside the normal auspices that the legislation is dragging the other super funds into?

Mr Jones—Historically, certain government funds have been exempt from APRA supervision and it is pretty much an opt-in process and so over time different state and Commonwealth funds have moved in under the APRA processes.

Senator JOYCE—Do you have any involvement with the Commonwealth superannuation liabilities and their relationship to the Future Fund?

Senator Sherry—Just before Mr Jones gives the answer, I do have some familiarity with what is proposed with the Commonwealth public sector super fund. There are a number of elements to superannuation funds. One is the trustee governance arrangements. They are to be merged, so there will be one trustee board. The administration of the funds, the actual accounts and the payout of investments in pensions et cetera, are with ComSuper. ComSuper is the administrator. The decision there is that the defined contribution administration, which is very much the smaller part of ComSuper's operation, will be contracted out to the private sector. The administration of the defined benefit, which is the much larger and more complex component, will remain in ComSuper.

The decision to contract out the defined contribution followed a scoping study which showed that the costs of the defined contribution administration were in excess of comparative private sector providers; therefore, the decision was made to contract it out. Then of course the investments of the entities will be pooled and managed together. I am not sure

what the total pool value is. This does not include moneys in the Future Fund. There is a cost efficiency, savings, in doing that.

Senator JOYCE—What is the membership? It is about 650,000 or so, isn't it?

Senator Sherry—I do not know. There are active as well as retired public servants and military personnel. We can take it on notice. It certainly would be a substantial fund, if not the largest fund in the country. They are already very large anyway.

Senator JOYCE—In your oversight of the return on funds last year, how did they fare basically?

Mr Jones—All super funds last year?

Senator JOYCE—Yes. Is there a general assessment on returns across the board and the best super funds? What was the general result?

Mr Jones—We published yesterday, in fact. The audited annual results go through to 30 June 2009.

Senator JOYCE—What do they show? A 10 per cent loss or what?

Mr Jones—They certainly showed a loss for the 12 months. Total superannuation assets decreased by 5.8 per cent and the total loss was minus 0.6 per cent.

Senator JOYCE—Did you go into the average age and investment mix?

Mr Jones—For the first time we have done some limited work on looking at that relationship. We have not been able to do much of that in the past, but in our annual publication yesterday we did some of that and looked at the relationship between return and age profile based upon what we had. That work was based upon some of our earlier work that suggested that the returns for retail funds were sometimes lower because of a different age cohort. In the publication yesterday we were able to show that there was no significant difference in the age cohort between the different types of funds. That was part of the publication that came out yesterday.

Senator JOYCE—This question is going to a separate issue. In your supervision of banks, have you noticed any tightening of lending or any tightening of assessment of lending?

Dr Laker—Yes. It is not surprising in the context of the global financial crisis that banks and all deposit-taking institutions—we talk more about banks, building societies and credit unions—have revisited their credit assessments. More recently there has been a tightening by some institutions of their criteria for housing lending. There has been tightening of criteria for lending to business through the course of the crisis, yes.

Senator JOYCE—Are we looking at tightening across the board or in certain sections? Is it tightening for domestic borrowing, housing loans or small business? Is there any section where the tightening of lending criteria is more prevalent than others?

Dr Laker—I would have to take it on notice to give you a fuller answer. Individual banks approach it from the point of view of what portfolio base they have, what customers they have and what their spread of risks is across their whole lending portfolio. They have gone back and revisited different sectors to see whether or not their previous credit assessment was sufficiently robust and whether they had priced adequately for risks. That is how they build it

up from that base. I will take on notice whether or not there is a clearly established difference in the way the banks have approached the different sectors. Clearly, the higher risk sectors like property development have come under much closer scrutiny by lenders in the period of the crisis than, say, other areas. We would certainly encourage them to do so—to look very closely at the risks they are carrying in different sectors.

Senator JOYCE—How much of the banking securitisation is currently held in the housing market. How much of a bank's backing is now the residential house market?

Dr Laker—How much of bank lending is residential?

Senator JOYCE—I want to know how much of the security base they hold is represented by residential property.

Dr Laker—I cannot give you the specific figure off the top of my head but it would be in the order of 50 to 60 per cent. It has been for some time the largest portion of the balance sheet of our ADIs—more than half for some years now.

Senator JOYCE—In discussions with other people overseas is our exposure to the housing market typical of other countries?

Dr Laker—Our banking system in Australia is essentially a retail banking system, so it would be comparable. I do not know the exact comparison, but it would be comparable to banking systems in other countries which have specialised in consumer lending. It is quite different to, say, some of the US larger banking institutions which have not been significant investors in or lenders to real estate and do not hold that on their books. A lot of that was packaged up and bundled into securitisation vehicles in the United States in particular. Our banking system is fundamentally a retail banking system.

Senator JOYCE—I have asked this question before. You hear the commentary all the time that Australia's housing prices are very high when compared to other places in the world. We have seen the problems that a collapse in the housing market can cause in such places as the United States and the credit problems that were caused there. Do we have any form of contingency plan? Are there any concerns about the Australian exposure to a housing market that relied on two incomes to buy a \$750,000 McMansion in the western suburbs of a capital city near you?

Dr Laker—We have been looking at that question for a number of years because clearly when markets are strong and housing prices are rising quickly as they were in 2002 or 2003 we, as a prudential regulator, have to satisfy ourselves that our lenders are not taking on excessive risks. We have done stress tests. We tightened our capital requirements for housing lending several years ago. That is really bread-and-butter business for APRA. What comes through all the work that we have done is that residential housing lending has been a safe asset for our banking system.

Senator EGGLESTON—There is a lot of comment in the press about the need for tighter regulation of the banks which has come, I gather, from the Basel meetings and so on. Can you enlarge upon the case for tighter regulation and liquidity issues especially?

Dr Laker—Three words: the global financial crisis.

Senator EGGLESTON—Yes.

Dr Laker—I will give you a longer answer if you like. The impetus for strengthening regulatory arrangements around the globe has come from the leaders of the G20. The impetus really reflects the view that no financial system should be dependent upon substantial government and central bank support to the extent to which the global financial system ultimately relied on it in the course of 2008. Clearly the foundations were not strong enough. That level of public intervention was unprecedented. As a consequence, the global financial system needs stronger foundations. It needs stronger capital underpinning. It needs stronger liquidity buffers to cope with stress. It needs a better set of incentives for senior executives of banking institutions in taking risk. There are a range of other requirements as well which the G20 is pursuing and which do not cross our territory; they are really to restore the trust of the community in the operations of financial systems and the trust of financial participants in each other—both of which were very badly frayed in the course of the global financial crisis.

Senator EGGLESTON—There is an article by John Edwards in the *Financial Review* of 4 January. In conclusion, he says:

The global crisis reminded us that the success of free markets depends on refusing the finance sector quite the freedom it wants.

Would you agree with that? We have always, I suppose—or over the last year or so—had the view that regulation in Australia has been quite effective and the envy of much of the rest of the world. To what degree do we really need to tighten our regulatory requirements?

Dr Laker—To respond to the quote, banking systems throughout the globe have always had their freedoms restricted in one form or another because they, unlike any other system, rely fundamentally on the confidence of the users of the system and they have been, through history, prone to contagion when confidence in one institution wavers and that spills over to other institutions. So there has been a framework of direct controls through long periods of history and our prudential regulations are really designed to ensure that the risks that are carried by banking systems are prudent and appropriately managed. Nothing has changed; this is really about whether the rules in place over the last few years have been effective, and clearly in many areas they have been found wanting. That is the impetus for the G20 reform initiatives.

I have spoken publicly about Australia's involvement in the global reform initiative. It is quite understandable to hear the comments, 'We did well as the Australian banking system; we don't need reforms.' Where the reforms are directed at weaknesses in the behaviour of banking institutions and our banks did not incur those weaknesses and did not carry those risks, they will not be affected by the tightening. That is apparent from one of the reforms I described—the tightening of capital for certain high-risk trading activities. Our banks did not participate in those activities on any large scale, so they will not be affected by the tighter rules.

But our major institutions do participate fully in offshore funding markets. Those markets virtually froze and Australian banks were not given a free pass. When those markets virtually froze, the Australian banks, despite the fact they were well capitalised and, we believe, very well managed, could not access funds either. So this initiative is really designed to restore confidence in banks overall so that our banks can go to these wholesale markets and tap them

as any other bank does. For that, you need strong banks around the globe. That is why it is a global initiative.

Senator EGGLESTON—I have some other questions, which I will put on notice for APRA.

Senator CAMERON—You are the agency who gathers statistics on the finance sector, aren't you? You do statistical work.

Dr Laker—We call ourselves a national statistical agency for the finance sector, yes.

Senator CAMERON—Do you have any statistics on executive salaries in the finance sector?

Dr Laker—No.

Senator CAMERON—Why not?

Dr Laker—The issue of executive remuneration had not arisen as a prudential issue really until the global financial crisis. It had not been amongst the wide range of indicators we get about the prudential soundness of institutions, and it had not been one that was prominent in our considerations. So it had not been a statistic that we collected.

Senator CAMERON—Do you think it is a statistic that you should collect?

Dr Laker—My colleague Mr Trowbridge, who handles remuneration issues in APRA, may want to comment as well but I think there is a great danger in collecting just absolute statistics. What we have said throughout our involvement in establishing the prudential framework for remuneration is that we are not focused on the numbers. What is most important is the structure of a package for an executive. A package of a certain level that is made up of a single bet that a particular portfolio will grow in value is a very different package to one that requires the executive to take a substantial cutback if the entity is not performing well.

Senator CAMERON—How can you understand where the structure is effective if you do not know what the final outcome is?

Dr Laker—Now that our proposals are finalised and they have been issued what we have said to our institutions is that we want the boards to develop their remuneration policy, setting out what is the basis for the packages, what are the incentives, what are the risks, what is the deferment and what is the clawback. We want them to articulate the approach they take to the remuneration of people in positions of responsibility.

Senator CAMERON—But if you do not understand the drivers and you do not have information on the drivers—

Dr Laker—We will then be able to sit down with institutions and look at what is driving those remuneration arrangements.

Senator CAMERON—So if you do that then you must deal with the final salary otherwise the drivers are meaningless?

Mr Trowbridge—I do not think the numbers are particularly relevant. What is relevant is the structure. We would not expect to collect these numbers—

Senator CAMERON—So it is form not substance, is it?

Mr Trowbridge—No, not at all. The substance is about the relationship between the structure of the package and the risk in the institution. A lot of these institutions publish a lot of the information. We do not intend to collect separate information because they are obliged under other rules to publish—at least the listed companies are obliged to publish information. So our interest is in the prudential management of the institution not in the salaries or the specific incomes that these people might receive.

Senator CAMERON—But the salaries could drive a diminution of prudential oversight from boards.

Mr Trowbridge—They could do, but that does not mean that the numbers of themselves are important.

Senator CAMERON—So it is not important. So that is APRA's view: salaries in the finance sector are not important?

Mr Trowbridge—That is not what I said.

Dr Laker—No, he did not say that. What we are saying is that the structural—

Senator CAMERON—Let me ask you this: when do they become important?

Mr Trowbridge—Of course the salaries are important, but they are important in several ways—for example, in most financial institutions something like 70 per cent of their expenses are salaries of one form or another. So clearly they are relevant to the economics of the business. But whether a particular executive gets paid amount A or B and whether you or I might think that is a high number or a low number is not of itself fundamental. What is fundamental from our perspective is how the structure of that package relates to the risks, the risk-taking and the risk management in the institution.

Senator CAMERON—Sure, that is one aspect of the salaries. So the main driver for executive salaries in the finance sector, as I read the Productivity Commission report, is comparative ways justice; is that correct?

Mr Trowbridge—It is quite clear that, in every industry, comparative salaries have an effect on what individual companies pay.

Senator CAMERON—But more so in the finance sector?

Mr Trowbridge—I couldn't comment on that.

Senator CAMERON—Did you read the Productivity Commission report?

Mr Trowbridge—I have read parts of it, yes.

Senator CAMERON—I assume you were interested in the finance sector, where it demonstrates that the finance sector is different from every other sector in Australia in terms of executive salaries. That is correct, isn't it?

Mr Trowbridge—I have not checked that piece of the report.

Senator CAMERON—It is different because it benchmarks against the outlier, and the outlier is the US. So the outlier in executive salaries—the biggest executive salaries in the world—are in the US and every other company, according to the Productivity Commission in

Australia, is benchmarked European level except the finance sector, and the finance sector benchmark is US level. Why?

CHAIR—I think there was discussion in the Productivity Commission. I'm sorry, Senator Cameron, but our time is very short. I might just—

Senator CAMERON—I have only had about four or five minutes—

Senator JOYCE—You are the government. You might not have realised that. You are actually the government.

Senator CAMERON—We know we are the government and we know where you are.

Senator JOYCE—When you are the government, you do not ask—

CHAIR—We are already out of time. As Senator McGauran has one question, I will hand over to him.

Senator CAMERON—Okay, I'll have to put some questions on notice on this because it is very important and I really think if you are the statistical body then you need these statistics—

Senator JOYCE—Senator Cameron is going to bring the government down.

Senator CAMERON—I know what you're going to do.

Senator JOYCE—He's going to bring it down.

Senator CAMERON—What are you talking about—

CHAIR—Senator Joyce, your colleague is trying to ask a question before we finish.

Senator CAMERON—What a fool you are. No wonder Tony Abbott's got real problems with you.

CHAIR—Senator Cameron, you asked your question; let Senator McGauran ask his.

Senator McGAURAN—Just for the minister's sake, I am reading from the annual report and not a newspaper—

Senator CAMERON—Barnaby—

Senator McGAURAN—Give us a go. This—

Senator Sherry—Let Senator McGauran go; this could be an incisive question that really—

CHAIR—I don't want conversation across me and the table. I cannot hear what is going on. If senators want a conversation, please take it outside.

Senator JOYCE—It's that goose over there that's causing you all the problems.

Senator CAMERON—And you said nothing! Don't call me a goose.

CHAIR—Senator Cameron, can I ask you to go out.

Senator CAMERON—I can't help that Senator Joyce is incompetent in his portfolio.

CHAIR—The committee is suspended.

Proceedings suspended from 8.17 pm to 8.20 pm

CHAIR—We are going to have to move on to the next session. Thank you to APRA for appearing this evening.

[8.21 pm]

Australian Office of Financial Management

CHAIR—We welcome Mr Hyden and other officers of the Australian Office of Financial Management.

Senator JOYCE—Thank you very much, Mr Hyden, for the flow of information we are getting on Australian government securities outstanding. As of today, do you know what they are?

Mr Hyden—We are now putting this information on our website on a weekly basis. The figures are updated there. There are at \$122 billion as of yesterday.

Senator JOYCE—Is that 122.01?

Mr Hyden—I have 122.03.

Senator JOYCE—That is 122.03.

Mr Bath—Billion.

Senator JOYCE—You do not have to remind me, Mr Bath! I have got the message. But there are a few others who have been making the same mistake today—it is contagious! It has been going all around the room.

Senator Sherry—It is contagious, yes.

Senator JOYCE—Could you give me a range and the yields that you are currently paying?

Mr Hyden—Mr Bath might answer that.

Mr Bath—The yields are ranging from around four per cent for an August 2010 bond—we are not actually issuing into that line at the moment, so that is our shortest bond—up to just over 5½ per cent for the May 2021 bond.

Senator JOYCE—May 2021 bond?

Mr Bath—Yes. But we are only really issuing from the 12 April bond, which is about 4.4 or 4.5 per cent, up to about 4½ per cent. That is current as of a few days ago.

Senator JOYCE—Are the yields pushing up?

Mr Bath—They moved up today after the employment data was stronger than the market expected. Do you want me to explain the trend?

Senator JOYCE—Yes.

Mr Bath—Since about June or July, the yields have been relatively range-bound. You might recall that at my last testimony I noted that the yields bottomed out in about January or February 2009. So the 10-year bonds then were about four per cent and they rose from that low point in about January or February of last year through to June or July of last year, reaching a peak of about six per cent for the long bonds. The yield curve also steepened through that time. So, where back in, say, September 2008 yields were relatively consistent

across the board from the shortest maturities to the longest maturities, they rose to about six per cent for the longest bonds, peaking at about July, down to about three per cent for the shortest bonds. Since then, the yields on the shortest bonds have risen with cash rates—

Senator JOYCE—Long rates have come down.

Mr Bath—Long bond rates are lower today, but they have been relatively range-bound for just under 5½ per cent to six per cent. At the moment they are at around 5½ per cent.

Senator JOYCE—Are you aware, of what you have appropriated, what you are allowed to borrow to? Is it still the case that \$200 billion is the upper limit?

Mr Bath—That is correct.

Senator JOYCE—So you would also be aware that the peak debt position in gross that we have been given today is \$245 billion? What does that mean? Does that mean that we have to now go back and do an appropriation for another 50 or so to give you the capacity to meet your peak debt position as delivered today?

Mr Hyden—If the current projections work out, then it will be necessary for the cap to be raised at some point, and that will require legislation.

Senator JOYCE—I notice that in the last two months the current rate has gone up by \$7 billion. Are you planning on moving around about \$4 billion a month in bonds and notes?

Mr Bath—Thereabouts. I think it is slightly more. So we are issuing about \$1.2 billion a week. So it is probably closer to \$5 billion per month.

Senator JOYCE—\$1.2 billion a week?

Mr Bath—At the moment, but it ebbs and flows. So January is a quiet month, because bankers go to the beach and we tend to give them a holiday. But other months are busier. It is around about \$5 billion per calendar month.

Senator JOYCE—So you would be looking at—all things going along—somewhere in the range of \$60 billion to \$70 billion of extra issuance in the year?

Mr Bath—I think I have that here. Around about \$60 billion per year.

Senator JOYCE—So within a years time we would have about \$18 billion. It would be getting close to our limit within about a year?

Mr Bath—There is about \$19 billion or \$20 billion worth of maturities over the 2010-11 year. So you would have to take that into consideration.

Senator JOYCE—As well?

Mr Bath—You would have to take it off. So the issuance that I outlined is not just to cover the cash deficit; it is also to cover the maturities. So, if you are working your way backwards to work out the movement in the stock of debt, you would have to adjust for the fact that about \$19 billion or \$20 billion of the \$60 billion issuance is going to be covering—

Senator JOYCE—So you would be up to around about \$160 billion to \$170 billion of Australian government securities outstanding within a year?

Mr Bath—That sounds about right, but that is based on those calculations.

Mr Hyden—We would estimate that we would have a bit over \$150 billion in June 2010 and just on \$200 billion a year after that. But I should make the additional point that there are of course considerable fluctuations over the course of the year in the government's cash position, which requires us to issue short-term paper Treasury notes—T-notes—and they are counted as part of the cap. So you are not looking at a smooth monotonic figure over the course of a year; you get these fluctuations according to the cash flows.

Senator JOYCE—And have you got any requirements for those coming up in the immediate future? What I am thinking about is if you have got \$17 billion worth of stimulus package, or stimulus that are still going to be expended, are they just part and parcel to be absorbed in the \$1.2 billion a week or does that have to go on top of what we have got there at the moment?

Mr Hyden—The figure that Mr Bath referred to is basically bond issuance, so that is long-term debt. The treasury notes on top of that, but we are issuing those each week—

Senator JOYCE—That 1.2 is only long-term, it is not Treasury notes?

Mr Bath—That is correct.

Senator JOYCE—I put the treasury notes on top of that. How much are the treasury notes? I know they fluctuate.

Mr Hyden—They fluctuate. We are maintaining a minimum volume on issue of 10 billion to maintain an active market in them. At present we are issuing basically at that minimum level, so the maturities each week are being replaced, but at different points over the course of the year we will need to issue more than that.

Senator JOYCE—When that \$17 billion is required, because I imagine the requirement will come through for that, because that is a substantial requirement, do they notify you in some way, shape or form? How does the instruction come down the line to you to have the money ready for them?

Mr Hyden—We manage what is called the official public account, the account in which all the government's daily transactions take place. We have reporting links with the major expenditure departments and with the tax office on the revenue side as to what flows will be occurring on the days ahead. That is an active thing we are doing every day. So each day we are assessing what term deposits we will place with the Reserve Bank or short-term deposits with the short-term money market and what T-Notes we will need to issue each week. So this is a constant process and it tends to even out over time. What I am saying is that if you are trying to say when will we reach the \$200 billion cap, that depends not just on the longer term bonds on issue but also in terms of these short-term fluctuations.

Senator JOYCE—So we are saying that in longer term securities we are going to be about \$160 billion within about a year. But you have also got the T-Notes, which are revolving around the \$10 billion mark but at times you require more so you go to the market and issue more T-Notes. What is the most that amount goes up to? Does it go up to \$40 billion, \$50 billion at times? Is it \$20 billion? How many T-Notes before you do not bother issuing T-Notes but issue a longer term facility?

Mr Hyden—We have only resumed issuing them recently, because of the global financial crisis, so we do not have a long period to draw on here that is relevant. But I think they could be up to \$20 billion. I might say that those figures I gave you of \$152 billion and \$200 billion include T-Notes on issue at the end of the financial year.

Senator JOYCE—And the figures we get from you that you put on the website, they include T-Notes, don't they?

Mr Hyden—Yes.

Senator JOYCE—What is the comparative yield from what we are issuing compared to, say, the United States? What is it costing them?

Mr Bath—In the US the 10-year rate is probably just a bit over 3.5 per cent whereas ours is 5.5 per cent. It is about 200 basis points or two per cent in 10 years. It is going to be more in the shorter end because their cash rates are close to zero.

Senator JOYCE—So the two per cent premium at the longer end and probably about a three per cent premium in the shorter end for Australia.

Mr Bath—Probably a bit more than three per cent.

Senator JOYCE—Is that margin between us and the US growing?

Mr Bath—It tends to fluctuate. If you go back a long time, you might find a period where Australian yields traded below US yields, but it is a rare event.

Senator JOYCE—So it is about three per cent at the lower end and two per cent at the higher end. It was tighter before, so it seems to be getting wider.

Mr Johnson—As of the end of 2008 it was around 1.7 per cent, at the end of 2007 it was 2.2 and at the end of 2006 it was 1.2, approximately. So it is slightly wider at the moment.

Senator JOYCE—I know it is a vague science, but basically who from overseas is buying our debt?

Mr Hyden—There is a wide range of buyers. In large part we are seen as a very high credit quality issuer, issuing at the high-quality end of the AAA part of the spectrum, so we basically appeal to very conservative investors who are looking for quality ahead of yield. We have a very geographically dispersed investor base, quite strong amongst asset management firms, insurance and life insurance companies, central banks and sovereign wealth funds.

Senator JOYCE—About 60 per cent, so I hear—and correct me if I am wrong—is purchased by nonresidents. Of that 60 per cent of nonresidents, what venue is the greatest? We are told it is China. Is that right or is that wrong? Have I got the tiger by the tail and it is not China but actually the United States? We hear it is predominantly China, then Japan and then a range of areas surrounding the Middle East.

Mr Hyden—We do not have figures on the country distribution of the ownership of the bonds, but impressions are that it is well dispersed. There is strong ownership particularly in East Asia and Europe. East Asia includes Japan, China, Korea and—

Senator JOYCE—How much is East Asia compared to Europe?

Mr Hyden—I do not really have a figure.

Senator JOYCE—Are there any real sensitivities about this information getting out?

Mr Hyden—It varies between investors. Some investors would not be concerned about it; others are. For some funds managers, how they are placing their investments and when they do it is something that they would regard as commercially sensitive, because they do not want their competitors to find out about it. For others, such as central banks, they may have policy reasons related to monetary policy or exchange rate management where they would not want the public to know what transactions they were undertaking at any particular time.

Senator JOYCE—Finally, do you get delivered a prospective future debt requirement of where the Treasury expects the debt to go for you to plan by, or is it just a day by day issue? Is there any correspondence of, 'This is basically how we see we will be drawing down funds,' or do you just read about it in the morning and go out and do it?

Mr Hyden—The framework is basically set by the budget and revised in the Mid-Year Economic and Fiscal Outlook figures, which are published by the government. They are basis on which we plan the debt issuance for the year as a whole. We do that over the forward estimates period using the figures that the government publishes for the forward estimates. That is the framework, and then we have week by week cash management.

Senator JOYCE—Looking at the budget estimates, what do you presume the gross peak debt position will be?

Mr Hyden—We would rely on Treasury figures for the budget position in order to assess where that will get to. The only figures I have are those in the MYEFO.

Senator JOYCE—If they say \$245 billion today, do you presume that would be right?

Mr Hyden—Yes.

Senator JOYCE—Thank you very much.

Senator PRATT—I note over recent months that the Australian Office of Financial Management has facilitated significant levels of funds to the residential mortgage securities market. It seems that there have been some significant lump sums rolled out to various institutions over recent months. I want to ask about the strategy behind that, the extent to which those institutions are now able to seek funds from elsewhere and how that general scenario looks at the moment.

Mr Hyden—I will make some general comments. The government's program was designed to support competition in lending for housing after the securitisation market was severely affected by the global financial crisis, which of course was not really anything to do with the quality of securities in Australia but was the impact of overseas. We were initially given \$4 billion and then another \$4 billion to make it up to \$8 billion, and a further \$8 billion was provided in December.

Senator PRATT—What is the total now?

Mr Hyden—We have a total of \$16 billion to invest and we have invested a bit over the \$8 billion. The market has, I think, shown significant improvement over recent months, but it is by no means plain sailing and are, I think, at the moment still looking for our support in order to continue to function in an effective way in lending for housing.

For the extended program, with the additional \$8 billion, we have effectively divided the program into two. We have invited the issuers to put proposals to us for programs of serial investment—that is, where we undertake to consider investing in a series of issues over a period of time. We have completed the process of inviting proposals, considering them, selecting them and announcing the participants. They will come to us under that program as time goes by. That provides for up to \$3.4 billion to be available in that way.

We are also inviting arrangers and issues to put proposals to us on a reverse inquiry basis—that is, they come to us when they are ready and we consider their proposal more or less on the spot or in a very, very short time. Initially, we were doing it through a more ordered process where we invited proposals and then considered them together over a period of time. We think the market has improved sufficiently that we can be much more flexible in proceeding on a reverse basis.

Senator PRATT—It is certainly a very significant program and I might ask the minister to comment about the extent to which many Australians have not really appreciated that their access to finance to buy a home has been dependent on these kinds of initiatives—it is probably an unsung part of the response to the global financial crisis—and also the extent to which it is been an important support to the building and construction industry and housing market in Australia.

Senator Sherry—I will be brief because of the time. I think the discussion and questions that have occurred highlight an important part of the range of interventions as a consequence of the financial and then economic crisis. Some of these issues are reasonably complex. So, yes, I think it is understandable that the community broadly find it difficult sometimes to comprehend the degree of intervention, the level of intervention and the consequences of that intervention.

Mr Hyden—I might just add that the global financial crisis has tended to strengthen the position of the major four banks as the key lenders for housing in Australia. Some of that has come through amalgamation and takeovers which have been stimulated on occasion by the crisis. The action that this program is taking to support competition from the smaller lenders is important in the long term in maintaining a competitive market.

Senator PRATT—Yes. I am certainly very pleased to note that myself.

Senator BUSHBY—Most of the areas I wanted to cover have been covered, so I will be reasonably quick. Just on the yield, you provided in response to my question on notice No. SPT69 a graph. I am not sure but I think Mr Bath may have been looking at that when speaking earlier.

Mr Bath—I was looking at it.

Senator BUSHBY—I thought so. That was very useful. I greatly appreciated that graph. I was wondering whether you would mind taking it on notice to update it with the most recent figures. This goes back to 2007. Probably if we just did it over the last 12 months we could use it to work forward from there.

Mr Hyden—Yes, we can do that.

Senator BUSHBY—Thank you. I think everything else on the yield has probably been covered. On MBS I take it from the answers to questions that we have just heard that all of the initial \$8 billion has now been spent.

Mr Bath—We can do that.

Mr Hyden—Yes.

Senator BUSHBY—As of October last year the second \$8 billion facility only just recently announced by the Treasurer was in development. You indicated at that time that you were then still considering with Treasury moving forward with it because there were some concerns that the market might become welded on to the government and that could be counterproductive. Presumably those concerns were resolved prior to the facility being finalised and put into place.

Mr Hyden—Yes. I should just say that we did not quite use all the \$8 billion under the first arrangement. The amount that was left over from that was included with the additional \$8 billion.

Senator BUSHBY—As of October last year you said you had not quite spent the \$8 billion.

Mr Hyden—It is proceeding under those terms.

Senator BUSHBY—But in terms of the concerns you held about the market becoming welded on to this support, have those concerns been resolved or do you still hold some concerns for the longer term or even the medium term as to the degree to which the market might see this as a crutch and get very used to it and not want to let go?

Mr Hyden—I think the market has been exhibiting a willingness to look to other investors. Where the interest in a issue by other investors has been greater than the ranges we were initially expecting they have been happy for us to step back and take a smaller share. So I think that indicates that there is a healthy desire to see the market get back to normal and not a lingering wish for us to be there forever.

Senator BUSHBY—I am asking this question because it was in response to a question that I asked at the last estimates that you indicated you were still working through with the government in respect of that—or AOFM did.

Mr Hyden—I was not at the last estimates. Perhaps I will let Mr Bath answer.

Mr Bath—One of the aspects that was announced with the announcement of the second \$8 billion was the potential to look into what was called a liquidity facility. So a lot of feedback had been received, particularly early in the 2009 calendar year and late in 2008, that the real issue was the overhang in the secondary market and that the conduits in the special purpose vehicles that owned a lot of these assets were trying to liquidate them and could not find a bid. One of the aspects that the Treasury and the AOFM explored in consultation with stakeholders and the market was whether to extend the program in the direction of also having a liquidity facility attached to it.

Senator BUSHBY—So that did not happen?

Mr Bath—That did not happen.

Senator BUSHBY—Because that was a key plank of the announcement by the Treasurer at the time.

Mr Bath—I would not—

Senator BUSHBY—Not that he was saying that it was finalised, but that it was—

Mr Bath—I think what was announced was that Treasury and the AOFM would consult with the market and explore the feasibility of a liquidity facility.

Senator BUSHBY—So essentially this \$8 billion is running in the same terms or similar terms to the original \$8 billion?

Mr Bath—There are two key differences, as Mr Hyden said. We have created what we call a pipeline or serial investment arrangement where smaller lenders in particular, who have been particularly reliant on RMBS in the past, have been able to make proposals to us for a series of investments. So rather than just relying on an all-or-nothing one-shot-in-the-locker approach where they put in a proposal which is simply either accepted or rejected and they can really only plan three months out, what we have said is bowl up your proposal for funding over the next 12 months and we will potentially support a series of investments, so \$3.4 billion was allocated to that across five issuers. That was part of the program.

The other part, as Mr Hyden said, operates on a reverse inquiry basis. So again we are not getting maybe 20 or 30 proposals, which we then work through gradually. We can actually be more responsive to the market and act more like a typical investor and less like the big elephant in the room that is propping the market up. We are responding to improvements in the market, but we are also trying to act in a way that does not weld the market on to us.

Senator BUSHBY—And is the welding of the market the reason why the liquidity facility was not proceeded with?

Mr Bath—In part, but there was no real consensus among market participants as to what was meant by ‘liquidity facility’. Some of the market participants, particularly those who are sitting on old mortgage-backed securities, wanted it to mean essentially a free-put option so that they could sell their existing inventory on to the government.

Senator BUSHBY—A buyer of last resort type of thing?

Mr Bath—That was one view of what it would mean. Another view was could we facilitate the call options that are embedded in these things so could investors get comfortable that the underlying bonds were not going to be extended on them. There were other variations on the theme. There was no consistent, coherent desire from the market participants for a single type of liquidity facility, and essentially we reached the conclusion that it would not be workable.

CHAIR—I thank the AOFM for coming in this evening.

[8.55 pm]

Australian Bureau of Statistics

CHAIR—I welcome officers from the Australian Bureau of Statistics. Senator Eggleston, you had some questions?

Senator EGGLESTON—I have only a very general question. I understand that the ABS has had some budget cuts. Is that true?

Mr Pink—Reductions in the ABS budget were largely reinstated in the most recent Commonwealth budget. We are now in a position where we have had a range of new work, and in fact our budget has been expanded. So two years ago we were in a situation where we had to reduce our work program; now we are in a situation where the work program has been largely reinstated and expanded.

Senator PRATT—Good to hear.

CHAIR—Any more questions? Senator Abetz.

Senator ABETZ—Last time we met I asked you some questions about the census. Minister, has it gone to cabinet and have the questions changed?

Senator Sherry—Yes. In fact, I am very sure Mr Pink can give you an outstanding outline of the census now, the largest peacetime—

Senator ABETZ—With respect, time is brief. Therefore, if you can just tell us if any questions have been changed or—

Senator Sherry—No.

Senator ABETZ—No. Thank you. That is easy. Good.

Senator Sherry—But, just in terms of the time, I am sure Mr Pink should at least have a minute or two to outline other key aspects of the census, because it is a massive logistical operation.

Senator ABETZ—It is, but, with great respect, estimates is not for ministerial or departmental statements, and if—

Senator Sherry—It is for answering questions, and you posed the question. You have led us, and we have only been here for—

Senator ABETZ—Go for two minutes, but ASIC start at nine o'clock.

Senator Sherry—All right—two minutes on the key features.

Senator ABETZ—Yes, two minutes is fine.

Mr Pink—Thank you, Senator. The census is very hard to cover in two minutes, but I will certainly try. As the minister said, this is the largest peacetime exercise regularly undertaken. One of the points I would make this time is that 2011 is the centenary of national censuses. It will be 100 years since the first national census in 1911. We are very pleased with all of the work that has been done in the lead-up to this census. We are on budget and on timetable. In fact, we are slightly ahead of where we had expected to be. We have some particular challenges that emerged out of some of the quality issues associated with some aspects of the last census, and we are concentrating on them with different strategies this time. Just very briefly, some of those are to ensure that we have a set of strategies to get better counts in some parts of Australia, in particular of our Indigenous peoples. There is a focus on the homeless, a strategy generally for Northern Australia, which is a more difficult area of Australia to enumerate, and a strategy that we are developing to try and deal with the growing secured

apartment and gated estate environments that make it much more difficult for our enumerators to get access to the front door of the dwellings that we are seeking to enumerate, particularly in the major urban areas.

I think the only other couple of points I will make as I go through is that 2006 was the first time that we offered households the opportunity to complete their census form using the internet, but it was a relatively low-key exercise. It was the first time and there were a lot of questions that we wanted to test in terms of that form of response. This time we are extremely confident—

Senator ABETZ—What was the uptake in 2006?

Mr Pink—It was around nine per cent in 2006. I think we would be extremely disappointed this time round if we did not get somewhere between 20 and 30 per cent. If we can do better than that, we will be extremely pleased.

Senator ABETZ—Chair, it is nine o'clock.

CHAIR—The program is not correct. Senator McGauran has a question.

Senator McGAURAN—It is not a searching question but, at the same time, we have been here for two days and these blow-ins who come in and wind you up from time to time—

Senator ABETZ—I was not allowed to go past one o'clock today.

Senator McGAURAN—I say that with the greatest affection of course.

Senator ABETZ—I was shut down, as you would recall, Minister.

Senator Sherry—I do.

Senator McGAURAN—Now I feel that my question will not be up to standard. I am just flicking through the annual report, Minister, not the newspaper, which you scolded me for recently. I want to ask some questions about the official statistics for climate change. I have to say, Minister: there is a picture of you in this annual report which is the most unbecoming picture I have ever seen, or perhaps the most out-of-place picture, of you. It is hardly a picture of a minister of the Crown; it looks more as though you ought to be on the website for a dating service. You are looking very cutesy and smiley. I would have that removed by the next time—if you are still minister, of course.

Senator Sherry—I was not even aware, to be honest, that my picture was in the annual report.

Senator ABETZ—So what have you done to upset the ABS that they did this to you?

Senator McGAURAN—There is a section entitled 'International developments in climate change and official statistics'. You have been asked to compile them. You say you have put together official statistics that 'can provide input and add value to the analysis of the environmental, social and economic aspects of climate change.' When you say environment, are you talking about temperature and sea levels? What exactly are those statistical collections?

Mr Pink—I will briefly answer, and then if you want more detail I will call Peter Harper to provide it. The ABS is not directly involved in the collection of biophysical measures. That is

left to agencies such as the Bureau of Meteorology and state government agencies. Our involvement in the environmental statistics area is more in collecting data about the supply and use of energy, the natural resources that we collect data on through our agricultural census and information that we collect in our household surveys on energy.

Senator McGAURAN—I do not need anymore. That is what I thought. But, in reality, you have always collected those statistics; you have just put a new title on them. You have always collected household usage of energy.

Mr Pink—No, we have not put a new title on them. We have been collecting a range of environmental statistics for quite some time.

Senator McGAURAN—But you have just put on the title ‘climate change’ because the government has asked you.

Mr Pink—The other area of climate change that we were involved in, and Mr Ewing could give you more detail, is the provision of a lot of support to the modelling work that Treasury did on their work in the climate change space, using the supply-use tables developed in the National Accounts.

Mr Harper—As a point of clarification, the ABS does not produce what we would call climate change statistics. We produce a range of statistics that can be used by those interested in analysing climate change, in particular what might be causing climate change or what impacts it might have. They are statistics about businesses and households and how they may be affected and how they may be contributing to it.

Senator PRATT—I note that you have commented on the scale of the census and that it is a huge undertaking. How many staff are associated with this exercise and where do they come from?

Mr Pink—We have permanent staff who work over the five-year cycle of a census, from the design of the census through to the dissemination of the results, and that would be about 150 people. In our processing centre somewhere around 800 people are brought on to process the actual census. The enumeration phase, which is by far the biggest phase in terms of people, involves over 40,000 enumerators who come on board and assist us for eight to 10 weeks. One of the challenges in every census is to find enough people, particularly in times of high employment and in regions such as the Pilbara, in particular, where it is very difficult to find anybody to do enumeration-type jobs.

Senator PRATT—I am quite familiar with your census collection districts, as most members of parliament are, if they do their fair share of doorknocking. I would like to ask you about the Northern Australia strategy. I think there has been some comment at previous estimates about budget pressures within the ABS, particularly the flow-on effects that had in collecting statistics, in particular from Aboriginal communities: it was harder to collect information from communities. What is the significance of the Northern Australia strategy, particularly when it comes to things like the national Closing the Gap strategy and some of those kinds of initiatives that we really need good information for?

Mr Pink—There are a number of levels at which one can talk about that Northern Australia strategy. If we relate it to our Indigenous communities, the first thing is engagement.

We learn at each census, and we have learned a number of lessons from reviewing our experience in 2006. We are putting a lot more effort earlier into engaging communities and community groups to help them understand the value of participating and the importance of participation. We have learned lessons from the 2006 census and earlier censuses, but particularly 2006 in terms of some of the ways in which we went about enumeration, particularly of some of the remote communities and in the camps and fringe communities living around some of the urban centres in Northern Australia. We are adopting different approaches there. We are also looking to work with and engage more Indigenous people as enumerators who are familiar with and well known to their communities. So there are a number of different levels of the Northern Australian strategy, as we describe it in that overarching sense, that we are putting in place to try to ensure both that there is stronger engagement and that we have the people on the ground who are going to be able to collect good information this time around.

Senator PRATT—I must say that I am very pleased to hear that put on the record. Just a year ago there were concerns about the ABS's capacity to deliver in that area, so I am really pleased to see that strategy off the ground.

Mr Pink—We have received additional funding, I would have to add, which we are very pleased about, because the census overall is becoming more challenging in all sorts of contexts. Australians are more mobile, they are busier—they are harder to contact. Indigenous people, particularly in the remote areas, are quite mobile as well. I think our strategy last time—to spread the enumeration in many of those areas over around 12 weeks—meant that that mobility created real problems in overcounts and undercounts. The strategy for Northern Australia this time is to move in and enumerate very, very quickly right across those communities.

Senator ABETZ—Do you do a census of the people who are residing on Christmas Island or not?

CHAIR—That is not part of Australia, as I understand it.

Senator PRATT—I am sure they have plenty of statistics on it!

Mr Pink—They will be included.

Senator ABETZ—They will be included?

Mr Pink—Yes, they will.

Senator ABETZ—So have you printed an extra 5,000 forms for them?

Mr Harper—We would make sure we have printed enough forms to cover everybody who is in Australia on census night.

CHAIR—Thank you to Mr Pink and the ABS. It is a function that informs a lot of our work.

Australian Securities and Investments Commission

CHAIR—Welcome to ASIC. Mr D'Alosio do you have an opening statement you would like to make?

Mr D'Aliosio—I do—I want to spend a little bit of time on an opening statement. As you would be aware, since we last met ASIC has lost three litigation cases which have been the subject of wide media coverage. They were OneTel, AWB and Fortescue Group.

The current position in relation to OneTel is that we have filed an intention to appeal. A final decision has yet to be made on whether or not we will lodge a final appeal. Costs were awarded against us and we have agreed by court order to pay Mr Rich \$9.6 million for costs and \$4.1 million in interest. There were some other orders in relation to costs and other defendants.

In terms of AWB, the loss there concerned whether we could take only one action or two actions against a particular defendant—that is, commencing two actions one after the other. The judge at first instance ruled against two cases. We have appealed that and are awaiting a decision.

The Fortescue case was on continuous disclosure and alleged misleading and deceptive conduct. We lost at first instance and we have appealed.

ASIC does have the financial resources to meet the costs order in OneTel and will, unless we lodge a final appeal and the payment is stayed, draw on what is known as the enforcement special account, otherwise referred to as ESA funding. While costs will impact the ESA funds that are available to ASIC for new cases, current major investigations using ESA for cases such as Storm Financial and Westpoint will not be affected.

I would like to make some points to reassure the committee that ASIC is properly discharging its regulatory responsibilities, that ASIC has acted, and continues to act, responsibly in the way that it selects and runs litigation and that it approaches those cases in a focused way, with considerable due diligence.

First, in relation to that, ASIC has strong enforcement as a key part of its mandate. In the 2008-09 annual report you will have noticed that we completed something in the order of 186 litigation or enforcement matters. We had a 90 per cent success rate. We achieved 19 jailings and eight suspended sentences.

The second point is that our percentage of success in major cases is not as high, but nevertheless we believe it is quite acceptable. In 2008, in contrast to the three decisions I am talking about, we achieved success in James Hardie, which is subject to appeal. We achieved success in a number of investor recovery matters in Westpoint. The major action against the auditors is ongoing. There was the Panchal insider trading conviction. The Somerville case involved some eight defendants of unrelated companies engaging in illegal phoenix activity. Stuart Ariff, liquidator, was banned for life. In relation to Opus Prime, we worked successfully for an out-of-court settlement with the parties of some \$250 million for retail investors.

Another illustration of ASIC's success in major litigation is the HIH litigation with the Commonwealth Director of Public Prosecutions. In that case there were 10 defendants convicted, with nine of the defendants sentenced to a total of 27 years in jail, civil penalty proceedings successfully brought against three defendants and compensation of \$8 million. There were a number of bannings, including two for a total of 30 years. There were four

defendants where ASIC took action and we were unsuccessful in those cases, but we and the CDPP considered that the cases should be brought.

It needs to be borne in mind that litigation, by its nature, is adversarial, and cases are won and lost. But even if cases are lost—this is an important point—they still provide important guidance to the market on, for example, such issues as market integrity. The deterrence impact of ASIC being prepared to take on large and complex cases cannot be underestimated. Needless to say, when we take on major cases we do not do that lightly. In running those cases we comply with the Attorney-General's model litigation rules. In major matters we will use external barristers who are experienced in proper case management and the strategy in running cases in a proper way. In Fortescue and in James Hardie we also used experienced external law firms. I believe that these successes reflect well on the commitment and dedication of the ASIC staff.

These recent losses have prompted calls from some quarters for improvement in the way that we run our litigation, and I want to make three comments in relation to that. First, to lump these three cases together is not appropriate. Fortescue was handled by experienced and competent outside solicitors and focused on specific issues. AWB, as I said earlier, is very much about whether there is one action or two. OneTel, on the other hand, was quite a complex case. Corporations are large and they are complex, and when you are looking at the trading and financial positions of a corporate group necessarily it will be complex. In the OneTel case, with the vigorous defence, that vigorous defence clearly added to the length of the case. But to say that ASIC should not run complex cases, for example, would be to say that it should not investigate such things as Storm Financial or Westpoint. We do not believe that is what our mandate should be.

Speaking generally and not just about OneTel, trial judges, ASIC and defendants all carry the responsibility for keeping cases focused, not just ASIC, as some commentators may be suggesting. Nevertheless, we are carefully reviewing the comments that were made by the judge in OneTel. It should be also noted that in OneTel the judge did not just make negative comments about ASIC; he also made positive comments. At the close of the case, for example, when the case finished, before he went to write his judgment—which did take a considerable period of time because, presumably, of the complexity of the case—he said:

I am grateful to counsel and instructing solicitors for the substantial assistance they've given to the court during the hearing, especially in the preparation of final written submissions. Conducting cases by careful, measured and dispassionate advocacy without the distractions of flair and temper is one of the best traditions of commercial equity litigation in this court. It is the approach most likely to assist the court to reach well reasoned conclusions based firmly on relevant evidence and applicable propositions of law.

I believe I am tolerant of most things, but I have no tolerance at all for any substantial departure by counsel from this tradition. Senior counsel for the parties in this case—

that includes ASIC—

respected the tradition in the approach they took to the presentation of evidence and submissions and I very much appreciated their doing so.

On another occasion in the judgment—it is a minor point but it is important to illustrate ASIC's approach to costs—he says:

An example of possibly lavish expenditure might be accommodation expenses during the London hearing. According to information provided to me during the hearing, counsel for ASIC was accommodated modestly, while the defendants and their team stayed at the Savoy ...

He also praised ASIC in relation to limiting creditor evidence and what he had asked ASIC to do.

My second comment in relation to these calls for review is that these cases were commenced and underway prior to the recent strategic review of ASIC, which was completed towards the end of 2008. Following that review, we made a significant number of changes in the way litigation is run at ASIC. Following that review, we put in place the following things. First, we created a new office of chief legal officer. We appointed an experienced lawyer and former barrister with a strong legal team behind him. The office of CLO is there to assist the commission with strategy and preparation and running of major cases, and to independently review our proposed approach.

The enforcement division was too large as one division and we broke it down into eight deterrence teams. The objective was to create smaller teams with an increased number of senior leaders to run and focus on specific cases, so that we can manage and run these cases better. New leaders were appointed to these deterrence teams from internal promotions and external hires. This added new and experienced leaders and a number of lawyers with litigation experience. We recommended to government, and the government agreed, to increase the number of commissioners. The increase in size of the commission to five means that we have increased involvement by the commission in the strategy and tactics of major cases. Finally, we put in place new and improved training and development programs for lawyers and investigators. ASIC is investing in skills training and development. We have also reviewed our performance measures and improved our recruitment processes to continue to attract top people.

I am the first to recognise that cultural change takes time. I have said that it will take three to five years to see the full benefits of ASIC's strategic review. However, these changes are leading to improved results. I will illustrate that with our work in the area of market integrity. We have a number of market integrity cases at different stages of development through the courts. Last calendar year, we had five convictions in markets cases: one for insider trading, two for market manipulation and two for misrepresentation to the ASX.

The following cases have either been through the courts this year or will be in the coming months. In the Citrofresh matter, the court found misleading statements made by a director. In the Genetic Technologies matter, which relates to market manipulation, one person has agreed to plead guilty and the other two accused were committed for trial. In addition, we already have five persons charged and awaiting trial on insider trading, with two who have indicated they will enter guilty pleas, and two persons charged and awaiting trial on market manipulation. We also currently have a number of other matters before the DPP where we expect more charges will be laid in the coming months.

Senator ABETZ—Chair, on a point of order. How many more pages are you about to read?

Mr D'Aloisio—One.

CHAIR—Members of the committee will be pleased to know that the witness is answering most of my questions, so I will have very few to ask.

Senator ABETZ—All right.

Mr D'Aloisio—My third point is that we are not dismissing these three losses. We are seeing what we can learn from them and what we can improve further. An internal review by our senior leaders and the commission of these cases is underway. This is over and above what would be done in a usual post matter review. We are particularly concerned to be able to assess and respond appropriately to all comments made by the judges in these cases. We are also having senior counsel review the judges comments to assist us with any lessons. Depending on the outcome of that review, we will assess the need for any further reassessment on the way we run our investigations and litigation changes.

I have taken longer to provide my comments, but they are to enable you to better understand these losses and put them in context. We recognise we have more to do to deal with the perceptions created by these losses. We are working hard to do that. Importantly, I can assure the committee that ASIC staff and the commission remain committed to discharging our functions in this enforcement area. Thank you for the time to make my opening statement.

CHAIR—Thank you. You have answered most of my questions about the progress with various cases. I will go to my one remaining point which concerns the frozen mortgage funds. I understand that ASIC has developed a task force to deal with that issue.

Mr D'Aloisio—Yes, we actually established a task force several months ago in response to the frozen funds. It is actually made up of a number of stakeholder groups at ASIC. Basically, what the strategy of that has been is to see what we can do in the immediate situation, which was getting money back to those who really suffered hardship. During last year we extended the hardship relief that was in place. We have also been working with funds to try to streamline those moneys that are available in the funds and try to make it administrative simpler for them to get the money back to the funds. That is in the immediate situation and dealing with those who really needed the money.

Longer term, what we have been doing with the frozen funds is exploring ways with them that perhaps they might accelerate getting the money back to investors. We did look at a number of options with the funds. You can break the funds into types. You have got those that have got assets that are essentially good and, if you wait until maturity, the money will come back. I will call it money in good funds—or, if you want, the prime mortgage trusts. Their big concern is not breaking the par value of a fund and therefore liquidating and taking losses. Basically, most of those mortgage funds, as you probably know, have maturities on the underlying mortgages, three to five years. So basically the money is coming in but, assuming no lending, it will take several years for the money to come back. Most of those funds are generally not lending new money, but the money that is coming in is actually then being distributed back out—which really means, if you think about it, they are distributing for five years at, roughly, 20 per cent per annum, five per cent a quarter. So, basically, most of them

are distributing three to five per cent a quarter back to the investors, which is money that comes in and be offered out on a pro rata basis.

Then you have the other funds, which are more aggressive funds. We are developing a strategy with those to really explore whether it is in the best interests of unit holders that they continue to exist or whether they should be wound up. That is a strategy that we are looking at at the moment. In the next month or two we are looking to come out with a revised regulatory guide, looking at mortgage funds and how to improve the 'if not; why not' disclosure to make sure that investors are more aware, in a stressed situation, as we had, that these funds are probably not suitable for short-term investment—the prime ones—and, fundamentally, they are a mismatch and should be seen as medium-term investments; not short-term investments.

The task force meets every few weeks and we review where we stand. We have been working very closely with IFSA on trying to develop across a number of different funds and we are also working with the individual funds, monitoring what they are doing and having a dialogue to see if we can find solutions.

Senator EGGLESTON—I have some questions relating to the matters that you raised in your opening statement. How many court proceedings are ASIC currently involved in? On notice, can ASIC provide a list of each current case and the amount of money spent on each case to date?

Mr D'Aloisio—I will come back and give you more exact numbers, but on average it is probably running at any given time at about 200 matters. They will range in size and so on.

Senator EGGLESTON—Two hundred; okay then.

Mr D'Aloisio—As I said in the statistics I gave you earlier, we completed 186 matters in the last 12 months. In order to complete that many, you would have quite a significant number of others in the pipeline. Our annual report does have some figures, but I will take that on notice and give you more exact numbers.

Clearly we do keep track of costs that we incur on cases, particularly in the way we need to report to the ESA fund. I will need to look at the issue as to whether we can make that available to this committee and how we could make that available to this committee, preferably—I would assume—on a confidential basis because it would be sensitive information for those cases and the defendants that may be involved in those cases. I will take that issue on notice as well and see how we can assist you. We do record costs for budget and planning purposes and for proper management of the cases. The records would also include external fees and so on.

Senator EGGLESTON—Do you have a record of the amount of money you spent on failed court cases, for example failed court cases in the last 12 months?

Mr D'Aloisio—We would have records of both successes and failures. We would not differentiate for record keeping because there would be no sense in doing that. We would have it for both, yes.

Senator EGGLESTON—Do you also record the amount of time spent on each case?

Mr D'Aloisio—Unlike law firms, ASIC does not have lawyer or investigator time sheets as such. In order to be able to track the costs, we do keep a record of those who are involved and

estimates of the time they are involved in cases. We do not have the sophistication of time sheets but we do have records that we think are sufficient for our purposes.

Senator EGGLESTON—How much money has ASIC budgeted for the three court appeals it has undertaken against the Australian Wheat Board, One.Tel and FMG?

Mr D'Aloisio—Each of those three cases has reached the limit where we would be drawing from the Enforcement Special Account fund. Yes we would have budgeted and we know that we have the funds to deal with those but, again, I would rather take it on notice and assess whether I can give you that as an open answer or as a confidential answer.

Senator EGGLESTON—That is fine. I understand that ASIC has sought new laws improving your ability to telephone intercept and also to expand the search warrant powers available to ASIC. Given that ASIC has only prosecuted one case of insider trading and two of market manipulation over the 2009 financial year, why does ASIC feel that the new powers are warranted and why are ASIC's current powers insufficient?

Mr D'Aloisio—There are a number of points. Firstly, that we have only run one insider trading case is not correct. I can refer back to what I said earlier. Fundamentally, at the moment, we would have something in the order of over 50 active cases in market manipulation and insider trading. I mentioned earlier the successes we were having.

Secondly, yes, we are using the existing powers we are pushing and we have made market integrity, insider trading and market manipulation a priority. I have spoken to this committee about this on previous occasions.

Finally, concerning the issue of needing the additional powers; when we looked at our record of insider trading we felt that, in addition to the efforts we have put in and what I talked about earlier following the strategic review, we should be put in the same position as the ACCC is in cartels and as a number of international regulatory agencies are in relation to insider trading and market manipulation. Insider trading and market manipulation is akin to cartel in the ACCC space. It seems to us that the penalties, the deterrence impact of the penalties and our ability to have access to real-time speaking, subject to the proper safeguards that apply for other agencies, is important.

One of the key reasons that it has been difficult in getting convictions on insider trading has been the ability to run a circumstantial evidence case from which judges can draw inferences—exceptionally difficult cases to run—yet you need to run those because of the deterrence aspects you need. The ability to get access to telephone intercept in real time is an important additional power that ASIC needs, and the government has responded to that and built in appropriate safeguards. We do not do telephone or electronic interception ourselves; that is done by another agency subject to proper court safeguards.

Senator EGGLESTON—The *Financial Review* reports that almost half of the 278 matters the ASX referred to ASIC for investigation since 2005 are yet to be finalised. Can ASIC give the exact number of cases that are yet to be finalised from 2005?

Mr D'Aloisio—That is something that I would like to take on notice and give you a written answer, because I need to check the source of where that has occurred. What I can say is this: ASX in its surveillance role has got to kind of detect, smell, have a look. I think its former

chairman referred to it as being a bit like Neighbourhood Watch: you see something that looks a bit iffy or tricky and you refer it to ASIC with some appropriate work. ASIC then has to take that, do proper and full investigations and collect evidence that would then stand up in court and convince a DPP to take those actions. That necessarily will mean that, just by the nature of the number of referrals, there will be a number of those matters that will not be actioned beyond a certain point. There will be a number that proceed to extensive investigation and then of those that proceed to investigation a fewer number may end up in court. I think I will take that on notice and see if I can give the committee a better run-through of how what starts off as behaviour that looks a bit smelly or whatever tracks its way through. The notion that because ASX has reserved 200 matters to ASIC that should convert to 200 insider trading cases is with respect just a nonsense; it does not translate in that way.

Senator EGGLESTON—The FMG appeal was the first of the appeals against the three big cases you have lost this year or last year. May I ask if that appeal is being made on the basis of advice from senior counsel?

Mr D'Aloisio—I think AWB was the first. Anyway—

Senator EGGLESTON—I thought FMG—

Mr D'Aloisio—Both. Yes, absolutely. ASIC would not do so in the normal course on major cases. As I said earlier ASIC retains experienced senior counsel and ASIC would take advice. The decision on whether to appeal the decision or to launch proceedings at the end of the day are matters for the commission; they are the commission's decisions. Certainly we have filed the notice of grounds of appeal in FMG. Those grounds of appeal, I think, name the counsel that we have retained and the law firm that is acting for us.

Senator ABETZ—Do you engage separate counsel to consider the worthiness of the appeals as opposed to the counsel that actually undertook the initial case for you?

Mr D'Aloisio—It is case by case. We run filters. Depending on the case, it may well be extremely important to retain the counsel that has run the case. We may get a second opinion. We also have the Chief Legal Officer, as I mentioned earlier, and his function and his team are to provide the commission with independent advice. We have separated out—this is an important point, Senator—the people, the leaders and the teams that are actually investigating and running the case from the decisions on whether as a matter of law we have a good case. In some of these cases, it is by using external law firms and senior counsel; in other situations, senior counsel. The judgment on how much advice we get is a case-by-case matter. We are also conscious of the fact that senior counsel are an expensive commodity.

Senator EGGLESTON—As I am advised, the case has been taken on the business judgment rule as applied to the FMG directors and it has been said by some business commentators or observers that, if this case succeeds, company directors would lose the legal protection they now have for acting on the basis of good faith and good judgment and making a reasonable business decision. What is your answer to that comment?

Mr D'Aloisio—I prefer to take the question in a more general context rather than directly on the FMG case, because that case is on appeal.

Senator EGGLESTON—Of course—just the general principle. If you succeed, will this change the business rule?

Mr D'Aloisio—Our grounds of appeal are filed. ASIC is not seeking to change the law on the business judgment rule, nor is it seeking to change the law under section 180 that directors are required to act with due care and diligence. The two main appeal grounds in FMG relate to the extent to which the tests of whether the market are properly informed are more of an objective test or whether they are more of a subjective test and the particular facts in that situation. We have appealed. The defendants have got a view. We have a view. We exercised our right of appeal and the matter is now before the court of appeal. ASIC is not arguing a change in the law; ASIC is actually saying what it believes the law has been and should continue to be.

Senator EGGLESTON—Thank you very much. Of course, some people disagree with you fairly strongly and there was a letter in the *Australian Financial Review*, which I might just read because it is fairly short, from Nicholas Callinan of East Melbourne, who said:

The Australia Securities and Investments Commission's appeal in the Fortescue Metals Group case is, inter alia, "against the ruling that holding an 'honest and reasonable' belief of the truth of an announcement to the market is enough to satisfy directors' duties." ("ASIC to appeal over Fortescue", February 5).

What is happening in our society when ASIC wants to hold liable in hindsight those people whose contribution to a company is to conscientiously exercise their judgement day-to-day?

Do they want directors to announce other than what they hold honestly and reasonably?

Were ASIC a business, holding it to such a standard of responsibility in hindsight for its track record over the last few years, a conscientious board of directors would exercise its judgment and replace the top management.

What is your comment to that?

Mr D'Aloisio—I have not got a comment on that. There are letters in newspapers that have also supported ASIC. We are not seeking to change the law. I think that is an opinion. We have taken advice in relation to this appeal. We have appealed. The issue of the performance of the senior management of ASIC is a matter for the government.

Senator EGGLESTON—You said in the beginning that you are seeking to change your culture somewhat. In the past I am told there was a culture of negotiated settlement over these sorts of business cases with ASIC, as in the Vizard case in Melbourne where there was a \$150,000 settlement over two cases of insider trading. Is it part of your purpose in these very expensive prosecutions to change the reputation of ASIC? Are you seeking to say in a very strong way: 'Look, we are prosecuting these cases very vigorously at enormous cost, perhaps beyond our capacity to bear the cost. Here we are going in for three appeals even though we have lost these three cases'? Is that what you are doing?

Mr D'Aloisio—No. Each case is taken on its merits, and we have had a combination of these three. If I can contrast that, in the Opes Prime matter, ASIC worked hard to get parties settled through mediation without needing court action. In the Westpoint matter, ASIC, in taking proceedings, is working hard and instituted a global mediation which led to a number of the cases being settled and resolved. ASIC will, depending on the case, look at settlement

of those cases. Settlement of a case is a two-party thing. Where it considers that the matter is of significant public interest and a deterrence aspect is needed, ASIC will take the case on and will take it right through. There is not a general rule about these—as I said, you have to act responsibly and carefully and take proper advice—but we need to look at each case on its merits. The cases we are talking about are significant cases of corporate governance that go to setting corporate culture within Australia. The issues of continuous disclosure, the issues of misleading the market, are fundamental to the proper operation of the Stock Exchange.

So ASIC does have to look at those cases carefully. In the past, ASIC has been criticised for different things but that is part of the job, I guess. But, basically, we will take each case on its merits, and the realm of tools that we use will range from enforcement, negotiation and mediation. Indeed, in 50 or 60 per cent of our work, we never go near a court. We talk to the parties; we release regulatory guides. We have released consultation papers on the use of confidential information and management of rumours. Those are aimed at assisting companies so that they do not get into the problem of crossing the line that then requires expensive litigation and affects their reputation. We are very careful about that. If you are referring to some sort of gung-ho culture, there is no such thing.

Senator EGGLESTON—Thank you very much. I might just say in conclusion that the fact remains that you lost these three cases on the grounds that you have mentioned. They were not held to be proved against these three companies. I think it is a matter which perhaps ought to be of great concern to many people involved in the business world that you are seeking to appeal those three cases, notwithstanding the three losses.

CHAIR—We will take a tea-break and resume with ASIC following the break.

Proceedings suspended from 9.47 pm to 9.59 pm

CHAIR—The committee will now recommence. Senator Abetz has questions.

Senator ABETZ—I invite the chair of ASIC to consider providing an opening statement in written form about an hour or so before the hearing. Then it can, hopefully, simply be incorporated so that it becomes part of the record of this committee, just to save time. But I just make that as a gratuitous suggestion to you.

Are the three big appeals—this is following on from Senator Eggleston's questions—on findings of fact or on the interpretation of the law?

Mr D'Aloisio—Just to clarify the three appeals, Senator, and then I will answer the question. There is an appeal on Fortescue and there is an appeal on AWB. All that we have done in OneTel is filed a notice of intention to appeal. Because of the length of the judgment and so on there is a three-month period.

Senator ABETZ—Can I then rephrase my question and ask in relation to the two big ones. Thank you for that clarification; that is important.

Mr D'Aloisio—In relation to AWB the issue there is about whether it is fair to the individual that they are subjected to two cases or one case. That is an issue of both fact and law in terms of what the law is and how the facts apply. In terms of Fortescue the question is whether or not the market was misled. That is also an issue about the law and the relevant test to apply by a director and the facts. So they are both law and fact.

Senator ABETZ—I thought I heard you say ‘ASIC doesn’t want to change the law,’ but, if the appeals were not taken, is it not the case that those cases would be precedent and would be seen as the law? By seeking an appeal aren’t you in fact trying to change the precedent law?

Mr D’Aloisio—In our system appeals are very much part of what litigants are entitled to and have rights to do. If the general accepted approach is in relation to, say, continuous disclosure, the test to be applied is an objective test, and that is what market has been working with. If a judge in a case takes a different interpretation, we are entitled to test that in a court of appeal.

Senator ABETZ—Of course you are. You are entitled to test with an appeal.

Mr D’Aloisio—I am saying that these two cases fall into what I have just described. We are not seeking to create new law. We feel that we are looking at the law as it is as we have understood it and as it has been applied in these cases.

Senator ABETZ—I will not take that any further.

Mr D’Aloisio—It is important, Senator, in the sense that we are not doing anything different than what ordinary litigants would or would not do.

Senator ABETZ—Yet the assertion that you were not wanting to change the law is something else. I do not want to pursue that anymore.

Mr D’Aloisio—I am sorry if I put that badly. Simply stated, there is an accepted approach by the market on issues such as continuous disclosure and misleading statements and that is how we have been working. If we have a judgment that does not follow that, we need to test as to whether the judge was right or whether it should be subject to an appeal.

Senator ABETZ—Having clarity in the law is important and I agree with that. Can I pursue the question that I intervened with Senator Eggleston on and that is: with these two big cases that you are appealing did you get fresh senior counsel unrelated to the legal firms that actually took the case?

Mr D’Aloisio—These cases are before the courts and we are appealing them. I have indicated that we satisfy ourselves that the advice we are getting is advice that we can rely on as independent. Beyond that I really do not think I should be going into how we actually prepare and run our cases. I have said that we will in some cases take additional independent advice if we feel we need it. We have the Office of Chief Legal Officer for that purpose. We have experienced lawyers also on the commission.

Senator ABETZ—We know all that. It was a very direct question and that is: did you get fresh senior counsel unrelated to the conduct of the case at first instance and unrelated to the legal firm that had been engaged prior to the appeal? The answer must be either yes or no.

Mr D’Aloisio—I think it is an operational matter. I would like to take that on notice and come back to the committee.

Senator ABETZ—You are entitled to do so, but I find that passing strange. A member of the Financial Planning Association of Australia tells me that these are different tax treatments—a fee based advice and commission based advice. Are you aware of that? They

were wondering whether ASIC had factored that into their consideration of these matters, especially in their submission to the PJC.

Mr D'Aloisio—We did not specifically address the taxation issue. We have taken the view that it is really a matter for Treasury and government. So in our submission to the PJC, we did not focus on the deductibility of commissions and fees.

Senator ABETZ—I am advised—and I do not know if it is the case or not—that fee based advice is not fully deductible whereas commission based advice is. But I cannot take that any further. Can I follow up with you the ABC childcare situation? Is it correct to say that ABC Learning Centre's major asset on its balance sheet was its licences?

Mr D'Aloisio—I do not know directly. I assume that the licences would be an important asset. I do not have direct information on that.

Senator ABETZ—You could take that on notice.

Mr D'Aloisio—I can take that on notice.

Senator ABETZ—Can we establish whether childcare licences are a valid asset?

Mr D'Aloisio—You mean for accounting valuation purposes?

Senator ABETZ—Yes.

Mr D'Aloisio—I will take that on notice.

Senator ABETZ—I understand that a lot of childcare centres, especially not-for-profit ones, do not put the licences on. In one of your answers, you said, 'the revaluation of intangible assets where there is an active market as defined in the standard' and the standard was AASB 138. Is it ASIC's view that there is an active market in relation to childcare licences?

Mr D'Aloisio—We do not have a policy position on it that I am aware of. I will take that on notice.

Senator ABETZ—As I understand it, in most states you can get a childcare licence for no cost. If you can achieve one for no cost but then whack it onto your balance sheet as a major asset, it could have the potential to skew things.

Mr Dwyer—I can perhaps shed some light on that. We reviewed the 30 June 2007 accounts of ABC and I believe that the valuation of licences was considered at that time. As I understand it, based on advice from their own financial advisers, they reversed the goodwill portion of the revaluation in the 30 June 2007 accounts.

Senator ABETZ—Given the time constraints, I will not take this any further, but I might put some more questions on notice.

CHAIR—I might clarify an issue about the opening statement. I think it is standard practice in all committees to invite agencies coming in to make an opening statement, which I did. As far as I am aware that will be part of the record of this committee and it is the normal practice.

Senator BUSHBY—Since the last round of questions took us away from the failed prosecutions, I might just ask a few questions on other matters and then I will ask some about

that. In your answers to my question on notice, SBT-18, you stated that ASIC received an appropriation of \$308 million for the 2008-09 year but that it spent only \$295 million. Is that correct? You had a higher appropriation than you actually spent?

Mr D'Aloisio—I would need to check on this through the annual report but it may well be the case that we had a surplus. Is this the 2008-09 year?

Senator BUSHBY—Yes.

Mr D'Aloisio—It is not unusual, in the sense that you are working within budget, and if you can finish ahead that is usually a good thing.

Senator BUSHBY—If you finish ahead, did you actually receive the \$13 million that was appropriated that your figures show you didn't spend?

Mr D'Aloisio—Can I take that on notice and speak to our chief financial officer and come back to you. My recollection is that we can't carry forward what is unspent; it kicks in again the following year—you start again.

Senator BUSHBY—There have been varying approaches by governments over the years to that sort of thing.

Mr D'Aloisio—But I will clarify that and give you a written answer on that. I'm sorry I can't answer it.

Senator BUSHBY—Okay. Your 2009-10 budget is \$315 million and it includes an extra \$15.5 million provided for the first time for enhanced monitoring. If you take away that \$15.5 million it leaves you with a budget of \$295.5 million, which is some \$8.5 million less than your appropriation for the previous year—or about a 2.7 per cent reduction. Is that the efficiency dividend?

Mr D'Aloisio—Again, it may be. I will take that on notice as well.

Senator BUSHBY—Okay. So you are not aware of that, but I was going to ask you if you actually assume that you spent that full \$15.5 million on the enhanced surveillance, will that 2.7 per cent reduction in your budget reduce your operations in any way?

Mr D'Aloisio—If you look at the overall position and the way we are travelling, we are working within the budgets that we have been allocated and I feel comfortable that we are working within those. You get some pluses and minuses along the way but there is nothing in that that would trouble me. I may not be understanding the question properly, Senator.

Senator BUSHBY—You may not be. I am just noting that according to your 2008-09 budget you had an appropriation of \$308 million, and in 2009-10 it looks like it was \$295 million. So it has reduced significantly and I would imagine at a time when your responsibilities have actually probably increased.

Mr D'Aloisio—Can I look at it and answer it for you, because—

Senator BUSHBY—I'm happy for you to take it on notice.

Mr D'Aloisio—Thank you.

Senator BUSHBY—Now, the \$15.5 million to be spent on surveillance, is that the money for the enhanced activities in regard to market abuse measures?

Mr D'Aloisio—In terms of the way we have reallocated and spent the budget we have reallocated quite a significant part towards the market integrity side of the business in terms of priorities as part of the restructure, yes.

Senator BUSHBY—So you are saying there that you have actually moved funds around within the commission.

Mr D'Aloisio—Yes, within ASIC.

Senator BUSHBY—But you have actually been given an extra \$15.5 million for, according to this answer that you provided, and to use your words, 'enhanced monitoring'.

Mr D'Aloisio—Yes, and that would be in the market integrity market cases in terms of the surveillances on the stock exchange and taking enforcement action insider trading market manipulation—adding additional resources and technology to do that.

Senator BUSHBY—So it is a broader enforcement, and the market manipulation phone tap type things that were announced.

Mr D'Aloisio—Yes. The statistics I quoted earlier following the strategic review have been very much about getting a greater focus on the market manipulation insider trading area so it is natural that we would spend more resources in that area.

Senator BUSHBY—In answer to question on notice SBT-21 you provide a table showing the number of complaints received in the past three years and the average times for dealing with them. The number of complaints in that table appears to have been steadily rising as does the average time taken to resolve them. For example, in 2006-07 there were 10,682 complaints, in the next year there were 11,436 and in the third year there were 13,633. The average number of days to finalise has gone from 19 to 23 to 31. So that is just an observation to start with—that, obviously, there were more complaints. But if you actually break them down from the information you have provided, it appears that the number of complaints about financial services seems to be, at least on the basis of those numbers, the main reason for the increase, and in fact if you do the sums and remove the financial services complaints, the complaints in other areas seems to be falling. Is that an accurate conclusion?

Mr D'Aloisio—Yes, it is. Certainly, with the market collapses, the company collapses and those issues and the retail investor losses, you would expect, as part of the 2008-09 year and indeed this year, complaints to go up and also to go up in the financial services area.

Senator BUSHBY—Okay. Are complaints falling in other areas? Would you like to comment on that?

Mr D'Aloisio—I do not think there is any sort of pattern and I cannot say it is because of our work. But it is just one of those things that is happening, maybe depending on the cycle we are in.

Senator BUSHBY—What about the average number of days taken to finalise financial services complaints?

Mr D'Aloisio—That is always difficult. We have put a lot more emphasis over the last couple of years on the complaints and resolving them, and we are probably looking at more complaints in depth than we may have in the past with the additional resources we have put in

that area. We have put a lot more focus on complaints in terms of being smoking guns for what could be other, underlying problems that are going on. It may also be that Storm, Westpoint and Opes Prime—and they have been difficult cases—are skewing the complaints and the time that it takes to resolve them, because we have had some substantial, complex ones. But, certainly, our people are very diligent about trying to resolve the complaints.

Senator BUSHBY—I understand that. Given that the number of days it takes to finalise financial services complaints, not overall complaints—I had to correct myself earlier—is increasing and the number of complaints about financial services is increasing significantly, is there a need for a matching, corresponding increase in resources to address them?

Mr D'Aloisio—There is always a judgment about being able to grow your resources, so there may be an element of that in there. I will have a look at it with our people. I suspect it is probably more about complexity than resources, but I will look at it more closely.

Senator BUSHBY—Okay. Just a quick follow-up: at past estimates you mentioned a pending agreement with the union on staffing conditions; is that all finalised and approved by the minister now?

Mr D'Aloisio—No. There are two classes of agreement. The ASIC levels 1 to 4 agreement has been finalised, approved by the minister and is an operation. With the so-called EL1 and EL2 agreement, we had reached what we thought were final negotiations before Christmas, but the staff vote narrowly defeated it. So now we are in discussions and looking at putting a revised offer, working within the government's direction on staff increases and with ministerial approval.

Senator BUSHBY—What are the main types of issues that are still in dispute?

Mr D'Aloisio—The main issues are around quantum, around bonuses—yes, mainly that sort of thing.

Senator BUSHBY—So, ultimately, there is the potential for further resource issues, depending on how that goes? Basically, you are saying 'we can't afford it' and they are saying 'we want more'. So, depending on how it is resolved, it may end up costing ASIC.

Mr D'Aloisio—Yes, it may. But we are engaged in proper, bona fide discussions with our staff, as our staff are with us. We are very fortunate at ASIC that we have got very good staff, and I think this is an issue that we will resolve with them, subject to the government's overall policies and direction.

Senator BUSHBY—And within your budget?

Mr D'Aloisio—And within our budget. I am certainly pushing to achieve that.

Senator BUSHBY—Okay. Do you have any projections for changes in staff numbers in the coming year?

Mr D'Aloisio—No, not at this point. We are flat out with the number of cases that we have. We will start the planning process probably around April-May. Then we will know the government's budget and we will do the normal business planning for the year.

Senator BUSHBY—What about consultants? Are you able to give me any indication of the current level of expenditure, budgeted and actual, on consultants?

Mr D'Aloisio—We can get you that information. I will take it on notice and—

Senator BUSHBY—In doing so, can you provide a list of the consultants engaged and the purpose of their engagement?

Mr D'Aloisio—We can do that. It is on our website, as well. We will give you that. One point to note is that we are engaged in a very significant refreshing of technology, so our external consulting spend will probably look higher than it would otherwise, but we will make that point in the answer. We can give you the information. Most of it, I think, is on the website.

Senator BUSHBY—We mentioned the additional \$15.5 million you received for enhanced surveillance and monitoring. In October, you said that those funds were conditional upon fees being charged to market participants. Can you expand on that? What do you mean by that? What fees do you need to charge to market participants, and how does that create a conditionality in respect to those monies?

Mr D'Aloisio—I may have misunderstood your earlier question. I think the funds that we are talking about are for ASIC taking the market surveillance function from ASX. In relation to that, the government, in making the decision that that function would come across to ASIC, also allocated additional funding to enable ASIC to do that. I think the government has also said that it expects those costs will be recovered. In the current draft legislation it says that they are to be recovered from the market operators on the basis that at the moment those fees for running the surveillance function are absorbed within ASX's trading fee, because it is a cost that would be incurred by ASX in taking the surveillance function across to ASIC. So the view would be that the costs of that function should continue to be borne by the market through the market operator and not by the government. There will be legislation in relation to that and there will need to be negotiations with ASX to sort that issue out.

Senator BUSHBY—So there will be more work to finalise the takeover of the ASX responsibilities?

Mr D'Aloisio—Yes.

Senator BUSHBY—What stage has that reached? I understand a bill has been introduced and passed by the House this week. How are you proceeding with that? You indicated last time that you have a task force.

Mr D'Aloisio—Yes, we have a team headed by one of our commissioners and senior leaders. We are working well with ASX in relation to bringing across systems and people, and we are gearing up, as we have said, to be able to go online in the third quarter of this year, subject to the passing of the legislation and issues that are being worked through. We are on track to achieve that. We are comfortable that we can achieve that. We are also in the process of completing the transition for the credit legislation. We are on track to do that, as well. So our people are working hard to meet those deadlines, and we should be able to do so.

Senator BUSHBY—You mentioned that you are hoping to go online by the third quarter of this year. When you say 'online', do you mean with the trading monitoring system or—

Mr D'Aloisio—I mean in the sense that the changeover has occurred from ASX to ASIC.

Senator BUSHBY—Are you also looking at the trading monitoring system?

Mr D'Aloisio—Yes. Do you mean the real-time surveillance systems?

Senator BUSHBY—Yes.

Mr D'Aloisio—Yes. We will have, as ASX has had, real-time surveillance of the market by nanosecond or by—

Senator BUSHBY—In October, you mentioned that at that point you were looking at the substantial technology requirements—

Mr D'Aloisio—My understanding is that the tender process is complete. I have received a recommendation, which I am currently considering.

Senator BUSHBY—Will that work in with your current systems or will it stand alone and separate?

Mr D'Aloisio—We are in the process of upgrading our own technology, so we do not want to take a risk in doing too much at the one time. We will go with a system that is going to do the job well and then it will be slowly integrated back into our main operations as we complete our technology refresh.

Senator BUSHBY—I will move to a different subject. I have been advised that some of the obligations placed on financial services licence holders who dealt in forestry products in notices sent from ASIC placed unreasonably high burdens on them—for example, requiring them to provide details of clients as they stood at the time of purchase of the products, information that in many cases required manual checking of historical paper records. It may have been some time since that went on, and providing the details as they stood at the time of purchase required manual checking of paperwork to see how it went. Are you aware of those problems? Have they been raised with ASIC?

Mr D'Aloisio—I am not aware of them but I am happy to take that on notice and have a look. If that is part of what is seen as a tightening up or adding additional obligations, I will need to check with our surveillance team, but it would be understandable. These products have been the subject of concerns. We have had failures. It would be part of ASIC to be looking at that a lot more closely.

Senator BUSHBY—I am not criticising the intent behind the notices. It is more in terms of streamlining the way that they work. Basically I think it would work better for ASIC if it were as easy as possible for the people who are being asked for the information to be able to provide it. Maybe asking for historical information is not necessary. I am just hoping that there will be some lessons learnt.

Mr D'Aloisio—Let me take it on board and see what we can do.

Senator BUSHBY—Particularly given that the Ripoll report and your submission to it both suggested that there is a need for greater levels of targeted surveillance of financial services licence holders and that there may well be an increase in this type of activity.

Mr D'Aloisio—Yes.

Senator BUSHBY—We will move into failed prosecutions and proceedings. You mentioned the ESA account. How much is in that?

Mr D'Aloisio—The ESA account is \$30 million a year.

Senator BUSHBY—And, over time, that may build up? It is a cumulative account?

Mr D'Aloisio—The ESA account receives an annual appropriation of \$30 million of the funds. In order to utilise that account, the first one and a half million dollars of a matter needs to be borne in our normal appropriation. Then, as chairman, I have the authority to draw the ESA by sending a letter to the minister. If the draw is more than \$20 million, then the minister has to approve that draw. You are able to carry forward that \$30 million, so you can use what is not used over a period. At the end of the 2008-09 period, I think we had drawn \$24 million. I can get you the numbers.

Senator BUSHBY—You had withdrawn \$24 million. What was the balance?

Mr D'Aloisio—The balance would be whatever was able to be carried forward and also the difference with the \$30 million.

Senator BUSHBY—If it has been getting \$30 million a year for a number of years, it may have hundreds of millions of dollars in it, depending on how regularly you access it. Maybe if you could take on notice to provide advice on how much has gone in over recent years and how much has come out.

Mr D'Aloisio—Yes. I may give it to you again in confidence or to the committee. I will just check the confidentiality issue.

CHAIR—Sorry, Mr D'Aloisio, but in response to estimates you cannot give information in confidence. It needs to be all on the public record. So please bear that in mind.

Senator BUSHBY—I do not need the details of the cases, just the quantum.

Mr D'Aloisio—Okay. We can do that.

Senator BUSHBY—Particularly since you are probably about to take out some \$14 million.

Mr D'Aloisio—\$13.8 million.

Senator BUSHBY—\$13.8 million, is it? I wrote down '4.7 interest'. It was 3.7 interest, was it?

Mr D'Aloisio—Yes.

Senator BUSHBY—Getting on to the specific cases: correct me if I am wrong, but did you undertake in response to Senator Eggleston's question to provide full details of the costs of all cases?

Mr D'Aloisio—That was one where I will probably need direction from the chair. Certainly I have taken on notice to provide that, but I do want to check, in terms of running those cases—they are live cases—whether I can actually do that. I will take it on notice and comply with whatever it is we need to do.

CHAIR—I think you can take it on notice. If it is going to compromise the cases, obviously let us not. There is a public interest test.

Senator BUSHBY—Prima facie, it is hard to see how an indication of the costs involved would compromise the arguments in the case, but certainly it would be good if you could provide the total explicit and implicit costs of the cases. You have indicated you keep an

internal track or estimate of the overall cost but also the specific costs of external legal assistance, court costs and so forth. The Rich, Wilkie, Lindberg, Citigroup and Fortescue cases are the ones I am most interested in.

Mr D'Aloisio—Sorry, Rich—

Senator BUSHBY—It would be in the *Hansard*. Rich, Wilkie, Lindberg, Citigroup and Fortescue. Thank you very much as well for your opening statement. I think that provided a lot of information about ASIC's approach to these major cases and the steps you have taken to improve processes in future. Specifically given those three cases at the end of last year, have you taken any internal reviews to examine those? I know they are very different, but have you examined the overall approach to these major cases in particular to see what whether there is room for improvement?

Mr D'Aloisio—Yes. We clearly as a matter of proper process review any case, win or lose, what the lessons are. Fundamentally on this, because of the nature of them, we have an internal review going on at the moment of commissioners and senior leaders and also getting senior counsel assistance in relation to some of the comments the judges made. When we have completed that we will then assess whether we need to do additional review, including whether we need to bring in any external assistance to help in that review improve the effectiveness of the way we investigate and run our cases. As I said in my opening statement, I believe that a lot of the changes we have put in place, because these cases do relate to both pre- and post-strategic review, I think the steps we have taken in place and the results we are achieving, some of the results I mentioned earlier, are starting to give us at the commission level the comfort that we are running these cases as well. However, because of the public and community responsibility and generally because we want to improve, and we are concerned that there are perceptions that have arisen from those cases, we are doing that further work and will continue to do that work. I will make the results of that work available to the committee.

Senator BUSHBY—I appreciate that. The work that you are referring to is a specific review that ASIC decided to undertake following the high profile losses at the end of last year, not something that was generally in place but specifically set up.

Mr D'Aloisio—Yes.

Senator BUSHBY—I would like to ask some questions about process. I do not know how we will go in terms of your answering those, but what separation of personnel is maintained between ASIC investigators conducting the investigation and other ASIC staff that might be assisting in the preparation and running of actions.

Mr D'Aloisio—As I said earlier, if we take a criminal case, for example, ASIC's role with a criminal case would be to do the investigation, quite detailed examination, get it to the point of what would be called briefs for the DPP, for the Commonwealth Director of Public Prosecutions. At that point the briefs would be handed over to the Commonwealth Director of Public Prosecutions and we would work at their direction in terms of how the case is then run through the courts. So, if you like, in the criminal area there is a clear separation between the prosecutors, the investigators, counsel assisting in the case.

In relation to civil cases, depending on their complexity, a lot of civil cases and administrative cases are more routine. That separation is not as clear, but again if it is an administrative matter we have delegates within ASIC who would handle that and make the decisions on administrative matters separate from the people that actually investigate and look at the conduct. In the civil litigation area, the teams that develop the investigation and get to the point of running civil litigation cases in coming to the commission will be assisted by external counsel and we have instituted the office of Chief Legal Officer to provide independent advice so that when it comes to the commission we have a process where we can be comfortable that the rigour of an independent review has gone into the major case and then the commission is able to assess the team's view, is able to assess the external legal counsel's view and our own internal CLO.

Senator BUSHBY—I know Senator Williams has some questions for you about some other matters, so I will just ask one final question now, but, Chair, if Senator Williams finishes before 11 pm, if you could come back to me that would be appreciated. We will see how we go. Clearly, particularly with the high-profile cases which get widely reported in the media, the impact on the defendants is real and immediate, regardless of the outcome. What considerations do ASIC give to the fact that their case may well not be proven, whether because they are innocent or because the evidence is not there, given the enormity of the impact that may well happen?

Mr D'Aloisio—The decision to institute a case against individuals is a very serious one for a law enforcement agency, and we are very conscious of the reputation impact. We would not commence a case on speculation. From a legal point of view as a commission, we would always have to be satisfied that it has much more than reasonable prospects of success—real prospects, strong prospects. Only if you get to that threshold issue would you then look at other public issue considerations as to whether you should or should not commence that proceeding. It is an extremely serious thing, and we are very conscious of the impact it can have on individuals.

Senator BUSHBY—That is all right. I do not argue; I am sure that that is the approach you take, but are you hamstrung at all by the fact that you do not necessarily always have the resources to fully investigate matters? For example, in the Lindberg case, it was reported—and I note your comments to Senator McGauran about reporting in newspapers—that a senior manager with ASIC's fraud investigation unit, Brendan Caridi, estimated that just five per cent of the transcripts of the Cole commission report were actually read by staff. Presumably the other 95 per cent may have information that is quite relevant to the case. If you do not have the resources to thoroughly analyse these things before you actually make decisions—

Mr D'Aloisio—The AWB case is a complex piece of litigation, and there is an appeal—and it is an ongoing case so I have to be mindful of that. The comment that our senior manager was making was that when the Cole inquiry was running it was not an ASIC governance corporate issue at that point. At that point it was AFP issues of criminal breaches of the law, a commission of inquiry. Our resources were following that case but, at that point, my recollection of it was that it was not clear that ASIC would be looking at it from a corporation's point of view. Later on, it became clear that there were Corporations Act issues. ASIC formed a team, did the investigation, put the resources in it that were needed and

launched the proceedings. That is the background. In the appeal on AWB I think this issue will get aired some more. Once we know the result of that we can talk about it further. But I just want to assure you that when we take a case on—if you take Storm Financial, this committee has been critical that we have not gone fast enough in relation to it. That is because it is a complex case and, if we are going to get to the point of taking some proceedings, we have to complete our investigations.

Senator PRATT—I have a brief question. I note that late last year a consultation on market supervision reforms was launched. That included a change in the way the obligation on domestic financial market operators supervise their financial markets. Instead, market operators are responsible for the operation of their markets and the supervision and enforcement of their operating rules which relate to operational issues. But it also included a new type of rule called the ‘market integrity’ rule. I note the words ‘market integrity’ have come up a few times this evening. I think I have a general sense of what it is, but I would be interested in hearing from you what is sought to be introduced through the introduction of that new rule, given the changes I have outlined.

Mr D’Aloisio—Is that an ASIC or ASX consultation? I cannot get it in my mind quickly.

Senator PRATT—It is ASIC. Minister Bowen’s press release states:

This follows on from the announcement on 24 August this year by the Treasurer and Minister Bowen that the Australian Securities and Investments Commission ... would take over the supervision of real-time trading on all of Australia’s domestic licensed markets.

... ..

The government is consulting on a new system for rule-making and enforcement of those rules by ASIC in relation to the domestic licensed financial markets in Australia.

Mr D’Aloisio—Can I take that on notice and give you a specific answer. It is really around the operating rules and so-called rule around market integrity?

Senator PRATT—Yes. What is a market integrity rule? It has been described as a new type of rule. I would like some clarity about what that means.

Mr D’Aloisio—I will provide that.

Senator WILLIAMS—When can we expect a report on Storm Financial? It was due last August. Hundreds and even thousands of people are awaiting this report. It will affect their lives. When can we expect a report?

Mr D’Aloisio—I checked with the team before coming here this evening. The commission will be able to look at the results of our investigation at the end of this month and we are hoping to be in a position to outline the outcome of that in early March.

Senator WILLIAMS—Will you make that public in early March?

Mr D’Aloisio—That is what we are planning to do. At this stage, that is the advice I have received from the team. As a commission, we have not received the final results of our investigations, but I am told the team is targeting the end of February commission meeting.

Senator WILLIAMS—Does ASIC lack the resources to carry out these investigations? If you had people working on it, could you do it quicker?

Mr D'Aloisio—No. The Storm matter is ASIC's highest priority and has been for some time. I am well aware and you would be too, we have seen on a number of occasions the impact that it has had on these individuals. To give you an example, if you have 3,000 investors and they have been dealing in shares over a lengthy period of time, we have to check all the transactions and we have to reconstruct those transactions, and we have to be in a position that it is evidence of a nature that could be admitted in a court of law. I spoke earlier about OneTel which is also a complex case. It is the nature of these cases.

Senator WILLIAMS—I believe it is complicated, but we are running out of time. I want to take you to another issue. Accounting standards for ADIs treat all loan contracts, including unsecured loans, as tangible assets. Is this not the case with, for example, debenture issuing companies?

Mr D'Aloisio—Debenture issuing companies are not ADIs.

Senator WILLIAMS—That is right. How do you define tangible assets when it comes to debenture issuing companies?

Mr D'Aloisio—I do not know.

Mr Dwyer—I can define tangible assets. In what context is the question?

Senator WILLIAMS—I have been informed that smaller companies that are not ADIs that are not covered under APRA but under ASIC have had a tough time, especially when the government decided to underwrite the investments in the banks, credit unions and building societies but not in those smaller companies. They have had a horrid time because people withdrew their money to put into safe havens during the global financial crisis. It appears they have been treated unfairly and that, for example, unlisted debenture companies must display a warning that investors may be at risk of losing part or all of the principal and interest they have invested. Is that true?

Mr D'Aloisio—I think that you may be referring to the guidelines that we give in relation to unlisted, unrated debenture products. We found when a number of these debentures failed that they were typically advertised as being 'sleep easy at night, nine per cent interest, give us your money, put it in, no problem.' There were no ratings—nothing associated with those—and what was not being focused on was the risk that the principal, in terms of how it was going to be used by the group to build property or whatever, was not going to come back. So we have insisted that, if you are going to raise money through debentures from retail investors, you have to focus on the risk of that money, the principal, not being there. If you have invested the principal in an ADI and you tell the investor that, you have discharged your duty in that and the investor knows. But, if you have invested that in a speculative property investment somewhere else and you have lent the money you have raised to that property development company, we want you to tell them that as well, because that may affect whether or not they are comfortable with the risk on the repayment of the principal. So we see quite a difference between putting your money on term deposit and putting it in a debenture that may be on-lent—the company on-lends the money raised through that debenture—to speculative property or other types of investors. We are focusing the retail investor by telling the retail investor to ask the hard questions about where the principal is and the chances of getting it back. We are saying to the issuer of the debenture, 'You have to disclose certain things on an

“if not, why not” basis, and if you are not going to have a particular sort of leverage or you are not going to invest in certain assets then you have to tell the investor why not.’

Senator WILLIAMS—Are you lodging a submission to the Senate inquiry into liquidators and administrators?

Mr Dwyer—Yes, we are.

Senator WILLIAMS—You have not lodged it as yet?

Mr Dwyer—No, we have not.

Senator WILLIAMS—Will you tomorrow?

Mr Dwyer—We have spoken to the office and we have an extension until early March. We expect to lodge our public submission in early March.

Senator WILLIAMS—Is there any particular reason you require that much time?

Mr Dwyer—We have taken the inquiry and ASIC’s role in the insolvency industry very seriously. I guess you are aware that insolvencies have increased substantially in the last two years, and the resources that ASIC has put into insolvencies during those last two years have been substantial. Clearly it has taken us a lot of time to accumulate and analyse the statistics that we require from our complaints area so we can provide appropriate information and outcomes for us to comment appropriately through our submissions. The reason we want extra time is to ensure that the report is fulsome and that it does provide reasonable information for the Senate to base its conclusions on.

Senator WILLIAMS—Thank you. I want to move to some liquidators: Stuart Ariff who has been scrubbed out for life—I believe he is an accountant; Geoff McDonald, out for two years—I believe he is a barrister; and Dean McVeigh, out for 18 months. When these people are suspended or scrubbed out for life as liquidators, can they still practise in their other profession? For example, could Stuart Ariff practise as an accountant?

Mr Dwyer—Yes, he could, but that would depend on his qualifications and what his foundation body—

Senator WILLIAMS—I would assume, as he was a registered liquidator, he would be an accountant.

Mr D’Aloisio—And the nature of the disqualification, if it has involved issues of honesty and so on.

Senator WILLIAMS—Sure. I have heard a lot of things about Stuart Ariff, none of them very good. Justice Bergin—

Senator Sherry—And you are about to use privilege to put them on the public record.

Senator WILLIAMS—No, this comes from court cases, Minister. If you listen, I will explain it to you. This is from an article in the *Australian* about the 83 allegations of misconduct proved against him:

The case was completed in one day, with a listing of examples of gross misconduct.

... ..

CarLovers' main creditor, the Malaysian-based Berjaya Group reckons Ariff ripped out \$13m in disbursements and fees over four years ...

Ariff admitted to charging CarLovers for family holidays, hairdressing appointments, big restaurant bills and other outlandish expenses.

For instance, there was a \$208,300 consultancy bill involving Ariff's father for services that had no relationship to the administration of CarLovers ...

... ..

He accepted ASIC's allegation that he was paid \$170,213 from a creditor of Sid Fogg for the GST—but never paid the tax office. The article goes on:

He also admitted to wrongdoing concerning Bulla Tip, including the "fictitious" creation of a charge to secure a payment of \$400,000 to State Securities, a company fronted by Mr Karas.

... ..

He then paid Mr Karas's State Securities \$400,000 when he knew State Securities had not paid that amount to the Bulla companies.

... ..

The case that really got the court going was HR Cook Investments, which was liquidated in June 2006 after the principal died, leaving the money to members of the family, including minors.

Ariff was appointed liquidator of HR Cook and used hundreds of thousands of dollars of its money for legal fees that had nothing to do with that company.

... ..

... ASIC to continue what it said it would do in court and pursue further investigations against Ariff.

When did you start investigating Stuart Ariff?

Mr Dwyer—Our initial complaints came in late 2005 and early 2006. There were a number of complaints at that time, which were investigated by ASIC. No further action was taken at that time.

Senator WILLIAMS—You had some complaints in 2006 and no further action was taken at that time?

Mr Dwyer—On those complaints, yes.

Senator WILLIAMS—CarLovers spokesman Ian Fong said it was a shame ASIC did not act earlier. He said:

It's a shame ASIC didn't act when we made our first complaint back in 2005. The damage that Mr Ariff and his group caused would have been much less.

Adele Ferguson said in her column:

The Berjaya Group, frustrated with ASIC, came to The Australian in 2007 and told their story. Within days many more victims of Ariff contacted the newspaper, and ASIC started action.

Is there any truth in that, because of the public display of Ariff's actions brought out in Australia by Adele Ferguson? Is that what made you act?

Mr Dwyer—I cannot comment on that.

Mr D'Aloisio—We will look at that. I do not think that is the position but we will look at it and give you a response.

Mr Dwyer—We pick up intelligence from everywhere in relation to complaints. Certainly if there were allegations in the press as well as complaints then that would be something we would certainly consider, Senator.

Senator WILLIAMS—Mr Dwyer, since I have instigated this inquiry, I have been inundated with calls from people. The first question I say to them is: you have problems; have you reported this to ASIC? It is like a scratched record: 'I have done that and received nothing.' That is a common thing of not once or twice, but probably 30 or 40 times people have said to me: 'I have reported to ASIC. I get an automatic response on the computer and there is never any action taken.' That report to me is so common that I am of the opinion that you are either underresourced, or you do not look at the little issues or whatever. What is the situation?

Mr D'Aloisio—I think, as Michael was saying in our submission to the inquiry, we will go through these complaints and the complaints records in some detail with that committee. It is one thing to say, 'I have given some information to ASIC,' and it is quite another to conclude from that that ASIC then has a case that it can take action on and, indeed, that it can find the evidence to take action on. I think you do have to look at the complaint, what it was and its nature. We will, as Michael said in what we put to the committee, go through the complaints that we have received and see how we have handled them. We did this, you may recall, with the PJC in relation to Storm.

Senator WILLIAMS—That is fine. There was a case in Adelaide that I have been very involved in and thank goodness Mr Justin Owen from your organisation came to Adelaide with me. I asked the man there if he reported it to ASIC and he said he did years ago and could not get a response. Luckily, thanks to Justin Owen, the files are now taken and I believe ASIC is looking at this situation, and they certainly should be. He is just a typical person who said that he had been to ASIC and just got the cold shoulder.

This is a common complaint I get, and I come back to the situation: no matter how small or how big the issue, I question if you are resourced enough. Are you lacking staff? Why are so many people saying, 'Waste of time going to ASIC.' This is what I get on a regular basis: why is it? Are you not resource enough? Are you not staffed well enough? What is the reason?

Mr D'Alisio—Your propositions there are too general in the sense that, in terms of the inquiry we have said we will go through those complaints and see if, indeed, there is a resource issue. I do not think there is; I think we are handling the complaints and taking them through, and simply because people are dissatisfied with the result of our inquiry does not mean that there was wrongdoing, or that ASIC has been slack. But we have said that we will, in the submission to the inquiry, put that information there for you and for us to debate further.

Senator WILLIAMS—Okay. Liquidators are registered with you—is that correct?

Mr D'Alisio—It is my understanding.

Senator WILLIAMS—About 562 in Australia, I believe. Is there an annual return or examination that a person has to go through when they are a liquidator to ASIC?

Mr Dwyer—There are approximately 700 registered liquidators, of which about 550 are practising. We register liquidators, we do not licence them. When they are registered, they complete the necessary documentation. They do not, like bankruptcy trustees, go through any interview process.

Senator WILLIAMS—They don't?

Mr Dwyer—No, they do not.

Senator WILLIAMS—So they do not fill in a report to you each year saying, 'We have kept our nose clean, we have done everything right'?

Mr Dwyer—Each year they lodge an annual return.

Senator WILLIAMS—Okay, they just fill that in themselves?

Mr Dwyer—Yes, they do.

Senator WILLIAMS—Do you ever question them on their—how can I put it—ethical standards and behaviour et cetera?

Mr Dwyer—No, we do not. It is really not within—

Senator WILLIAMS—It is left up to them?

Mr Dwyer—I do not think it is left up to them; it obviously comes through the system in terms of complaints.

Senator WILLIAMS—I want to take you to personal indemnity insurance. Do all liquidators have to have that?

Mr Dwyer—Yes, they do.

Senator WILLIAMS—Okay. If they do not renew it, or cancel it, are you informed?

Mr Dwyer—I would have to take that one on notice.

Senator WILLIAMS—So, it is law that they have to have PI insurance? Is that correct?

Mr Dwyer—Yes.

Senator WILLIAMS—That insurance—does it cover things like fraud?

Mr Dwyer—Yes.

Senator WILLIAMS—It does?

Mr Dwyer—Yes.

Senator WILLIAMS—Good-oh. I noticed Ariff's PI insurance had not been renewed. Was ASIC aware of that early in the days?

Mr Dwyer—ASIC is aware of that, yes.

Senator WILLIAMS—Before the end of the court case? Was it only after the court case of Ariff that you discovered that?

Mr Dwyer—I could not comment on that.

Senator WILLIAMS—If they do not renew their PI insurance, is it up to them to notify ASIC?

Mr Dwyer—It would be declared on their annual return, I think.

Senator WILLIAMS—The annual return might be done when?

Mr Dwyer—If it expired before the annual return they would not have to declare it until the annual return was due.

Senator WILLIAMS—Do you think they should?

Mr Dwyer—I think that is probably worth looking at, yes.

Senator WILLIAMS—I think it is too. We are running out of time; no doubt we will meet again in the near future.

Senator Sherry—You have not joined the corps and financial services committee?

Senator WILLIAMS—No, I have just joined this committee.

Senator Sherry—You can have seven goes a year, from what I understand!

Senator WILLIAMS—Can you?

Senator Sherry—It used to be six.

Senator WILLIAMS—That will do me at this stage, thank you, Chair.

CHAIR—Thank you Mr D'Aliosio, ASIC and Minister. Thank you also to the secretariat, *Hansard* and broadcasting. The committee is now adjourned.

Committee adjourned at 10.59 pm