CHOICE REPORT
BETTER BANKING

choice The People's Watchdog

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Foreword

CHOICE exists to unlock the power of consumers, with a vision that Australians become the most savvy and active consumers in the world.

It's our job to provide both the unbiased information people need to make informed choices and to campaign for reforms that ensure consumers come first. For much of our past fifty years the changing face of banking has driven a substantial amount of this work.

This Better Banking report comes at a time when Australia has a once-in-a-generation opportunity to bring about lasting reform in an industry that matters to everyone.

Some in the banking industry spend their time resisting change and arguing that negative 'unintended consequences' will always flow from reforms. In this report we focus on the positive and the achievable, basing our priorities on what Australians have told us of their experiences.

CHOICE believes we all have a responsibility to take action to bring about better banking, whether as consumers, government or bankers. This report makes a series of recommendations which – taken together, and acted upon by all – would ensure that the consequence would be a more competitive banking system that works for consumers.

I would like to thank the many, many people who have contributed to this report. Your voices appear throughout and CHOICE is committed to making sure you are heard.

Nick Stace
CEO, CHOICE

Images/Cover: istockphoto

Summary and recommendations

Efficient, flexible and responsive banking is essential for Australian consumers. It is hard for people to play a full and productive part in the community without banking products and services. As a minimum, we need bank accounts to be paid by employers; to receive income in welfare or retirement; to hold our savings securely; and to carry out millions of transactions every day.

Banking is also a **key part of Australia's economy,** and a thriving, healthy banking sector is good for economic growth. But successful markets are driven by informed consumers making good choices in a truly competitive environment – what is good for consumers helps good businesses to thrive. So the consumer interest and consumer welfare should be at the heart of interventions aimed at making the banking sector work properly.

It was in recognition of the importance of banking to the Australian economy that in October 2008 the government announced a **guarantee scheme** for banks' large deposits and wholesale funding. Some liabilities remain guaranteed by the government, for a fee, for terms extending to 2015. In December 2010, the scheme was still guaranteeing more than $143 billion of bank liabilities. The government also continues to **guarantee consumer deposit balances** up to $1 million per customer per institution, free of charge to the banks, although this is under review.

That the wholesale funding guarantee scheme is being phased out does not mean that banks no longer enjoy government protection against insolvency. The size and impact on the economic system of the major banks means it is inconceivable that any government would allow them to collapse. This **implicit government guarantee for banks that are "too big to fail" must have a distorting effect on the financial services market,** and has led to governments and bankers in other major economies contemplating the break-up of the largest banks or the imposition of restrictions on their trading activities.

Banking is also special because of the extraordinary **power of banking institutions relative to their customers.** Consumers often tell CHOICE of their feeling of powerlessness when dealing with banks. This is because understanding the market and the terms of different products is usually impossible for individuals to do alone. The extent of this **"information asymmetry"** between the banks and people who need their products is unusual.

In a genuinely competitive market, banks that offer the best value to consumers would win the greatest market share. Yet in Australia, as we describe below, **the banks that consistently rate bottom in customer satisfaction surveys are the biggest and often the most expensive.**

It is for these reasons that banking is too important to be left to market mechanisms to ensure it is providing the products and services the country needs.

CHOICE **supports continuing strong prudential regulation of banks** because in addition to protecting consumer deposits it enables competition by setting a standard around which the banks can compete. Sensible rules requiring banks to hold sufficient capital, for example, put risk on a level playing field that can help give consumers confidence to bank with the institution that offers the best deal, not just the one that appears "solid" because of its size. But CHOICE rejects the suggestion by some in the banking industry that we must choose between financial stability, competition and consumer protection.

The banking Australians get

Based on our engagement with consumers, CHOICE believes that there is clear evidence of a **lack of competition in retail banking in Australia.** In recent years this appears to have been exacerbated by the consolidation in the sector and, since the GFC, the absence of a competitive discipline imposed on most other businesses by the risk of failure. This is also shown in the conduct of banks; in particular, we have heard numerous reports that suggest banks exploit consumer inertia rather than genuinely competing on the basis of the quality and value of their products or services.

In Australia there is a long history of attempts to promote better banking through competition. Despite this, **the big four banks together account for 81 per cent of all lending to households** by the 54 banks in Australia and 78 per cent of all bank deposits.

CHOICE has regularly surveyed our members for their views on banking. We have found the performance of the major banks appears to be improving compared to that of their smaller rivals. However, the **major banks consistently rank bottom** in our surveys. There is a significant gap – 25 points – between the best performer and the worst.

CHOICE members have also provided numerous views as to what makes bank customers dissatisfied. The most **common complaints** include hard-to-decipher terms and conditions, fees and charges, and poor customer service. Consumers have also felt aggrieved about changes to interest rates that leave savers in uncompetitive accounts, and have questioned the time it takes for basic transactions to be completed.

Despite the levels of customer dissatisfaction, there are low rates of switching in Australia. In the Netherlands, where there is a bank **switching** service designed to ease movement between banks, 100,000 people used the service in 2008. This compares to the Australian system which issued 2,541 lists of regular payments to consumers seeking to move their transaction accounts in the year to September 2010. At present, almost all of the costs of switching are borne by consumers, including small businesses – itself another cause of customer dissatisfaction.

Finally, consumers have expressed their anger to CHOICE at the level of **profits and executive remuneration** enjoyed by major banks and their senior executives. Many complain about the sales techniques employed to sell products to existing customers.

Recommendations

CHOICE has overarching recommendations for consumers, government and the banks themselves. To **consumers,** our message remains consistent: do not accept the unacceptable but become more active. Compare the market using an objective comparison website; ask your existing bank for a better deal; but if they will not, or if their customer service is poor, take your business elsewhere by switching to a different financial institution.

The key objectives of **government** intervention in the banking industry should be to ensure consumers are more effectively protected from unfair practices and enabled to secure a better deal; and to create a more competitive, stable, level playing field on which every player is required to behave responsibly and no individual bank can bring down the system itself. A comprehensive reform agenda is essential so that the consequences of reform taken together achieve these twin objectives.

To the **banks,** our recommendation is to respond positively to consumer demand, commit to taking customer service to a new level, and end resistance to changing unfair and uncompetitive practices. Banks that respond progressively have much to gain.

CHOICE also makes 14 specific recommendations aimed at building on existing reforms to secure a more competitive banking system that works for Australian consumers.

1. Introduction of portable account numbers

CHOICE recommends that we learn from improvements in customer mobility in other sectors (including telecommunications and superannuation) and introduce portable bank account numbers in Australia. This will reduce barriers to switching institutions and improve competition and efficiency in the sector.

2. A permanent consumer deposit guarantee

To maintain consumer confidence in all banking institutions, whatever their size, the consumer deposit guarantee should remain in place permanently at a level that recognises the international best practices in this area. To promote understanding and confidence, the government should ensure the guarantee is properly explained to consumers in a consistent way, on all relevant banking products.

3. Removal of barriers to switching home loan products

CHOICE strongly supports moves to make it easier for consumers to move their mortgage, including a ban on mortgage exit fees. CHOICE recommends a comprehensive review of Lenders Mortgage Insurance to ensure that it does not remain a barrier to switching home loans. And we urge the government to find further ways to make the entire process of mortgage switching as seamless as possible by cutting the paperwork required.

4. Removal of ATM fees for on-screen balance inquiries and improved disclosure on ATMs

CHOICE recommends the removal of ATM fees charged for on-screen balance inquiries. Regulators should require banks to meet a new, improved standard of external disclosure on ATMs, including the external disclosure of typical fees.

5. An obligation on banks to provide affordable access to payment systems

The banking sector should have an obligation to ensure that all communities have access to affordable payment services. Banks should take urgent steps to ensure that this obligation is met through solutions such as community fee rebates, the introduction of alternative ATMs or the provision of alternative access to the payment system. To enable this to be effectively monitored, regulators should also collect and publish regular information on the locations, costs and revenue generated by ATMs.

6. Improved disclosure for all credit products

Regulators should require banks to meet a new, improved standard of disclosure for credit products, in plain language, including:

- An annual statement of the cost of credit including all charges;
- Mandatory summary sheet for all mortgages that includes the total cost of repayments;
- Repayment time on credit card statements if the consumer is to repay only the minimum repayment;
- Better information and mandatory warnings for credit card cash advances;
- Introduction of a new mandatory comparison rate for all credit cards; and
- Clearer disclosure in advertising that credit card interest rates are variable.

7. Improved disclosure for other banking products

Regulators should require banks to meet a new, improved standard of disclosure for some other banking products, including:

- Mandatory comparison rates for term deposits and savings products;
- Prohibition on certain types of misleading marketing for savings products; and
- A comprehensive overhaul of disclosure documentation for Lenders Mortgage Insurance.

8. Publication of complaints statistics that name institutions

The Financial Ombudsman Service and/or ASIC should publish a regular table showing complaints received by category, and identifying the institution responsible. This information should be used to monitor and identify systemic issues.

9. Introduction of a super-complaints mechanism

A super-complaints mechanism should be introduced to enable consumer organisations and dispute resolution providers to formally raise significant issues directly with the regulator.

10. Introduction of a systemic issues register

Regulators should be tasked with monitoring and identifying systemic issues in the banking sector in a more proactive way. Regulators should (jointly) publish a regular report on complaint patterns and trends, and maintain a public register of systemic issues noting how each issue is being addressed.

11. A specialist consumer representative organisation on financial services

A specialist consumer watchdog is needed to represent the consumer interest in financial services issues, including retail banking and superannuation. It could be financed by a proportion of funds from dormant or lost accounts.

12. Bank executives' remuneration linked to good customer service not sales targets

Regulators should ensure in their scrutiny of remuneration arrangements that senior executives and front-line bank staff are rewarded for good customer service. The emphasis on sales targets in bank staff remuneration should be removed, and pressure should be reduced to push new products and product upgrades. Much greater emphasis should be placed in senior executives' remuneration packages on long-term, measurable improvements to customer service.

13. Further reform of corporate governance rules for banks

The regulators should review corporate governance requirements for banks to ensure shareholders and boards have a duty to hold executives and board chairs to account for failures in customer service.

14. Banks to meet in full their obligations to the community

The Treasury should publish a review of the tax arrangements in place for banks, end any special treatment and instead consider new mechanisms to ensure the banking sector helps fund the cost of remedying market failures.

Introduction

CHOICE on banking

CHOICE, the people's watchdog, exists to unlock the power of consumers. For many years we have provided objective, independent information so that people can find a better banking deal. At the same time we have campaigned for regulatory reform and engaged with the banks directly so that they understand con sumer concerns and to persuade them to improve their products and services.

In recent years, our focus has been on challenging unfair fees and charges. Thousands of CHOICE members have taken action to recover excessive penalty fees from banks. We have also campaigned for the industry to make it easier for consumers to switch providers in pursuit of lower fees and charges and better rates of interest, and strongly opposed further consolidation in the sector when this was being considered by regulators.

In 2010, our 200,000 members rated banking reform as one of the three most important issues for CHOICE to pursue on their behalf. A further reason why CHOICE takes banking so seriously is the special place the industry occupies in our community, as well as its importance to the Australian economy; it is an industry that matters to every consumer, every day.

Why banking is special

Banking is essential for Australian consumers. It is hard for people to play a full and productive part in the community without effective banking products and services. We need bank accounts to be paid salaries by employers, to receive incomes in welfare or retirement, and to hold our savings securely.

We also carry out millions of transactions every day through the payments system. This involves individual banks working closely together in sharing the basic infrastructure that makes banking work, so that the payments system transmits funds from one party to another. According to the Reserve Bank of Australia, in 2009 withdrawals from ATMs averaged $12.6 billion a month, or around $575 per person; and on average, non-cash payments worth around $220 billion are made each business day, equivalent to about 20 per cent of GDP. [1]

Banking is also a key part of Australia's economy, and a thriving, healthy banking sector is good for economic growth. But successful markets are driven by informed consumers making good choices in a truly competitive environment – what is good for consumers helps good businesses to thrive. So the consumer interest and consumer welfare should be at the heart of interventions aimed at making the banking sector work properly.

The banks' social safety net

It was in recognition of the importance of banking to the Australian economy, and the complexity and interconnectedness of banks in a system that was close to failure in other parts of the world, that in October 2008 the government announced the Australian Government Guarantee Scheme for Large Deposits and Wholesale Funding. Although the Scheme closed for new liabilities in March 2010, large deposits and wholesale liabilities remain guaranteed by the government, for a fee, for terms extending to 2015 in some cases. In December 2010, the scheme was still guaranteeing more than $143 billion of bank liabilities. The government also continues to guarantee deposit balances up to $1 million per customer per institution, free of charge to the banks. [2]

That the funding guarantee scheme is being phased out does not mean that banks no longer enjoy government protection against insolvency. The size and impact on the economic system of the major banks means it is inconceivable that any government would allow them to collapse. This implicit guarantee for banks that are "too big to fail" must have a distorting effect on the financial services market, and has led governments and bankers in other countries such as the UK to contemplate the break-up of the largest banks or the imposition of restrictions on their trading activities.

Bank power
Banking is also special because of the extraordinary power of banking institutions relative to their customers. Individual consumers often tell CHOICE of their feeling of powerlessness when dealing with banks. This is partly because understanding the market and the terms of different products is usually impossible for individuals to do alone. The extent of this "information asymmetry" between the banks and people who need their products is unusual.

It is for these reasons that banking is too important to be left to market mechanisms alone to ensure it is providing the products and services the country needs. It is why a succession of governments have intervened in the financial services market to protect consumers, promote competition and ensure the behaviour of individual bankers does not threaten the national interest.

A time for change

CHOICE wants Australians to be the most savvy and active consumers in the world. But there has been a perception among our members, confirmed by customer surveys, that Australians are exceptionally willing to stay with one service provider for the long run, however poor their treatment at the hands of that institution.

However, since the mortgage rate increases of late 2010, there have been signs that consumers are converting their anger into increased mobility. One survey has estimated that more than one million consumers are considering switching their home loan provider to a different institution – if true, an extraordinary proportion of borrowers. [3] In December 2010, CHOICE launched a "Compare, Ditch and Switch" website to enable quick, easy and independent comparison of the cost of different financial products. Tens of thousands of Australians have used the service – 1,500 people every day in December 2010 alone.

Some commentators have speculated as to whether this amounts to a tipping point in banking where many more consumers become willing to switch their banking providers than ever before; this might be possible, assuming the right regulatory changes are made by the government, along with increasing public awareness of the alternatives available and easy access to market comparison information. If this were to happen, Australians and the Australian economy should benefit on a huge scale because it would drive a more competitive, less concentrated market where consumers save substantial amounts of money in the long run. But achieving such a change will take determination on the part of the government and regulators and a willingness to embrace change on the part of a good number of banks.

This is also a pivotal period for banking globally. Regulators around the world are grappling with the need for more stability, competition and stronger consumer protection in financial services in the aftermath of the global financial crisis (GFC). In the UK, the chairman of the main regulator, the Financial Services Authority, has called for a "radical rethink" of consumer protection, including the possible imposition of fee caps and bans on some retail financial products. [4] The former chief executive of one of the world's largest banks, the Royal Bank of Scotland, has suggested that the largest banks in the UK that were allowed to merge during the GFC should now be broken up. [5] The US has created a new agency for financial consumer protection, while the French government intends to place written warnings on investment products considered too complex for consumers. And at the G20 Summit in Seoul in 2010, leaders including the Australian Prime Minister committed to enhancing consumer protection in financial services.[6]

"I ask that you consider the fairness and **balance of power in the relationship between banker and consumer.** I think it has gone too far in favour of the banks and a correction is needed."

Stability and competition

Some in the banking industry have suggested that we must choose between financial stability and enhanced competition or consumer protection. It is of course true that all consumers depend on a stable financial system and it is right that governments intervene to secure financial stability. But the very dependence by consumers on banking is a key reason for regulators to ensure there is also effective competition.

In a genuinely competitive market, banks that offer the best value to consumers would win the greatest market share. Yet in Australia, as we describe below, the banks that consistently rate bottom in customer satisfaction surveys are the biggest and often the most expensive.

CHOICE supports strong prudential regulation of banks because in addition to protecting consumer deposits it enables competition by setting a standard around which the banks can compete. Sensible, proportionate rules requiring banks to hold sufficient capital, for example, should put risk on a level playing field that can help give consumers confidence to bank with the institution that offers the best deal, not just the one that appears "solid" because of its size.

Consumer voices

Since July 2010 thousands of consumers have given CHOICE their views on banking – through town hall meetings, surveys, radio talkback and comments submitted through our website and phone lines. This insight into what Australian consumers think about banking gives CHOICE a unique perspective. Because many consumers complained to CHOICE that they were not being heard by others, we committed to bringing their voice to decision-makers and bankers as the future of banking in Australia is considered.

This report contains, verbatim, a sample of the concerns articulated to us by consumers *(shown in the margins or speech bubbles)*. Of course, many people have also told us of good experiences with banks, which is always encouraging. But where clear patterns of problems in the treatment of consumers by banks have emerged, we have taken these consumer concerns as a means to identify priorities for reform.

This report

This report is divided into two parts: the first section summarises, from a consumer perspective, some key aspects of Australian retail banking today. It describes a sector that is heavily concentrated, where the players with the largest market share also often offer the least competitive products and services. It identifies some of the main problems faced by consumers of banking.

The second part of the report aims to set out the key changes necessary to tackle these problems. We believe that change in banking is inevitable and indeed trying to avoid necessary change will only increase the long term costs. Our proposals are relevant to the current debate on banking reform, but go beyond the present focus on competition and banks' funding costs.

In short, this report describes the banking we get in Australia, and proposes further steps towards getting the banking we need.

PART ONE: THE BANKING CONSUMERS GET IN AUSTRALIA

Based on our engagement with consumers, CHOICE believes that there is clear evidence of a lack of competition in retail banking in Australia. In recent years this appears to have been exacerbated by the consolidation in the sector and, since the GFC, the absence of a competitive discipline imposed on most other businesses by the risk of failure.

This is shown in the conduct of banks; in particular, we have heard numerous reports that suggest banks exploit consumer inertia rather than genuinely competing on the basis of the quality and value of their products or services. Indicators of a lack of competition in banking include:

- Consumers are typically not able to compare the price, quality, characteristics or performance of different financial products and firms;
- There remains widespread dissatisfaction with poor customer service;
- Products continue to include excessive fees, hidden charges or unfair contract terms;
- There are significant barriers to consumer switching;
- There is reduced access to essential banking services, particularly in remote and indigenous communities;
- Consumers complain they are unable to pursue effective and speedy redress when they need it.

The banking industry often claims there is no evidence of a lack of competition, pointing to recent efforts by banks to attract depositors and mortgage borrowers. The mouthpiece of the industry, the Australian Bankers Association (ABA), says: "The evidence shows that Australian bank customers enjoy competitive financial markets and are able to access products and services at fair and competitive prices. For example, competition has led banks to reduce and abolish many unpopular fees as they compete to attract and retain customers". [7]

This does not amount to evidence of a genuinely competitive market; for example, statistics released by the Reserve Bank show that major banks have also recouped the income they lost after cutting "unpopular" transaction account penalty fees, such as overdrawn account fees and direct debit dishonours, with new penalty fee revenue from credit cards and personal loans.

The ABA also claims that "competition is not a panacea for people's concerns about banking and there is such a thing as too much competition. We need to be careful in managing this balance between competition and stability... the public focus has been almost exclusively on the need for more competition, despite any evidence that the Australian banking sector lacks effective competition. We need to be careful that the balance is not tipped too far towards unsafe competition". [8]

CHOICE is not arguing for "unsafe competition", quite the opposite; we strongly support regulation that protects consumers and ensures that banks behave responsibly on a genuinely level playing field. As the Chair of the US Federal Deposit Insurance Corporation puts it: "there can no longer be any doubt about the link between protecting consumers from abusive products and practices and the safety and soundness of the financial system". [9]

In Europe, the European Commission says that "safeguarding systemic stability in the short-term should not result in longer-term damage to the level playing field and competitive markets".[10] In the UK, some of the largest mergers that were allowed to take place to prevent the collapse of banks during the GFC have been reviewed by the authorities and banks have subsequently been required to sell off parts of their businesses.[11]

With the deposits of consumers protected through the government's compensation scheme, at least for now, a more diverse marketplace with more players competing for business would also reduce the likelihood of a catastrophic failure in future.

"Effectively, the banks have, for years now, run their businesses in their own interests and not in the public's interest... The way they set their matters it means that **you have to acquiesce to them and they make very little effort the other way around.** When you find a difficulty, they quickly run to their big book of rules and they read out those rules as if they're actually God-given. **And there's nothing you can do about it even if you do know those rules** or you actually started to apply whatever you needed to apply in good faith. It's bad luck. This is what the rules are."

"We sit back and let it all happen because you know why? They know damn well we Australians are so apathetic. We'll let anything happen."

A brief history of banking competition[12]

In Australia there is a long history of attempts at promoting better banking through competition.

When Australian financial markets were deregulated in the 1980s, it was predicted that greater competition would deliver efficiency gains and a better deal for banking customers.

The architects of financial-market reform assumed that deregulation would lead to an increase in the level of competition because it would remove barriers to the entry of new financial institutions. Yet precisely the opposite has occurred: since 1983, the major banks have steadily consolidated their market power at the expense of credit unions, building societies, foreign banks and home-loan originators. In the 1980s, banks accounted for 50 per cent of all lending in Australia. In April 2010, this figure was 91 per cent, and banks accounted for all but five per cent of the total deposits raised in Australia.

Banks dominate the financial system, but banking itself is dominated by the big four banks – Westpac Banking Group (Westpac), Australia and New Zealand Banking Group Limited (ANZ), Commonwealth Bank of Australia (CBA) and the National Australia Bank Limited (NAB) – which in September 2010 together accounted for 81 per cent of all lending to households by the 54 banks in Australia and 78 per cent of all bank deposits.

Concerns about the exploitation of market power by Australian banks go back to before Federation, as do the efforts by policymakers to counter them, often by failed attempts to find competitors to pit against the banks. One of the early examples followed the crisis of 1841–43, which saw banking collapses and banks forcing borrowers into insolvency. The Legislative Council of New South Wales established a Select Committee on Monetary Confusion, which proposed a central bank that would compete against the private banks with its own notes issue. The legislation that followed the Committee's report was refused assent by the King's representative in NSW.

At the Commonwealth level, the government established the government owned Commonwealth Bank of Australia in 1911. At the time, "the argument for the national bank was based on the proposition that the existing banks were avaricious and incompetent" and had contributed to the earlier speculation and subsequent slump of the 1890s. It was thought that the private banks needed competition from a socially responsible institution.

In the 1960s and 1970s, competition from building societies and credit unions was seen as the answer to the power of the banks. In the 1980s, it was argued that foreign banks would provide the necessary competition. More recently, regional banks and mortgage originators (for example RAMS) were expected to challenge big-bank market power, but these organisations have suffered as a result of the global financial crisis and have either been acquired by the big four or lost significant market share to them.

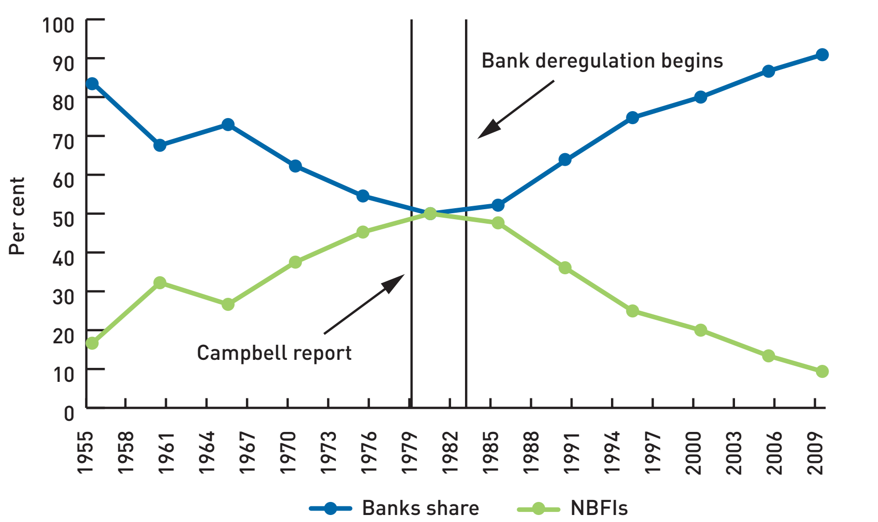
Despite the faith of successive governments in the capacity of new entrants to prevail over the big banks, their impact never reached expectations. Figure 1 illustrates the results of such policies by tracking the market share in loans and advances across all financial institutions in Australia since the mid-1950s. The top line traces the shares for banks and the bottom for non-bank financial intermediaries (NBFIs), which include building societies and credit unions as well as finance companies, mortgage originators and a host of other financial institutions. The figure shows that soon after World War II, banks occupied a dominant position in the credit market, holding 83 per cent of all loans and advances. By 1980, however, their share had shrunk to 50 per cent. When the deregulation phase that began in the 1980s was complete, the share of overall lending attributable to the banks had increased again and now exceeds 90 per cent. Table 1 gives a snapshot of the position in September 2010.

In recent decades, an important theme has been the prevention of further mergers between the remaining big four banks, a policy sometimes termed as the "four pillars" banking policy. It is generally believed that, bad as the present situation might be, it would be worse if any of the remaining banks merged. The four pillars policy evolved from the "six pillars" policy formulated by Keating in 1990, which prohibited mergers between the big four banks and the big two life-insurance companies, AMP and National Mutual Life Association (now AXA Asia Pacific). Nevertheless, there has been a history of consolidation as the big four banks have gone about acquiring competitors.

Recent legislative developments

In recognition of widespread concern about the state of the industry, the Treasury announced in December 2010 a package of measures to promote competition in

FIGURE 1: MARKET SHARE: BANKS AND NON-BANK FINANCIAL INTERMEDIARIES



Source: RBA.[13,14]

TABLE 1: MARKET SHARE: HOUSEHOLD LOANS SEPTEMBER 2010

September 2010	Household loans ($ million)	Market share
Building Societies	17,721	1.52%
Credit Unions	34,853	2.99%
Money Market Corporations	20	0.00%
Finance Companies and General Financiers	30,208	2.59%
TOTAL BANKS	1,084,222	92.9%
- Big 4 Banks	942,925	80.8%
TOTAL OTHERS	82,802	7.10%
TOTAL	1,167,024	100%

Includes all types of loans to households including owner-occupier and investor housing, personal loans and credit cards.[15]

"It is all well and good to say switch if you're not happy, but the fact is, with the lack of competition, you are unlikely to get a better deal."

"You cannot ignore the many bank customers who are stuck with exorbitant bank fees, interest rate hikes above the RBA increases and low interest on their savings accounts. It is entirely justifiable to complain strongly when a small club of banks offer negligible competition, providing no real choice for customers who end up stuck in high cost accounts, unable to get ahead. True competition is needed, not a cosy gang of four who are owned largely by the same shareholder groups."

banking.[16] This included:

- Mandatory key fact sheets for people looking for a home loan, a ban on all mortgage exit fees from 1 July 2011, and a review into transferability of Lenders Mortgage Insurance;
- A review into the feasibility of portable bank account numbers;
- A public education initiative to promote consumer financial literacy and mobility in banking;
- Fast tracked credit card reform legislation;
- A review of ATM reforms;
- A range of support for credit unions and building societies to enable them to better challenge the major banks;
- Finance measures to enable all lenders to access new wholesale funds for mortgage lending.

CHOICE and other consumer groups welcomed the package as good for consumers, although many pointed out that these measures alone are unlikely to transform the banking sector. Much of the detail of the December 2010 package is now the subject of consultation or ongoing review. The government has confirmed that this package is not intended to be the last word in reform for banking.

Prior to that the government had introduced significant new legislation affecting the rights of consumers. This includes changes to the Australian Securities and Investments Commissions Act 2001 (ASIC Act) as part of the Australian Consumer Law and to the National Consumer Credit Protection Act 2009 as part of the Consumer Credit Protection Reform Program.

The ASIC Act continues to provide protection for consumers of banking products against misleading or deceptive conduct and unconscionable conduct. It also continues to protect against other conduct including referral selling, undue harassment or coercion and unsolicited credit cards.

Since 1 July 2010, new laws have come into effect dealing with unfair contract terms. These deal with "standard form" consumer contracts. A standard form contract is typically a contract prepared by a supplier and offered to a consumer on a "take it or leave it" approach. This includes home loan, credit card and saving account agreements.

The unfair contract laws mean that where a court or tribunal finds that a term is unfair, that particular term will be void. A term is unfair if it would cause a significant imbalance in the rights and obligations of the consumer and a bank under the contract; if it is not reasonably necessary to protect the legitimate interests of the party who would be advantaged by the term; and it would cause detriment, financial or otherwise, to a consumer if it were to be applied.

ASIC can also now apply to the courts to seek orders for the benefit of other consumers that have not been directly involved in a legal action that resulted in a contract term being declared by the courts to be unfair. This could include an order varying a contract, declaring all or part of a contract to be void or directing the bank to refund money to other consumers.

From 1 January 2011, the National Consumer Credit Protection Act introduced:

- A national licensing regime for lenders and brokers, under which they must ensure their credit activities are engaged in efficiently, honestly and fairly;
- Enhanced responsible lending obligations, under which lenders must not provide credit that is unsuitable for the consumer. That means they must: make reasonable inquiries about a person's financial situation, requirements and objectives; take reasonable steps to verify their financial situation; make an assessment about whether the credit contract is "not unsuitable" for the person (based on the inquiries and information obtained in the first two steps); and be able to provide a written copy of their assessment to the consumer.

Customer satisfaction with banking services

CHOICE has regularly surveyed our members about their banking experiences, most recently in 2010. We consider their responses important for the banking sector because CHOICE members are highly engaged with the services they buy; they are likely to have had a higher education and to be mature and relatively prosperous. In other words, they are exactly the affluent segment of the population that banks most value. They are also consumers who are most likely to be in a position to assert their consumer rights.

In our surveys CHOICE members have pointed to good service and bad, and in the past ten years the performance of the major banks appears to be improving compared to that of their smaller rivals. However, the majors consistently rank bottom in our surveys. Table 2 shows CHOICE member satisfaction scores for the key product area of transaction accounts, based on a survey carried out before consumer opinions about specific institutions became strongly influenced by the interest rate hikes of late 2010. This shows a significant gap – 25 points – between the best performer and the worst.

These results are broadly aligned with satisfaction surveys conducted by other monitors. Roy Morgan conducts regular surveys of 3,000 to 5,000 bank customers to measure satisfaction, split into consumer and small-business categories. The large banks perform poorly in both categories when compared to building societies, credit unions, and smaller banks. Although the overall satisfaction ratings reported by Roy Morgan are slightly higher than in the CHOICE surveys, the large banks still only achieve an average rating of 72 per cent for retail customers and 63 per cent for small business customers. [17]

That the smaller banks outperform the majors in customer satisfaction is also the main finding of surveys using the “net promoter score” method. This calculates the likelihood of a customer recommending a service provider to a friend; the higher the score the more likely the customer will be an advocate for that bank. Again, this is significant for banks, as nearly half of consumers say that “word of mouth is the greatest influence when making a purchase decision for a product or service”.[18] In a competitive market, a bank’s ability to deliver a quality service, and by doing so increase the likelihood

TABLE 2: CHOICE MEMBER BANKING SATISFACTION SURVEY 2010

Institution	Mean satisfaction rating, transaction accounts
Teachers Credit Union	91
Members Equity Bank	86
Credit Union Australia	83
Bendigo/Adelaide Bank	77
Suncorp Metway	72
Bankwest	72
St George	72
ANZ	69
CBA	68
NAB	66
Westpac	66

“I commenced working in the banking sector in 1953 and there were eight banks... and there was competition.”

that it will be recommended to others, would be a key driver of growth in market share. That the major banks net promoter scores are relatively low in a period when their market share has grown suggests other forces are at work – the power to acquire other banks, and customer inertia, for example.

What makes customers dissatisfied?

CHOICE members have provided many insights into what makes bank customers dissatisfied. The most common complaints include hard-to-decipher terms and conditions, fees and charges, and poor customer service. Consumers have also felt aggrieved about changes to interest rates that leave savers in uncompetitive accounts, and have questioned the time it takes for basic transactions to be completed.

Much of this is in line with findings from Canstar's regular surveys of 5,000 bank customers and published "star ratings" for customer satisfaction. Their 2010 survey noted major areas of dissatisfaction, including "bank fees, interest rate increases above the RBA rate and poor interest returns on savings". [20]

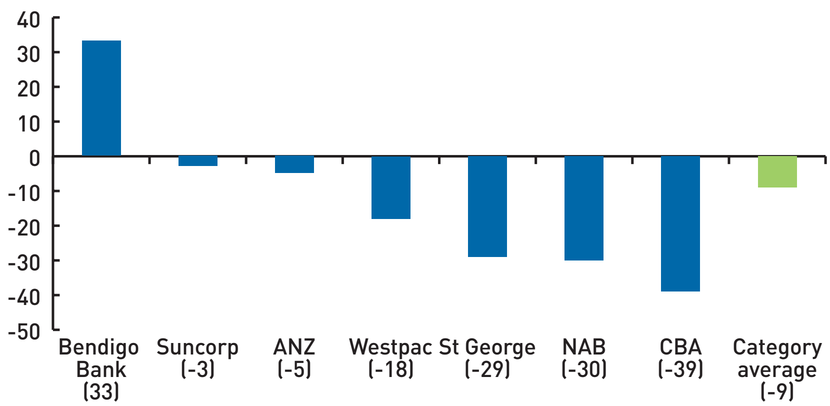
The industry-funded Financial Ombudsman Service (FOS) exists to resolve disputes between customers and service providers where customers feel their complaint has not been adequately addressed by their bank. The

SMALLER IS BETTER

Engaged Marketing published a survey in 2010 showing net promoter scores for respondents' primary financial institution. There was a tie for the top performing brand with Bank of Queensland and Bendigo Bank both achieving the highest score of 30 per cent. The overall industry average score for the category was only three per cent. In terms of categories the results are as follows:

- Building Societies are clear leaders achieving a score of 49 per cent.
- Credit Unions also achieved an excellent score of 37 per cent.
- Second Tier Banks (Bank of Queensland, Bendigo Bank, Suncorp, St George & Bankwest) jointly achieved 12 per cent.
- The Big 4 (NAB, ANZ, CBA & Westpac) achieved -21 per cent.
- Australian banks didn't fare nearly as well as US banks who achieved an average category score of 20 per cent.[19]

The graph below illustrates findings from the same source, based on a 2009 survey.



SOURCE: ENGAGED MARKETING, THE 2009 CONSUMER RECOMMENDATION & LOYALTY STUDY

FOS publishes data on the disputes it is handling, which show a huge increase in the volume of complaints primarily as a result of the economic conditions brought about by the GFC. In particular, complaints about consumer credit rose by one third in 2008/09, many related to customer difficulties with products they had been sold which they could not afford. The most significant disputes about transaction accounts centred on charges (25 per cent of disputes), transactions (25 per cent) and service (20 per cent). In 96 per cent of these cases banks were the provider, four per cent were credit unions. [21]

Consumer inertia

In the early 1990s the then Governor of the Reserve Bank observed that:

"Competition in the real world, however, seldom works in the manner described in the textbooks. There it is assumed that customers will actively play their part, and be prepared to shop around and switch their business if necessary... But in practice many borrowers are reluctant to shop around for a number of reasons, including inertia and the convenience of current "packaged" services (comprising housing loan, cheque account, credit cards and so on), reluctance to try non-traditional sources of funds, and the actual or perceived costs of switching some or all transactions from one bank to another. To the extent that customers do not shop around for individual products, however, the competitive pressure on banks is reduced." [22]

This remains true. The rate of transaction account switching in Australia remains low, and many consumers have told CHOICE that they stay with their provider for a long time, sometimes since they first opened an account whilst at school. A survey recently commissioned by CHOICE found that:

- 78.5 per cent have not even thought about switching in the last two years;
- 11.8 per cent have thought about switching and not done so;
- 7.6 per cent of people surveyed have switched bank accounts;
- The most common major reason people choose not to switch is because it takes too much effort to sort out all the paperwork (50.4 per cent);
- Not having enough time to research the best deal (48.4 per cent) and not believing they will be better off anyway (44.1 per cent) were also major reasons for not switching.
- Older people – 50 years+ - are least likely to switch (3.4 per cent).[23]

Australia Institute research in 2010 showed that 43 per cent of people banking with one of the big four banks have never considered switching to a smaller bank or credit union. [24]

Separately, CHOICE's bank customer survey in 2010 found that one in four participants said they would be more likely to switch if they could keep the same account number. Another issue identified in the 2010 CHOICE bank satisfaction survey was the hassle of setting up new passwords and PINs.

Some in the banking industry have tried to argue that these findings show high levels of consumer satisfaction with the major banks; but this is contradicted by the bank satisfaction survey data which show the opposite is true.

Recent surveys of mortgage holders have indicated a dramatic increase in the proportion of mortgage borrowers looking to switch to a new provider. A December 2010 study of more than 15,000 people with mortgages found that 23 per cent had started to look for a new lender, compared to four per cent in 2009. If the study is representative of all borrowers, about one million are looking to switch. CoreData suggest their study indicates a tipping point has been reached, as more consumers convert their anger with banks into action. More than 43 per cent of the people surveyed said the banks lifting mortgage rates

I am locked into my mortgage because I can't afford $24,000 to pay a new lender for more LMI. They tell you LMI is not transferable between lenders but when my lender was bought out by a new lender miraculously the name on the LMI policy changed to the new lender. Also if you default on the loan and the LMI is paid to the lender then [the insurer] will come after the borrower for the money, what sort of insurance is that? Basically you are paying $24,000 for the privilege of being taken to court by [the insurer] instead of your lender.

They come with the General Conditions. They come with the contract that says, "sign here". And you see there are 150 pages of General Conditions… You wouldn't understand the contract, probably not at all. But that is the main problem. You become unsure what's going on, what you are dealing with, actually.

The banks [must] become moderate community citizens instead of plunderers.

Banks need to take a good hard long look at the charges they put on Internet users. I do 97 per cent of my banking business on the internet - which, from my viewpoint, means I'm doing their job - yet I pay the same bank fees everyone else does. The only time I go to a branch is when I am unable, because of their rules, to conduct my business via the internet, and when I go to their branch I'm charged an extra fee. Also, this business of charging for the number of transactions in a world where cash is discouraged and EFTPOS is encouraged is unfair and to me, a cynical money making exercise.

I have an investment account and recently my interest rate dropped off which naturally I queried. I was advised that the interest earned on this account had decreased - how on earth can they justify a decrease in interest rates and at the same time increase interest rates on home loans - they must think we are idiots - I am sure they won't think that when I and no doubt a lot of other customers shop around for a better deal.

When [old bank] punished me for being an old loyal customer and gave new customers 0.5 per cent more interest, I opened an account with [new bank] and moved my savings. What I would like to know is where exactly my money is floating around when I transfer at 9am from [old bank] and it still hasn't arrived one day later at 2 pm at [new bank].

Bank fees for receiving a telegraphic transfer from overseas. They all charge 10 or 12 dollars for this - I can't understand how it involves them in any cost whatsoever, since the sending banks also charge a fee, and convert the money into AUD. How can they get away with charging $10 for receiving a deposit into your account just because it comes from another country?

My bank introduces new types of accounts at about 12 monthly intervals and reduces the interest paid on the existing accounts without informing customers. Once I realise that the existing account is paying a very low interest, I then have to open a new high interest account and close the old account. I find this particularly frustrating, particularly when the bank does not inform me that the interest rate on the old account has been substantially reduced (from 4.5% to 0.01%).

Overall I am happy with the product. My pet hate is monthly fees. When we first took it out about four years ago it was advertised as a free product. Turns out the "free" product was the offset account and the mortgage has a $15 monthly fee. I would change banks to get rid of this fee but that will cost me $500.

They do need to look at some of the fees. I mean you get fees on fees with some of the banks. You go over for the monthly fees or something, they charge on your overdraft and hit you with more fees on fees.

I find that front line staff, with few exceptions, are insufficiently skilled when dealing with most customer requirements. The stock answer of "it's bank policy" when dealing with complaints is seldom correct and generally reflects the branch or regional managers' attitude towards non sales related matters. Far too much emphasis is placed on up selling customers rather than retention of customers.

I have had a number of issues with service etc in the past. One was when it was time to renew our two home loans. We wanted a rep to come and see us to discuss best options. They delayed and then said they only come out to new customers. At the start of this the fixed rate was 6.00 per cent: by the time we got talking with them it had jumped to 6.5 per cent. We had to buy the wealth package to save on variable, it was 0.7 per cent which was reduced within days of us taking it out to 0.5 per cent.

> "I wish taking my business elsewhere was less complex. I believe the loyalty that has been given to our bank to build up a relationship is no longer rewarded or beneficial. We would get a better deal if we walked in off the street as a new customer, which is very disappointing."

more than the official Reserve Bank rise prompted them to actively consider changing financial institutions, while more than 16 per cent of disaffected mortgage customers were considering switching to credit unions.[25]

There are higher rates of switching in the UK: the Office of Fair Trading, the consumer protection regulator, reports that the annual rate of switching in the personal current account market was 9.2 per cent in 2009 compared to around six per cent in 2006, that around 12 per cent of consumers in 2010 had switched cash ISA (a tax exempt savings product) provider in the last year and 24 per cent of residential mortgage customers switched provider in 2010.[26]

In the Netherlands, where there is a bank switching service designed to ease movement between banks, 45,000 Dutch consumers used the service to switch their transaction accounts in 2004, its first year. In 2008, nearly 100,000 people used the service. [27] This compares to the Australian system which, according to the industry body APCA, issued 2,541 lists of regular payments to consumers in the year to September 2010. [28] The adult population of the Netherlands is 3.5 million fewer than that of Australia.

Large banks are most concerned about losing transaction account customers because it is in this pool of customers that they can most easily sell many other financial products. They therefore have little incentive to enable switching. It is also the banks who collectively control the payments system which exists to transmit money from one party to another. One respected British commentator has described this situation in banking as akin to "Google managing the internet". [29]

It is the payments system that would have to be reformed to enable easier switching through portable account numbers.

The bank industry payments body APCA states that "there is substantial and effective competition in transactional banking. There are opportunities to enhance account switching both to improve customer convenience and to enhance competition, but structural or systemic changes solely for this purpose [i.e. portable account numbers] are not justified on a cost/benefit basis". [30]

CHOICE disagrees. At present, almost all of the costs of switching are borne by consumers, including small businesses. Because this acts as a disincentive for consumers to move to a more cost-effective provider, there is a negative impact on small business efficiency and consumer welfare, which in aggregate must impose a cost on the rest of the economy. That the banking industry controls and seeks to block pro-competitive reform to such an essential part of the nation's infrastructure is remarkable. It seems inevitable that the payments system, APCA and its members will be exposed to greater scrutiny by the relevant regulators.

I’ve had a lot of trouble getting anything done when I don’t remember a new set of numbers and passwords - they seem to distance themselves from customer service and want you to do it all online - even when you go into a branch they point you to a computer!

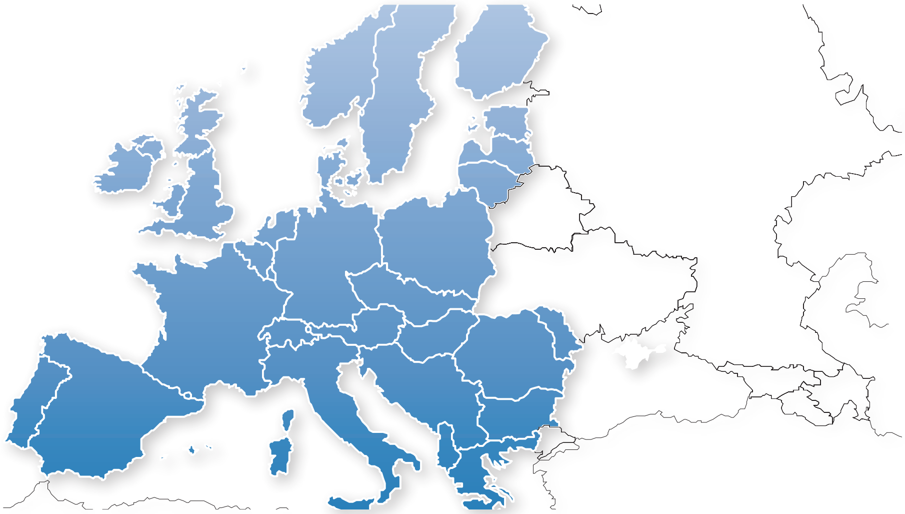
The hassles of changing to a new bank- redirecting direct debits, payments etc is all so difficult and is my main reason for staying.

I’ve finally memorised my full credit card number, PIN and two passwords/codes – it would be too hard to reset all these.

"I think it's difficult to change as I have many direct debits coming out my personal banking account - includes all bill payments including rates, insurances, mortgage, credit card - banks make it your responsibility to contact all the institutions to organize."

"All the majors appear to be much of a muchness, suggesting there is comparatively little real competition for our business. Further they all tweak offers for the short term but it's too difficult to keep switching to take advantage of the offers."

EASIER SWITCHING IN EUROPE



The "Overstapservice" (Interbank Switch Support Service) was introduced in the **Netherlands** in January 2004.[31] This works as follows: the customer completes a form at their new bank. The service begins two weeks later. For the next thirteen months all direct debits and direct credits are automatically rerouted by the customer's old bank to the new bank through a clearing house.

Any merchant that had initiated a direct debit is automatically notified by the bank of the customers new account number and asked to update their records. The customer is provided with a standard card to notify the new account number to anyone such as their employer who has a direct credit set up with their old account.

The old bank stops all standing orders and within seven working days of the service commencing provides a list of standing orders to the customer for them to forward to their new bank. After 12 months the customer receives a warning that the service will end in one month's time, after which direct debits will no longer be automatically rerouted.

The cost of the service has been estimated at €10-20 million initially and €2-3 million annually. The scheme was initially promoted in a joint brochure and nationwide advertorials, and is now integrated in the full range of bank communications on opening new accounts.

The equivalent organization to CHOICE in the Netherlands, the Dutch consumers' association (Consumentenbond) reports that this works well, and has received a positive response among users with high ratings for ease of use (in a survey of 1,500 people it was rated seven out of ten). However, Consumentenbond are clear that this system is not as effective as it might be if there were portable bank account numbers. Almost 16 per cent who used the service said there were problems; that they still had to chase things when using the service was their biggest frustration. Consumentenbond continues to campaign for portable account numbers.

In the UK, a report by the Office of Fair Trading (OFT) found that ineffective competition was caused by consumers being unwilling or unable to switch current accounts due to high switching costs. These included a cumbersome process and the strong fear of errors in transferring direct debits. [32]

The UK government-funded consumer advocacy body, Consumer Focus, reports that the OFT has made significant efforts to remedy the detriment it identified. It has sought to create a "virtuous circle" of transparency of charges, greater consumer control and efforts to improve the consumer experience of switching. It states "by giving consumers effective control over when charges are incurred; by making them more aware of the costs of their current account; and by improving confidence in switching as a means to get better value for money, [transactions account] providers will need to offer more competitive products and innovative services to attract custom". [33]

As part of the wider strategy, the OFT proposed a range of measures to improve both the switching experience for consumers and increase awareness of the benefits of switching. The OFT hoped these changes would lead to significant increases in current account switching, or consumers thinking about switching. This should in turn lead to an improvement in the current account marketplace for consumers as banks improved their products accordingly.

Specifically, the OFT agreed several reforms with the Banks Automated Clearing System (BACS), direct debit originators and industry to improve the switching process through an account switching service.

Member banks of the UK BACS payments scheme now offer a common approach when customers move their current (transaction) account to them, which they aim to complete within three weeks. At most banks the customer needs to fill in two forms – an application form and a transfer form. After that the switch is largely automated by the new bank.

Under the scheme, the new bank commits to telling the customer how the switching process works, and who is responsible for each step in the process, and how long the switching process is likely to take. When the application for a new account is approved, the new bank will ask the old bank for a list of all the direct debits and standing orders that the customer has. The old bank will provide this list within three working days of receiving the request.

The new bank will then make a copy of the list available to the customer; set up the standing orders on the new account; advise direct debit merchants of the new account details and ask them to change their records, as it remains their responsibility to maintain accurate records (in other words there is no automated redirection of payments); and ask the old bank to cancel all payments that they previously handled.

The customer has to advise their employer or pension provider and anyone else who regularly sends payments of the new account details.

The banks involved commit not to impose any charges "caused by their mistake or unnecessary delay" during the transfer process. Some banks offer an interest-free "switcher" overdraft which covers direct debits and standing orders that go through before money is paid into the new account.

Rules agreed by representatives of the **European** banking industry also aim to make the process easier. The European Banking Industry Committee (EBIC) Common Principles on Bank Account Switching set clear deadlines for the old and new bank:

- The old bank has to provide all the available information about the consumer's recurrent payments within seven banking days of a request from either the new bank or the consumer.
- The new bank has to set up recurrent payments on the new account within seven days of receiving the necessary information and will either inform third parties about the consumer's new account details or assist them in doing so.

The Common Principles apply to domestic switching of current accounts and recurring direct debits, standing orders for credit transfers and recurring credit transfers which are linked to these current accounts.

"Other reasons why I haven't changed is that it is **too much effort to know the differences** between the financial institutions and whether those differences even mean anything in the long term."

> "[My bank] charges an iniquitous one per cent 'cash handling fee' if you dare to deposit cash into your account. Hello, isn't that what banks used to do? Since when do you get charged for depositing your own money? Since that little sting, if I come into a sum of cash, I now keep it under the bed and use it up gradually, which helps keep me under my 15 transactions per month and not having to withdraw cash from an ATM."

Bank fees and charges

Consumer dissatisfaction with banking in a number of countries in recent years has revolved around the level of fees and charges people incur when carrying out the most basic, often electronic, transactions. One result has been a dramatic rise in collective legal actions to recover disproportionate overdraft charges, actions which are ongoing in Australia.

Under pressure from consumers, the big four banks have responded with fee reductions. NAB has gone furthest, removing account penalties altogether. Australian consumers can now choose a transactions account with no monthly fee, no fees for certain "everyday" transactions and no penalty fees. Some institutions allow an unlimited number of transactions without paying any fee, including ATM transactions at the bank's own network; BPAY; branch cash deposits and withdrawals; cheque facility; direct credits and debits; EFTPOS; and "pay anyone" internet transactions. Some accounts have specific conditions to waive the monthly fee – commonly, to make a regular monthly deposit of at least $2,000.

But even with the best accounts, not all services are free and interest usually is not paid. All accounts charge fees to use debit cards for cash withdrawals and purchases overseas.

Of the major banks, ANZ and Commonwealth have yet to introduce an account with an avoidable monthly fee for standard customers (though like most banks, they offer low-cost basic accounts for pensioners and other low income groups and in some cases as part of home loan packages).

Statistics released by the Reserve Bank[34] show that major banks have also recouped the income they lost after cutting transaction account penalty fees, such as overdrawn account fees and direct debit dishonours, with new penalty fee revenue from credit cards and personal loans. Income from penalties, known in the industry as "exception fees", has been maintained at approximately $1 billion per year. According to the RBA, "there was a shift in household exception fee income away from deposit accounts towards loans... exception fees on credit cards continue to make up the largest share of exception fees paid by households, growing by 10 per cent over the past year. Exception fees on personal loans also grew significantly".

Overall, bank fee income (including penalties) from households increased by three per cent to $5 billion in the year to 30 June 2009. Table 4, below, shows this was due to housing loan fee income increasing by 17 per cent, which was much higher than the average annual growth of 7 per cent recorded between 2003 and 2008, and broadly in line with growth in housing lending. According to the RBA, the increase in housing fee income was "driven by establishment and early exit fees, with the available

TABLE 3: PENALTY FEE INCOME FROM HOUSEHOLDS ($MILLION)

	2008	2009	Annual growth
Deposit accounts	516	476	-8%
- transaction	503	465	-8%
- other deposits	13	11	-13%
Loans	493	536	9%
- housing	45	42	-6%
- personal	21	24	13%
- credit cards	427	470	10%
Total	1,009	1,012	0.3%

Source: RBA

information suggesting that break fees on fixed-rate loans accounted for a significant proportion of the overall growth in fees... fee income from personal loans grew by 14 per cent, which is attributable to both an increase in account-servicing fees and an increase in exception fees".

Many people have complained to CHOICE about ATM fees. Substantial public opposition to the fees was found in a recent survey by the Australia Institute, which indicates that the great majority of Australians (82 per cent) believe it is unfair for banks to charge $2 to use their ATMs.[35]

Consumers are dissatisfied despite regulatory intervention. A key reform in March 2009 was the abolition of interchange fees by which banks charged each other for their customers ATM use, and the introduction of direct charging for the use of an ATM at the time of the transaction. The reforms mandated that the direct charge be displayed to customers prior to them completing the transaction. These reforms increased transparency of ATM fees as cardholders see the ATM fee at the time of the transaction, rather than when they receive their account statement. The reforms also included a number of industry measures to make it easier for potential competitors to access the ATM system.

The 2009 reforms have led to an overall reduction in total ATM fees paid in Australia, as consumers changed their transaction payments (withdrawing more cash, using specific network ATMs) and banks offered fee free use of ATMs for their own networks. Smaller institutions banded together to offer reasonable sized ATM networks, allowing their consumers to also avoid fees.

In the year following the reforms, the use of foreign-bank ATMs (that is ATMs provided by banks other than a consumer's own bank) fell 18 per cent, delivering consumer savings of some $120 million. But the price of many ATM transactions has not fallen and Australians are still paying an estimated $750 million per year in foreign-bank ATM fees.[36]

Australia Institute survey findings also show that young people bear a disproportionate burden of ATM fees. One in four survey respondents (26 per cent) reported paying a $2 ATM fee at least once in the past week, but some 40 per cent of those aged between 18 and 24 years paid an ATM fee.

At the time of the 2009 reforms, CHOICE and other consumer organisations warned that these might have a negative impact on low income and disadvantaged consumers, particularly in remote and regional areas. The government and regulators promised that the impact of the reforms would be closely monitored, and that any price exploitation of disadvantaged consumers would be addressed.

In practice, the RBA's monitoring of the

"Dear Choice, thank you for raising the focus on banking practices. **My biggest beef is the $2 fee charged for using ATM's** that are other than your own banks. I can appreciate there might be **a need for some type of administration fee, but $2 is way over the mark."**

TABLE 4: BANK FEE INCOME FROM HOUSEHOLDS ($MILLION)

	2007	2008	2009	Growth 2009	Average growth 03-08
Housing loans	997	1057	1235	17%	7%
Personal loans	445	485	552	14%	11%
Credit cards	1,199	1,332	1,434	8%	17%
Deposits	1,797	1,918	1,713	-11%	6%
Other fees	87	107	97	-9%	9%
Total	4,525	4,890	5,032	3%	9%

Source: RBA

"The transactions are all processed electronically, with little if any human intervention, so the banks are just making a fortune out of millions of consumers for minimal actual work done by them. Please raise this as the next burning issue for banks to be accountable for."

ATM reforms turned out to be minimal. The annual review published in mid 2010 was based on high level monitoring of average transactions and the overall total volume of transactions. The review reported that the reforms were a complete success and did not identify a single issue of concern.[37]

In contrast, a review by the Australian Financial Counselling and Credit Reform Association (AFCCRA) in November 2010 looked at the impact of the ATM reforms on individuals in regional and remote communities (particularly indigenous consumers). [38]

That report found a wide range of significant consumer issues, including:

- The cost of ATM fees is having a significant and detrimental impact on indigenous people living in remote communities.
- Indigenous consumers have no choice but to use the single ATM in a remote community. All ATMs charge fees and these are impossible to avoid. It commonly costs $2.00/$2.50 per transaction to check an account balance. Many people check their balances multiple times on the day a Centrelink payment is due.
- ATM fees of $20 - $40 are commonly incurred by people on the day Centrelink payments are due. As well, indigenous consumers are more likely to withdraw small amounts of cash and so incur more fees. This can occur for budgeting reasons, for cultural reasons or because food storage in some remote communities is problematic.
- Community stores also charge fees of $2.00 per EFTPOS transaction, so this alternative source of cash withdrawal, one used by many people in Australia, is not available.
- There is one community where the ATM fee is $10.00 per transaction. One trader charges an EFTPOS fee of $5.00 per $50.00.

This report highlights two significant problems with the ATM reforms. Firstly, the reforms are having a disproportionate impact on low income and vulnerable consumers (as predicted by consumer organisations). Secondly, the RBA monitoring of the impact of the reforms is inadequate, as none of these issues were identified by the RBA's high level economic review.

TECHNOLOGY DRIVING SMARTER, SIMPLER BANKING

There is growing evidence of the impact that information technology will have on the retail banking industry.

Banks are now increasingly dealing with highly empowered individuals who expect and demand a new age of customer service. As in other sectors of retail, customers are able to ruthlessly select the channel and interaction that gets them to a solution swiftly, in the most efficient manner.

Brett King argues that consumers are arriving at a point where "overall expectations of my service providers in the finance sector have been lifted to where I now expect an element of self-control, efficiency and choice that I didn't have available to me previously. This then moves from being a nice change of pace to becoming a driver of choice and selection, and I penalise providers who aren't able to provide me with this flexibility and level of control and empowerment".[39]

This is centred on the internet, smart phones and mobile payments. King believes that the key learning from the new wave of technology innovation is that "if banks are not introducing innovations into the customer experience, at the same rate with which customers are adopting these new technologies, banks are at a considerable disadvantage and risk losing customers as more agile intermediaries and third parties capture the benefit of the innovation".

Early adopters of technology have decisively moved on from the rules and structures that banks have created in the past.

A shift seems to be taking place from the open internet to semi-closed platforms such as Facebook, itunes, and Skype, where the major search engines such as Google cannot extend their influence, fuelled by the arrival of the iphone and smartphone model of mobile computing. In this new reality, screens (or applications) come to the customer rather than the customer going to the screen.

The time when mobile payments go mainstream is probably closer than banks think.

Companies like MoBank in the UK, aspiring to become a banking alternative, recognise that customers are ready for more than smart mobile banking applications, and aim to provide the payments and activities consumers demand whenever and wherever they need it.

Zopa.com is an online financial network. Through Zopa, borrowers get access to lower rates and investors higher deposit rates than those available through the banks. Zopa connects people who enter into an agreement that looks like a traditional personal loan, bypassing the need for a banking license. In exchange, they take a small fee.

It is likely that this social networking will be the source of the biggest challenge to retail banks because of the vast amount of information providers already have on customers and the capacity online social networks have to provide alternative banking services.

For exemple, it is only a matter of time before Facebook has an unparalleled amount of information on over a billion people. Its ability to anticipate customer needs and to help companies disseminate more efficient, competing banking solutions amongst its members, will make it a force to be reckoned with.

It is through social networking that the old foundations of trust built between customers and retail banks are also under attack. The new breed of information technology platforms that have arisen take transparency to a new level. Banks cannot generate the same level of trust that platforms such as Facebook do intrinsically, because the platforms were built with the ability to harness our most trusted contacts – friends and family and in turn their networks.

Facebook's COO argues that "ultimately 20-30 per cent of Facebook revenues will come through the sales of virtual goods or the operation of an on-site currency".[40] Facebook will undoubtedly become a platform from which new companies will challenge the dominance of today's transactions and payment platforms.

In summary, to become organisations that can anticipate customer needs and deliver a very high degree of customer satisfaction, banks must keep up with today's technology and customers. Being the bank is not enough anymore: the bank needs to work for the customer. That is the new reality. Unless retail banks can work with these new technological platforms and exceed customer experience, they will be left behind.

PART 2: THE BANKING AUSTRALIANS NEED

"I joined a company that had a staff credit union. I immediately ditched the banks and gave them a go. Although the credit union hasn't always led with new products and services, they haven't been far behind either. If you are looking for a fair go, respect and competitive banking products, there are alternatives out there."

CHOICE believes that the absolute key to driving improved service in retail banking is increasing customer mobility within a fairer playing field. Improving mobility depends on the government and regulators looking across the board at barriers to switching key products and services, and overcoming industry opposition to measures that would put consumers in the driving seat.

A fairer playing field itself would be characterised by greater proportionality, transparency and disclosure in products, contracts and charges, and oversight of the system aimed at improving the culture and governance of banking as well as securing a stable and competitive system. On such a playing field, with banks genuinely competing on the basis of the quality of products and services, all the players would be "forced to become efficient and offer greater choice of products and services at lower prices... [giving] rise to increased consumer welfare and allocative efficiency". This vision of competition in banking also includes "the concept of 'dynamic efficiency' by which firms engage in innovation and foster technological change and progress". [41]

I switched, it was quite difficult. I think the banks, a lot of the big banks, deliberately make it that way. But it was difficult getting accounts closed from the old bank. It wasn't difficult to open a new account because the new bank, were quite happy to basically do it for me as long as they had a signature. But certainly, the older banks were fairly reluctant in closing accounts although there wasn't ever any question asked why you're doing this. So therefore, we need account numbers which can be portable and forms cut down, the number of forms cut down to make it much easier, I'd say.

Surely, we can have bank accounts that are portable. Just like phone accounts are portable. I saw in the paper this morning, only five per cent of Australians do actually walk with their feet between banks when they're dissatisfied. And that's an agonizing low number. I think we're much more proactive. And walk with our feet if we're not happy. Just as if we're not happy with our phone company, we walk. If I was going to walk from the big bank, I wouldn't be walking to another big bank. I'd be walking to one of the second tier banks or a credit union, who I believe are much more interested in individuals than corporations.

As noted above, the banking industry has attempted to blame the GFC on "too much competition".[42] But it was the erosion of values at senior levels in banking over a number of years in many parts of the world and the aggressive pursuit of short-term gains that has led to the collapse of consumer confidence in banking. Rebuilding trust in banking will require a reversal of the culture and ethics that put short-term risk-taking above stability, customer service and community. This is not merely a matter of better communicating with customers.

Improving bank customer mobility

We can learn from the experience of other sectors in addressing concerns about customer mobility.

In the telecommunications sector competition has been enhanced by allowing complete number portability for mobile phones. After an initial period of industry resistance, followed by a reasonable transition period, consumers can now keep a permanent mobile phone number, while still being able to enjoy the full benefits of competition amongst network providers. This has allowed consumers to switch from networks that have provided poor service or uncompetitive pricing. It has also helped consumers when they have moved to geographic areas where their original network may not provide the best service.

Similarly, in the superannuation sector, reforms have been introduced to increase customer mobility. Over time the sector had developed a number of barriers to portability, resulting in serious problems such as lost and multiple accounts. The introduction of choice and portability requirements in the superannuation sector now allows consumers to consolidate all of their holdings in a single account, and to change providers in search of better service or pricing. Reforms to be introduced in 2011 will further enhance customer mobility, by allowing lost and multiple accounts to be consolidated using a single identifier (in this case, the Tax File Number).

By far the best prospect for increasing mobility and competition in the banking sector is the potential introduction of portable account numbers. These would be extremely popular with consumers and they would enhance consumers' ability to "shop" for better deals. The onus would then be on institutions to improve customer service, provide better information about their products and make their pricing more sensitive to retain existing customers, rather than relying on barriers to switching.

The banks have raised two initial objections to the introduction of portable account numbers:

- The banks argue that the introduction of portable account numbers raises significant technical challenges, and that system changes will be time consuming and expensive; and
- The banks argue that the presence of portable account numbers might have an impact on liquidity requirements and may be detrimental to confidence in any institution during a crisis (as consumers can withdraw their business more easily).

While both of these constraints will need to be addressed, they are not so significant that they cannot be overcome during the development of portable account numbers. The initial costs of introducing number portability in the telecommunications sector were quickly absorbed by industry, and are far outweighed by the efficiency gains delivered by improved competition in that sector. A similar result is likely in the banking sector.

Any concerns about a "flood" of consumers leaving a particular institution during a crisis appear to be overstated. Consumers are already able to withdraw their funds immediately during a crisis, so the impact of account portability is likely to be marginal. Consumers are far more likely to withdraw funds than switch accounts following the early signs of any potential bank failure. And even this potential effect is countered by the government's guarantee of deposit balances, which presently extends up to $1 million per customer per institution.

RECOMMENDATION 1

INTRODUCTION OF PORTABLE ACCOUNT NUMBERS

CHOICE recommends that we learn from improvements in customer mobility in other sectors (including telecommunications and superannuation) and introduce portable bank account numbers in Australia. This will reduce barriers to switching institutions and improve competition and efficiency in the sector.

"Competition is what's needed and so I would like the politicians to do everything they possibly can, be it legislation, be it creating facilities, whatever to make switching as easy as possible."

> "We are in the process of leaving one of the pillars that has outgrown the traditional Australian sense of being humble and understanding the 'fair go' attitude. They are making life very difficult. Minute details on the forms cause the bank to stop the settlement process and leave it hanging for days. The onus is on me to keep the process moving. When I call them I am placed in very lengthy delays - there must not be a lot of staff in the 'close home loan' department. Statements are suddenly costing me money each time I request them."

RECOMMENDATION 2

A PERMANENT CONSUMER DEPOSIT GUARANTEE

To maintain consumer confidence in all banking institutions, whatever their size, the consumer deposit guarantee should remain in place permanently at a level that recognises the international best practices in this area. To promote understanding and confidence, the government should consider applying the guarantee to each brand rather than each institution, and ensure the guarantee is properly explained to consumers in a consistent way, on all relevant banking products.

Ensuring confidence in banking

In Europe, governments recognized the vulnerability of banks to "bank runs" – the situation that occurred during the GFC when bank account holders believed that their savings were not safe and tried to withdraw them all at the same time. Since 1994, a Directive (94/19/EC) has required that all European Member States have in place a safety net for bank account holders. If a bank is closed down, national Deposit Guarantee Schemes are to reimburse account holders of the bank up to a certain coverage level.

The European Commission has now amended these rules for bank customers across Europe to have their deposits protected up to Euro 100,000 per institution. Consumers must receive their money back within seven days and are provided with better, standardized information about this on their account statements. [43]

The government has announced that it is reviewing the coverage of the Australian consumer bank deposit guarantee. In the absence of the guarantee, consumers would be likely to believe the major banks are more secure and as a consequence be less confident about switching to or remaining with smaller institutions, especially mutuals such as credit unions and building societies. To avoid handing such an additional competitive advantage to the largest banks, the consumer deposit guarantee should remain in place permanently at a level that recognises the international best practices in this area.

CHOICE is concerned that consumers may be confused about whether their deposits are covered when they are held by different bank brands but within a single institution. To promote understanding and confidence, the government should consider applying the guarantee to each brand rather than each institution, and ensure the guarantee is properly explained to consumers in a consistent way, on all relevant banking products.

Easier switching of home loan products

In addition to promoting customer mobility in relation to transaction accounts, it is important to enhance mobility in relation to home loan products.

The key barriers to customer mobility in home loan products are entry and exit fees and Lenders Mortgage Insurance. Paperwork and stamp duty are also disincentives to switching, although the amount of paperwork is improving and stamp duty on the mortgage documentation (as opposed to stamp duty on the property purchase) is a relatively small amount.

Entry and exit fees are the subject of current reform proposals in Australia and there has recently been some movement among providers, with two of the major banks scrapping exit fees (ANZ and NAB). The Treasury has committed to boosting consumer flexibility to transfer mortgages, and is "accelerating its development of potential frameworks to allow consumers to avoid lender fees, as well as mortgage discharge and re-establishment costs, through the introduction of a central repository to hold all mortgages so that refinancing a mortgage would not involve a borrower discharging and reinstating their mortgage".[44]

CHOICE strongly supports the abolition of exit fees proposed by the government. It is important that in implementing this, the regulator bears down on any attempts by the industry to shift disproportionate fees to entry charges or service charges throughout the lifetime of a loan. To ensure transparency in this area, the regulator should carry out and publish an annual review of progress in implementation. We also strongly support other potential steps to make the transfer of mortgages seamless, once the relevant credit checks have been carried out by the new lender, for example by reducing the amount of repeat paperwork required.

CHOICE members have pointed to Lenders Mortgage Insurance (LMI) as a significant barrier to switching home loans.

One of the biggest costs / obstacles to refinancing a home loan is the cost of paying Lenders Mortgage Insurance. LMI generally costs thousands of dollars and, unlike most other insurances, no credit is given for the unused portion of the previous loan LMI. The LMI insurers and banks have a very cosy arrangement indeed and neither of them is willing to change the current unfair system, so laws should be introduced to make LMI fairer and more flexible - to support easy refinancing.

Lenders Mortgage Insurance is required in a reasonable proportion of loans, especially for first home purchasers. However, it is a product that has many peculiar features. The beneficiary of the insurance is the lending institution, not the consumer, but the consumer pays the premium (often borrowing this amount from the lender). The insurance technically covers default during the entire life of the loan (25-30 years) but the premium is paid in a single up-front lump sum.

If a consumer considers switching to another lender, they may find that they have paid a large up-front sum for an insurance product that has provided no benefit. The premium will not be rebated despite only using a fraction of its cover. This "lost money" becomes a significant barrier and disincentive to switching.

Lenders mortgage insurance is a product that requires a significant review. Ideally, the product would either be portable (for consumers) or it would be part of the bank's annual cost, and passed on to the consumer in a fair and transparent way. The entire

RECOMMENDATION 3

REMOVAL OF BARRIERS TO SWITCHING HOME LOAN PRODUCTS

CHOICE strongly supports moves to make it easier for consumers to move their mortgage, including a ban on mortgage exit fees provided this comes with action by the regulator to ensure unfair fees do not emerge elsewhere in the system. CHOICE recommends a comprehensive review of Lenders Mortgage Insurance to ensure that it does not remain a barrier to switching home loans. And we urge the government to find further ways to make the entire process of mortgage switching as seamless as possible by cutting the paperwork required.

"Either way you look at it, the difficulty involved in switching banks for people with a mortgage is staggering. Even the bank I switched to made my life difficult, although I suspect an element of this was the staff I dealt with. There is just no ownership or accountability taken by individuals. The fact that I did not talk with, nor deal with, the same person at the same branch over the course of weeks in switching my bank and mortgage annoyed the hell out of me. Having said that, I am now in receipt of an approximately 40 per cent discount on part of my loan, over two thirds of the loan life."

"I've been trying to do a top up and fixed rate mortgage though my 'relationship' manager at the bank. It's been two weeks since he received my paperwork and over a week since he returned a call or email. The bank won't let me deal directly with their call centre due to size of account but the 'relationship' manager doesn't return my messages. I honestly want to change banks but I hear horror stories about all of them! Plus I'll have to start the whole process again with a new bank. Paperwork, time on phone, emails. No wonder people don't switch. Why can't a bank make it easier to take another bank's mortgage on?"

product needs an overhaul if it is to serve the future needs of consumers, and avoid remaining a barrier to switching.

Tackling unfairness in ATM fees

It is essential that affordable payment systems are available to all consumers. There should be an obligation on the banking sector to deliver affordable basic services to all sections of the community – not just the wealthy. The 2009 ATM reforms have clearly failed to address the needs of remote communities, and several key changes are required to ensure equality in the provision of payment services across Australia.

First, fees should not be charged for on-screen balance inquiries. Especially in communities where there is no other way to check balances, these fees are inequitable. Fees for balance inquiries range from 50c to $2.50, indicating that they are unlikely to bear any relation to costs. An on-screen balance inquiry uses a minimum of resources, as there is no requirement for paper, ink, security or cash handling. As interchange fees are prohibited, the actual costs to operators must be very small. Many balance inquiries will obviously result in a withdrawal, and the withdrawal will help recoup the minimal costs of balance inquiries.

Improved disclosure of ATM fees

Disclosure of ATM fees is still inadequate for many consumers. It can be difficult for consumers to identify an expensive ATM before they have queued up, inserted their card and PIN, and selected a transaction. The "price signal" therefore occurs very late in the transaction process, and some consumers will be unwilling to abandon the transaction and queue elsewhere.

The result is that the price signal is ineffective, and this reduces any downward pressure on ATM pricing.

To address this issue, all ATMs should carry some clear information regarding pricing on the exterior of the machine. Typical examples might include:

This machine is privately owned and costs $2.50 for a withdrawal for ALL card holders; or *This machine is part of the XYZ bank network and is free for members of that network. All other cardholders will be charged $2.50 for a withdrawal.*

This external disclosure will have the dual benefit of informing consumers and putting downward pressure on ATM fees.

It is also essential that improvements are made to the branding and network membership of ATMs. While the majority of ATMs can be clearly identified as belonging to a specific bank or network, there are still examples of ATMs where the brand and network are obscure. For example, a large number of Bank of Queensland branded ATMs are in fact operated by the independent company, Customers Ltd, and customers incur different charges when using these ATMs compared to traditional Bank of Queensland ATMs. [45]

Access to payment systems

In the UK, 57 per cent of around 58,000 ATMs are free of charge to any customer. Typically these free machines are found in locations attracting a high volume of transactions such as in bank branches. As in Australia prior to the 2009 reforms, interchange fees are paid by the customer's bank. Charging ATMs handle only around five per cent of withdrawals, revealing a strong consumer preference for free withdrawals. In response to concerns about the lack of machines in certain areas, the UK government, industry and consumer groups agreed on a scheme of financial support for cash machine operators to expand into low-income areas, which by June 2009 resulted in the installation of an additional 601 free cash machines serving 1.5 million consumers. [46]

In Australia there should be a clear recognition that all communities have a right to access affordable payment services. In regional and remote indigenous communities, where income and opportunities are sometimes limited, it is essential that income is not depleted by

RECOMMENDATION 4

REMOVAL OF ATM FEES FOR ON-SCREEN BALANCE INQUIRIES AND IMPROVED DISCLOSURE OF OTHER ATM FEES

CHOICE recommends the removal of ATM fees charged for on-screen balance inquiries. Regulators should also require banks to meet a new, improved standard of external disclosure on ATMs, including the external disclosure of typical fees, and much clearer information on ATM brand and network membership.

expensive payment systems.

Where banks are providing accounts and services to the local community and local businesses, they should have an obligation to ensure that local consumers can gain affordable and secure access to their funds. As the banks gain the benefit of the accounts, deposits, loans and transaction business in that community, they are also responsible for ensuring access.

Currently, some remote communities are only served by private ATM operators. However, the banking sector needs to find a way to ensure that the fees collected by private operators do not have a detrimental impact on these local communities. This could be through a system of fee rebates or through the provision of alternative ATMs or other payment systems.

Better product information

CHOICE supports pro-active initiatives by regulators and banks that will deliver specific improved outcomes for consumers in relation to customer service, customer mobility and competition. But we do not believe that the significant issues in the sector can be addressed by improved disclosure alone. Disclosure has delivered limited improvements to consumers in the past, and has a poor record of addressing concerns for low income

RECOMMENDATION 5

AN OBLIGATION ON BANKS TO PROVIDE AFFORDABLE ACCESS TO PAYMENT SYSTEMS

The banking sector should have an obligation to ensure that all communities have access to affordable payment services. Banks should take urgent steps to ensure that this obligation is met through solutions such as community fee rebates, the introduction of alternative ATMs or the provision of alternative access to the payment system. CHOICE will support collective initiatives by the banks on this issue, subject to authorisation by the ACCC. To enable this to be effectively monitored, regulators should also collect and publish regular information on the location, costs and revenue generated by ATMs.

and disadvantaged consumers.

A general problem is the complexity of product information for consumers. The regulators and industry should work together with consumers to find ways to simplify, and write in plain language, explanations of terms and conditions so that consumers are more likely to read them and understand them.

We have already addressed disclosure in relation to ATMs. The following sections outline other areas of specific product information that do require further reform, especially where these will aid increased switching.

Improved disclosure for credit products

Significant improvements are required in the disclosure of the true costs of some credit products, particularly credit cards and mortgages. These products are complex and the costs include multiple fees and interest rates that may vary for

> "You get rid of exit fees, they'll bring in an establishment fee. If you get rid of penalty fees, they'll put up interest rates. And that is how our banking system is run in Australia."

"Banking should be made more transparent to people so that they understand what's going on. I don't understand it anymore. I need a lawyer, probably, when I want to deal with the bank. That's the biggest problem I see."

different periods or transaction types. Key improvements that are required include:

- An annual statement of the cost of any credit product, either electronic or paper, so that the consumer has a clear understanding of the cost of their credit in that year and the ongoing cost.
- Provision of a mandatory summary sheet for all mortgages that allows easy side by side comparison of key features and costs. The important comparative items here are the inclusion of a comparison rate based on a standard scenario, and the provision of a "total cost" covering the full repayment over the expected life of the loan. The Treasury is consulting on the possible introduction of such a key facts sheet.
- Provision of a repayment time on credit card statements and estimated total cost if the consumer is to repay only the minimum repayment. This will inform the consumer of the true costs of using the credit card and may also encourage more rapid repayments.
- The introduction of better information and mandatory warnings on credit card products for the most expensive transactions – cash advances. The warning should appear on any credit card statement where a cash advance has been included, instructing the consumer that such transactions are an expensive way to obtain cash and showing the total costs for the cash advance (combining the fees and the extra interest charged for the advance).
- The introduction of a new mandatory comparison rate for all credit cards. This initiative has been resisted by industry for many years but it is now essential that consumers are able to compare the costs of credit card products. This may also lead to some downward pressure on fees and interest rates. The comparison rate should include a simple scenario (similar to the mortgage comparison rate) and be displayed as X% (purchases) and Y% (cash advances). The comparison rate should incorporate typical annual fees and loyalty program fees.
- Clearer disclosure in advertising that credit card interest rates are variable, and that they may move many times during the life of the credit card. The word "variable" or abbreviation "var" should appear after any use of interest rates in the marketing of credit cards.

RECOMMENDATION 6

IMPROVED DISCLOSURE FOR ALL CREDIT PRODUCTS

Regulators should require banks to meet a new, improved standard of disclosure for credit products, in plain language, including:

- An annual statement of the cost of credit including all charges;
- Mandatory summary sheet for all mortgages that includes the total cost of repayments;
- Repayment time on credit card statements if the consumer is to repay only the minimum repayment;
- Better information and mandatory warnings for credit card cash advances;
- Introduction of a new mandatory comparison rate for all credit cards; and
- Clearer disclosure in advertising that credit card interest rates are variable.

Improved disclosure for other banking products

Some additional improvements are required for other banking products. Specific initiatives should include:

- The introduction of a comparison rate for savings products is essential as these products have become very confusing. For example, it is now very difficult to compare the interest that could be earned amongst the myriad of term deposits available. Interest may

"There's too much documentation, we need more simple English so that everyone can understand it."

be paid monthly or at maturity, or it may be reinvested and compounded. This is rarely disclosed in the initial marketing of term deposits making it difficult for consumers to compare products. The "headline" interest that is advertised should be complemented by a comparison rate in brackets that is based on a typical savings scenario. This would apply to term deposits and specific savings accounts (e.g. high interest online accounts). It may not be necessary for all accounts (e.g. transaction accounts).

- Specific prohibitions should be introduced for some forms of misleading marketing in relation to savings accounts, for example products that advertise a high headline rate of interest where that rate only applies once a minimum balance is reached. This could be addressed in part by the introduction of a comparison rate, but may require an additional pro-active prohibition. Consumers must be able to compare accounts free from misleading information.
- Regulators should undertake a complete and total overhaul of disclosure documentation and information provided to consumers regarding lenders mortgage insurance. This is one of the most expensive products in the sector, requiring up-front payment by the consumer, yet it is the subject of minimal disclosure. It is often unclear to the consumer whether or not the product is required, who the provider is, what the true costs of the product is, whether or not the costs will be added to the loan, what the insurance covers, the length of coverage, the beneficiary of the product, the availability of any alternatives (or alternative providers) and the availability of any internal or external dispute resolution service. Insurance is also currently excluded from legislation prohibiting unfair terms in contracts; the government should bring insurance into the legislation without any further delay.

RECOMMENDATION 7

IMPROVED DISCLOSURE FOR OTHER BANKING PRODUCTS

Regulators should require banks to meet a new, improved standard of disclosure for some other banking products, including:

- Mandatory comparison rates for term deposits and savings products;
- Prohibition on certain types of misleading marketing for savings products; and
- A comprehensive overhaul of disclosure documentation for Lenders Mortgage Insurance.

Measures to improve customer service

A key missing ingredient in the regulation of banking in Australia is that we have no tools available to monitor and address systemic customer concerns and issues. While individual consumers may take a complaint to their own bank, sometimes followed by a complaint to the Financial Ombudsman Service (FOS), there is no history of regulators intervening to address key systemic issues.

For example, the issue of unfair penalty fees was never addressed by regulators, despite numerous individual complaints, and numerous attempts by consumer advocacy organisations to seek a regulatory response. Ultimately this major issue has ended up being addressed by private and collective action in the courts. Similarly, there has been no regulatory intervention when consumers have suffered from massive technical failures in the banking system, such as the loss and deletion of transaction histories by NAB in 2010, or the widespread delay in mortgage settlements amongst the big four banks in 2008 and 2009.

Relying on individual consumers to

"I used to write corporate policy [documents]. We might have some really detailed policies with really complex information in them. But we had to simplify them to a level that the employees understood and make them simple English. Every single clause, you had to go through and make sure that it was able to be explained. I think it was Grade 4, in Primary School, level. So every person could understand and would not misinterpret that clause. And therefore, the banks could follow the policy. Their terms and conditions are just too complex and they're written in, I guess, lawyer speak as opposed to consumer speak. And that would be a big difference if they were actually forced to provide that."

> "It's hard to know whether you're getting value for money or an 'improved' product because of banking jargon, changing rates, limited-time-only special offers and inability to compare products on a like-for-like basis."

pursue specific complaints, or relying on expensive private litigation, will not achieve sector-wide improvements in customer service. CHOICE submits that a radical overhaul of bank regulation is required to ensure that systemic issues can be identified and addressed, resulting in significant improvements in customer service.

There are a number of key regulatory tools that are required.

Publication of complaints statistics that name the institution

The Financial Ombudsman Service (FOS) and the Australian Securities and Investments Commission (ASIC) are the two organisations most likely to receive a complaint about banking customer service. However, neither organisation has any obligation to name the institutions that are the subject of complaints, and no such information is made available to the public.

This is in contrast to other regulatory regimes, such as the Telecommunications Industry Ombudsman (TIO) and some of the energy complaints schemes. For example, the TIO publishes the number of complaints received in each category in a table that names the institutions responsible for the complaints. This has allowed regulators, government agencies and consumer organisations to identify and address systemic issues. For example, a spike in complaints relating to billing issues was identified at OneTel that resulted in regulatory intervention. Recent spikes in complaints relating to service have been noted at Telstra and VodaFone, resulting in new service initiatives at both companies, and greater regulatory scrutiny. No such information is available in the banking sector.

Recognition of "super-complaints"

A more innovative approach to complaints in the banking sector may also be required, particularly in relation to systemic problems. CHOICE believes it is time to introduce a system of super-complaints – similar to the model operating in the UK (see box p.38). Super-complaints are made by designated consumer bodies to consumer regulators, who must make a considered response within ninety days to properly investigated complaints.

The super-complaint mechanism is not intended for complaints about matters that can be handled directly by existing enforcement powers or complaints resolution agencies, particularly single-firm conduct. In that regard super-complaints would neither replace nor crowd-out standard complaint processes in the banking sector. Instead, the super-complaint mechanism enables consumer groups to bring to the attention of the regulator market features harming the interests of consumers.

RECOMMENDATION 8

PUBLICATION OF COMPLAINTS STATISTICS THAT NAME INSTITUTIONS

FOS and/or ASIC should publish a regular table (at least quarterly) showing complaints received by category, and identifying the institution responsible. This information should be used to monitor and identify systemic issues.

Greater regulatory intervention in systemic issues

At present there appears to be little interest by the key regulators in intervening in systemic issues in the banking sector. In recent years a number of major systemic issues have been virtually ignored by regulators, resulting in significant consumer detriment. Key examples include:

- No regulatory intervention in relation to unfair penalty fees charged by the

RECOMMENDATION 9

INTRODUCTION OF A SUPER-COMPLAINTS MECHANISM

Dispute resolution in the banking sector should be aligned with best practice in co-regulation. A super-complaints mechanism should be introduced to enable consumer organisations and dispute resolution providers to formally raise significant issues directly with the regulator.

banks and card companies;

- No regulatory intervention in relation to slow and delayed mortgage settlement times;
- No regulatory intervention in relation to significant technical issues, such as the loss of transaction histories or service outages; and
- No regulatory intervention in relation to over-charging following the RBA payment system reforms (e.g. credit card surcharges, ATM fees).

It is important for the key banking regulators to take a much more pro-active role in monitoring and addressing systemic customer service issues in the banking sector.

This could be achieved by the regulators being required to publish a regular report that analyses current complaints in the sector and that lists any systemic issues and notes the steps being taken to address those issues. The key regulators would include ASIC and the RBA (in relation to payment system matters), perhaps with input from the Financial Ombudsman Service. The report could summarise the overall number of complaints, any patterns or spikes in the complaints data, plus provide commentary on any other data or indicators of customer satisfaction. A register of systemic issues could be maintained so that the public can monitor how these issues are being addressed.

A specialist watchdog

There is a strong case for a specialist consumer watchdog to represent the consumer interest in financial services issues, including retail banking and superannuation.

The superannuation system, for example, is complex and is the subject of constant changes through government reforms, technology and new product features. However, the interests of superannuation members (consumers) are not represented by a specialist consumer organisation or service. There have been requests made to the government to fund the establishment of a superannuation consumer representative organisation

RECOMMENDATION 10

INTRODUCTION OF A SYSTEMIC ISSUES REGISTER

Regulators should be tasked with monitoring and identifying systemic issues in the banking sector in a more proactive way. Regulators should (jointly) publish a regular report on complaint patterns and trends, and maintain a public register of systemic issues noting how each issue is being addressed.

RECOMMENDATION 11

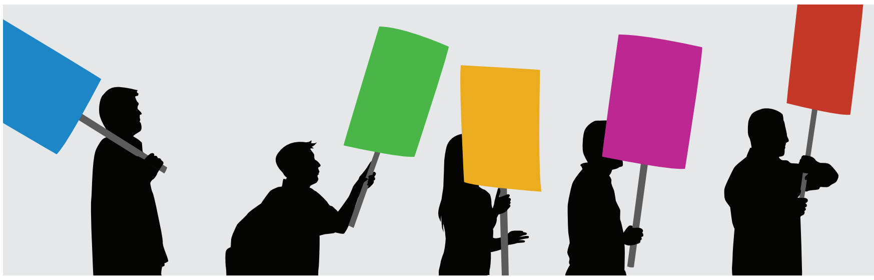
A SPECIALIST CONSUMER REPRESENTATIVE ORGANISATION ON FINANCIAL SERVICES

Such a specialist consumer watchdog would represent the consumer interest in financial services issues, including retail banking and superannuation. It could be financed by a proportion of funds from dormant or lost accounts.

"I think banks should make profits and I am happy for them. But **the amount they make is unethical.** I wish at least they would put it to a good cause, I would be more forgiving then."

"Another experience with the bank recently was that my son, who has a disability, went into the bank to do a simple transaction. And the **staff person was under instructions to do her best to sell him two products.** And at that stage, he was relatively naïve, quite young. He didn't really understand any of it. But **they managed to convince him to buy two products which, as far as I'm concerned, he didn't need.** And so he went in for a simple transaction and he came out with a lot more than he bargained on."

SUPER-COMPLAINTS IN THE UK



In the UK, a small number of bodies have the power to take a "super-complaint" to regulators on behalf of all consumers. This includes the UK consumers' association, the equivalent of CHOICE. The super-complaint process is intended to be a fast-track system for designated consumer bodies to bring to the attention of the regulators, market features that appear to be significantly harming the interests of consumers.

Guidance issued by the main national regulator responsible for enforcing competition and consumer law (the Office of Fair Trading) sets out the scope, process and possible outcomes, as follows.

A super-complaint, as defined in section 11(1) of the Enterprise Act 2002, is a complaint submitted by a designated consumer body that "any feature, or combination of features, of a market in the UK for goods or services is or appears to be significantly harming the interests of consumers".

A feature of a market may be:

- the structure of the market concerned or any aspect of that structure
- any conduct of one or more than one person who supplies or acquires goods or services in the market concerned, or
- any conduct relating to the market concerned of customers of any person who supplies or acquires goods or services.

The market in question may be regional, national or supranational (where the UK forms part of the market) although the authority can only consider the effects within the UK.

Super-complaints are given fast-track consideration. Those with the duty to respond to super-complaints are required to publish a reasoned response within 90 calendar days from the day after a complaint is received.

The possible outcomes of a super-complaint include:

- Enforcement action by the Office of Fair Trading's competition or consumer regulation divisions
- Finding that another authority with concurrent duties is better placed to deal with the complaint
- Launching a market study into the issue
- Making a market investigation reference to the Competition Commission if there is a competition problem
- Action by a sectoral regulator with concurrent duties
- Referring the complaint to another consumer enforcement body
- Finding the complaint requires no action
- Finding the complaint to be unfounded
- Dismissing the complaint as frivolous or vexatious.[48]

for over fifteen years. Consumer representative organisations operate effectively in consumer credit, energy and communications, with a mix of community and government support.

CHOICE believes the complex issues surrounding banking and superannuation are good examples of where public policy making would benefit from a dedicated, independent consumer voice. This new organisation would be free from the industry conflicts of interest that may arise for other associations and interest groups that currently operate in the sector.

This could be financed by a proportion of swept-up funds from dormant or lost accounts. This would allow the sector to fund the independent representative organisation without any additional burden on the government or industry. Alternatively, direct funding from the Commonwealth government would provide stable resources and could be justified by the scale of the banking sector and the mandatory nature of superannuation contributions.

Remuneration

One of the greatest causes of complaints by bank customers is that bank staff are too focused on selling them a new product (or upgrading an existing product) rather than addressing their immediate customer service needs. This practice also causes longer waiting and transaction times in branches and call centres and is the source of considerable customer frustration.

Some of this frustration is shared by the bank staff themselves, who feel under pressure to meet sales targets but who receive little reward for improving the customer's overall experience. Front-line staff report that their remuneration is too heavily weighted towards sales targets.

Customers and staff both also report concerns that the selling of credit products is driven by bank targets, rather than by the needs of the consumer, and that responsible lending practices are often pushed into the background by the constant pressure to sell products. People coming under pressure to buy higher-cost services or products that they had no intention of even discussing with their bank may make poor choices and buy unsuitable products.

One example of this is the growing problem of payment protection insurance, which is the subject of a large increase in complaints to the Financial Ombudsman Service in recent years.

CHOICE supports efforts to re-focus front-line staff on customer service, rather than selling; we also believe that customer service should be at the centre of compensation standards for senior bank executives. While remuneration policies for senior executives in some banks now explicitly include long-term improvements to customer service among criteria for awarding executives performance-related pay, too often this is

RECOMMENDATION 12

BANK EXECUTIVES' REMUNERATION LINKED TO GOOD CUSTOMER SERVICE NOT SALES TARGETS

Regulators should ensure in their scrutiny of remuneration arrangements that senior executives and front-line bank staff (branches and call centres) are rewarded for good customer service. The emphasis on sales targets in bank staff remuneration should be removed, and pressure should be reduced to push new products and product upgrades (particularly credit products). Much greater emphasis should be placed in senior executives' remuneration packages on long-term, measurable improvements to customer service.

"I am involved in the lending side of banking and totally disagree with selling insurance to customers which is not cost effective for them. The insurance sold on loans is very rarely to the customers benefit. It is extremely expensive and very hard to make a claim on. Unfortunately employees are required to sell this to the customers or they will not receive the quarterly incentive payments. These payments should be called 'blackmail' payments as many staff actually do not agree with the policies of the companies they work for."

> "The public outcry against banks has been escalating for many years. Increasing competition is only one small part of the answer to the problem and the government needs to put the wheels in motion for change that will make the banks much more accountable. Of course you can't legislate for 'respect' and banks will never have this while they treat their customers with such disrespect."

still not given the priority it deserves.

At the Commonwealth Bank, for example, customer satisfaction is one of eight indicators for short term rewards. Only one third of remuneration for senior executives is based on performance over four years, of which half is based on customer satisfaction, half on shareholders' return. [47]

Improving the governance of banking

The special position of banks in Australia should bring with it special responsibilities, including a duty to be leaders in standards of corporate governance. Ultimately, responsibility for the behaviour of banks lies with their governing bodies – boards of directors and general meetings of shareholders.

One way in which banking might win back trust and confidence is if it changes from behaving as an unaccountable, self-interested industry to something more like a profession. That would require those employed in banking to abide by an industry code that puts their duty to the community and the well-being of their customers on a par with their institution's profitability. The ABA's Code of Banking Practice and the recommended changes in its current review will fail to deliver this.

Such a cultural change in banking must also depend on a deep and long-term commitment to a broader definition of shareholder value at the board and senior management level of all banks. This broader definition of shareholder value would have responsible and ethical behaviour at its heart. Boards should hold themselves accountable for improved long-term performance to shareholders and the public.

Existing regulatory rules on corporate governance in financial services are not geared towards securing such a change, although they do require a closer alignment of risk management with remuneration policy and set some minimum standards for the composition and operation of boards. APRA reforms to prudential standards in this area have been necessary but not sufficient; they have focused on promoting "greater independence on the part of the board, its chair and the board audit committee; and they require boards to have a formal policy on board renewal and procedures for assessing their own performance".

CHOICE believes it is time for APRA and ASIC to carry out a further review of corporate governance rules for banks, with a view to ensuring boards and shareholders are equipped to properly hold executives to account across the full range of performance criteria. This might involve a requirement that boards have the right level and composition of skills to be able to pursue improvements in customer service, for example through the appointment of more independent non-executive directors on boards with the expertise and a specific remit to drive cultural change, and the annual election of board chairs.

RECOMMENDATON 13

FURTHER REFORM OF CORPORATE GOVERNANCE RULES FOR BANKS

The regulators should review corporate governance requirements for banks to ensure shareholders and boards have a duty to hold executives and board chairs to account for failures in customer service.

Ensuring all banks meet their obligations to the community

Banks are often proactive at reporting their contribution to society through corporate social responsibility initiatives and more generally through their contribution as tax-paying corporations. CHOICE strongly supports voluntary efforts by all major corporations to play a better role as corporate citizens, whether through reducing their impact on the environment, supporting charities or encouraging voluntary work amongst their staff. In 2010, for example, ANZ in its CSR Review reported $11.9 million of expenditure in the community, through donations, volunteering and in-kind support. They also reported bringing SaverPlus, a matched savings and financial capability program to 3,320 low income people. [49]

But major banks also make strenuous efforts to limit their corporation tax liabilities and some report paying significantly less than the current thirty per cent rate of corporate tax, in particular on certain divisions of their businesses, through the use of offshore entities where corporate tax is charged at a lower rate.

Of course, many consumers benefit from profitable banks through share dividends, and in particular retirees have voiced support for a profitable banking system in meetings with CHOICE. Many others have expressed their anger at the level of profits reported by major banks. If banks are indeed earning "excessive" profits, as some commentators suggest, it is arguably inefficient to permit these to flow back to Australians through returns on shareholdings as the banks themselves take a higher proportion of their profits through higher salaries for executives and commissions.

In other jurisdictions, special taxes have been placed on banks to fund measures to tackle market failures in banking, and to put a brake on excessive bonuses. In the UK, the government recently announced its plans "to make sure that we get the maximum sustainable tax revenues from the financial sector". A one-off bank payroll tax designed to encourage responsible remuneration has raised £2.3 billion, and levies have been raised from banks to meet the costs of financial inclusion and education measures. This has been followed with a new and permanent bank tax which was increased in February 2011 so that it raises £2.5 billion this year. The UK government has also required that all the major banks operating in the UK comply in spirit and by the letter with the national Code of Practice on taxation. [50]

In Australia, the banks obtain great commercial benefits from government guarantees. The government also supports the banks' payments systems by making so many official transactions dependent on the recipient possessing a bank account.

CHOICE recommends that the Treasury reviews the extent to which Australia's largest banks are contributing to the community through voluntary corporate social responsibility efforts, and considers the establishment of a special tax to support remedial action where there are specific cases of market failure.

This could include meeting the costs of a speedy move to bank account portability, ensuring the availability of ATMs in remote and indigenous areas, and financing an extended program for financial literacy or other action to promote financial inclusion.

RECOMMENDATON 14

BANKS TO MEET IN FULL THEIR OBLIGATIONS TO THE COMMUNITY

The Treasury should publish a review of the tax arrangements in place for banks, end any special treatment and instead consider new mechanisms to ensure the banking sector helps fund the cost of remedying market failures.

"You must remember return of dividends is minimal compared to what [bank] execs are getting paid in terms of bonuses and shares options. It makes me sick to see how bank CEOs make 10 million plus a year just for being an employee. That is what we call greed and they (CEOs) up the interest rates amongst other things just so they can pocket a few more millions. That is why the GFC came about, because of greed."

"We are sick of their tricks to rip off people, they really don't show much regard for customers... it's all about results so the executives can get big bonuses."

Notes

"The banks make very good profits without raising their interest rates above that of the RBA's [cash rate] increase. I'm glad [people] are making a bit out of bank shares, but there are plenty of people doing it tough. Maybe if you were in your twenties (I'm in my fifties) and trying to buy a house, you would be thinking differently."

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