

PARLIAMENT OF THE COMMONWEALTH OF AUSTRALIA

Review of the Four Major Banks: First Report

House of Representatives Standing Committee on Economics

November 2016
CANBERRA

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Chair's foreword

Banking regulation should have two key goals: promoting financial stability and achieving strong outcomes for consumers. Financial stability is critical – but so is ensuring that consumers get a fair deal from the banking sector.

Due to Australia's strong regulatory framework and the banking sector's prudent management of financial risk, no Australian bank regulated by the Australian Prudential Regulation Authority (APRA) has ever failed. We need only consider the economic impact of bank failures in other nations to understand the importance of a stable banking system.

However, while they have remained financially strong, Australia's major banks have let Australians down too frequently in too many other ways.

Australians turn to banks for assistance when making some of the most important decisions and facing some of the most serious challenges of their lives: borrowing to buy their first home; investing to support their retirement; and, in some cases, accessing insurance policies that they had hoped they would never need.

Australians should be able to trust that their bank will act in their best interests when they turn to them for help. It is clear that in some cases this has not happened.

The Government and regulators recognise this and are taking steps to remedy the failings that have occurred. This committee's inquiry into the conduct of Australia's major banks is an important part of this process.

This inquiry offers the banking sector the chance to transparently account for its conduct. This is a critical opportunity for an industry that has too often failed to live up to the expectations of Australians.

The committee's investigation of these issues will help hold the industry to account while informing future policy changes.

While the committee strongly endorses the measures being implemented to reform the banking sector, it is clear that gaps remain.

Australia's banking sector is an oligopoly. The major banks have significant market power that they use to protect shareholders from regulatory and market developments.

Despite this market concentration, under our current regulatory structure no entity is tasked with regularly making recommendations to improve competition. This must change.

The culture of Australia's financial sector also needs to be reformed. While significant changes have been announced that will better protect consumers, not enough has been done to force banks' senior leaders to change their behaviour. When consumers are continually let down, senior executives should go.

In addition, when things do go wrong, consumers and small businesses need one place to go where disputes can be quickly and easily handled. This does not yet exist.

To fill these gaps in the reform agenda and deliver better outcomes for consumers, the committee's recommendations include:

- the launch of a 'one stop' Banking and Financial Services Tribunal to replace the existing external dispute resolution schemes by 1 July 2017;
- public reporting of significant regulatory breaches, including the names of relevant senior executives and the consequences that they faced, as well as enforcement action in the wealth management industry;
- continual monitoring of competition in Australia's banking sector;
- the creation of a data sharing framework for consumers' and small businesses' data by July 2018; and
- a review of the regulatory barriers to starting a bank.

The committee looks forward to the Government's response to the recommendations contained in this report.

David Coleman MP
Chair

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Membership of the Committee

Chair

Mr David Coleman MP

Deputy Chair

Hon Matt Thistlethwaite MP

Members

Mr Adam Bandt MP

Ms Julia Banks MP

Mr Scott Buchholz MP

Mr Pat Conroy MP (to 7 November 2016)

Mr Trevor Evans MP

Mr Kevin Hogan MP

Mr Craig Kelly MP

Mr Matt Keogh MP

Ms Madeleine King MP (from 7 November 2016)

Committee Secretariat

Stephen Boyd, Committee Secretary

Ryan Walsh, Inquiry Secretary

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Terms of Reference

On 15 September 2016, the Treasurer requested that the House of Representative's Standing Committee on Economics undertake – as a permanent part of the committee's business – an at least annual inquiry into:

- the performance and strength of Australia's banking and financial system;
- how broader economic, financial, and regulatory developments are affecting that system; and
- how the major banks balance the needs of borrowers, savers, shareholders, and the wider community.

In undertaking its inquiry, the committee was asked to hold at least annual public hearings with the four major banks, with a particular focus on the banks' perspectives on:

- domestic and international financial market developments as they relate to the Australian banking sector and how these are affecting Australia;
- developments in prudential regulation, including capital requirements, and how these are affecting the policies of Australian banks;
- the costs of funds, impacts on margins and the basis for bank pricing decisions; and

- how individual banks and the banking industry as a whole are responding to issues previously raised in Parliamentary and other inquiries, including through the Australian Bankers' Association's April 2016 six point plan to enhance consumer protections and in response to Government reforms and actions by regulators.

In undertaking its inquiry, the committee was also asked to, as appropriate, engage with Australia's key economic regulators and give due consideration to the Government's Financial System Program and other relevant financial sector reforms and reviews.

Abbreviations

ABA	Australian Bankers' Association
ACCC	Australian Competition and Consumer Commission
ACCP	Australian Council for Competition Policy (proposed)
ADI	Authorised Deposit-taking Institution
AFSL	Australian Financial Services License
ANZ	Australian and New Zealand Banking Group
API	Application Programming Interface
APRA	Australian Prudential Regulation Authority
ASIC	Australian Securities and Investments Commission
BSB number	Bank-State-Branch number
CBA	Commonwealth Bank of Australia
CEO	Chief Executive Officer
CMA	Competition and Markets Authority (UK)
CIO	Credit and Investments Ombudsman
EDR	External Dispute Resolution

FCA	Financial Conduct Authority (UK)
FOFA	Future of Financial Advice
FOS	Financial Ombudsman Service
FSI	Financial System Inquiry
FSSA	<i>Financial Sector (Shareholdings) Act 1998</i>
GDP	Gross Domestic Product
GFC	Global Financial Crisis
IDR	Internal Dispute Resolution
IRB model	Internal Ratings Based model
NAB	National Australia Bank
NPP	New Payments Platform
ODI	Open Data Institute
PRA	Prudential Regulation Authority (UK)
RBA	Reserve Bank of Australia
SCT	Superannuation Complaints Tribunal
SMR	Senior Managers Regime (UK)
SVR	Standard Variable Rate
TBTF	Too-big-to-fail
UK	United Kingdom

Recommendations

Recommendation 1

- 2.1 The committee recommends that the Government amend or introduce legislation, if required, to establish a Banking and Financial Sector Tribunal by 1 July 2017. This Tribunal should replace the Financial Ombudsman Service, the Credit and Investments Ombudsman and the Superannuation Complaints Tribunal.
- 2.2 The Government should also, if necessary, amend relevant legislation and the planned industry funding model for the Australian Securities and Investments Commission, to ensure that the costs of operating the Tribunal are borne by the financial sector.

Recommendation 2

- 3.1 The committee recommends that, by 1 July 2017, the Australian Securities and Investments Commission (ASIC) require Australian Financial Services License holders to publicly report on any significant breaches of their licence obligations within five business days of reporting the incident to ASIC, or within five business days of ASIC or another regulatory body identifying the breach.
- 3.2 This report should include:
 - a description of the breach and how it occurred;
 - the steps that will be taken to ensure that it does not occur again;

- the names of the senior executives responsible for the team/s where the breach occurred; and
- the consequences for those senior executives and, if the relevant senior executives were not terminated, why termination was not pursued.

Recommendation 3

- 4.1 The committee recommends that the Australian Competition and Consumer Commission, or the proposed Australian Council for Competition Policy, establish a small team to make recommendations to the Treasurer every six months to improve competition in the banking sector.
- 4.2 If the relevant body does not have any recommendations in a given period, it should explain why it believes that no changes to current policy settings are required.

Recommendation 4

- 5.1 The committee recommends that Deposit Product Providers be forced to provide open access to customer and small business data by July 2018. ASIC should be required to develop a binding framework to facilitate this sharing of data, making use of Application Programming Interfaces (APIs) and ensuring that appropriate privacy safe guards are in place. Entities should also be required to publish the terms and conditions for each of their products in a standardised machine-readable format.
- 5.2 The Government should also amend the *Corporations Act 2001* to introduce penalties for non-compliance.

Recommendation 5

- 5.38 The committee recommends that the Government, following the introduction of the New Payments Platform, consider whether additional account switching tools are required to improve competition in the banking sector.

Recommendation 6

- 6.1 The committee recommends that by the end of 2017:

- the Government review the 15 per cent threshold for substantial shareholders in Authorised Deposit-taking Institutions (ADIs) imposed by the *Financial Sector (Shareholdings) Act 1998* to determine if it poses an undue barrier to entry;
- the Council of Financial Regulators review the licensing requirements for ADIs to determine whether they present an undue barrier to entry and whether the adoption of a formal 'two-phase' licensing process for prospective applicants would improve competition; and
- APRA improve the transparency of its processes in assessing and granting a banking licence.

Recommendation 7

- 7.1 The committee recommends that the major banks be required to engage an independent third party to undertake a full review of their risk management frameworks and make recommendations aimed at improving how the banks identify and respond to misconduct. These reviews should be completed by July 2017 and reported to ASIC, with the major banks to have implemented their recommendations by 31 December 2017.

Recommendation 8

- 8.1 The committee recommends that the Government amend relevant legislation to give the Australian Securities and Investments Commission (ASIC) the power to collect recurring data about Australian Financial Services licensees' Internal Dispute Resolution (IDR) schemes to:
- enable ASIC to identify institutions that may not be complying with IDR scheme requirements and take action where appropriate; and
 - enable ASIC to determine whether changes are required to its existing IDR scheme requirements.
- 8.2 The committee further recommends that ASIC respond to all alleged breaches of IDR scheme requirements and notify complainants of any action taken, and if action was not taken, why that was appropriate.

Recommendation 9

- 9.1 The committee recommends that the Australian Securities and Investments Commission (ASIC) establish an annual public reporting regime for the wealth management industry, by end-2017, to provide detail on:
- the overall quality of the financial advice industry;
 - misconduct in the provision of financial advice by Australian Financial Services Licence (AFSL) holders, their representatives, or employees (including their names and the names of their employer); and
 - consequences for AFSL holders' representatives guilty of misconduct in the provision of financial advice and, where relevant, the consequences for the AFSL holder that they represent.
- 9.2 The committee further recommends that ASIC report this information on an industry and individual service provider basis.

Recommendation 10

- 9.21 The committee recommends that, whenever an Australian Financial Services Licence (AFSL) holder becomes aware that a financial advisor (either employed by, or acting as a representative for that licence holder) has breached their legal obligations, that AFSL holder be required to contact each of that financial advisor's clients to advise them of the breach.