



Australian Government



Australian
**Small Business and
Family Enterprise**
Ombudsman

22 December 2017

Mr Mark Fitt
Committee Secretary
Senate Economics Legislation Committee
PO Box 6100
Parliament House
Canberra ACT 2600

By Email: economics.sen@aph.gov.au

Dear Mr Fitt

RE: FINANCIAL SECTOR LEGISLATION AMENDMENT (CRISIS RESOLUTION POWERS AND OTHER MEASURES) BILL 2017

Thank you for the invitation to make a submission to this Inquiry. This submission does not focus on the bill specifically but seeks to inform the Committee regarding the small business issues and unintended consequences of decisions taken to ensure bank stability taken during the global financial crisis. In times of crisis, the powers provided to the Australian Prudential Regulatory Authority (APRA) as outlined in this bill could have significant impact on the economy and small business. We recognise the requirement for APRA to be able to respond effectively and quickly to ensure effective management and support the bill in principle.

The focus of our submission is on potential consequences of APRA exercising these powers and leading to situations where banks or insurance companies can exploit the regulator's decisions for future revenue generation purposes. Already there are a range of challenges facing small businesses in dealing with financial institutions and accessing finance, particularly where they don't own real property assets.

Access to finance: prudential rules and biases in the banking system

The prevailing focus of bank lending against real property security has the effect of increasing the cost of capital on other lending. It has also contributed to reducing the ability of small business to obtain funding secured against other business aspects such as cash flow. It does have an impact on limiting finance to small businesses that have no or limited access to real property. Consequently, whilst the current prudential regulatory environment and capital holding rules have ensured Australia has a stable financial system on an international scale, this has been at a real cost to the financing options available to small business and family enterprise. The focus on 'bricks and mortar' funding is constraining capital for businesses with good cash flow and business prospects, but lacking in real property holdings that may be mortgaged. As a result, for many small businesses funding is simply unavailable at a reasonable cost.

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Prudential standards and actions providing opportunities for banks to generate revenue

The circumstances around Bankwest's acquisition by CBA has been covered extensively including the allegations of deliberate impairment of customer loans. We would draw the Committee's attention to the excellent coverage of the matter outlined in the Parliamentary Joint Committee (PJC) on Corporate and Financial Services Impairment of Customer Loans report (May 2016) which dedicates a chapter to the circumstances and actions of all parties.¹ The report covers the allegations of the impact of prudential standards and CBA's Project Magellan. While the PJC Committee was unable to determine if such allegations were true it did form the view that with the acquisition of Bankwest there was a culture of placing profit and shareholder returns ahead of the interests of borrowers²

This raises the question, of when there is a crisis and APRA exercises these new powers, what will be the consequences for an institution's customers, particularly its small business customers? We are supportive of overall financial system stability in times of crisis and the judicious exercising of these powers by APRA. The question is what happens next? Will APRA exercising certain powers ensure, that once the crisis is over, the institution affected won't seek to profit from the crisis at the expense of their borrowers?

We propose that where these powers are used, an automatic review mechanism is required to assess the subsequent steps taken by a bank or insurance company at an appropriate time after APRA has intervened. The review should be undertaken by a government entity (for example, ASIC). The review should examine the outcome on the institution's customers (both depositors and borrowers) including any allegations the institution has used the crisis to generate profit at the expense of its customers. We accept that in the event of a crisis, every customer's financial position is at risk. However, by ensuring there is an automatic review of the financial institution's actions subject to an APRA intervention there is a powerful disincentive for the institution (or rescuing institution) not to abuse its position and profit from the crisis.

Please do not hesitate to contact me or my advocacy director Mr James Strachan on [REDACTED] if you would like to discuss this submission or if you require any further details.

Yours sincerely,

[REDACTED]

Kate Carnell AO

Australian Small Business and Family Enterprise Ombudsman

¹ See Impairment of Customer Loans Report May 2016 at https://www.aph.gov.au/Parliamentary_Business/Committees/Joint/Corporations_and_Financial_Services/customer_loans/Report

² Ibid. pp 142-143.