

Senate Economics References Committee
ANSWERS TO QUESTIONS ON NOTICE

Treasury Portfolio

Inquiry into the Post-GFC Banking Sector

8 August 2012

Question: #1

Topic: Recommendations by Mr Stiglitz

Senator Cameron asked:

Senator CAMERON: Joe Stiglitz has written a book called *The Price of Inequality*. It deals, to a great extent, with the role of the banks and the global financial crisis. On page 269 he outlines a number of recommendations relating to reduced rent-seeking and levelling the playing field in the banking industry, and curbing the excesses of the financial sector. That runs through onto page 270. It runs from recommendation (a) to recommendation (f). Could I ask the Market Group to have a look at these recommendations from Joe Stiglitz and to provide us some advice as to whether they have any relevance or beneficial application within Australia?

Mr Murphy: Yes, okay.

Mr Beckett: I will talk to the Treasurer. We will provide that through the Treasurer to you.

Senator CAMERON: Thanks.

Answer:

Professor Stiglitz's recommendations largely reflect the regulatory approach already undertaken in Australia. While Professor Stiglitz's comments are directed to US and European regulators, his recommendations support Australia's approach to banking regulation.

Australia's banks are subject to strong prudential standards and intensive ongoing supervision, which has mitigated risks in the financial sector that have crystallised in other economies.

Recommendations from *The Price of Inequality*, by J. Stiglitz:

a) Curb excessive risk taking and the too-big-to-fail and too-interconnected-to-fail financial institutions; they're a lethal combination that has led to the repeated bailouts that have marked the last thirty years. Restrictions on leverage and liquidity are key, for the banks somehow believe that they can create resources out of thin air by the magic of leverage. It can't be done. What they create is risk and volatility.

APRA has continued to maintain, and revise where appropriate, standards related to leverage and liquidity.

APRA intends to introduce new liquidity and leverage rules in line with emerging international practice that will further strengthen the resilience of the banking sector.

b) Make banks more transparent, especially in their treatment of over-the-counter derivatives, which should be much more tightly restricted and should not be underwritten by government-insured financial institutions. Taxpayers should not be involved in backing up these risky products, no matter whether we think of them as insurance, gambling instruments, or, as Warren Buffet put it, financial weapons of mass destruction.

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At the G20 summit in Pittsburgh in 2009, the Australian Government joined other jurisdictions in committing to promote greater transparency and improve risk management practices in the over-the-counter (OTC) derivative markets.

In April 2012, the Australian Government announced it will develop a legislative framework to ensure the implementation of G20 OTC derivative commitments, including: reporting all OTC derivatives to trade repositories; clearing of all standardised OTC derivatives through central counterparties; and the execution of all standardised OTC derivatives on exchanges or electronic trading platforms, where appropriate.

c) Make the banks and credit card companies more competitive and ensure that they act competitively. We have the technology to create an efficient electronic payments mechanism for the twenty-first century, but we have a banking system that is determined to maintain a credit and debit card system that not only exploits consumers but imposes large fees on merchants for every transaction.

The Government has taken action to promote a competitive and sustainable banking system. The Government introduced three broad streams of reform: to empower consumers to get a better deal; to help smaller lenders put more competitive pressure on the major banks; and to secure Australia's financial system, to provide a sustainable flow of credit to households and businesses.

Measures include the new 'tick and flick' transaction account switching service, the ban on exit fees, a standardised key fact sheet to help consumers compare mortgage products, and greater powers for the ACCC to prosecute anti-competitive price signalling.

The Reserve Bank of Australia is charged with promoting efficiency and competition in the payments system as part of its statutory objectives. The RBA regulates credit card and debit card interchange fees. As a result of the RBA's regulatory activities, there is greater competition in the market and merchant fees are lower than they otherwise would be.

The RBA recently announced the outcome of its review of innovation in the payments system. The conclusions paper can be found on the RBA's website at

<http://www.rba.gov.au/payments-system/reforms/strategic-review-innovation/conclusions/pdf/conclusions-062012.pdf>

d) Make it more difficult for banks to engage in predatory lending and abusive credit card practices, including by putting stricter limits on usury (excessively high interest rates).

The Government has introduced credit card laws to give consumers more control over their borrowing, and stamp out lender practices that disadvantage consumers. Credit providers are now required to provide consumers with a simple, standardised document setting out the key terms of any proposed credit card contract, with information that includes interest rates and fees, to enable consumers to easily compare the features and costs of different credit cards.

The Government is also introducing Australia's first national cap on credit card borrowing costs.

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Further, the Government has introduced a number of credit card reforms that help protect consumers and came into effect from 1 July this year. These reforms include:

- a ban on offers by card providers to increase credit limits unless the consumer has expressly agreed to receive them, to avoid consumers being burdened with inappropriate credit limits.
- a requirement on credit card providers to direct repayments to the most expensive part of a credit card debt first, making it easier for consumers to reduce their debt faster.
- a new 'minimum repayment warning' in monthly credit card statements, that specifies both the amount of time and the interest charges that would be incurred if the debtor repaid the outstanding balance under the contract:
 - if they only paid the minimum repayment required under the contract; and
 - if they made repayments sufficient to repay the outstanding balance within 2 years.

e) Curb the bonuses that encourage excessive risk-taking and short-sighted behaviour

APRA's prudential standards require banks to adhere to a sound remuneration governance framework, which discourages pay practices that incentivise inappropriate risk taking.

In addition, the Government introduced executive remuneration reforms which give shareholders more power to influence remuneration, improve the requirements for disclosure of remuneration consultants, and prohibit directors from hedging their remuneration or voting on the remuneration of key management personnel.

f) Close down the offshore banking centres (and their onshore counterparts) that have been so successful both at circumventing regulations and promoting tax evasion and avoidance. There is no good reason that so much finance goes on in the Cayman Islands, there is nothing about it or its climate that makes it so conducive to banking. It exists for one reason only: circumvention.

Australia is at the forefront of the implementation of the international standards for exchange of taxpayer information through membership of the G20 and the OECD and, particularly, as Chair of the *Global Forum on Transparency and Exchange of Information for Tax Purposes* (Global Forum).

The Global Forum comprises more than 100 jurisdictions to ensure that international standards of transparency and information exchange are met.

The Global Forum has made significant progress in ensuring international cooperation in the exchange of information with over 800 agreements that provide for the exchange of information in tax matters having been signed by various jurisdictions.

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Australia's own exchange of information network consists of almost 80 countries (bilateral tax treaties and tax information exchange agreements (TIEAs)). Australia has signed TIEAs with prominent offshore financial centres including Andorra, the Bahamas, Bermuda, the British Virgin Islands, the Cayman Islands, Dominica, Gibraltar, Guernsey, Jersey, the Isle of Man, Liechtenstein, Monaco, St Kitts & Nevis and Vanuatu.

In addition to the bilateral tax treaties and tax information exchange agreements, Australia has also signed the *Multilateral Convention on Mutual Administrative Assistance in Tax Matters* which authorises the exchange of taxpayer information and assistance in the collection of outstanding tax debts. The Convention has been signed by 38 countries, with more expected to sign. The G20 has strongly encouraged all jurisdictions to join the Convention.