Chapter 7

Moving between banks

7.1 The costs and other impediments to moving between banks are important factors with the potential to weaken competition significantly:

> …consumer switching costs (whether real or perceived) are widespread and our analysis suggests that the resulting welfare losses may be substantial: switching costs generally raise prices and create deadweight losses…in a closed oligopoly…public policy should discourage activities that increase consumer switching costs (such as airlines' frequent-flyer programmes) and encourage activities that reduce them (such as standardisation that enhances compatibility and reduces costs of switching, and quality regulation and information sources that reduce consumer uncertainty about untested brands).[1]
>
> Changing banks is too hard and unduly complicated.[2]

7.2 National Australia Bank's CEO concedes this:

> The two key drivers of competition are search cost, so how long does it take in terms of time and what is the cost to find a deal—this applies to any industry—and, secondly, what is a switching in time and cost? They are the key drivers.[3]

7.3 A survey of Queensland businesses found that those banking with regional banks are more satisfied than those banking with the majors.[4] The failure of this to translate into increased market share for the regional banks suggests some barriers to customers moving between banks.

7.4 The same survey found that of businesses that had not switched banks, only about a third said this was because they were satisfied with their bank. A third said they thought all banks were the same and a third said it was too difficult and expensive to change banks. Almost half the businesses that switched banks found the process difficult or extremely difficult, and that it cost over $5,000.[5]

7.5 There are not just explicit costs to moving between financial intermediaries. There is also an inherent inertia. One submitter wrote of the 'fear of the unknown' as a deterrent:

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1 Klemperer (1995, p 536), cited in Consumer Action Law Centre, *Submission 87*, p 5.

2 Council of Small Business Organisations of Australia, *Submission 90*, p 10.

3 Mr Cameron Clyne, Chief Executive Officer, National Australia Bank, *Committee Hansard*, 13 December 2010, p 63.

4 Chamber of Commerce and Industry Queensland, *Submission 43*, pp 7 and 13.

5 Chamber of Commerce and Industry Queensland, *Submission 43*, pp 14-15.

> If you've been with your lender for a period of time…You're familiar with their internet and phone banking. You know where the branches and ATMs are located…What if you move to a new lender and find out that it's a lot more difficult to get things done or the products don't work like you would expect? Sometimes it's better to deal with the devil you know.[6]

7.6 Mrs Amanda Watson put the blame more on the consumer:

> It is my belief that many Australians are somewhat apathetic in regards to their banking choices and while I note that there is a fair level of 'bank bashing' most people appear to choose not to switch in order to find a better product for their needs.[7]

7.7 This chapter discusses the factors which may deter customers from moving between banks, including mortgage exit fees, financial illiteracy and mortgage insurance, and considers possible improvements in this area.

Mortgage exit fees

7.8 Banks charge a variety of fees if customers repay a loan early. In the case of *fixed rate* loans a large exit fee may be quite reasonable. A prudent bank offering a fixed rate loan will fund it through fixed rate borrowing. If interest rates fall, and customers are free to repay loans early and take out new loans at a lower rate, the bank will be caught still paying a high interest rate but earning a low rate. The rest of this section is concerned with the case of *variable rate* loans, where there is not this justification.

7.9 Some exit fees are modest administrative fees, or mortgage discharge fees, as would be paid at the maturity of a loan. But some lenders charge large 'early repayment' fees or have 'deferred establishment' fees which may be waived if a loan is maintained until maturity. Both of these may not be clearly disclosed at the time the loan is taken out and both can act to impede competition by locking customers into their current bank even when a rival offers a lower interest rate.

7.10 Some examples of exit fees are given in Tables 7.1 and 7.2. The fees are generally high for non-conventional lenders and low for building societies and credit unions.

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6 ProSolution Private Clients, *Submission 30*, p 1.

7 Mrs Amanda Watson, *Submission 64*, p 1.

Table 7.1: Exit fees after three years on $300,000 owner-occupied home loan ($)

	Upfront fees	Exit fees
ANZ simplicity Plus	600	160
NAB base variable rate home loan	600	150
Westpac flexi first option home loan	600	950
Commonwealth Bank economiser	600	1050
St George basic home loan	100	1500
Bendigo residential variable home loan	730	250
Bank of Queensland standard variable	595	1450
Aussie Classic	600	1215
Mortgage House basic home loan	569	5250
Homestar No Fee	0	3600
AIMS gold standard variable home loan	660	4230
Community CPS Credit Union basic variable	595	0
Mecu Credit Union basic home loan	595	100
Greater Building Society great rate	0	0
Heritage Building Society standard variable	600	0

Source: Infochoice website (www.infochoice.com.au) as at 23 March 2011.

Table 7.2

Average Fees on Variable Housing Loan Products
$250 000 owner-occupier loan, terminated within 3 years

	Setup Fee $	Service Fee $	Discharge Fee $	Exit Fee $	Total $
Current					
Credit unions and building societies	595	122	106	364	1,187
Major banks	431	513	229	462	1,635
Other banks	459	468	271	676	1,874
Non-ADI	584	254	363	2,066	3,266
Change since 2008					
Credit unions and building societies	13	10	14	-37	0
Major banks	-23	203	115	-620	-324
Other banks	36	113	43	-28	165
Non-ADI	-149	38	133	121	143

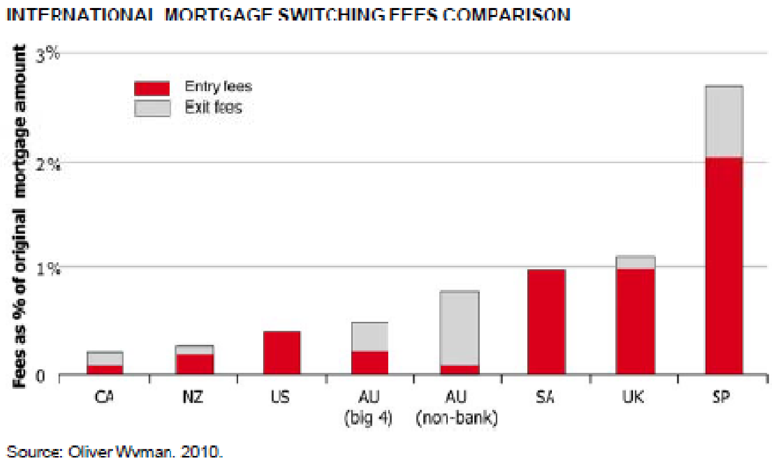
Sources: ASIC; Canstar Cannex; InfoChoice; RBA

Source: Reserve Bank of Australia, *Submission 41*, p 24.

7.11 Westpac do not charge an exit fee if the customer remains for more than four years.[8] Presumably the argument is that the interest charged has covered the upfront costs by then. This seems inconsistent, however, with the argument that the fee is necessary to recover the costs of establishing the loan. These costs would be fixed rather than varying with the size of the loan, and so if recouped from interest would be recovered more quickly for larger loans. Nor do interest rates drop for ongoing borrowers after four years.[9]

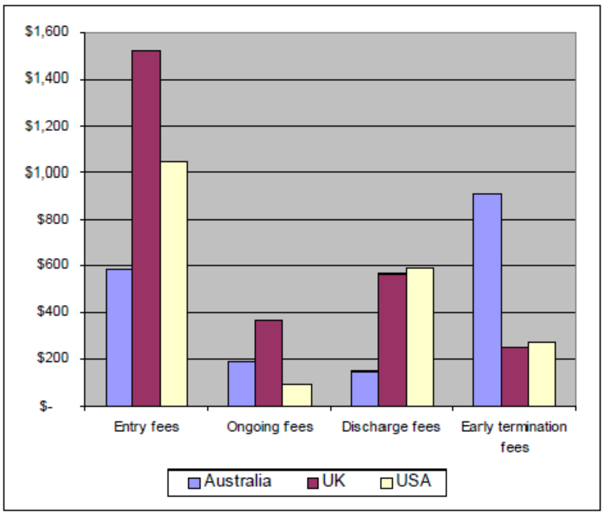
7.12 Exit fees for mortgages in Australia are higher than in most comparable countries (Charts 7.1 and 7.2).

Chart 7.1: Mortgage switching fees



Source: Westpac, *Submission 72*, p 36.

Chart 7.2: Comparison of selected bank fees



Source: ASIC, 'Review of mortgage entry and exit fees', *Report no. 125*, April 2008, p 11.

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8 Ms Gail Kelly, Chief Executive Officer, Westpac, *Committee Hansard*, 21 January 2011, p 92.

9 Ms Nicole Rich, Director, Policy and Campaigns, Consumer Action Law Centre, *Proof Committee Hansard*, 25 January 2011, p 17.

The case against excessive exit fees

7.13 There is considerable support for action to limit exit fees, particularly but not exclusively in relation to home mortgages:

> Consumers of mortgage products dissatisfied with the product or service they receive from their bank or mortgage provider feel trapped by the exit fee, which discourages them from switching.[10]
>
> Lenders should only be allowed to charge loan exit fees on a cost recovery basis…[11]
>
> …excessive and unjustified early exit fees represent a serious barrier to switching in the mortgage market, inhibiting competition...Across the market more broadly, this reduces the pressure on lenders to provide better and more competitive products.[12]

7.14 Exit fees differ from other bank charges in that there is no incentive for an individual bank manager to waive or lower these charges in an attempt to retain a valued customer, as they are only relevant to a customer who has decided to move their custom elsewhere. It was suggested that if establishment fees are being deferred due to the borrower's cash flow constraints, it would be more transparent just to add the fee to the loan amount.[13] When comparing potential lenders, a borrower is unlikely to pay much attention to differences in exit fees as they are likely to be focused on the purchase of their current home, not thinking about when they will sell it to buy their next.

7.15 One example of the anti-competitive impact of excessive exit fees was the following:

> …our client chose a variable rate home loan based on representations that the product‘s interest rate would remain competitive, but after several rate rises over approximately an 18 month period, her home loan rate was considerably higher than other rates in the market, but she felt unable to switch because she faced an early exit fee of over $12,000.[14]

The case for exit fees

7.16 The main opposition to restrictions on exit fees comes from some non-bank lenders. They are unable to raise funds as cheaply as the major banks, so may rely on fees to offer competitive interest rates:

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10 Redfern Legal Centre, Senate Economics Legislation Committee inquiry into the Banking Amendment (Delivering Essential Financial Services for the Community) Bill 2010, *Submission 2*, p. 2.

11 Australian Chamber of Commerce and Industry, *Submission 37*, p 28.

12 Consumer Action Law Centre, *Submission 87*, p 13.

13 Professor Kevin Davis, *Committee Hansard*, 25 January 2011, p 59; *Submission 8*, pp 8-9.

14 Consumer Action Law Centre, *Submission 87*, p 13.

> The offer that they [some non-bank lenders] make to consumers is: 'We can offer you an interest rate which is at the moment around 0.7 per cent less than the banks, but to come on board with us we want some assurance that you are going to stay with us for a reasonable amount of time. Also, to make it attractive, we won't change you any upfront fees, any establishment fees. But if you leave us within three years—or five years, depending on who the non-bank lender is—we will then ask you to pay those establishment fees; thus the term 'deferred establishment fees'…I know that there has been a focus on non-bank lenders charging $7,000 as a deferred establishment fee, and I suppose people always tend to look at the worse possible example to prove their point. Yes, that could happen, but it would only happen if someone had a pretty high loan—about $700,000—and they switched within the first 12 months of the loan.[15]
>
> There is a real tangible cost to 'writing a loan' which has a commercial impact, as does the manufacturing production and sale of any product. This commercial cost cannot be ignored, and should not be hidden elsewhere. Removing the same will have an impact which most likely will not be to the benefit of the consumer borrower as it has the potential to significantly increase the cost up front to obtain a loan.[16]
>
> Exit fees *per se* (apart from questions of scale) are a reasonable charge.[17]
>
> The proposed removal of exit fees is not a measure we believe will enhance competition. It is the smaller, non-bank lenders that will be hurt most by this. For the majority of banks, the deferred establishment fee was put in place as a competitive response to reduce the upfront albeit legitimate costs of taking on a new mortgage.[18]

7.17 The Australian Bankers' Association commented:

> …exit fees do reflect genuine costs incurred by banks and others. To the extent that they are genuine costs, removing the ability to recover those costs is likely to hit smaller lenders disproportionately compared to larger lenders.[19]

7.18 Asked about any prudential concerns, APRA responded:

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15 Mr Phillip Naylor, Chief Executive Officer, Mortgage and Finance Association of Australia, *Committee Hansard*, 14 December 2010, p 71.

16 Finance Brokers' Association of Australia, *Submission 133*, p 2. See also Mortgage House of Australia, *Submission 115*, pp 1-2.

17 Dr Evan Jones, *Submission 81*, p 7.

18 Mr David Foster, Chief Executive Officer, Suncorp Bank, *Committee Hansard*, 9 February 2011, p 2.

19 Mr Steven Münchenberg, Australian Bankers' Association, *Committee Hansard*, 14 December 2010, p 83.

> …it is important that ADIs are able to cover and/or recoup their legitimate costs in originating, managing and closing out a mortgage.[20]

7.19 The Committee heard claims that banning exit fees would lead to a corresponding increase in establishment fees or interest rates, which would be paid by all borrowers:

> If you ban exit fees you will push costs to up-front…[21]

7.20 Furthermore, as exit fees are only charged to those customers repaying early, this provides an advantage for those customers who stay with the lender. Aussie noted that:

> Regulation or banning of exit fees would result in cross subsidisation by the stable customers of those customers who routinely move between financiers.[22]

ASIC action on unfair exit fees

7.21 As described in Chapter 10, some provisions of the National Credit Code under the *National Consumer Credit Protection Act 2009* relate to exit fees. These provisions came into effect in July 2010 and from this date borrowers have been able to challenge the validity of early termination fees they think are 'unconscionable' or 'unfair'. Borrowers may also complain to ASIC or to an external dispute resolution scheme; the borrower or ASIC can seek review of fees by a court.[23]

7.22 ASIC have explained their stance as:

> Mortgage exit fees are acceptable provided they reflect—and are limited to—the lender's losses which can be directly connected to the borrower exiting the loan early.[24]

7.23 This statement has been interpreted as implying:

> Under the Australian Consumer law, an unfair contract term that includes payment of early exit fees can be declared void.[25]

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20 APRA, *Responses to questions on notice*, no 6, 31 January 2011, p 3.

21 Mr Peter White, National President, Finance Brokers Association of Australia, *Proof Committee Hansard*, 4 March 2011, p 4. This possibility is also raised by Professor Milind Sathye, *Submission 28*, p 8; and Australian Chamber of Commerce and Industry, *Submission 37*, p 24.

22 Aussie, *Submission 39*, p 2.

23 Dr Peter Boxall, Commissioner, ASIC, *Committee Hansard*, 21 January 2011, p 3.

24 Mr Tony D'Aloisio, Chairman, ASIC, *Herald-Sun*, 19 November 2010, confirmed by Mr Greg Kirk, Senior Executive Leader, ASIC, *Committee Hansard*, 21 January 2011, p 5. A similar view is put by ACCC and ASIC in 'A guide to the unfair contract terms law', p 16.

25 Care Financial Counselling Service, *Submission 3 to basic banking inquiry*, p 3.

7.24 The Consumer Action Law Centre advocated a narrow or literal reading of this which would make the permissible fees quite small:

> …if you section out exit costs that apply whenever the exit occurs and simply focus down on the costs attaching to early exit, we think that the numerical value of that cost would be very small.[26]

The Government's December 2010 package

7.25 The Government announced in its package that from July 2011 exit fees would be banned on new variable rate mortgage loans.[27]

7.26 The measures which came into force in July 2010 relating to unconscionable exit fees would continue to apply to existing mortgages. The reason the new measures do not apply to existing loans is constitutional:

> …that would be an acquisition of property. The property is the property of the financial institution. We took legal advice on that.[28]

7.27 Treasury clarified that the ban refers to a fee 'triggered by the consumer's action to pay out the mortgage early, which would not ordinarily happen.'[29]

7.28 Perhaps trying to make a virtue of necessity[30], two of the major banks have abolished exit fees ahead of the ban.

7.29 On 23 March 2011, the Government amended the National Consumer Credit Protection Regulations 2010 to prohibit exit fees.

Committee view

7.30 The Committee regards the Government's decision to ban exit fees as a kneejerk reaction. The new consumer protection provisions which would restrict exit fees to reasonable amounts only came into effect a few months ago and are not well known. They should be given a chance to work. Exit fees should be limited to underlying costs and a reasonable profit margin, rather than banned.

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26 Ms Catriona Lowe, Co-Chief Executive Officer, Consumer Action Law Centre, *Committee Hansard*, 25 January 2011, p 15.

27 The ban will be implemented through amendments to the National Credit Code; Australian Government, *Competitive and Sustainable Banking System*, December 2010, p 7.

28 Mr Jim Murphy, Executive Director, Department of the Treasury, *Committee Hansard*, 13 December 2010, p 41.

29 Mr John Lonsdale, General Manager, Financial System Division, Department of the Treasury, *Proof Committee Hansard*, 9 March 2011, p 7.

30 As Treasury's Jim Murphy explained: 'Put yourself in their position—you are facing a ban on something you have been doing so you may as well adapt and get some credit points out of it.'; *Proof Committee Hansard*, 9 March 2011, p 5.

7.31 The Committee notes the importance of fees in underpinning the business models of non-bank lenders which bring competitive pressures to the market.

7.32 The Committee believes that banning exit fees will lead to higher upfront fees, including for borrowers who never incur exit fees. It is notable that the only financial intermediaries that accepted the abolition of exit fees were the major banks.

7.33 It is important, however, that borrowers are made aware of the extent of exit fees at the time they take out their loans.

Recommendation 4

7.34 The Committee recommends that the Government reconsider its decision to ban exit fees, before the amended regulations come into effect, with a view to allowing enough time for the effectiveness of the existing ban on unfair and unconscionable exit fees (as implemented through ASIC Regulatory Guide 220) to be assessed. If it proceeds with the ban, it should only apply to authorised deposit-taking institutions.

Recommendation 5

7.35 The Committee recommends that lenders be required to inform borrowers when they take out a loan of the provisions of the *National Consumer Credit Protection Act 2009* which relate to unconscionable charges.

Recommendation 6

7.36 The Committee recommends that borrowers be required to sign off on a form clearly disclosing any exit fees applicable to their home or small business loan before making any commitment.

Recommendation 7

7.37 The Committee recommends that lenders charging exit fees be required to explain on their website how the exit fee relates to relevant costs.

Other factors influencing inhibiting customers moving between mortgage providers

7.38 In addition to costs and related impediments, a number of other issues affecting decisions to move between banks were raised during the inquiry.

Lenders mortgage insurance

7.39 Lenders mortgage insurance (LMI) is a product intended to protect lenders by covering any shortfall if a property has to be sold as a result of the borrower defaulting on their loan and realises less than the outstanding balance of the loan.[31] It became evident during this inquiry that LMI can represent a significant cost for borrowers:

> But the biggest inhibitor of switching—in over half the cases we see, probably 70 per cent—is not the exit fee; it is the duplicating cost of mortgage insurance. If you borrow over 80 per cent of the value of your property, you have got to obtain mortgage insurance. That can cost you anything. It can cost you $10,000 or $7,000...That is something that the Treasurer said he was going to have a look at, and I think that is a great thing. To have a look and do something about it would be fantastic.[32]

> The real deterrent in the LMI premium, as the policy is not portable from one bank to another. As a result a customer wishing to move a mortgage from one bank to another will need to pay LMI twice…LMI policies should be made portable…[33]

> …that is a problem for consumers in terms of the initial insurance premium being a sunk cost and if they switch they have to pay another one…the premium for a lender's mortgage insurance policy is in the thousands of dollars…[34]

> …if the loan is discharged early there is regularly no premium rebate to the borrower albeit in some cases it is 'partially' available for the first 2 or 3 years of the loan only (and note the premium is paid based on the total loan term not just 2 or 3 years) this rebate is not on a pro-rata or proportional basis given the total period covered in some cases if you don't ask for a rebate/refund on the premium you won't get it as only some LMI Providers have an automatic system to do this – others do not. Colloquially if you don't know you don't get, and you can't ask for something you don't know about…[35]

> Mortgage insurance is typically required for loans which are 80% or more of the property value (i.e. loan-to-valuation ratio of at least 80%). It is not portable. The cost of mortgage insurance varies with loan size and, like

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31 LMI is not to be confused with mortgage protection insurance, which covers borrowers to allow them to maintain mortgage payments in the event of illness or unemployment.

32 Mr John Symond, Executive Chairman, Aussie Home Loans, *Committee Hansard*, 14 December 2010, pp 111 and 128.

33 Mr Dinesh Warusavitharana, *Submission 98*, pp 2 and 4. Credit Union Australia, *Submission 85*, p 10 also calls for improvements to the portability of mortgage insurance.

34 Mr Greg Kirk, Senior Executive Leader, ASIC, *Committee Hansard*, 21 January 2011, pp 12-13. Concerns were also expressed by Ms Nicole Rich, Director, Policy and Campaigns, Consumer Action Law Centre, *Committee Hansard*, 25 January 2011, p 23, and Mr Chris Whitehead, Chief Executive Officer, Credit Union Australia, *Committee Hansard*, 25 January 2011, p 88; Abacus, *Submission 53*, p 24; and Mr Peter White, National President, Finance Brokers Association of Australia, *Proof Committee Hansard*, 4 March 2011, p 2.

35 Finance Brokers' Association of Australia, *Submission 133*, p 4.

legal fees and State government taxes and charges, can run into the thousands of dollars.[36]

7.40 LMI is usually paid by the borrower but the benefit accrues to the lender. If the borrower repays early, they will only sometimes get any refund for the premium paid for the remainder of the loan:

> Generally speaking, there is somewhere between a 12- to 24-month window. If you discharge your mortgage in that period of time, you are possibly eligible for a rebate of up to about only 40 per cent of that premium only, remembering the premium covers the lender for right of recourse for 20 to 30 years. But the consumer is the one who has paid for it and the consumer is the one who only gets a rebate if they ask for it.[37]

7.41 Treasury commented:

> Lenders' mortgage insurance is one thing that, when it is raised, is an impediment to people moving forward to seek to switch their accounts. We are working on that at the moment and looking at a process whereby lenders' mortgage insurance could be portable—could go with the mortgage. We have not finalised it yet but it is the clear intention of the government to introduce such a system.[38]

7.42 The Insurance Council of Australia defended the current arrangements:

> While the cost of LMI protecting the lender is typically borne by the borrower, the borrower obtains significant benefit from the use of LMI by the lender. LMI provides greater access to home ownership, particularly for low income, low equity or higher risk borrowers who would otherwise have difficulty obtaining a home loan. These borrowers are able to obtain a loan that would otherwise not be available, or to obtain a loan much earlier than they would be able to if they had to save for a full (20%) deposit.[39]

7.43 The Insurance Council also observed:

> Importantly, with LMI, lenders do not have to charge a higher interest rate to cover the increased risk a low deposit borrower presents. The cost of the once only up front LMI premium borne by a borrower is significantly less than higher risk based interest pricing that would apply to a higher risk borrower over the life of the mortgage loan.[40]

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36 Commonwealth Bank of Australia, *Submission 88*, p 14.

37 Mr Peter White, National President, Finance Brokers Association of Australia, *Proof Committee Hansard*, 4 March 2011, p 2.

38 Mr Jim Murphy, Executive Director, Department of the Treasury, *Committee Hansard*, 13 December 2010, p 34.

39 Insurance Council of Australia, *Submission 137*, p 2.

40 Insurance Council of Australia, *Submission 137*, p 2. No reason was given why a lender would charge more to a customer in increased interest than an insurer would charge as a premium for offsetting the same risk.

7.44 Genworth Financial, a provider of LMI insurance, claims that LMI is not an impediment to borrowers switching:

> ...LMI is typically only required on HLTV [high loan-to-value] loans (above 80%). If a consumer does take out a high LTV loan and looks to switch to another lender, our analysis shows that the consumer is unlikely to be asked to pay LMI again if they switch after two to three years, given the LTV for the new loan is likely to be below 80% given long run home price appreciation assumptions.[41]

7.45 The Government has indicated its intention to make LMI transferable between lenders, perhaps through a clearing house, or refundable, and consultations are underway with key insurers.[42]

7.46 If the market for LMI is competitive, these additional requirements will push up its cost. As with exit fees, this would mean that those borrowers who stick with their lender will be paying more to assist borrowers who switch lender.

7.47 There were doubts raised, however, about whether the LMI market is very competitive, with some submitters arguing it was opaque and concentrated:

> If you go back in history, there was a government mortgage loss insurer and there were four or five at one stage. We are down to two…it is important that we keep competition in that market…because that is an input into making sure that the securitisation market operates effectively and efficiently, which means players like us can provide that competition to make sure that mortgage spreads do not increase.[43]

> Currently lenders mortgage insurance is a duopoly market…The Federal Government agency, the Housing Loans Insurance Corporation (HLIC), operated from the early 1960s before being sold to GE Capital in 1999. The sell off of HLIC has greatly reduced competition and exacerbated the competitive disadvantage suffered by securitisers relative to banks funding on balance sheet.[44]

> There is also a lack of disclosure of commissions (if any) paid to banks/lender for the sale of LMI…[45]

7.48 The borrower will generally be required to pay an LMI provider nominated by the lender, often an entity owned by that lender, and cannot shop around for a cheaper

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41 Genworth Financial Mortgage Insurance, *Submission 136*, p 5.

42 Australian Government, *Competitive and Sustainable Banking System*, December 2010, p 9; Mr Jim Murphy and Mr John Lonsdale, Department of the Treasury, *Proof Committee Hansard*, 9 March 2011, pp 9-10 and 14.

43 Mr James McPhee, Chief Executive Officer, Members Equity Bank, *Committee Hansard*, 25 January 2011, p 112.

44 Members Equity Bank, *Submission 77,* p 3.

45 Finance Brokers' Association of Australia, *Submission 133*, p 4.

LMI provider. As the premium is paid in a lump sum at the time the loan is taken out, it is equivalent to an additional 'establishment fee' but is often excluded from comparisons of interest rates and fees charged by different lenders. There are also concerns that there is no product disclosure statement on lenders mortgage insurance.[46]

Recommendation 8

7.49 The Committee recommends that lenders mortgage insurance always be made either pro-rata refundable or transferable and that this be made clear to borrowers.

7.50 As an alternative, lenders mortgage insurance should be payable by instalments (eg. monthly, quarterly or annually) rather than as an upfront lump sum payment (as occurs in other jurisdictions).

Interest rate disclosure

7.51 There have been calls for a standardised annual percentage interest rate to be prominently displayed, to avoid confusion over compounding.[47]

7.52 Ideally the single standardised interest rate would also include fees:

> I would like to see all fees (excluding fixed rate break costs) converted into the interest rate, including any deferred establishment or exit fees, so that the true cost of the facility at any point in time is known and borrowers are not hoodwinked about how much they are really paying…[48]
>
> …banks should be required to…publish comparison rates for business loans;…[49]
>
> Suggestion: A regulated central comparison website across all financial products, by type & features with full disclosure of fees & charges.[50]

7.53 The Financial Ombudsman Service commends the one-page disclosure statement required in the United States (see following page).

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46 Finance Brokers' Association of Australia, *Submission 133*, p 4.

47 Mr Alan Mills, *Submission 15*, p 1.

48 Mrs Maria Rigoni, *Submission 86*, p 1.

49 Mr Andrew Canion, Manager, Western Australian Small Enterprise Network, *Committee Hansard*, 21 January 2011, p 110.

50 Mr John O'Brien, *Submission 117*, p 2.

FEDERAL TRUTH-IN-LENDING DISCLOSURE STATEMENT
THIS IS NEITHER A CONTRACT NOR A COMMITMENT TO

Loan Number: **(Insert Alpha-Numeric – TO BE ADDED)** Date: **(Month Date,Year –TO BE ADDED)**
Creditor: **(Insert Corporate Name – TO BE ADDED)**
Address: **(Insert full address, city, state and zip – TO BE ADDED)**

Borrower(s): **(Insert borrorer(s) full names – TO BE ADDED)**

Address: **(Insert full street address, city, state, zip – TO BE ADDED)**

Lines containing an "x" are applicable:

ANNUAL PERCENTAGE RATE	FINANCE CHARGE	Amount Financed	Total of Payments	☐ Total Sale Price
The cost of your credit as A yearly rate	The dollar amount the credit will cost you.	The amount of credit provided to you or on your behalf	The amount you will have paid after you have made all payments as scheduled.	The total cost of your purchase on credit including your down-payment of
(Insert Perc.Rate – TO BE ADDED) %	$ (Insert Finance Amount – TO BE ADDED)	$(Insert Total Amount Financed – TO BE ADDED	$(Insert total dollar amount of payments	$(Insert Amt. TO BE ADDED) $(Insert Amt. TO BE ADDED)

PAYMENT: Your payment schedule will be:

Number of Payments	Amount of Payments **	When Payments Are Due Monthly Beginning	Number of Payments	Amount of Payments **	When Payments Are Due Monthly Beginning	Number of Payments	Amount of Payments **	When Payments Are Due Monthly Beginning

(Insert Number of Payments – TO BE ADDED) (Insert Amount of Payment – TO BE ADDED) (Insert Month/Date/Year – TO BE ADDED)

____DEMAND FEATURE: This obligation has a demand feature.
____VARIABLE RATE FEATURE: Your loan contains a variable rate feature. Disclosure about the variable rate feature have been provided to you earlier

INSURANCE: The following insurance is required to obtain credit:
___Credit life insurance and credit disability ____ Property Insurance ____Flood Insurance ____Mortgage Insurance
You may obtain property insurance from any insurer that is acceptable to the Lender.
SECURITY: You are giving a security interest in: (Insert full property address – TO BE ADDED)
____The goods or property being purchased ____Real property you already own
FILING FEES: $(Insert numerical amount w/decimal – TO BE ADDED)
LATE CHARGE: If payment is more than (Insert number of days – TO BE ADDED) days late, you will be charged (Insert percentage amount – TO BE ADDED)% of the payment.
PREPAYMENT: If you pay off early, you
____may ____will not have to pay a penalty.
____may ____will not be entitled to a refund of part of the finance charge.
ASSUMPTION: Someone buying your property.
____may ____may, subject to conditions ____may not assume the remainder of your loan on the original terms.
See your contract documents for any additional information about nonpayment, default, any required repayment in full before the scheduled date and prepayment refunds and penalties.
____"e" means an estimate all dates and numerical disclosures except the late payment disclosures are estimates.

Each of the undersigned acknowledge receipt of a complete copy of this disclosure. The disclosure does not constitute a contract or a commitment to lend.

Applicant	Date	Applicant	Date
Applicant	Date	Applicant	Date
Applicant	Date	Applicant	Date

**NOTE: Payments shown above do not include reserve deposits for taxes, assessments, and property or flood insurance.

FEDERAL TRUTH-IN-LENDING DISCLOSURE STATEMENT WCM DIRECT, LLC
05/17/06

Regz4.1st

7.54 The Consumer Action Law Centre advised that better disclosure would help:

> We would certainly support disclosure that occurs pre-contractually that enables consumers to visit a number of institutions, obtain a range of information and make a carefully considered decision rather than quickly being provided with disclosure at the point of contract. We would say it needs to be of standard form and key terminology.[51]

7.55 A lacuna is a site where financial products can be readily compared:

> A consumer would be better informed by a transparent price mechanism. A better informed customer can then make a decision to switch if the price differential is found attractive. Currently, there is no official website/data resource where such information could be available at one place.[52]

> Competition would be enhanced by increasing the information available to the public so that they could more easily compare different banking products from different institutions.[53]

7.56 One bank had found that simplifying charges benefited the bank as well as customers:

> One of the positive learnings from the last 18 months is that the abolition of a number fees and changes in process around this has removed a number of complexities in our business. This simplification of our offers means that we are able to better explain our products and services to our staff and customers, and do so at a reduced cost.[54]

Better information to assist moving between banks

7.57 The movement of customers between banks is facilitated if information about different offers is easy to compare. The Consumer Action Law Centre warned:

> It is also in the interests of industry participants to do the opposite, making it harder to compare deals by producing more complex products and information about those products, and attempting to differentiate products on a basis other than price, even where products are essentially commoditised or homogenous goods. In Australia, the telecommunications market provides an excellent example of this phenomenon in action – we believe it is currently impossible for consumers to undertake an effective comparison of mobile phone plans and choose the best deal for their usage pattern.[55]

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51 Ms Catriona Lowe, Co-Chief Executive Officer, Consumer Action Law Centre, *Committee Hansard*, 25 January 2011, p 13.

52 Professor Milind Sathye, *Submission 28*, p 15.

53 Name withheld, *Submission 52*, p 2.

54 National Australia Bank, *Submission 91*, p 10.

55 Consumer Action Law Centre, *Submission 87*, p 17.

7.58 The Reserve Bank and the Australian Prudential Regulation Authority already receive a lot of information from ADIs about their products. For example, the Reserve Bank is able to calculate a measure of the cost of mortgages, including both interest and (establishment, service and exit) fees. The Reserve Bank provided an example of this in a chart in their submission (reproduced as Chart 5.8) but did not identify the individual lenders. Providing such information, with the names of the credit providers, would be very useful to consumers.

7.59 Another impediment to consumers comparing across accounts is confusing differences in product names:

> A valuable way of rectifying the information asymmetry that fosters the current anticompetitive environment in respect of exception fees is to require all financial institutions to adopt equivalent nomenclature and terminology when describing exception fees, in order to enable consumers to genuinely compare banking products with ease.[56]

> …banks should be required to standardise banking terminology, to help business customers make easier product comparisons…We believe some simple changes would be helpful, such as requiring standardised terminology to be used and cutting out some of the more confusing lingo.[57]

7.60 Another submitter refers to:

> …extensive product suites with complex pros and cons. The resulting consumer confusion allows the banks to harvest greater revenues through inefficient selection.[58]

7.61 A small business representative referred to a major bank which gave them a document about terms and conditions which ran to 75 pages.[59]

7.62 The Commonwealth Bank itself cast doubt on the usefulness of advertised interest rates for comparing between banks (see further discussion in Chapter 5):

> The vast majority of the Group's mortgage customers do not pay the headline standard variable rate…[60]

7.63 Behavioural economics warns of 'decision paralysis'; an increasing number of options may not lead to a better choice being made, it may lead to a reversion to a default option.[61]

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56 Maurice Blackburn, *Submission 31*, p 7.

57 Mr Andrew Canion, Manager, Western Australian Small Enterprise Network, *Committee Hansard*, 21 January 2011, pp 110 and 117.

58 Accounts4Life, *Submission 128*, p 3.

59 WA Small Enterprise Network, *Responses to questions on notice, no 13*, 1 February 2011, p 1.

60 Commonwealth Bank of Australia, *Submission 88*, p 10.

61 Heath and Heath (2010, p 50).

7.64 One component of the Government's December 2010 package is a uniform mandatory key fact sheet for new home loan customers, which will show consumers how much they will pay every month and over the life of their loan (see next two pages).[62] Treasury's Jim Murphy is particularly enthusiastic about it:

> If you wish to go and shop around, this will enable you in terms of what deal you can get. This is a simple document which would give you the terms and conditions for that loan. To me that is a huge advance.[63]

7.65 ASIC released an online mortgage-switching calculator in 2010, which allows consumers to work out how long it would take them to gain in interest savings what it costs to switch mortgage providers. It is part of the new personal finance website (www.moneysmart.gov.au), which replaced ASIC's previous FIDO website.

7.66 Choice expounded their initiative to provide customers with better information:

> One of the reasons Choice launched its Compare, Ditch and Switch website—and we have had tens of thousands of Australians using that tool since we launched it a few days ago—is to make it easier for people to compare products in the market and easier for people to use our data comparison to match one product against another. But, for lots and lots of consumers, the complexity of the information about products, the speed with which the market sometimes changes and the speed with which you need to be able to transfer, for example, your direct debits and direct credits to a different transaction account is just too much, and we have to recognise that.[64]

7.67 The Brotherhood of St Laurence shared with the Committee results from their research:

> …over 70 per cent of low-income clients surveyed were not aware of basic bank accounts and had not taken them up, leaving many paying bank fees unnecessarily. The analysis also shows that banks are not promoting these products and that information about them is difficult to find or unnecessarily complex.[65]

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62 Australian Government, *Competitive and Sustainable Banking System*, December 2010, p 10.

63 Mr Jim Murphy, Executive Director, Department of the Treasury, *Committee Hansard*, 13 December 2010, p 33.

64 Mr Richard Lloyd, International Policy Adviser, Choice, *Committee Hansard*, 14 December 2010, p 33.

65 Mr Gerard Brody, Senior Manager, Financial Inclusion, Brotherhood of St Laurence, *Committee Hansard*, 25 January 2011, p 3.

CONSULTATION DRAFT

This information sheet is an Australian Government requirement under the *National Consumer Credit Protection Act 2009*

KEY FACTS ABOUT THIS HOME LOAN

Personalised for: John Smith Date produced: 1 December 2010	[Mortgage provider logo]

What you have told us	
Loan Amount: $300,000 Term of the mortgage: 30 years Repayment method: Principal and interest	Value of the property: $400,000 Loan to valuation ratio (LVR): 75%

HOW DOES THIS HOME LOAN COMPARE?

Description of this home loan	
Mortgage Lender	XYZ Mortgages
Product name	Variable Rate Package
Interest rate	7.16%
All-in rate: (including fees)	7.33%
Product features	0.70% discount off standard variable rate, interest off-set account, repayment redraw, free transaction account and free credit card.

Cost of the XYZ Mortgages Variable Rate Package	
Total amount to be paid back (including the loan amount and fees)[1]	**$742,019**
This means you will pay back	**$2.43 for every $1 borrowed**
Repayment per month (including fees)	**$2063**
Repayment per year (including fees)[2]	**$24,756**

[1] Based on minimum monthly payments over the full term of the loan at the current interest rate and current fees and charges
[2] Based on current interest rates.

What fees will you have to pay on the XYZ Mortages home loan?[3]	Fee Amount
Total establishment fees	$0
Ongoing fees (per year)	$395
There may be circumstances in which you have to pay other fees (for example, if you ask for extra statements or miss a repayment).	

[3] On 20 days notice, the fees may change and new fees may be imposed. Additional government charges may require payment and these have not been included. Stamp duty on transfer of land has not been included.

What happens if interest rates increase?
This is a **variable rate product.** If your interest rate was to increase by one per cent, your monthly repayment would increase by around **$208.**

Where can you shop around for better deals?
There may be better deals available. Ensure that you obtain Key Facts sheets like this one from other home loan providers to compare this mortgage with deals from other lenders. For more information about home loans visit the ASIC financial tips website: www.fido.gov.au. For information on other lenders and their products, visit: betterbanking.choice.com.au, www.canstar.com.au, www.infochoice.com.au, www.ratecity.com.au or www.mozo.com.au.

CONSULTATION DRAFT

This information sheet is an Australian Government requirement under the *National Consumer Credit Protection Act 2009*

IMPORTANT INFORMATION

This is not a legally binding mortgage offer and it does not oblige XYZ Mortgages to provide you with the mortgage described in this key facts sheet.

You will need to satisfy the lending criteria to qualify for this loan.

This key facts sheet is an Australian Government requirement.

To help you compare and select the most appropriate product, you must be provided with a key facts sheet before you can apply for a home loan.
All firms selling mortgages are required to give you a key facts sheet like this one, that contain similar information presented in the same way.

Ensure that you obtain key facts sheets from other home loan providers to compare this mortgage with deals from other lenders.

It is important to shop around and compare interest rates, fees and features before you apply for a home loan. Choosing the home loan that is most appropriate for you can save you tens of thousands of dollars. You'll see many different types of home loans advertised, with a range of fees and terms. While they have some features in common, interest rates and repayment options vary, so choosing a home loan that suits your needs takes time and involves shopping around.

You may have to pay other fees and charges in addition to any fees shown in this key facts sheet.

Ask your mortgage provider for a list of all fees that apply to this mortgage.

Some features may be appropriate for your situation and result in savings over the life of the loan.

- Loans may vary depending on:
- fees (establishment, ongoing);
- interest type (variable/fixed);
- loan term (including term of any fixed portion);
- repayment type (interest only or principal and interest);
- loan amount;
- purpose (owner occupy, investment property);
- ability to transfer mortgage property;
- ability to split;
- ability to make extra repayments, redraw, or offset;
- access (e.g. phone, online);
- linked accounts (credit card, cheque/savings); and
- Loan to Value Ratio (LVR).

For more information about home loans

Visit the ASIC financial tips website: **www.fido.gov.au**
Websites that compare home loan products include:
betterbanking.choice.com.au
www.canstar.com.au
www.infochoice.com.au
www.ratecity.com.au
www.mozo.com.au

7.68 Choice argued that even when impediments to moving between banks are removed, there may be a need for education before consumers make the most of the opportunities. They spoke of the need:

> …to encourage people to change their behaviour and move accounts, move mortgages and so on, because we have had centuries, if you like, of consumer inertia, and it does not just change overnight. So there is a period of time where it will take efforts on all of our parts, really, to encourage the market to work better than it has worked before, even with those new mechanisms.[66]

Recommendation 9

7.69 The Committee recommends that the Reserve Bank and the Australian Prudential Regulation Authority draw on their data collections to publish regular information about the total cost of home loans (based on standardised assumptions on the average size and term) for the twenty largest ADI home mortgage lenders.

Recommendation 10

7.70 The Committee recommends that a working group be set up including Treasury, the Australian Prudential Regulation Authority, the Australian Securities and Investments Commission, the Australian Competition and Consumer Commission, the Reserve Bank, the Financial Ombudsman Service, the Australian Bankers' Association, Abacus, consumer representatives and relevant academics to develop standardised words for financial products and their characteristics to allow consumers to more readily compare offers from different financial intermediaries.

Psychological or privacy barriers

7.71 There is a natural reluctance of borrowers about revealing to bank officers personal details about their income, their regular expenses, and the value of their home and other assets. Having to repeat this process when moving between lenders inhibits customers moving.

7.72 A possible means of overcoming this problem would be personal credit ratings. An agency could make an assessment of a customer's creditworthiness and give them a certificate they could give to a lender. Part of the assessment process could involve positive credit reporting. If the customer wishes to change to a new lender they could show the same certificate to the new lender rather than having to repeat the disclosure process.

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66 Mr Nick Stace, Chief Executive Officer, Choice, *Committee Hansard*, 14 December 2010, p 39.

Recommendation 11

7.73 The Committee recommends that the Government ask Treasury to investigate the feasibility of personal credit ratings to facilitate borrowers moving between lenders.

Financial literacy

7.74 There were a number of calls from witnesses and submitters for improved financial literacy:

> There does not seem to be a large amount of switching between transaction account providers in the general population. I guess that those with lower financial literacy might have greater reticence.[67]
>
> …for any banking reform to be successful it needs to include better consumer education…[68]

7.75 The Governor of the Reserve Bank remarked:

> It is a hard balance to strike, isn't it? As you say, you do not want to say to people in some overly nanny state sort of way, 'You can't have this loan.' You certainly do not want them to be in a position where they have taken on a commitment without fully realising what is actually involved. That is the balance to strike.[69]

7.76 The banks indicated their contribution to improving financial literacy:

> …the banking industry is committed to a long-term strategic priority of helping improve Australians' financial literacy. Australia's banks have a strong tradition of free education in financial skills and have in place a wide range of financial literacy, financial inclusion and capacity and enterprise building programs. In the year to June 2010, it is estimated these programs also received over $36 million of direct support from the main retail banks. Program contributions include building understanding in the areas of managing money, finance and banking, developing budgets, managing debt, building basic investment, insurance and superannuation knowledge, planning for life stages, including home ownership and retirement. These programs target efforts to assist the most vulnerable parts of the community.[70]
>
> The Federal Government should enhance levels of financial literacy of all Australians by developing and publishing a "National Strategy on Financial

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67 Mr Gerard Brody, Senior Manager, Financial Inclusion, Brotherhood of St Laurence, *Committee Hansard*, 25 January 2011, p 7.

68 Mr Ken Longshaw, *Submission 134*, p 1.

69 Mr Glenn Stevens, Governor, Reserve Bank of Australia, *Committee Hansard*, 13 December 2010, p 9.

70 Australian Bankers' Association, *Submission 76*, p 43.

Literacy" …[and] provide additional funding to ASIC so that dedicated efforts on financial literacy can be implemented…[71]

7.77 The CEO of ANZ Bank also emphasised the role of financial literacy in his opening remarks:

> Turning to customer empowerment: active, well informed customers help lift competition…The idea of the proposed mortgage fact sheet is to provide a simple statement which will help consumers compare the costs and features of mortgages. Financial institutions can also assist here by providing simple, transparent products. In the longer term, more financially literate and informed customers will grow competition in the market. ANZ has made a significant investment in understanding the issues related to low levels of financial literacy, and which groups in the community are most affected, and in developing programs aimed at building the skills of the more vulnerable in the community. Our programs are delivered in partnership with the government and community organisations such as the Brotherhood of St Lawrence.[72]

7.78 Yellow Brick Road believes:

> …additional investment in financial education must be made, and that the Australian consumer should be encouraged to seek financial advice by making these services tax deductible.[73]

7.79 Treasury commented:

> If we are looking at competitive and sustainable banking, a major thrust is to better inform consumers as to the nature of the banking system and how they should invest their money—to empower them to increase their financial literacy.[74]

7.80 It was suggested the improvement in financial literacy needed to start in schools:

> Improve Australia's educational system to facilitate informed discussion about topics such as inter-bank competition.[75]

7.81 Regrettably, in 2008 the Government significantly cut funding from the financial literacy programme introduced by the Howard Government.

7.82 The Government recently announced some initiatives:

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71 Australian Bankers' Association, *Submission 76*, pp 60-61.

72 Mr Michael Smith, Chief Executive Officer, ANZ Banking Group, *Committee Hansard*, 15 December 2010, p 118.

73 Yellow Brick Road, *Submission 101*, pp 15-16.

74 Mr Jim Murphy, Executive Director, Markets Group, Department of the Treasury, *Committee Hansard*, 13 December 2010, p 30.

75 Mr David Allen, *Submission 126*, p 10.

> The Government will also launch a new, interactive consumer website with ASIC to help people boost their understanding of money matters through access to high-quality and independent online, personalised financial guidance that is free and readily accessible.[76]
>
> From 2011, the national school curriculum for Maths will contain a strong focus on the practical financial skills that students need…[77]

7.83 The National Financial Literacy Strategy was released by the Government on 15 March 2011. The Strategy includes four key elements:

- using educational pathways to build financial literacy for all Australians;
- providing Australians with trusted and independent information, tools and ongoing support;
- recognising the limits of education and information, and developing additional innovative solutions to drive improved financial wellbeing and behavioural change; and
- working in partnership and promoting best practice.[78]

7.84 Partly due to a lack of financial literacy many customers rely on advisers to select banking products. This raises the issue of 'Quis custodiet ipsos custodes?' Is it any easier to choose a good adviser than a good product? This is particularly problematic when advisers receive much of their income from commissions from the product providers rather than just being paid by the consumer.

7.85 After the Committee had completed its hearings, the Government released information on its 'Future of Financial Advice' reforms. These represent the Government's response to the Joint Committee on Corporations and Financial Services' report into financial products and services, which was set up in the wake of collapses such as Storm Financial and Opes Prime. The Minister characterised the reforms as designed to:

> …focus on improving the quality of financial advice and expanding the availability of more affordable forms of advice…The key reforms include a ban on conflicted remuneration structures, including commissions and volume payments, a requirement for advisers to obtain client agreement to ongoing advice fees every two years and the expansion of limited advice.[79]

7.86 It remains to be seen whether the aims of these reforms can be implemented successfully without undermining access to relevant financial advice by Australians,

76 Australian Government, *Competitive and Sustainable Banking System*, December 2010, p 14.

77 Australian Government, *Competitive and Sustainable Banking System*, December 2010, p 14.

78 Australian Securities and Investments Commission, Report 229: *National Financial Literacy Strategy*, March 2011, p 6.

79 'Future of Financial Advice' information pack, foreward by The Hon Bill Shorten MP, Assistant Treasurer and Minister for Financial Services and Superannuation, 28 April 2011.

particularly those on lower incomes. Finance brokers and other financial advisers do play a useful role is helping households find the best deal on a home loan. They thereby contribute to improving competition in this market. A poorly thought out or implemented FOFA could limit the reach of that role. It is important to balance ensuring that advisers are not conflicted by commission arrangements with not preventing the impartial advisers being able to do their work effectively and in an accessible manner. The CEO of the Mortgage and Finance Association of Australia noted:

> ...there are conditions imposed on brokers, such as clawback provisions. If the customer decides to switch, the broker gets penalised by having their commission taken off them within a certain period of time. Some lenders have volume hurdles that say, 'We won't let you deal with us unless you produce so much business to us.' Those sorts of things make the broker's role more difficult. At the edge of the market, brokers who cannot comply with those conditions find it difficult to continue. As I have said, brokers are part of the competitive force in the market because they provide the retail face to the competition. A lot of the stuff we have been talking about is behind the scenes, the funding, but brokers provide the retail face.[80]

Committee comment

7.87 The Committee supports the renewed attention being paid to financial literacy. This is an important component of a more competitive financial system. The Committee is concerned, however, that the Government's approach may be too simplistic and prevent some customers gaining the benefit of informed and impartial advice.

Term deposits

7.88 There are odd spikes in the rates banks offer retail customers on term deposits; 'specials' as the banks term them. For example, they may offer 6 per cent for a seven month maturity but only around 3 per cent for six months or eight months. This disadvantages customers who just allow term deposits to roll over automatically on maturity.

7.89 Westpac were rather vague about the motivations:

> …all banks have specials at various points…it could be for seven months or 12 months and it fits in with your maturity profile—and there is also a little bit of a marketing element to it and a tracked and incentivised business element as well.[81]

7.90 Westpac also downplayed the extent to which less sophisticated investors ending up being rolled over into low interest terms:

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80 Mr Phil Naylor, Chief Executive Officer, Mortgage and Finance Association of Australia, *Committee Hansard*, 14 December 2010, p 76.

81 Ms Gail Kelly, Chief Executive Officer, Westpac, *Committee Hansard*, 21 January 2011, p 76.

> …customers do pay a lot of attention to the rates that they receive and, indeed, that was even intensified further through the global financial crisis with this intensity of preciousness of retail deposits. Customers do pay attention to that. We personally write to every customer, or communicate directly with every customer, when that term deposit is maturing and have a conversation with that customer about the options. We are not rolling over very attractive rates to much lower rates. That is simply not part of our philosophy or our style…[82]

7.91 Asked about this the Reserve Bank observed that the large majority of customers who initially invest in a term deposit at a ‘special’ rate roll over their deposit into a new ‘special’ (possibly for a different term).[83]

7.92 In 2009, ASIC conducted a review of the marketing and disclosure of term deposits by ADIs. ASIC noted that seven of the eight ADIs reviewed had dual pricing (i.e. they offer both high and low interest rates based on the term of investment, with significant differences between these rates), but none of the ADIs reviewed 'disclose the existence of dual pricing or the risk of rollover at a lower interest rate'.[84] The report recommended improvements to advertising practices and the disclosure of dual pricing, interest rates and grace periods.

Recommendation 12

7.93 The Committee recommends that banks should be required to contact customers before the expiry of term deposits advising them of the rate that will apply if they are automatically renewed and the current 'special' rates available.

Delays

7.94 Some bank customers are critical of the delays in banks effecting transfers of mortgages:

> Banks are able to settle properties for purchase readily in normal commercial time, but when they are receiving the settlement from outgoing customer this becomes in the main a painful exercise for the customer. It should be regulated that a bank is required to settle the transfer of a mortgage from one bank to another, within a maximum of 21 days of the date notified by the customer that they are transferring to another bank. There is no system impediment to this occurring. Mostly titles for properties exist both electronically and on paper and the exiting customer bank holding the title should be readily able to produce the physical title document, match it with the transfer signed by the customer, and transfer the title to the new lender within this period. If the bank cannot produce the title within 21 days and affect the transfer for the customer a penalty of

82 Ms Gail Kelly, Chief Executive Officer, Westpac, *Committee Hansard*, 21 January 2011, p 76.

83 Reserve Bank of Australia, *Responses to questions on notice, no 6*, 18 January 2011, p 6.

84 Australian Securities and Investments Commission, *Report 185: Review of Term Deposits*, February 2010, p 6.

> perhaps one month's interest expense for each day's delay by the bank be paid to the customer as compensation.[85]
>
> Abacus member ADIs have pointed to two factors that could be improved for borrowers wanting to switch lenders…long delays in discharge and settlement by the current lender.[86]

7.95 Brokers were also critical of delays:

> The actual processes employed by the banks internal departments which handle Discharge Documents and Payout Figures etc, use erroneously long delaying tactics which hinder and frustrates consumers and industry participants when trying to refinance a mortgage and or discharge the same,..[87]

Stamp duties

7.96 State stamp duties on mortgages will remain a barrier to shifting mortgages:

> Discharge fees of a mortgage—and that is where you get stamp duty—would still be applicable. That is a matter of state government regulation.[88]
>
> For those borrowers who live in jurisdictions where stamp duty is payable on mortgages, there is a significant barrier in switching as previously paid mortgage stamp duties are not transferable…[89]
>
> In some States and in some situations mortgage stamp duty can be charged on refinanced loans. This can be quite substantial. Also, the titles office charges mortgage registration and deregistration fees (which range from $180 to $260).[90]

7.97 Under the *Intergovernmental Agreement on Federal Financial Relations*, stamp duties on mortgages are scheduled to be abolished before 1 July 2013.[91]

7.98 The Government is examining the possible introduction of a central repository to hold all mortgages so as to avoid mortgage discharge and re-establishment fees.[92]

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85 Mr Mervin Reed, *Submission 5*, p 7.

86 Abacus, *Submission 53*, p 24.

87 Finance Brokers' Association of Australia, *Submission 133*, p 3.

88 Mr Jim Murphy, Executive Director, Department of the Treasury, *Committee Hansard*, 13 December 2010, p 36.

89 Bendigo and Adelaide Bank, *Responses to questions on notice*, no 7, 20 January 2011, p 1.

90 ProSolution, *Submission 30*, p 3.

91 *Report on Australia's Future Tax System*, December 2009, p 479.

92 Treasury, *Submission 102*, p 28; Australian Government, *Competitive and Sustainable Banking System*, December 2010, p 9.

Recommendation 13

7.99 The Committee recommends that the abolition of stamp duties on refinancing of mortgages be placed on the agenda for the forthcoming tax forum and that the agreement on their abolition be implemented.

Account portability

7.100 The Government has observed that impediments to deposit account portability (discussed below) may also inhibit movements of mortgages:

> Many bank customers hold their savings in a deposit account with the same bank as they have their home loan, so the inconvenience of moving their deposit account also acts as a significant barrier to moving their mortgage.[93]

Electronic conveyancing

7.101 The Bendigo and Adelaide Bank told the Committee:

> …there is currently a project about electronic or e-conveyancing. If the industry could get together and for the 80 per cent of people who just need a standard, everyday mortgage agree to the terms of what an industry mortgage might look like, we can put that into an e-conveyancing project. So if you wanted to swap from Westpac to us it would simply be a matter of it happening in a central electronic register. This reduces an enormous amount of the cost in the industry…[94]

7.102 The Australian Bankers' Association added:

> The National Electronic Conveyancing Development Ltd (NECDL) was established in January 2010 by the New South Wales, Queensland and Victorian Governments, following a Council of Australian Government's decision to develop the national electronic conveyancing system. We support this as an important initiative for national micro-economic reform and as being key to greater efficiency and convenience in conveyancing for consumers, practitioners and financiers... A national system will provide greater certainty of settlement date, delays associated with making appointments for settlement will be significantly reduced and the electronic settlement of transactions will obviate the need for bank cheques on settlement.[95]

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93 Australian Government, *Competitive and Sustainable Banking System*, December 2010, p 8.

94 Mr Mike Hirst, Managing Director, Bendigo and Adelaide Bank, *Committee Hansard*, 15 December 2010, p 90.

95 Australian Bankers' Association, *Submission 76*, p 65.

Deposit account number portability

7.103 Many consumers and small businesses find the process of moving between banks cumbersome as it involves telling large numbers of organisations or customers about a new account number. This is more burdensome for consumers now that many bills are paid using direct debits from accounts.

7.104 A recent survey commissioned by CHOICE showed that the most common reasons for not switching between ADIs were beliefs there was too much paperwork (50 per cent), not having enough time to research the best deal (48 per cent) and not believing they would be better off (44 per cent).[96]

7.105 The rate of transaction account switching appears lower in Australia than in the UK.[97] And the UK is considering measures to facilitate account switching there:

> …it may be possible to introduce greatly improved means of switching at reasonable cost, in which case the industry should be required to do this within a short timescale…[98]

7.106 As well as being a hassle for individuals, it is burdensome for small business:

> …at the moment in business if I need to change my account I have to go and tell all my customers my new account numbers. It happens to me, because I have suppliers. I will get an email, a letter, a phone call or whatever saying: 'Here's the new BSB and account number. Please change it.'... Most small businesses do not do it because it is difficult. It is not so much that they do not want to do it; it takes a lot of time and effort… you have your bank details on your stationery.[99]

7.107 Some bankers acknowledge the problem:

> When people switch banks, what they generally struggle with administratively is changing all of their direct debits and various other things, and that is obviously a barrier to people taking advantage of portability.[100]

> … direct debits and credits serve the purpose of tentacles for banks to hold onto customers by restricting them from moving to another provider. Unfortunately, for the Account Switching package to work effectively,

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96 CHOICE, *Submission 70*, p 9.

97 About 9 per cent of customers moved in a year in the UK, compared to under 8 per cent over two years in Australia; CHOICE, *Submission 70*, p 9.

98 Independent Commission on Banking (2011, p 5)

99 Mr Peter Strong, Executive Director, Council of Small Business Organisations of Australia, *Committee Hansard*, 15 December 2010, pp 8-9. Similar issues were raised by the WA Small Enterprise Network, *Submission 68*, p 9.

100 Mr Cameron Clyne, Chief Executive Officer, National Australia Bank, *Committee Hansard*, 13 December 2010, p 65.

> changes are required under the Bulk Electronic Clearing System ("BECS') rules. Currently consumers do not find the package convenient or user friendly and are reluctant to initiate switching to other banks even when they are not happy with the service provided to them by their current bank. Since the customer has to open a new account number and then take the responsibility to actually transfer the credits and debits over, there is reluctance on the part of consumers to initiate a change.[101]

7.108 Other banks and the Australian Payments Clearing Association regard the problem as overstated:

> Based on local data on account "churn" and overseas comparisons as well as RBA analysis of deposit account competition, there is substantial and effective competition in transactional banking services. If the challenges of switching transaction accounts are a barrier to competition, they are not a strong one – millions of Australians change provider every year.[102]
>
> The [Commonwealth Bank] Group opens and closes over 1 million personal transaction accounts a year, in the context of having over 5 million personal transaction accounts...These account opening and closure numbers show many customers change their personal bank accounts each year, contrary to popular opinion.[103]

7.109 Improving portability is welcomed by a number of witnesses and submitters:

> Bank account portability is very important…it should be pursued vigorously.[104]
>
> …portable account numbers would take the hassle out of moving from one FSP [financial service provider] to another, by eliminating the need to advise multiple parties of new account details…[105]

7.110 The Australian Bankers' Association is sceptical about the idea:

> …account portability, as frequently proposed, where a bank account number can be moved from financial institution to financial institution, would require significant investment, especially for smaller providers as well as other businesses and government departments. Furthermore, the benefits of account portability have not been demonstrated.[106]

7.111 Some submitters called for action to mandate improving account portability:

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101 ING Bank, *Submission 35*, p 4.

102 Australian Payments Clearing Association, *Submission 49*, p 1. APCA provide estimates of churn rates in pp 5-6 of the submission.

103 Commonwealth Bank of Australia, *Submission 88*, p 12.

104 Dr Richard Denniss, Executive Director, Australia Institute, *Committee Hansard*, 15 December 2010, p 31.

105 Financial Ombudsman Service, *Submission 78*, p 5.

106 Australian Bankers' Association, *Submission 76*, p 64.

> …the Federal Government needs to make switching banks as easy and as seamless as possible. Within this context, the best outcome for bank customers would be to have an ability to simply go the new bank, sign an authority to allow the new bank to move the customer's dealings over to the new bank and have the new bank do all the work with the old bank.[107]
>
> The other method used by banks to limit competition between themselves is the archaic bank state branch identifying numbering system, which together with the account number, supposedly drives the payment system. This antique framework was originally designed for the cheque clearance system specifically for Micra Ink readable cheques. It is readily easily replaced by each customer having a bank account number that becomes the universal number for that person. In other words each Australian citizen can have a number of bank accounts, each with a separate and unique identifying number solely for that person. The payments system for interbank clearances is readily adaptable to this identifier which would fully replace the bank state branch system of numbering, and thus make it very simple for a client to move banks whilst retaining their account numbers. Of course the banks will oppose this and provide significant reasons why this can't be done, but it can simply be legislated for with 12 months notice of compliance.[108]

7.112 The banks in general, however, expressed caution about the idea, whether through dislike for improved competition or genuine concern about technical problems:

> We are dealing with very complex and ageing infrastructure in the banking environment, so we would have to look into the time taken.[109]
>
> …this account portability and the fact that this is going to go out for further consultation is quite an important thing. The actual logistics and difficulties of doing this and the cost of it would be so huge.[110]

7.113 Some other parties were also wary:

> Bank account number portability may have limited benefits for small business lending, and may impose significant costs upon the banking sector.[111]
>
> Account number portability is an idea that should be examined, but the legal and compliance hurdles, along with their associated costs, are likely to be considerable, particularly for smaller mutual institutions.[112]

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107 Associate Professor Frank Zumbo, *Submission 56*, p 6.

108 Mr Mervin Reed, *Submission 5*, p 8.

109 Mr Cameron Clyne, Chief Executive Officer, National Australia Bank, *Committee Hansard*, 13 December 2010, p 65.

110 Mr Michael Smith, Chief Executive Officer, ANZ Banking Group, *Committee Hansard*, 15 December 2010, p 126.

111 WA Small Enterprise Network, *Submission 68*, p 3.

An attempt to force an artificial addressing constraint to support account switching would tend to dampen this competitive evolution.[113]

…we would have to replace the BSB number system with a different arrangement if we were to move to account number portability.[114]

7.114 A banking analyst was also wary on technical and cost grounds:

… the proposal to have account number portability will be very difficult. When we look at this, a lot of banks have the BSB number and the account number; the various banks have different numbers. Remember that some of the IT technology and the core banking processes go back to the 1960s and that there are more than 100 ADIs in Australia. Every bank has to try to redo their IT systems. Some of the banks that we have spoken to over the last couple of days and previously have suggested that it will cost the major banks several hundred million dollars each to implement this account number portability.[115]

7.115 He also raised a prudential concern:

Northern Rock is a classic example. When there was a run on a financial institution, the IT system spontaneously crashed. That was convenient but it meant that not as many people could go online and transfer their savings across. The queues went out the door and there were not that many tellers there. That slowed the run on the bank, and it eventually failed anyway. If you have account number portability, in the event that rumours go around that there could be a financial institution under stress, it will lead to instability… If you think about the Basel committee's reforms on liquidity, we want sticky deposits and we want term funding. With account number portability, it is diametrically opposed to sticky deposits because, by definition, deposits will become less sticky.[116]

7.116 This concern was not thought likely to be a problem by a major bank:

…if a customer had issues with a particular institution then they might just withdraw their money and then put it in somewhere else much more quickly rather than try to switch accounts like that.[117]

7.117 The Committee asked APRA about this and APRA responded that:

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112 Abacus, *Submission* 53, p 24.

113 Australian Payments Clearing Association, *Submission 49*, p 8.

114 Mr Christopher Hamilton, Chief Executive Officer, Australian Payments Clearing Association, *Committee Hansard*, 21 January 2011, p 31.

115 Mr Jonathan Mott, Bank Analyst, UBS Securities Australia, *Committee Hansard*, 14 December 2010, pp 146-7.

116 Mr Jonathan Mott, UBS Securities Australia, *Committee Hansard*, 14 December 2010, p 147. A similar concern was raised by Mr Nicholas Palmer, *Submission 22*, pp 3-4.

117 Mr Graham Hodges, Deputy Chief Executive Officer, ANZ Banking Group, *Committee Hansard*, 15 December 2010, pp 131-2.

> From a prudential perspective, portability would expose ADIs to greater liquidity management pressures and would be likely to require them to hold higher levels of liquid assets to compensate for increased customer movement.[118]

The September 2008 package

7.118 The Government announced a package of measures in September 2008 aimed at facilitating movement between financial intermediaries. A key part of the package was the requirement for ADIs to provide their customers, if they wanted to switch, with a list of direct debit and credit payments going back 13 months.

7.119 It appears to have had a limited impact so far:

> Usage of the switching package has been low…In the year to September 2010, 2541 lists of regular payment arrangements were issued to consumers at their request.[119]
>
> …consumer awareness of this is relatively low and CUA's experience has been that very few consumers have taken advantage of the legislation.[120]
>
> A recent internal ASIC survey reportedly showed '40% of 1,207 respondents couldn't be bothered switching banks because of the hassle, 10% said there was no point changing because all banks are the same and 10% found switching too hard a process'.[121]

7.120 ASIC conducted a review of the initiative and its report was later released under Freedom of Information. ASIC summarised the results for the Committee:

> …implementation had happened consistent with the requirements. But there was a relatively low level of usage at that point—this is probably going back two years—though consumers who had used the new procedures generally reported a better experience switching than those who had not. We identified that one of the problems in the situation is making sure consumers are aware of this possibility of the service. It is very difficult to compel an institution to advertise to its customers that it will give them help to leave, and that is probably too much to expect from institutions… there was a relatively low level of understanding or knowledge of this facility by consumers.[122]

7.121 The Government attributes the limited take-up so far to the GFC:

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118 APRA, *Responses to questions on notice,* no 6, 31 January 2011, p 3.

119 Australian Payments Clearing Association, *Submission 49,* p 5.

120 Credit Union Australia, *Submission 85,* p 10.

121 Maurice Blackburn Pty Ltd, *Submission 31,* p 6.

122 Mr Greg Kirk, Senior Executive Leader, ASIC, *Committee Hansard,* 21 January 2011, pp 10-11.

> During the turbulence of the global financial crisis it is understandable that many savers would have had a preference for the stability of their existing institution…more consumers will utilise the account switching service as competition returns to the banking sector and the benefits of the package become more widely known.[123]

Alternative approaches

7.122 The Committee received evidence on possible alternative approaches to full deposit account number portability:

> You might be in a situation where you could have a user interface that allowed you, if you had multiple bank accounts, for example, to redirect a direct debit from one banking institution to another. That would require you to have accounts in other banks, but if you had an account with bank A and you decided you preferred the deal with bank B then you could redirect direct debits from A to B. There are things that can be explored that may not be as complex or timely as total account portability.[124]

> I am not sure that we need an expensive, high-tech solution. We see in some other countries that there is a process where you tell the new bank that you want to leave the old banking institution and they have a positive obligation to provide standard information in a set time frame and a way of verifying that it is the right person.[125]

> There are solutions that have been tried in Europe. There is a solution short of portable bank account numbers which we have supported, which is to require the new bank to take the hassle out of switching for you as a customer by authorising them to deal with your old bank within a clear time frame and transfer your direct debits and direct credits across.[126]

> …there are a number of other mechanisms significantly beyond what we currently have in Australia in other jurisdictions such as New Zealand, Europe and the Netherlands which stop short of actual account number portability but still enable a significantly more effective switching by consumers than we currently have in Australia.[127]

7.123 The European Union has recently introduced measures, falling short of full account portability, but which sound like they would facilitate account switching. They provide that:

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123 Australian Government, *Competitive and Sustainable Banking System*, December 2010, p 9.

124 Mr Cameron Clyne, Chief Executive Officer, National Australia Bank, *Committee Hansard*, 13 December 2010, p 65.

125 Ms Louise Petschler, Chief Executive Officer, Abacus, *Committee Hansard*, 13 December 2010, p 89.

126 Mr Richard Lloyd, International Policy Adviser, Choice, *Proof Committee Hansard*, 14 December 2010, pp 33-34. He later (p 35) referred to the Netherlands as a specific example.

127 Ms Catrinoa Lowe, Co-Chief Executive Officer, Consumer Action Law Centre, *Committee Hansard*, 25 January 2011, p 14.

- banks must provide consumers with a switching guide explaining what steps need to be taken in the switching process, by whom and within which timeframe;
- if the consumer chooses, their new bank must act as a complete intermediary between the consumer and their old bank as well as third parties, by which we mean that the new bank (not the consumer) performs all the relevant steps, including obtaining the necessary information about the consumer‗s recurrent payments from their old bank, reinstalling these payments on the new account, asking the old bank to cancel these payments on the old account, and informing third parties about the consumer‗s new account details;
- the new bank must assist the consumer to request that their old bank close their old account and transfer the remaining balance;
- there are clear timeframes that must be followed, including that the old bank must provide the information about recurrent payments within seven banking days of receiving the request to do so and the new bank must set up the recurrent payments on the new account within seven days of receiving this information; and
- the information provided by the consumer's old bank and the closure of their old bank account should generally be free of charge.[128]

7.124 The Netherlands system works as follows:

> Once a consumer (or a small business) applies to use the switching service, for 13 months their new bank ensures that their old bank reroutes direct credits to the new account and as direct debits hit the old account, they are also rerouted and the creditor is informed of the new account and to change their details for future debits. (The consumer must inform their employer and other parties that direct credit their account about their change in account sometime within the 13 months – they receive a notification of the impending end of their switching service one month before it ends.) Rerouted transactions are separately noted on the consumer‗s bank account statements.[129]

7.125 A European entrant to the Australian market believes the Netherlands approach is a successful model:

> We understand the Dutch system has resulted in around 100,000 customers shifting each year as a result of that. It really did shift the dial.[130]

7.126 ING Bank refers to a new scheme in New Zealand:

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128 Consumer Action Law Centre, *Submission 87*, p 9.

129 Consumer Action Law Centre, *Submission 87*, p 9. See also Choice, *Response to questions on notice*, no 5, 17 December 2011.

130 Mr Matt Baxby, Managing Director, Virgin Money Australia, *Proof Committee Hansard*, 4 March 2011, p 29.

> …a new company called 'Payments NZ' owned by ANZ, Westpac, ASB, BNZ, Kiwibank, HSBC TSB and Citibank, has been established. Our understanding is that Payments NZ, will be taking over the New Zealand Bankers' Association's Electronic Credit System Code and the Direct Debit Systems Code, which documents the operational agreements and arrangements among member banks for clearing electronic credits and direct debits. Under this proposed model, the customers will fill out a form authorising the incoming bank to get all the customer's information relating to direct debits and credits linked to their existing account from the outgoing bank and the incoming bank will organise the entire switching process and have the direct debits and credits linked to the new account number with the incoming bank.[131]

7.127 The Consumer Action Law Centre contrasts the EU and Netherlands schemes with that developed in Australia. Among the deficiencies of the Australian scheme they highlight are that it only requires the old bank to produce a paper list of payments and the customer must then sort through these and notify the parties involved, it excludes credit card accounts and there is no restriction on customers being charged a fee by the old bank.[132]

7.128 The Centre concludes:

> …the Australian listing and switching service compares poorly with overseas practice and strongly recommend that it be improved.[133]

7.129 Choice referred to research suggesting 80 per cent of bank customers have not considered moving. Responding to a suggestion that this may be an indication of their satisfaction with their current bank, Choice had the following rejoinder:

> Our annual consumer satisfaction survey across the board for ADIs shows that the banks with the largest market share consistently have the lowest customer satisfaction ratings…You would think that, if they were competing genuinely on price and quality, that would not be the case… there were very clear reasons given by those who considered switching but did not switch in the last two years: the paperwork, the hassle of researching the market and the belief, rightly or wrongly, in the case of individual products that there is not a better alternative out there in the marketplace.[134]

7.130 The Government has announced a feasibility study of introducing full account number portability to report by June 2011. The study will be conducted by former Treasury secretary and Reserve Bank governor Bernie Fraser, and assess the current

131 ING Bank, *Submission 35*, p 4.

132 Consumer Action Law Centre, *Submission 87*, pp 10-11.

133 Consumer Action Law Centre, *Submission 87*, p 11.

134 Mr Richard Lloyd, International Policy Adviser, Choice, *Committee Hansard*, 14 December 2010, p 33.

technology, privacy issues, the potential need for a central account registry and the costs, benefits and risks of introducing account portability on various timelines.[135]

Recommendation 14

7.131 The Committee recommends that a scheme based on those in Europe be introduced requiring a bank, upon being advised that a customer has left for a new bank, to reroute all direct debits and credits for 13 months and provide the new bank with details of those direct debits and credits.

135 Australian Government, *Competitive and Sustainable Banking System*, December 2010, p 8.