Chapter 2

Treasury portfolio

2.1 This chapter summarises certain key areas of interest raised during the committee's consideration of additional estimates for the 2018–19 financial year for the Treasury portfolio. This chapter of the report follows the order of proceedings and is an indicative, not exhaustive, account of the issues examined.

2.2 On 20 and 21 February 2019, the committee heard evidence from Senator the Hon. Mathias Cormann, Minister for Finance, and Senator the Hon. Zed Seselja, Assistant Minister for Treasury and Finance, along with officers from the Department of the Treasury (Treasury) and agencies of the Treasury portfolio, including:

- Australian Taxation Office (ATO);
- Australian Charities and Not-for-profits Commission (ACNC);
- Inspector-General of Taxation;
- Australian Securities and Investments Commission (ASIC);
- Productivity Commission (PC);
- Australian Competition and Consumer Commission (ACCC) and the Australian Energy Regulator (AER); and
- Australian Prudential Regulation Authority (APRA).

2.3 Senators present over the course of the two days of hearings included Senator Hume (Chair), Senator Ketter (Deputy Chair), and Senators, Bernardi, Keneally, Leyonhjelm, Lines, McAllister, Patrick, Sinodinos, Stoker, Storer, Whish-Wilson, and Williams.

Macroeconomic Group and Corporate Group

Departmental Secretary

2.4 Mr Philip Gaetjens commenced the role of Secretary to the Department of the Treasury (Treasury) in August 2018. In this his second appearance at estimates, Mr Gaetjens commented on a number of recent global and domestic economic developments. These included, the Mid-Year Economic and Fiscal Outlook (MYEFO), the release of the final report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (Royal Commission), global economic uncertainty around Brexit, and the effect of recent floods and the ongoing drought on the Australian economy.[1]

2.5 In his opening statement, Mr Gaetjens highlighted the impact that the recent floods and the drought could have on the Australian economy. In particular, Mr Gaetjens commented that there had been major stock losses, as well as the loss of

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1 *Proof Estimates Hansard*, 20 February 2019, pp. 5–8.

many farms and houses. He noted that Treasury would 'continue to monitor the flood situation, both for its localised impacts and for any impacts on the macroeconomic outlook'.[2]

2.6 Mr Gaetjens also noted that the 'expected recovery from the current drought also continues to be a key uncertainty for the forecast':

> The drought continues to play out across various areas of the country, particularly south-eastern Australia. As stated in the mid-year review, the decline in agricultural production in 2018-19 is expected to subtract around a quarter of a percentage point from real GDP growth. Downgrades to winter crop production are expected to be partially offset in the short term by increased livestock slaughtering.[3]

2.7 The final report of the Royal Commission was released in February 2019. Mr Gaetjens informed the committee that Treasury had already begun implementing some of the report's recommendations.

> …for example with the APRA capability review team and terms of reference being announced. As you would be aware, Treasury made a number of submissions and provided other background information to the royal commission. We also established a task force to provide advice to government in preparation for the commissioner's final report. Before that, Treasury was involved in a large number of legislative and other measures to strengthen the financial sector and improve its performance.[4]

2.8 Mr Gaetjens also noted that the organisational structure had undergone some changes with the removal of the Structural Reform Group. He explained that the functions of this group had been split across a number of Treasury's other groups, mostly within the Macroeconomic and Fiscal Groups:

> Macroeconomic group will increase its focus on productivity and understanding the structural changes occurring in our economy, and the productivity and microdata work from the former structural reform group will move into the macro group. By combining macro and micro into a single group I want to achieve a sharper alignment between whole-of-economy aggregates, forecasting analysis and policy choices about growth drivers and productivity. There will also be greater synergies in analytical and modelling expertise to support work across Treasury.
>
> Treasury's work on industry and sectoral policy reforms will now be located in fiscal group. Having sectoral structural reforms sitting alongside the agency-facing functions within fiscal group will facilitate partnering with agencies on structural reform initiatives and also provide synergy benefits. I believe this dual focus on economy-wide productivity and sectoral structural reform will deepen Treasury's capability in this area of

2 *Proof Estimates Hansard*, 20 February 2019, p. 6.

3 *Proof Estimates Hansard*, 20 February 2019, p. 6.

4 *Proof Estimates Hansard*, 20 February 2019, p. 7.

> microeconomics, an area in which I have a deep interest and years of experience earlier in my career.[5]

2.9 Mr Gaetjens commented that this change would 'tangibly demonstrate that structural reform and competition are not the focus of a single group, but are enmeshed across the work of the whole department'.[6]

2.10 Ms Meghan Quinn, formerly the deputy secretary of the Structural Reform Group, is now the deputy secretary of the Macroeconomic group.

Wages growth

2.11 The committee discussed wages growth in Australia with Treasury officials. Noting the relatively positive figures around jobs growth and a falling unemployment rate, the committee asked Treasury officials about what other factors may be causing the seemingly slow wages growth.

2.12 Mr Gaetjens considered that attributing slow wages growth to one or two factors was not possible; however, he noted that Australia was not alone in experiencing a slowing of wages growth:

> I think this is an issue that has been happening around the globe as well as in Australia. I would say, though, that the latest figures in Australia would indicate that the wage price index has probably troughed. The last number for that was 0.6 for the quarter, and I think that was 2.3 per cent for the year.[7]

2.13 Mr Gaetjens also commented that although wages were not growing rapidly, neither was inflation:

> In fact, the inflation that relates to administered prices by governments is again quite low. It would depend upon the time you measure this, but we'd be round about saying that wages are keeping up in real terms, I think. So it is happening.

2.14 Ms Quinn also noted that the Australian economy has different characteristics to other economies, and noted that wages are picking up in some parts of the global economy:

> Globally there has been a shift, and one of the reasons for that is the technology and shifts in what's happening in particular industries. We've seen the productivity improvements in Asia, for example, reduce the price of manufacturing goods. That reduces inflation around the world, and it reduces nominal wages around the world as well. In terms of Australia, we've had the commodity cycle, which has been particular to the commodity countries, such as Australia and Canada.[8]

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5 *Proof Estimates Hansard*, 20 February 2019, p. 7.

6 *Proof Estimates Hansard*, 20 February 2019, p. 7.

7 *Proof Estimates Hansard*, 20 February 2019, p. 19.

8 *Proof Estimates Hansard*, 20 February 2019, p. 25.

2.15 Mr Gaetjens further noted that 'that there has been a preponderance of full-time jobs over a longer period':[9]

> …in terms of the national accounts, we see wages numbers driven by, in fact, good employment growth. So, in an aggregate sense, we are getting the impact of heads in employment rather than the wages themselves.[10]

Jobs Growth

2.16 The committee continued the discussion around jobs growth in Australia, noting the employment growth estimates and forecasts listed in the MYEFO. This forecast indicates that Australia will see the creation of 1.25 million jobs over five years to 2022-23.[11]

2.17 In explaining how the forecasts were able to reach this total, Ms Quinn noted that the employment projections only go to 2021–22:

> In order to achieve 1.25 million jobs, you need employment growth in the order of 1.9 per cent a year. To put that into some historical context, we've had 2.1 per cent as the average for the past five years.[12]

2.18 Ms Quinn noted that in order for the commitment of 1.25 million jobs created to be reached, average employment growth over the next five years would need to be at 1.9 per cent per year.[13]

2.19 The committee noted that the MYEFO forecasts were for a growth rate of 1.75 per cent in 2018–19 and 2019–20, and 1.5 per cent in the two following years. The committee considered that the rate of jobs growth would need to increase considerably in the fifth year, in order to reach the target of 1.25 million jobs in five years.[14]

2.20 Ms Quinn highlighted that increasing participation rates would also play an important role in jobs growth. Ms Quinn noted that workers remaining in the labour force longer as well as more women entering the labour force were key factors. Ms Quinn commented:

> Some of those workers will have been encouraged into the labour market off the back of the strong employment growth. Others will have done it because we've changed some of the administrative arrangements around retirement conditions, making it easier for people to work part time and transition into retirement. Also, flexible work arrangements have meant that

9 *Proof Estimates Hansard*, 20 February 2019, p. 19.

10 *Proof Estimates Hansard*, 20 February 2019, p. 19.

11 *Proof Estimates Hansard*, 20 February 2019, p. 30.

12 *Proof Estimates Hansard*, 20 February 2019, p. 30.

13 *Proof Estimates Hansard*, 20 February 2019, p. 31.

14 *Proof Estimates Hansard*, 20 February 2019, p. 31.

> it's easier for people to juggle family responsibilities. So there are structural and cyclical factors pushing up the participation rate in Australia.[15]

Markets Group

Banking Executive Accountability Regime

2.21 The committee asked Treasury about the implementation of the Banking Executive Accountability Regime (BEAR), following the recommendations of the Royal Commission.

2.22 Treasury officials noted that the BEAR was discussed during some of the Royal Commission public hearings and highlighted that the BEAR had been positively received by some banking officials as well as the regulators. Treasury officials explained:

> …the major banks that have been subject to the regime, there have been comments that they have found it useful. Mapping responsibilities and being clear who is held accountable are things you would have thought they would have already had knowledge of or clarity about within their organisations, but the imposition of the BEAR has helped them understand those things.[16]

2.23 Treasury officials also noted that the final report of the Banking Royal Commission includes several recommendations about the BEAR; notably, that it should be extended to include the superannuation and insurance industries. The final report also recommended that the BEAR should have a greater role in respect of conduct issues:

> At the moment, the BEAR has a prudential focus; conduct can affect the prudential standing of an organisation, but it doesn't necessarily cover the full scope of conduct.[17]

2.24 The government response to the final report noted its support for this extension of the BEAR. Treasury officials commented:

> It wanted to make sure that it covered the full field of conduct issues, and in that sense it gave it to ASIC, and it sets its own separate regime that covered conduct. So one difference that makes is that not only the prudentially regulated entities would be subject to this new accountability regime but that it would extend into areas such as management, which otherwise may not be captured.[18]

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15 *Proof Estimates Hansard*, 20 February 2019, p. 31.

16 *Proof Estimates Hansard*, 20 February 2019, p. 74.

17 *Proof Estimates Hansard*, 20 February 2019, p. 74.

18 *Proof Estimates Hansard*, 20 February 2019, p. 74.

2.25 Treasury officials also noted that one of the final report recommendations was to further extend the BEAR beyond the prudentially regulated entities, such as wealth management firms and other financial institutions.[19]

Australian Securities and Investments Commission

Chair's opening statement

2.26 Mr James Shipton, Chair of ASIC, made an opening statement to the committee which also focussed on the final report of the Royal Commission.

2.27 Mr Shipton noted that ASIC had recently released an update on its planned actions responding to the Royal Commission's final report, highlighting that:

> The royal commission's recommendations reinforce, and will inform part of the implementation of, steps ASIC has been taking as part of a strategic program of change that commenced in 2018 to strengthen our governance and our culture and to realign our enforcement and regulatory priorities. The royal commission's recommendations directed at ASIC are one of the key parts of this update. Along with ASIC's extended remit and strengthened powers and penalties, it also deals with referrals from the royal commission and mentions the establishment of an office of enforcement and a why-not-litigate posture. It also touches upon our broader strategic change program and the policy and regulatory reforms advocated by ASIC over the years.[20]

2.28 Mr Shipton commented that ASIC's deputy chair, Mr Daniel Crennan QC, had recently completed an internal enforcement review, which led to ASIC establishing an Office of Enforcement (Office). Mr Shipton explained that the Office would be accountable to the commission and would 'investigate and take enforcement action where there are contraventions of the law' that ASIC regulates.[21] Mr Shipton also highlighted that the Office would adopt a 'why-not-litigate enforcement stance'.[22]

2.29 Mr Shipton further noted that the impact of these changes would become visible over time, but that some progress had already been identified:

> However, as an early indication, since 1 February 2018 there has been a 15 per cent increase in the number of ASIC enforcement investigations on foot and a 50 per cent increase in the number of ASIC enforcement investigations of misconduct by large financial institutions, or their employees or subsidiary companies.[23]

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19 *Proof Estimates Hansard*, 20 February 2019, p. 74.

20 *Proof Estimates Hansard*, 20 February 2019, p. 85.

21 *Proof Estimates Hansard*, 20 February 2019, p. 85.

22 *Proof Estimates Hansard*, 20 February 2019, p. 85.

23 *Proof Estimates Hansard*, 20 February 2019, p. 85.

ASIC's funding

2.30 The committee discussed the level of funding for ASIC set out in the MYEFO. The committee noted that ASIC's revised level of funding for 2018–19 was $498 million; and further, that ASIC's funding was due to progressively decrease over the forward estimates as follows:

- 2019–20: $474 million;
- 2020–21: $424 million;
- 2021–22: $423 million.[24]

2.31 Mr Shipton acknowledged that these numbers showed a decrease in ASIC's funding; however, advised the committee that ASIC is in 'very active and positive discussions with the government right now on our funding and our forward funding for the periods into the future'.[25]

2.32 The committee also noted that similar decreases could be seen in the levels of funding for staff over the forward estimates in MYEFO. Mr Shipton commented:

> In the absence of an increase in funding, yes, there will be constraints and we would be asked—we would be compelled—to look at constraining our expenditure. But, again, I would highlight that I've been actively engaged for quite some time, along with my colleagues, in very productive discussions of this nature, highlighting the fact that resourcing appropriate staff levels, including investments in technology, are an important imperative.[26]

2.33 Mr Shipton also noted that ASIC's resourcing did not go only to staffing, but also to new technologies and beyond:

> But, of course, yes, we have desires in relation to the development of regulatory technology and the use of data analytics. We have a regulatory transformation program which is very technology driven. So, yes, there's a range of asks, and, of course, I would also like to take the opportunity to say that some of the expectations on us moving forward in relation to enforcement are going to require expenditure. We'd also like to expand the regulatory tools that we're applying, like close and continuous monitoring. So, yes, there's a range of different factors, and, again, I'd stress that we are in very positive constructive dialogue with the government, who are aware of what we want.[27]

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24 *Proof Estimates Hansard*, 20 February 2019, p. 97.

25 *Proof Estimates Hansard*, 20 February 2019, p. 97.

26 *Proof Estimates Hansard*, 20 February 2019, p. 97.

27 *Proof Estimates Hansard*, 20 February 2019, pp. 97–98.

Australian Competition and Consumer Commission and the Australian Energy Regulator

Retail Electricity Pricing Inquiry

2.34 The committee discussed the ACCC's final report on the Retail Electricity Pricing inquiry (inquiry). The committee noted that as part of the inquiry, the government asked the ACCC to identify measures which could reduce electricity prices.

2.35 Mr Rod Sims, Chair of the ACCC, noted that the report made a number of recommendations which could see residential and commercial customers' bills reduced by approximately 25 per cent.[28] Mr Sims explained:

> The first key recommendation was to write down—or introduce measures for similar effect—the regulatory asset base of the network companies in Queensland, New South Wales and Victoria. Of course, network assets are the biggest component of electricity pricing, which sometimes seems to be lost in the public debate.
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> We recommended ceasing the subsidy for small-scale solar, simply because it was no longer needed. Small-scale solar is now economic, so we weren't forming a view about the pros and cons of small-scale solar; we were simply saying it no longer needed the subsidy. Thirdly, we recommended a default offer—price replace the standing offers of retail electricity companies—both to get those standing offers down, because there are people paying hundreds of dollars more than they need to, and small business the same, and also to use that default offer as the reference point for discounts. At the moment, customers really can't tell whether a 40 per cent discount is a better offer than a zero per cent discount, so we wanted to standardise that. We also wanted to get rid of conditional discounts where you could be on a 40 per cent discount, you miss paying on time by a few days and, all of a sudden, you lose the 40 per cent discount, which could be a penalty of hundreds of dollars and which is completely unrelated to whatever cost the lack of paying on time caused the retailer.[29]

2.36 Mr Sims also noted several other recommendations including the creation of an underwriting scheme for new generation. Mr Sims explained that this would have 'strict conditions to make sure it was only supporting generation provided by new or currently small generators'.[30]

Consumer Data Right

2.37 The committee asked officials from the ACCC about open banking and the consumer data right (CDR). Mr Sims explained to the committee that 'there are many benefits to open banking':

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28 *Proof Estimates Hansard*, 21 February 2019, p. 4.

29 *Proof Estimates Hansard*, 21 February 2019, p. 4.

30 *Proof Estimates Hansard*, 21 February 2019, p. 4.

> …the dominant one I see it is that you can say to your bank, 'I want all my history in relation to my mortgage so that that information is there.' You can either go to another bank that you may be talking or you can go to some intermediary who can help you find the best deal. So you can find the best deal without having to go to all the trouble of going through torturous processes to provide what data is needed. It will help consumers get a cheaper mortgage and it will help competition in the market.[31]

2.38 Mr Sims pointed out that, with the introduction of open banking, the necessary financial information will be readily available and presented in a form that is usable.[32]

2.39 In discussing the relationship between open banking and the CDR, officials from ACCC considered that the issue is not 'how the CDR fits in with open banking but rather how open banking fits into CDR', noting that 'it provides for sector by sector, giving consumers access to their data that is currently held by the data holders'.[33]

> The scheme operates on the basis that the ACCC will write the rules. We'll accredit the third-party data receivers—they're the Fintecs or the switchers. The rules will set out the mechanisms by which the banks might release the data. Consumers will provide the consent and the data receivers how they use that material. We are not doing this alone. We are also working with the OAIC—the privacy commissioner—who is advising government on the designation of future sectors and the privacy issues there, and also advising us on the rules to make sure that there are secure and private platforms to use. We are also working closely with Data61 and the data standards board, who are connected, obviously, and they are providing the technical standards by which the data is released.[34]

2.40 The committee noted that there were some concerns around privacy and security of the CDR which had delayed its start date.

2.41 ACCC officials advised the committee that 'progressing things in a timely and ambitious way is often an appropriate path to take to achieve good for the economy'.[35] Officials noted that security and privacy were two of a number of complexities in developing the CDR:

> As we get our teeth into this and understand the issues, we find there's a lot of complexity. A lot of that came through the consultation that we've had, both publicly and with others. I think this is just par for the course when you're dealing with complex issues.[36]

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31 *Proof Estimates Hansard*, 21 February 2019, p. 11.

32 *Proof Estimates Hansard*, 21 February 2019, p. 11.

33 *Proof Estimates Hansard*, 21 February 2019, p. 11.

34 *Proof Estimates Hansard*, 21 February 2019, p. 11.

35 *Proof Estimates Hansard*, 21 February 2019, p. 12.

36 *Proof Estimates Hansard*, 21 February 2019, p. 12.

Australian Prudential Regulation Authority

Housing market

2.42 The committee asked officials from the APRA about the effect of the agency's recent macroprudential measures on house prices in Australia. Mr Wayne Byres, Chair of APRA, commented that APRA had not done any modelling on this issue.

2.43 Mr Byres also noted that Treasury or the Reserve Bank of Australia would be better placed to undertake this type of modelling. The committee noted that Treasury had confirmed it had not done any modelling on this issue.

2.44 Mr Byres pointed out that APRA's work was not focussed on house prices; rather, APRA's macroprudential measures were designed to address lending standards. Further, Mr Byres noted that any modelling of house prices in Australia would include many factors other than lending standards:

> There is a whole raft of issues beyond lending standards that impact on supply and demand for housing—for example, population growth, foreign investment. There have been changes to state government taxes, changes to interest rates. There is a whole raft of issues at play here, and any sort of modelling would probably have assumed all of those things anyway, but they have a big impact on house prices—I suspect more than we do.[37]

2.45 Mr Byres also noted that Australia does not only have one housing market, it has several:

> Sydney and Melbourne have obviously had big run ups and are now having a correction; Adelaide has been pretty flat through the period; Perth is still feeling the after effects of the commodities boom, and prices have been declining; Hobart prices have been increasing. So there are very different market conditions. Regional Australia has a different set of conditions and experiences, so modelling all of those things at that level would be extremely difficult I think.[38]

2.46 Mr Byres did indicate, however, that APRA had considered the impact of tightening lending standards on a range of other measures, including on the supply of credit, the impact on the average borrower, the average lender's loan size, and how would LVRs (loan to value ratios) adjust.[39]

2.47 Mr Byres also noted that the decrease in house prices in Sydney and Melbourne was 'probably inevitable':

> …it's been inevitable after such a sharp run-up that at some point the market has to pause. There has also been a delayed response from the supply of housing stock as well as the supply of housing stock, so there's now a lot of housing stock coming on the market, particularly in Sydney. Population growth has slowed. So you have a number of big macro impacts

37 *Proof Estimates Hansard*, 21 February 2019, p. 23.

38 *Proof Estimates Hansard*, 21 February 2019, p. 23.

39 *Proof Estimates Hansard*, 21 February 2019, p. 23.

> that are playing out, and as the demand for housing softens and the supply of housing increases, it's not unreasonable to think that prices will soften and maybe drop back a bit.[40]

Consumer data right

2.48 The committee noted that APRA had previously expressed concern about systems readiness of the big financial institutions to respond to the rollout of reforms including the CDR and asked APRA to update the committee on systems readiness for the introduction of the CDR.

2.49 Mr Byres commented that the introduction of the CDR presented a 'relatively ambitious agenda'; however, he also believed that the banks were working to prepare their systems to meet the obligations of the CDR when it commences.[41]

2.50 Mr Byres agreed that the CDR will have major implications for competition, for consumers, innovation, big data flows, privacy, and cybersecurity. Mr Byres also noted, however, that the aim of the CDR is to improve systems:

> It's good for the community, it's good for competition and, if done well, from my perspective there are not really any material prudential concerns. In the interests of getting it right, if that means taking a little bit more time—some of the timetables have been adjusted—then I think that's probably a very sensible thing. I'd much rather get it right than have something go wrong in the early days that means the community's trust in the system is undermined.[42]

2.51 The committee asked APRA whether a more staged approach would be beneficial to the introduction of these reforms. Mr Byres noted that ACCC would be managing the implementation of the CDR, but that APRA did not see the need for a more staged rollout.[43]

Other topics raised

2.52 The committee discussed a wide range of topics during the two days of hearings with the Treasury portfolio. The above reporting of discussions is not complete. Other topics discussed by the committee included:

- Real gross domestic product (GDP) growth factors;
- Treasury modelling of taxation policies;
- Infrastructure spending;
- House of Representatives Economics Committee inquiry into refundable excess franking credits;
- Methodology used by Treasury for forecasts and projections;

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40 *Proof Estimates Hansard*, 21 February 2019, p. 23.

41 *Proof Estimates Hansard*, 21 February 2019, p. 24.

42 *Proof Estimates Hansard*, 21 February 2019, p. 24.

43 *Proof Estimates Hansard*, 21 February 2019, p. 24.

- Tax integrity information campaign;
- Funding for the National Competition Council ;
- Protecting you superannuation package;
- Superannuation Guarantee—amnesty;
- Superannuation (Objective) Bill 2016 and the Super Saver Scheme;
- Procedures for costing revenue measures;
- Capital Gains Tax main residence exemption for non-residents, Treasury Laws Amendment (Reducing Pressure on Housing Affordability Measures No. 2) Bill 2018;
- First Home Super Saver Scheme—commencement of operation; number of participants; Treasury modelling and projections; complaints regarding release of funds; demographic information of participants;
- Disputed debt and ATO recovery action prior to the outcome of a review;
- Appointment of Mr Ian Klug as Chair of the Tax Practitioners Board;
- Small business claims for instant asset write-off;
- Establishment of ATO office in Gosford—staffing, including number of staff from central coast and number of transfers from other offices;
- ATO's enhanced compliance activities;
- Corporate tax minimisation—transparency and reporting;
- GST obligations of political campaigning entities that are not a political party;
- Distinction between subscriptions and donations for tax purposes;
- Tax Transparency Code—Defence companies;
- Black economy measures and procurement;
- Acknowledgment of country in ACNC staff emails;
- ACNC Staff survey;
- Beneficial Ownership register—proposal, consultation and inaction;
- Australian Business Securitisation Fund Bill 2019;
- Update on the office of the Inspector-General of Taxation;
- ASIC's investigation into Queensland Nickel and Clive Palmer;
- ASIC's involvement in ANZ/Goldman Sachs with Malaysia;
- New ASIC power for insurance claims handling;
- Enhancing Whistleblower Protections legislation;
- Unfair contract terms and insolvency;
- Responsible lending guidelines;
- Productivity Commission's final report on the Superannuation inquiry;

- Murray-Darling Basin Plan report;
- Inequality study in Australia;
- APRA's data capability—gaps identified by PC;
- National Energy Market;
- Food and grocery code of conduct;
- Complementary medicines taskforce;
- Milk prices—Woolworths' decision to increase price; and
- Manufacture of fish oil.