

FINANCIAL SYSTEM INQUIRY REPORT:

--- STAKEHOLDER VIEWS ON THE RECOMMENDATIONS

What follows responds to the Treasurer's call for stakeholder views on the final report of the 'Murray' inquiry into the financial system.

An overview indictment

The recurrent theme in my assessment of the Murray report is that the major recommendations are generally cast in vague and restrained terms and reasonable inferences and likely implications are not drawn or sensibly spelt out.

They should be. Governments typically need to have a bit of 'four by two' in clear sight before they see the light – this report does not demand needed reforms clearly enough.

More generally I had problems with the inquiry process being opaque – there was no record of what was said in the course of consultations and no opportunity for others to get a hearing or interact with the panel or secretariat in any meaningful way. Some substantial issues raised were simply ignored, or ducked, and that compromises the panel's credibility.

This is no 'Campbell' or 'Wallis' report – rather, it has hallmarks of a panel gently addressing an unreasonably limited agenda when a broader and stronger sense of purpose was called for. Lacking clarity, and having a too-narrow focus, there is no firm basis for the government to be held accountable for its response to the report.

More specifically, it is worrying that the Treasurer has already hand-passed some recommendations to APRA and the RBA *'to consider as independent regulators'*. This is hardly good enough when, for example, the 'independent' performance of the RBA, especially, falls short of being good enough (beyond its monetary policy responsibilities). The Treasurer alone has direct responsibility for deciding the Government's response.

As an aside, for example, a reasonable inference from the assessment of the regulatory framework, is that the performance of the RBA, beyond its monetary policy responsibilities, should be subject to merits review – so, the panel should have clearly said that the present exemption of the RBA from such independent performance reviews should be withdrawn. Not so said, the Treasurer may miss the point (as I fear he has).

A pervasive general concern arises in the panels' apparently prejudged complacency about the financial system being generally competitive and well regulated -- when it is anything but – and then turning a blind eye to the damning and burgeoning evidence to the contrary.

That said, some recommendations were very welcome – bank shareholders, and holders of their subordinated debt and deposits, do need to have much more skin in the game to ensure prudent management.

Fairly also, the game is about up for the current over reliance on snow-job disclosure rules that protect the institutional gaming which only confuses and misleads customers rather than protecting them.

Some particular shortcomings

My sense of particular shortcomings outlined below reflects my experience in regulation policy generally and for retail banking and retail payment systems in particular – especially issues about ‘competition’ and efficiency’ and ‘consumer protection’.

- consumer protection

On the consumer protection front the record of deliberate institutional misbehavior – including price gouging and exploitation -- is recurrently disturbing. Shifting the emphasis from ‘disclosure’ to ‘product design’ may simply open another front in the game of ‘complying’ but in a way that again defeats the spirit of the policy.

It is surely about time that financial institutions were put on notice that if their behaviour falls short of meeting a golden-rule test, they will be required to redress the damage done. It is not usually difficult to decide if something someone does is contrary to what they would like done to themselves or their dependants. Offenders would ‘golden rule’ against themselves.

Put differently, financial institutions, and their staff, should be required to subscribe to a code of conduct that precludes golden-rule offences – voluntary initiatives of that kind are emerging and official endorsement would reassure customers that they will get a fair go.

Against this background it is surely ‘second best’ to talk vaguely – as in **Recommendations 21 and 22** -- of ‘*principles based product design and distribution obligations*’ coupled with ‘*a proactive product intervention power.....where there is a risk of consumer detriment*’.

Spare my days -- consumers surely and simply want something akin to ‘golden rule’ reassurance that they will not be rorted and, if they are, that there will be a low-cost avenue for prompt redress.

- competition

On the competition front it seems the panel was determined to simply overlook the most glaring of impediments – impediments which are founded in bad public policy settings unfairly inimical to competition.

In short, for one thing, the four major banks unfairly have an unassailable competitive advantage while ever they are permitted to barter ‘free’ transactions for ‘interest-free’ deposits in transaction accounts – bank deposits, almost all with these major banks, on which ‘no’ interest is paid now run to some \$900 billion but the substitution of income-in-kind, for taxable interest, is tax free in the customers hands.

While ever this nonsense remains to be corrected there will, as for decades now, be no new entry to retail banking only further concentration.

For another thing, these same major banks are given ‘joint venture’ protections to fix gouging prices in the conduct of redundant credit card schemes. Stop this nonsense!

How could the panel be of a mind that retail banking is ‘competitive’ or has any prospect of being so? On the spectrum of being competitive or not, retail banking, as is, is more akin to a cartel.

Whatever, to the extent the panel seems to understand this failure, **Recommendation 30** is naive to the point of negligence – reluctant competition-regulators that need to be newly told to ‘*examine their rules and procedures..... to remove barriers to competition*’, should be summarily dismissed and the responsibility given to another regulator.

- **efficiency**

The efficiency of the financial system is similarly being mocked in the absence of competition and effective, compensating regulation.

Again, glaring examples are endemic in retail banking – the retail payments system is devoid of the proper price signals required to ensure that payment services used by customers are in any way consistent with ‘least cost’ as distinct from ‘most profit’.

30 years on, the RBA’s pride in its reluctance to meet its regulatory responsibilities for retail banking and the retail payments system is lamentable.

Again the panel seems to realize this – and again the panel minces its words to soften its conclusions when what was needed, again, was a verbal wielding of the bit of ‘four-by-two’.

Recommendation 17 is typical of the reluctance to call the shots fairly – it implicitly recognizes the dominant credit card schemes to be a racket but stops well short of demanding they be properly regulated, as they should be, by the RBA proscribing any and all transaction fees charged as a % of transaction values. There would be ‘nothing’ left to surcharge.

Recommendation 14 is so naïve as to question the panel’s competence and sincerity – in my experience, the long history of ‘regulating’ the retail payments system is testimony to the determination of the banking cartel to be willfully reluctant to collaborate in the public interest while ever willing to do so (collude) in their private interest.

..... and, in the context of ‘innovation’, there is a missing recommendation. The situation with the Australian currency issue is hardly defensible but was not addressed. Not much of the \$60+ billion of banknotes on issue is in active circulation as a day-to-day medium of payments. Over 90% of these notes on issue, by value, are in the fast growing \$50 and ‘never seen’ \$100 denominations. The reasonable inference is that most of the value of the notes on issue is hoarded for purposes of roting the public purse -- quite contrary to being ‘in circulation’ and quite inimical to the national interest. The RBA could do much better.

regulatory failure

Taken together, the so-evident shortcomings in respect of consumer protection, competition and efficiency, surely question the competence and commitment of the appointed regulators to meet their legislated responsibilities.

Equally, the also so-evident community concern with the inclination of major financial institutions to exploit their customers, should have ensured the panel ran annoying issues to ground rather than take refuge in some contrarily vague faith in the regulators doing their job well. They are not.

The panel does implicitly concede some regulatory defects – with ASIC, APRA and RBA payments system policy -- and proposes a new regulatory assessment board to ensure their accountability, effectiveness and capacity as well as them giving ‘competition’ more attention.

As presented, this proposal, at **Recommendation 27**, is fairly called ‘vague’ -- it would better, and best, be illustrated by more clearly identified instances of regulatory failure. There is no shortage of regulatory shortcomings buried in confused concepts of regulatory ‘independence’ displacing competence and effectiveness while denying accountability.

The minced words of the panel here need to be converted to plain-English to give a clear sense of direction – not least ensuring that any regulatory ‘auditors’ are able to hear ‘complaints’ that will focus their attention on actual problems presented in real terms by real people.

End piece

Having waited so long for this ‘next’ independent review of the financial system, the final report is very disappointing. The report filed by the Murray committee falls so far short of the appropriate scope of the task the community wanted done and it is written in such vaguely opaque terms as to be next to incomprehensible as to what is recommended be done and why.

We still need an inquiry into the Australian financial system. The community wants reform of present practices that are so contrary to a fair, competitive and efficient financial system. It is past time for regulation to be more purposefully in the public interest -- and less in the private interest of the major players monopolizing the system.

I would appreciate an opportunity to discuss my views with those advising the Treasurer, and Treasury Ministers, about what to do next.

Peter Mair

29 January 2015