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**From:** Section 22 @pm.gov.au>  
**Sent:** Thursday, 4 August 2016 11:53 AM  
**To:** Section 22  
**Subject:** RE: 160803 - Q and A - IR passthrough.docx [SEC=UNCLASSIFIED]

UNCLASSIFIED

Treasury may not be the best people to talk to on the mechanics of a committee.  
Section 22 is the Committee Clerk. You should talk to her

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**From:** Section 22 @treasury.gov.au]  
**Sent:** Thursday, 4 August 2016 11:35 AM  
**To:** Section 22  
**Subject:** RE: 160803 - Q and A - IR passthrough.docx [SEC=UNCLASSIFIED]

Thanks Section 22 is currently meeting with Section 22 and I understand they are discussing how your first point would work and are also working on a terms of reference.

I'll make the second point more clear.

I'm also waiting on advice from Treasury on the powers of the committee and mechanics of an appearance, as no doubt someone like Section 22 will get down into the weeds on that

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**From:** Section 22 @pm.gov.au]  
**Sent:** Thursday, 4 August 2016 11:29 AM  
**To:** Section 22  
**Subject:** RE: 160803 - Q and A - IR passthrough.docx [SEC=UNCLASSIFIED]

UNCLASSIFIED

Thanks Section 22

My initial thoughts:

1. The appearance of bank heads should be regular and scheduled – twice a year. This is similar to how the RBA Governor appears before House Eco twice a year.
2. In relation to the cash rate cut that occurred on Tuesday, our starting point is that the banks should pass it on in full.

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**From:** Section 22 @treasury.gov.au]  
**Sent:** Thursday, 4 August 2016 11:15 AM  
**To:** Section 22  
**Subject:** 160803 - Q and A - IR passthrough.docx [SEC=UNCLASSIFIED]

Comments/suggestions welcome

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**From:** Section 22  
**Sent:** Thursday, 4 August 2016 1:35 PM  
**To:** Section 22 [om.gov.au](mailto:om.gov.au)'  
**Cc:** Section 22  
**Subject:** Draft release and Q&A document [SEC=UNCLASSIFIED]  
**Attachments:** 040816 Joint MR Banks to face Parliament.docx; 160803 - Q and A - IR passthrough.docx

**Importance:** High

Hi Section 22

Please find attached draft MR and Q&A document (Q&A will require further revision).

Regards,

Section 22



## [JOINT LETTERHEAD]

### MEDIA STATEMENT

Thursday 4 August 2016

### BANKS TO FACE PARLIAMENT

Australia's major banks will be called to appear annually before the House of Representatives Standing Committee on Economics to enable the Committee to report jointly to the Treasurer and the Parliament on Australia's banking and financial system.

The Government recognises that at all times and particularly in challenging economic times globally, it is important that Australians retain faith in our financial institutions and the decisions they are taking.

The Australian economy depends critically on the performance and strength of our banking and financial system. As regulated entities banks operate under a social licence and have responsibilities to the Australian public.

As part of a broader terms of reference to be provided to the Committee by the Treasurer, the Committee will be asked to examine and report to the Parliament on the banking and financial system, calling Australia's banks separately to appear before the Committee. This will provide the opportunity for banks to explain how they are responding to funding issues to support Australian consumers and businesses.

In particular the banks will be required to explain:

- International economic and financial market developments and how these are affecting Australia
- Developments in prudential regulation, including capital requirements, and how these are affecting the policies of Australian banks
- The costs of funds, impacts on margins and the basis for bank interest rate pricing decisions
- how individual banks and the industry is responding to issues previously raised in Parliamentary inquiries through its industry package announced in April 2016
- bank perspectives on the performance of the Australian economy, including strengths and risks.

The appearance by the banks will ensure they have the important opportunity to transparently account for their decision making and how they balance the needs of borrowers, savers, shareholders and the wider community.

The Coalition Government has already taken significant steps to further strengthen our banking and financial system through the conduct of the Murray Financial System Inquiry and the ongoing implementation of the recommendations of this report. In addition, the Government has acted to strengthen the resources and capability of ASIC, which has all the powers and more of a standing Royal Commission to investigate and prosecute any malfeasance in the banking and financial sector.

Furthermore, the banking sector has announced their own reforms to banking culture and practice designed to put their customers at the centre of their business.

Tasking the HOR Economics Committee to monitor and report on the ongoing implementation of these policies and commitments, as well as addressing broader regulatory and economic impacts on the banking and financial system, will provide a useful contribution to improving public understanding and informing policy settings.

The appearance by the Banks will be supported by existing appearances by the RBA and APRA. Public hearings would be conducted annually with additional private hearings as appropriate to assist the committee.

It is envisaged a report would be tabled annually in February and that the Treasurer would provide a response to the report in the Parliament by no later than the Budget.

The House of Representatives Economics Committee already has hearings with the RBA and APRA and is therefore the appropriate body to hold the banks to account in a transparent, responsible, timely and cost effective manner.

**[MEDIA CONTACT]**

## Q&A – Bank pass through of interest rates

*What do you expect the House Economics Committee to do and when will they commence their examination?*

- Australia's banks play a significant role in our financial system and the economy. The Big 4 banks in particular hold over 80 per cent of housing loans and almost 80 per cent of deposits. Millions of Australians trust these banks with their loans and deposits, and deserve more transparency regarding decisions that affect their finances.
- The Government's view is that the banks should pass on the full amount of the recent reduction in the RBA cash rate.
- **An bi-annual public hearing before the House Economics Committee will ensure the major banks are given the chance to publicly explain their interest rate pricing decisions to the Parliament and the Australian people and if the full amount of any Reserve Bank cash rate cut was not passed on, why this was the case.**
- **The appearance of the major bank hearings before the House Economics Committee will be held to coincide alongside with regular appearances by the Governor of the Reserve Bank (RBA) and the Chairman of the Australian Prudential Regulation Authority (APRA).**
- **The Bank's appearances by major bank CEOs and senior executives will ensure interest rate pricing decisions are transparent and better understood by households, businesses and the community.**
- **The Government expect new members to be appointed to the House Economics Committee shortly after the resumption of Parliament and the Committee to begin work shortly thereafter.**

*How will the Government/Parliament respond to the hearings?*

- **The Committee will report the result of the hearings to the Parliament and, with the Treasurer will be required to respond to the report in the House of Representatives before the Budget.**

*What are the powers of a House Committee and how do these compare to a Royal Commission?*

- Both a House committee and a Royal Commission may administer an oath to any person appearing as a witness. However, evidence is not usually given under oath in a committee hearing.
- Both a House committee and a Royal Commission can compel attendance of witnesses and production of documents. In the past, witnesses have been summoned after first refusing to attend.
- Failure to comply with an order of a House committee is a contempt of the Parliament and could be reported to the House. The House has the power to impose penalties (including reprimands, fines and imprisonment).
  - A Royal Commission can impose criminal offences for failing to give evidence, providing false/misleading evidence, destroying documents etc.
- Both are able to hold *in camera* hearings if required.

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*The banks claim that increases in funding costs are the reason they could not pass on the full cut. Is this the case?*

- Treasury analysis indicates the overall funding costs for the banks remained relatively stable in the months preceding the RBA's recent interest rate reductions.
- Our strong view is that the banks should pass on the interest rate cut in full.

*Why did banks increase term deposit rates when the RBA cut the cash rate?*

- Lowering mortgage rates is not the only way banks can pass on reductions in the cash rate.
- After the most recent reduction in the RBA cash rate, the major banks chose to pass on part of the reduction in their costs by increasing the rate they pay on selected one-term deposits. For savers, this means the bank will pay you more to save through those particular products.
- This move is unusual. A lowering of the cash rate would usually see a reduction, not an increase, in deposit rates.

*Why can't the Government make the banks pass on their rate cut in full?*

- The Government's strong view is that the banks should pass the RBA's recent interest rate cut on in full.
- The determination of their interest rates is a commercial decision for the banks.

- The Government does not and will not regulate interest rates.
- It is not appropriate for the Government to intervene and regulate interest rates on financial products, any more than it would be to set prices for other goods and services.
- It's also not appropriate or possible for a Royal Commission to regulate interest rates or force the banks to pass on the rate cut in full.
- This is a matter that the banks have to explain to the Australian people and the Australian Parliament. The banks have made their decisions in their commercial interests, taking into account the needs of customers and shareholders. It falls to them to do that in the most transparent way so that all stakeholders and the community in general can possible in a way that is better understood by the decisions made community.
- There are over 100 mortgage providers in Australia, including many small banks, credit unions and building societies many of whom are offering very competitive rates. The Government encourages people to shop around if they are unhappy with their current provider.

*Is this just further evidence for a Royal Commission?*

- The Government is already working to improve the financial system.
- The Government commissioned a broad based review of the financial system, chaired by Mr David Murray AO, in late 2013.
- The Government has accepted the overwhelming majority of the recommendations arising from the Murray Inquiry's findings to improve our financial system and deliver a system that is efficient, resilient and fair.
- A Royal Commission risks delaying these important reforms and does not have power to enforce the law.
- ASIC has strong powers to investigate and to use the information they find to prosecute. This includes compelling persons to answer questions under oath, compelling the production of documents, seek search warrants, conduct investigations in a public forum **and** then use this information in prosecutions.
- ASIC has commenced legal proceedings against banks which are alleged to have engaged in market manipulation during periods from 2010 to 2012.

- The Government is getting on with the job of bolstering the Australian Securities and Investments Commission, the financial cop on the beat, with \$121 million to boost its powers and enhance surveillance capabilities.
  - This will better enable ASIC to combat misconduct in Australia's financial services industry and bolster consumer confidence. The Financial Services Ombudsman is also being granted greater access to claims and complaints.

*What impact has the Government's response to the Murray Inquiry had on banks?*

- The Government's response to the FSI will improve the resilience of the banks and increase competition in the financial system.
- Over the past year, the banks have undertaken significant capital raisings and improved their capital position relative to international peers. This is in response to the need to achieve 'unquestionably strong' capital ratios.
- One of the measures the Government endorsed was for APRA to narrow the difference in the capital that the major banks and other smaller banks must hold against their mortgages.
- This means that the major banks will need to hold more capital against these risks than they have previously. It will make them safer and improve the competitive position of smaller and regional banks.
- The Government is also explicitly including competition in ASIC's mandate and is supporting FinTech which will empower consumers and improve competition. We have also tasked the PC to look at data access and use, which has the potential to drive greater competition in financial markets, and to review competition in superannuation, including as it relates to banking groups.

*Are APRA's actions responsible for the banks' decision not to fully pass on the cut to the cash rate to mortgage rates? [detail on capital requirements below]*

- APRA's responsibility is to set how much capital banks need to hold to be unquestionably strong, a benchmark set by the FSI.
- If banks hold more capital, the financial system will be more resilient and stable, helping to promote economic growth, and ultimately, prosperity.
- How each bank meets that requirement and how they determine interest rates is a commercial decision for them, but the banks need to explain such decisions to their customers and the community.

- Globally, all banks are being required to hold more capital – it has been one of the key international reforms out of the global financial crisis.
- Having strong capital levels is important for the stability of Australia's financial system if we were ever to face another financial crisis.
- In responding to the Murray Inquiry, we agreed with its recommendation that APRA should ensure that the banks have unquestionably strong capital levels.
- Stronger capital requirements and a higher proportion of equity funding will improve Australian banks' resilience to losses and help protect the financial system in the event of a financial crisis.

*Is APRA's requirement for banks to hold more capital leading to higher mortgage interest rates?*

- Interest rates are affected by many factors other than bank capital requirements.
- The Murray Inquiry estimated that even if all lenders were affected, the impact on interest rates would be small. A one percentage point increase in capital requirements, all else unchanged, would result in lending rates increasing by less than 10 basis points on average – less than half a standard RBA rate change.
- Strong competition in the home loan market has ensured that Australians have access to affordable housing finance, and higher capital requirements for the major banks will level the playing field with smaller banks which already need to hold higher levels of capital.
- Historically low interest rates have been alleviating some of the pressure of rising house prices in recent years. Over the past five years, the RBA's cash rate has been cut 12 times – from 4.75 per cent to 1.5 per cent.
  - Each 25 basis point reduction in interest rates saves the typical family around \$750 a year on a \$300,000 loan. (325bp cut in this easing cycle equates to a **\$9750 saving if passed on in full**).
- The Government is working closely with the States and Territories to reduce the red tape that holds up the supply of housing and construction and to increase land release for new homes, which will help improve housing affordability.

*Do the banks' decisions put at risk short run economic growth?*

- Any reduction in lending rates puts more money in the pockets of consumers and businesses and will help boost confidence in the economy.
- The failure of banks to fully pass on cuts in the cash rate to borrowers may lessen the intended economic stimulus from an easing in monetary policy.
- However, the Board of the Reserve Bank has in the past noted that they take incomplete pass-through into account when determining monetary policy settings.

**What benefit do the banks get from the Government's AAA rating?**

- The credit rating agencies state that they provide the major banks with a two-notch uplift due to the Government's AAA credit rating.
- This helps to keep funding costs low for the major banks. This flows to consumers and businesses through lower interest rates than would otherwise be the case.
- This is part of the reason why maintaining our triple-A rating is so important. Both government borrowing costs and borrowing costs through the wider economy would rise if a downgrade were to occur.

## Figures and Charts

### Major banks' interest rates announced 2 August 2016

	Loans			Deposits		
	Owner-occupier ( <i>Principle and interest, Standard variable rate</i> )	Investor ( <i>Principle and interest, Standard variable rate</i> )	Business	1 year term deposit	2 year term deposit	3 year term deposit
<b>CBA</b> ( <i>effective 19 August</i> )	5.22 % ↓13 bps	5.49 % ↓13 bps	↓13 bps	3.00 % ↑55 bps	3.10 % ↑50 bps	3.20 % ↑50 bps
<b>NAB</b> ( <i>effective 19 August</i> )	5.25 % ↓10 bps	5.40 % ↓10 bps	↓10 bps	2.90 % ( <i>8 months</i> ) ↑85 bps		
<b>ANZ</b> ( <i>effective 12 August</i> )	5.25 % ↓12 bps	5.52 % ↓12 bps	↓10 bps	3.00 % ↑60 bps	3.20 % ↑75 bps	
<b>Westpac</b> ( <i>effective 23 August</i> )	5.29 % ↓14 bps	5.56 % ↓14 bps	↓10 bps	3.00 % ↑55 bps	3.10 % ↑45 bps	3.20 % ↑55 bps

### Section 45

## **Capital Requirements**

- Prior to the GFC, banks were required to hold minimum regulatory capital of 8 per cent of Risk-weighted assets. There were no buffers.
- In 2016, major banks are now required to hold 11.5 per cent of RWAs.
  - This is made of minimum regulatory capital of 8 per cent + A surcharge for major banks of 1 per cent + Capital Conservation Buffer of 2.5 per cent.

## **Section 45**

## **Section 45**

## Section 45

## Section 45

**From:** Section 22  
**Sent:** Thursday, 4 August 2016 3:56 PM  
**To:** Section 22  
**Cc:** Section 22  
**Subject:** DRAFT Q and A - Banks to face Parliament [SEC=UNCLASSIFIED]  
**Attachments:** 160804 - Q and A - Banks to face Parliament.docx

Hj Section 22 – re today's announcement...

We are looking to get this final version out to FYI once cleared by PMO.

Can you please let me know if you have any suggested changes?

Thanks.

## Q&A – Banks to face Parliament

*What do you expect the House Economics Committee to do and when will they commence their examination?*

- Australia's banks play a significant role in our financial system and the economy. The Big 4 banks in particular hold over 80 per cent of housing loans and almost 80 per cent of deposits. Millions of Australians trust these banks with their loans and deposits, and deserve more transparency regarding decisions that affect their finances.
- The Government's view is that the banks should pass on the full amount of the recent reduction in the RBA cash rate.
- Australia's major banks will be called to appear annually before the House of Representatives Standing Committee on Economics to enable the Committee to report jointly to the Treasurer and the Parliament on Australia's banking and financial system.
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- The appearance of the major banks before the House Economics Committee will be held to coincide with the appearance of the Governor of the Reserve Bank (RBA) and the Chairman of the Australian Prudential Regulation Authority (APRA). Public hearings would be conducted annually with additional private hearings as appropriate to assist the committee.
  - The House of Representatives Economics Committee already has hearings with the RBA and APRA so it is the appropriate body to hold the banks to account in a transparent, responsible, timely and cost effective manner.
- Appearances by major bank CEOs and senior executives will ensure interest rate pricing decisions are transparent and better understood by households, businesses and the community.
- **Timing:** The Government expects new members to be appointed to the House Economics Committee shortly after the resumption of Parliament and the Committee to begin work shortly thereafter.

*How will the Government/Parliament respond to the hearings?*

- The Committee will report to the Parliament and the Government will respond to the Committee's reports and any recommendations made.

*What are the powers of a House Committee and how do these compare to a Royal Commission?*

- Both a House Committee and a Royal Commission may administer an oath to any person appearing as a witness. However, evidence is not usually given under oath in a committee hearing.
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- *This move is unusual. A lowering of the cash rate would usually see a reduction, not an increase, in deposit rates.*

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compelling the production of documents, seek search warrants, conduct investigations in a public forum **and** then use this information in prosecutions.

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*Are APRA's actions responsible for the banks' decision not to fully pass on the cut to the cash rate to mortgage rates? [Additional detail on capital requirements below]*

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- Having strong capital levels is important for the stability of Australia's financial system if we were ever to face another financial crisis.
- In responding to the Murray Inquiry, we agreed with its recommendation that APRA should ensure that the banks have unquestionably strong capital levels.
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  - Each 25 basis point reduction in interest rates **if passed on in full** saves the typical family around \$750 a year on a \$300,000 loan. (325bp cut in this easing cycle equates to a \$9750 saving **if passed on in full**).
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*Do the banks' decisions put at risk short run economic growth?*

- Any reduction in lending rates puts more money in the pockets of consumers and businesses and will help boost confidence in the economy.
- The failure of banks to fully pass on cuts in the cash rate to borrowers may lessen the intended economic stimulus from an easing in monetary policy.
- However, the Board of the Reserve Bank has in the past noted that they take incomplete pass-through into account when determining monetary policy settings.

*What benefit do the banks get from the Government's AAA rating?*

- The credit rating agencies state that they provide the major banks with a two-notch uplift due to the Government's AAA credit rating.
- This helps to keep funding costs low for the major banks. This flows to consumers and businesses through lower interest rates than would otherwise be the case.
- This is part of the reason why maintaining our triple-A rating is so important. Both government borrowing costs and borrowing costs through the wider economy would rise if a downgrade were to occur.

## Additional information

### Major banks' interest rates announced 2 August 2016

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### Bank Capital Requirements

- Prior to the GFC, banks were required to hold minimum regulatory capital of 8 per cent of Risk-weighted assets. There were no buffers.
- In 2016, major banks are now required to hold 11.5 per cent of RWAs.
  - This is made of minimum regulatory capital of 8 per cent + A surcharge for major banks of 1 per cent + Capital Conservation Buffer of 2.5 per cent.

**From:** Section 22  
**Sent:** Thursday, 4 August 2016 4:29 PM  
**To:** Section 22  
**Subject:** RE: DRAFT Q and A - Banks to face Parliament [SEC=UNCLASSIFIED]

Thanks<sup>S22</sup> – will incorporate your points.

Cheers.

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**From:** Section 22 [@pm.gov.au\]](mailto:@pm.gov.au)  
**Sent:** Thursday, 4 August 2016 4:21 PM  
**To:** Section 22  
**Cc:** Section 22  
**Subject:** Re: DRAFT Q and A - Banks to face Parliament [SEC=UNCLASSIFIED]

Hi mate,

This looks good. My only suggestions would be to add that the banks could be compelled to appear more than once a year if necessary, and to perhaps include a line about how the aim of this measure is to impose greater scrutiny and hence transparency on the banks.

Cheers and thanks,

Section 22

Sent from my iPad

On 4 Aug 2016, at 3:58 PM, Section 22 [@treasury.gov.au](mailto:@treasury.gov.au) wrote:

Hi Section 22 – re today's announcement...

We are looking to get this final version out to FYI once cleared by PMO.

Can you please let me know if you have any suggested changes?

Thanks.

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<160804 - Q and A - Banks to face Parliament.docx>

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