

Submission to the
FINANCIAL SYSTEM INQUIRY

Second round 2014

About one hundred and fifty years ago, Abraham Lincoln wrote:

“I see in the near future a crisis that un-nerves me and causes me to tremble for the safety of my country Corporations have been enthroned and an era of corruption in high places will follow the money power of the country will endeavour to prolong its reign by working on the prejudices of the people until all wealth is aggregated in a few hands and the Republic is destroyed.”

Those prophetic words are borne out by the recent civil unrest in Cyprus, Greece and Spain, caused by banks being permitted to plunder depositors' funds to bail themselves out of incipient bankruptcy which was occasioned by irresponsible lending and investment practices. This is the moral equivalent of a lawyer taking his clients' trust funds to the nearest casino.

The Australian government's guarantee of depositors' funds falls very far short of what is required to secure them in the event of the failure of one or all of our major banks. No bank should ever be considered to be “too big to fail”.

The only foolproof and greedproof way to protect depositors' funds is to totally separate commercial and investment banking activities. One method proposed is to “ring fence” both types of activity within each bank. Ring fencing did not save depositors' funds in the 1929 crash. Money was pushed through the cracks in the fencing from the commercial to the investment arms and lost. There is no reason to suppose that the same will not happen again.

In 1933, the Congress of the United States enacted the Glass-Steagall Bill to entirely separate commercial and investment banking. The separation went so far as to include prohibiting company directors' membership of both commercial and investment bank boards. It is difficult not to escape the conclusion that the repeal of the Act in 1999 had nothing to do with the sub-prime lending crisis a few years later.

To protect individuals and businesses against loss of their bank deposits, Australia needs Glass-Steagall legislation. The separation of directorships should also require a period of, say, five years between leaving an investment bank board and becoming a director of a commercial bank, and vice versa. Government guarantees should only apply to commercial bank depositors' funds. Investment banks can be left to stand or fall on their own merits.

It is ridiculous that banks making foolish investments should be allowed to survive a financial crisis which would bring down a government. They should not become too big to be allowed to fail. In my opinion, there are too many who believe that the proper role of government is to protect the power and privileges of the privileged and powerful, rather than ensuring the common good.

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