FINANCIAL SYSTEM INQUIRY

MR S. WALLIS, Chairman
MR W. BEERWORTH, Member
PROF I. HARPER, Member
MRS L. NICHOLLS, Member
MR G. SMITH, Secretary

TRANSCRIPT OF PROCEEDINGS

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CHAIRMAN: Good morning, ladies and gentlemen. Thank you very much for joining us. My name is Stan Wallis and I'm the chairman of the Financial System Inquiry. I have with me today Prof Ian Harper, Mrs Linda Nicholls and Mr Bill Beerworth, who are my fellow members on the committee, plus Mr Greg Smith, who's the secretary to the inquiry.

I'm sure that you all know that the Honourable Peter Costello, the Federal Treasurer, established this inquiry on 30 May 1996 to undertake a stocktake of the results of financial deregulation since the early 1980s, to analyse the forces driving further change, and to make recommendations on future regulatory arrangements. The inquiry will report to the Treasurer by 31 March 1997.

To assist in our investigations the inquiry has received and examined over 250 submissions - I think we're through 270. It has also published a discussion paper outline options for regulating the financial system, which is this document here. The secretariat today has copies of the terms of reference and the discussion paper available for viewing.

I draw attention to the terms of reference because the purpose of the public consultations today is to focus on issues raised in the discussion paper, and on proposals for regulating the financial system. The inquiry is unable to consider particular complaints about individual financial institutions. Finally, I should point out that the inquiry has no special legal powers or parliamentary privilege, and for this reason I ask participants to avoid making adverse comments about particular individuals.

We have so far had public hearings in Sydney, Brisbane, Perth and Adelaide. We will be in Melbourne tomorrow and we're also by other means covering both Canberra, Tasmania, and even Darwin, so it's becoming a fairly extensive process. The proceedings are deliberately informal. We simply ask those contributing, those participating, to come to the table, to make an opening statement, and then we just set about some questions and useful discussion.

The first participants today are Mr Barry Fitzpatrick, the group managing director of Adelaide Bank, and I think Mr Fitzpatrick is joined by Brian Walker. Well, whoever is coming up, please join us, gentlemen. Could I ask you to start, gentlemen, just by identifying yourself by name, and the organisation you represent, so that

- that's largely for the purpose of the transcript and voice recognition. As I say, we would be very pleased to hear your introductory comments and we can proceed from there, thanks, Barry.

MR FITZPATRICK: Thank you very much, chairman, and thank you very much for allowing me to address the committee today. I'm Barry Fitzpatrick from Adelaide Bank, group managing director of Adelaide Bank. Just a little bit of background on Adelaide Bank, if I may. It was formed only 3 years ago in 1994, but has been around in its former guise as the Cooperative Building Society since 1900, and then merged with a number of other building societies in this state to form Adelaide Bank, as I said, on 1 January 1994.

Chairman, I'd like to have my remarks centred along the lines of the issues associated with customers. I'm very much aware that the inquiry has looked at the globalisation of commerce, technological and financial innovation, and the demands of customers, but I must say regional banks in their period of existence have not only assisted in the improvement of customer products and services in the marketplace, but have also demonstrated quite visibly the ability to have very high customer satisfaction ratings, and this has been borne out for many many years.

It's in the area of customers and customer satisfaction that I'd like to make a couple of observations to the inquiry today. I don't wish to go over the ground of the awards that Adelaide Bank has won, or what other regional banks have done, but more or less to move into the future of where the customers in our view are driving the changes that are occurring in the Australian financial system, and I'd just like to draw the inquiry's attention to the issues associated with the Australian payments system, APCA, and just to make an observation in that particular area on a couple of issues.

One is in relation to access to the electronic networks. Most banks are moving away from areas where the majority of their transactions are done at the branch network, and many of them now are done electronically. In fact in Adelaide Bank's case we're now up to 70 per cent of our transactions done electronically and we'd expect in the medium term for that to move to about 80 per cent. But when you recognise that to have your facilities associated with EFTPOS transaction they must be approved by APCA, and APCA really is controlled - and I say that in inverted commas - "controlled" by the four majors, one becomes a bit suspicious when it takes over 6 months to get accreditation for certain electronic equipment that other organisations are using in the marketplace out there, including the majors, and for regionals to be able to use that same equipment it becomes quite protracted. So our view is that APCA should be used for accreditation - we're not denying that - but it should be in the interest of competitive neutrality, and that's the observation I'd like to make there.

And also within that same framework APCA in our view should be the driving force for change in relation to cheque clearance. When it takes over 5 days for cheques to be cleared, one wonders whether it is on the agenda for change for APCA, again, being driven by the majors, because customer satisfaction is not enhanced by having 5 days to have their cheque cleared. So they're the two observations I'd like to make in relation to APCA.

Within that same framework I'd like to talk just briefly about securitisation. That is an area again where regional banks have come to the fore, and in our view it has enhanced consumer competition in the marketplace. Securitisation has the ability to make a housing loan a commodity, but there are a number of issues that need to be addressed over time; not least are the uniformity of stamp duty legislation in the various states, and perhaps the movement to a paperless system of registering mortgages. In our view these issues would enhance consumer satisfaction in the marketplace.

Finally, chairman - I am conscious of time - we would like to support fully the role of the Reserve Bank as a lead regulator-style model for banking institutions. We think the Reserve Bank really in its role is important to ensure the stability of the financial system. Having gone through two runs myself in my former days with building societies, one is very much aware of the fragility of the reputation of banks and building societies. Insurance for deposit just didn't work - it did not work in the Farrow crisis - and expecting consumers to read a lot of information about disclosures in our view is just not practical. And so I think the prudential supervision, looking at the credit risk, in particular - which is what the Reserve Bank does - I think should continue into the future. They are my opening remarks.

CHAIRMAN: Thanks, Barry. Would you like to venture a few more comments about APCA and the real issue there with the majors? I mean, what is it?

MR FITZPATRICK: I think if you look at the Reserve Bank as an organisation that supervises banks, you don't find senior executives of the major banks on the Reserve Bank board, and that would just be silly, but you look at APCA, and that is an organisation now with technology that is moving really to the forefront of the banking system - because, as I said, more and more transactions are done electronically. So what you really have in APCA is an organisation where the policy decisions are predominantly being made by your competitors, and so in our view in the interests of competitive neutrality, the APCA board should be independent of the majors and should be for the benefit of the consumers at large.

MR BEERWORTH: Chairman, just on that subject, if I may. You've given us two gentle examples, Barry, of problems with APCA. Are there any other examples that you can bring to mind?

MR FITZPATRICK: There are but I'd prefer to give those in private.

MR BEERWORTH: Right.

MRS NICHOLLS: I think the first question that I'd like to ask you is, certainly Adelaide Bank has been innovative, at least relative to some of the majors, in securitisation, for example, and in other areas. Could I ask you to offer some comment on what you've been doing in distribution, and particularly distribution as an alternative to bricks-and-mortar branches.

MR FITZPATRICK: Yes. I think over 2 years ago I think we were close to 67-odd branches, bricks-and-mortar branches. We're now down to 36 bricks-and-mortar branches. We're also - where we don't own any of our branches now, we lease them all. We are recognising that the mood of customers is changing, and customers really are the driving force here, and they are looking to do their transactions anywhere, anyhow, any time, and as a consequence of that we have moved to set up mobile bankers with laptop computers who will go into people's homes to handle the mortgage transaction in the house; we have also set up a call centre whereby nearly 40 per cent now of our personal lending is done through the telephone system, and we have moved very strongly to position ATMs in places where the customers are to the extent now that we are a net receiver on the Interchange associated with ATMs.

In relation to providing services for customers outside of South Australia, we joined the GiroPost network, and whilst that is only in its infancy - about 1 per cent of our transactions are done through GiroPost - but we see this as a big medium for Adelaide Bank. It is cheaper to do a transaction through GiroPost than it is through a branch network, and it gives Adelaide Bank now 2600 outlets around Australia.

MRS NICHOLLS: Chairman, a follow-on question to that, if I may. How has this reconfiguration of your network affected your deposit-taking?

MR FITZPATRICK: Basically we have not lost any deposits from the branch networks. We have monitored it very carefully, and I think it's providing the access to the customers in other places that's very important, and just as important is to ensure that the staff are not too disadvantaged. When we close a branch we offer the staff a move to any other branch of their choice, and staff are a big part of the strategy of Adelaide Bank because they are the frontline troops that communicate with the customers.

CHAIRMAN: We've been presented, Barry, with a good deal of comment about the advance of electronic banking and whatever, and there's certainly a fair body of view that has been expressed that there's large chunks of the consumer base out there, the depositor base, that can't adapt or won't adapt. I mean, can you say anything about that in relation to your existing customers?

MR FITZPATRICK: That's very true. I'll know when our strategy finally works - when my mother will use an ATM, and to date she won't and she'll still stand in the branch, and we must provide a service for people who do not wish to use that position of exchange.

MR BEERWORTH: But will she use GiroPost?

MR FITZPATRICK: Yes, because you're dealing, again, with a person.

MR BEERWORTH: You've got a person, right. So it doesn't have to be a bank?

MR FITZPATRICK: No.

MR BEERWORTH: Right.

MR FITZPATRICK: I think we have to be very careful that technology allows us almost to do anything, and we've got to recognise we are still dealing with people.

PROF HARPER: Barry, you made a comment about your bank's preference that the Reserve Bank remain as lead regulator for banks. Do you have any comment on an alternative model which would see the prudential regulation of banks taken outside the Reserve Bank, that there'd be no move away from prudential regulation as such, but that such an organisation for instance might also prudentially regulate other institutions that weren't banks - insurance companies, for example - but that the prudential function of bank regulation would be taken outside the RBA? Have you comments about that as an alternative?

MR FITZPATRICK: Yes. I think one has to look at the skill base that's required for regulation. If you look at like institutions - and I would lump banks, buildings societies and credit unions into that mode - that they predominantly raise deposits from the consumer base at short to medium term, and they tend to lend those deposits there to longer-term instruments - housing related, business, etcetera - so the particular risk there is really one of credit.

If you look at a superannuation organisation or insurance company it's almost just the opposite: their liabilities are longer and their assets are shorter, more liquid-style instruments, and as a consequence then you've got to look a lot closer at liability risk and market risk. So one would have thought then that there was going to be different skills necessary for the regulation of those different organisations.

PROF HARPER: So you're suggesting that therefore in your view it would be inappropriate to combine the prudential regulation of banks, or let's say deposit-taking institutions, with, for example, insurance companies and superannuation funds.

MR FITZPATRICK: Yes.

PROF HARPER: And as a result of that you would see no point in removing the prudential supervision of deposit-takers from the central bank.

MR FITZPATRICK: Yes, that's right. The other point I'd make, though, is I don't think the central bank should compete in the marketplace with private banks, and we have a case in South Australia where the Reserve Bank won the tender for the South Australian government business. I think the Reserve Bank should move out of the business of banking per se.

PROF HARPER: Thank you.

MR BEERWORTH: Given the history and background of your organisation, Barry, would it make sense for the Reserve Bank also to regulate building societies and other deposit-taking institutions - - -

MR FITZPATRICK: Yes, I think that should've happened at the last inquiry, and I think that was a mistake that occurred. In my view there is not a lot different between a larger building society or credit union in relation to what depositor protection is out there. That's really a

Reserve Bank's role - to act as a protector for those depositors, and to ensure that credit risks is maintained within the banking system.

MR BEERWORTH: I don't have much information on the mix of your business, but I understand that you're now starting to get into small and business lending. In your view is that really personal lending at the end of the day, it's done on the basis of mortgage or personal credit - - -

MR FITZPATRICK: No.

MR BEERWORTH: - - - as opposed to an assessment of the business or - - -

MR FITZPATRICK: No, it's an assessment of a business. 16 per cent of our assets are now in small to medium-size businesses, and the criteria to assess those is entirely different than what you would assess a mortgage for, and we have had to go through a huge learning curve and bring in expertise to set up a business banking operation.

MR BEERWORTH: What sort of collateral or guarantees do you require though at the end of the day? What's your security - - -

MR FITZPATRICK: Well, at the end of the day it can be security over the business, it can be security of the cash flow, it can be debt debenture-related instruments. If there's housing involved it can be housing or it can be property, but it's a matter of an assessment of the business that we're lending to, and the ability and the capacity for that business to be able to repay its loan.

MR BEERWORTH: Do you do much straight cash flow lending? Is that really something you do?

MR FITZPATRICK: Not a great deal, no.

CHAIRMAN: Would you see securitisation offering some prospects in the SME marketplace?

MR FITZPATRICK: Well, that's been discussed, and I'm not sure whether that's going to be something in the medium term because at the end of the day the fund managers are buying an instrument that hopefully they're going to get a return on, and in relation to housing there is a subordination clause to ensure that you get the triple A rating. Now, I'm not sure whether it is going to be possible to commoditise a small to medium size business loan. Credit card receivables is probably going to occur before SME lending.

MRS NICHOLLS: Thank you, chairman. Just a question about your very smallest accounts. We have had put to us by a number of other organisations that their very smallest transaction accounts are ones on which they lose money, and that they have concerns that as cross-subsidies in business are removed, that these accounts become increasingly difficult to maintain. Could I ask you to offer some comment on whether this is an issue for you, whether you have a view on the desirability or otherwise of banks offering a basic banking product, or whether you see some other way that community service obligations might be addressed.

MR FITZPATRICK: I think there is no question that low-value accounts are costly, and all banks I think have separated their customers into the A, B and C class, and we've done the same. As a small bank we have a very sophisticated customer information system, so we do know the profitability of customers, and we do know what balances that customers become profitable at. The trick is really - is to ensure that those unprofitable customers you are selling more products to, and in relation to Adelaide Bank, our relationships per customer are 2.7, our products per customer are about 1.5. If you can move that up to a relationship closer to 3 and two products per customer, you can make a lot of unprofitable customers profitable. But at the end of the day I think banks have to accept if they've got a real-time system in place, which is very transactional-based, and if you're using marginal costing, you've really got to take into consideration what really are unprofitable customers. An unprofitable customer today doesn't necessarily make an unprofitable customer tomorrow.

MRS NICHOLLS: So you don't really see it as a serious problem?

MR FITZPATRICK: No, not at our size, no.

PROF HARPER: Barry, we've heard of ABL's interest in the Reserve Bank remaining as prudential supervisor. Do you have any particular concerns about the bank's current approach to the prudential supervision of banks, and here I'm particularly thinking about the bank's rules in respect of securitisation, which ABL has been involved in, and possibly also investment in non-financial enterprises by banks. Are there issues that ABL would like to bring - - -

MR FITZPATRICK: We were the first bank in Australia - listed bank, any rate - to securitise a parcel of mortgage, and following the C2 promulgation by the Reserve Bank. We found that the process was quite protracted, but having said that, I think we also found that the people in the Reserve Bank were very helpful, so I'm not overly critical of that. I think it could be streamlined still, and I think that's probably a process that's going to be done over the next few years.

We were pretty slow off the mark to get securitisation in this country, and that could be a criticism. Securitisation has been in the States for 25 years or so, and works exceptionally well, but I still think in Australia one has to understand the components of securitisation and the costs associated with the various components, and I'm not sure C2 fully understands that - those - - -

PROF HARPER: So in your view it could be an obstacle to further development of securitisation?

MR FITZPATRICK: Yes.

PROF HARPER: And what about cross-investment?

MR FITZPATRICK: In our case, a small bank, we would not see us being involved in small business equity participation. However, we have approached the Reserve Bank to maintain ownership of our retirement villages which fall into that same process and so far we are receiving some very sympathetic hearings from them.

CHAIRMAN: Do you have a view in principle about that, though?

MR FITZPATRICK: Sorry?

CHAIRMAN: In terms of a non-financial type involvement by a bank in this country?

MR FITZPATRICK: In this country they're addressing that very issue, but retirement villages is an issue that is not going to go away in this country. The population is ageing. It's housing by another means, and for organisations to be associated with that, in our view it's quite logical, and I think I'm getting the Reserve Bank to understand that.

MRS NICHOLLS: Chairman, a follow-up question on that if I might. Certainly overseas we have seen examples of financial institutions quite active in what might termed lifetime care, that is a combination of long-term health insurance leading into retirement home and nursing home benefits, and yet we don't have that in Australia at the moment. Could I ask you to comment on whether you think that that's a desirable direction for financial institutions to pursue in Australia, and if so how you might see that coming about, given that health insurance is in a health department.

MR FITZPATRICK: I think it's something that will inevitably come here. Whether it comes in the form of banks being involved or whether it's more likely for insurance companies or superannuation-style companies, because at the end of the day an interest in a retirement village is more like an annuity than it is a mortgage, and one has to be very careful about providing full, long-term care, as they do in the United States in continuing-care retirement communities, because of the fact people are living longer, and as a consequence of that, the costs associated with health care is becoming prohibitive.

CHAIRMAN: Greg?

MR SMITH: I'd just like to take the questioning in another direction. You mentioned customers as the key focus. I was just wondering whether you had any views about the regulation in that area. We've had an enormous number of submissions about consumer protection regulations, the Credit Code, these types of areas. I'd be interested in your experience with the regulation of consumer protection.

MR FITZPATRICK: I think we all recognise and agree that there should be national consumer credit legislation, but the Uniform Consumer Credit Code that was brought in caused many organisations including Adelaide Bank real heartaches and sleepless nights, and the costs were quite prohibitive, and for a small organisation like ourselves, we spent over $1½ million in trying to get the rules straight. I think the big issue is not knowing what the rules are from day one, and I think where issues like this come about, the rules should be laid down so you can actually program your technology to account it. The delays that were causing this is where the cost run-out occurred, but now that it's implemented - and it's only been going a month or so - at this stage we're not finding too many difficulties.

MR SMITH: So the ongoing cost of that is relatively low?

MR FITZPATRICK: Ongoing would be relatively low. The cost of setting up was quite horrendous.

MR SMITH: What was the reason for that? Why is it that there was so much change driven by that legislation?

MR FITZPATRICK: Basically by not setting out the ground rules in very explicit terms from day one, and keep changing the yard posts. That's what happened, and that's why the delays occurred for, and the start date was continually put forward.

MRS NICHOLLS: Chairman, could I just follow up on that? Certainly a view has been put that those whose business was under the old credit acts are not unhappy with the current Uniform Credit Code, and indeed were not particularly unhappy with the process of getting there, but those whose products were not captured under the former credit acts have had more difficulty. Could I ask you to react to that statement?

MR FITZPATRICK: Yes. In general terms I suppose that's a realistic assumption, but having said that, I think the lessons to be learnt there is to really lay out explicitly what the rules are, get consensus on those rules, and then don't change it, because the big issues of programming computers these days - it's not easy, and you can't program computers unless you've really got very defined rules.

MR SMITH: I just wanted to follow up on one other aspect on that. You've told us that the cost for you now is relatively low on an ongoing basis. What about the customer? Is the customer better off with that code?

MR FITZPATRICK: Well, they have a lot of things to read, and if they read it I suppose they know what they're buying.

CHAIRMAN: Do they read it?

MR FITZPATRICK: Initially we found they did, which again slowed down a lot of the transactions in branches, because they actually sat down and read these documents, which they're entitled to, of course, but whether they will continually - to read these, one wonders.

MR SMITH: How many pages is your mortgage document, as a matter of interest?

MR FITZPATRICK: It's four or five.

MR SMITH: Still four or five post the code?

MR FITZPATRICK: Mm.

CHAIRMAN: That's interesting, because some majors would say it's taking them 60 pages to do a housing contract.

MR FITZPATRICK: Yes.

MR BEERWORTH: But there's a distinction between a mortgage and a loan contract. Do you have a separate loan contract?

MR FITZPATRICK: Yes, there is, yes.

MR BEERWORTH: And how long is that, just for interest to us.

MR FITZPATRICK: That's quite large. How many - - -

MR WALKER: It's about 15. The way we do it is we've got a standard document that covers everything, and to that we add schedules, and depending on the complexity of the loan (indistinct) some of those schedules are quite long, up to about 15, 16 pages.

MR BEERWORTH: We probably need to talk font and pitch as well. Again, Barry, I wonder if I could take you in a different direction. Just pondering your strategy, as it were, you are a regional bank, you have relatively small assets by national standards, I guess. As you think about these things late on Sunday evenings and wonder where you're going to go and how you're going to compete against the majors, and peeling back the marketing gloss, what really is your competitive advantage and how are you going to sustain it?

MR FITZPATRICK: I think organisations, whether they're - whatever they are, a bank, a credit union or whatever - they're either going to have to get big, get focused or get out, and I think Adelaide Bank is very focused on the customer, is able to move very quickly, and with the cost of technology coming down, we are able to deliver appropriate products to our customers very quickly, and we've just won through Cannex the national award for best business banking product in Australia.

We came second to NAB, and I'm quite happy to come second to NAB, overall, with our banking products, and our customer satisfaction rating has always been above 80 per cent, and last year we were equal to Bank of Melbourne, so I think really it's delivering products to customers and ensuring that you deliver those in a most comprehensive manner, whether in this or other state. We're now in a position where 24 per cent of our assets and 25 per cent of our profits are outside of South Australia, so for a small bank with a GDP in this state of about say 6 per cent, we've got markets now of 94 per cent, and the trick is not to get delusions of grandeur; keep focused on your customer, and don't lose sight of your customer.

PROF HARPER: Barry, do you regard yourself as a nationally operating bank?

MR FITZPATRICK: No, we regard ourselves as a full service bank in South Australia, and a niche player in markets where we have some distinctive competencies around Australia, like housing and securitisation of housing, like retirement villages, but you wouldn't see Adelaide Bank lending on office blocks or buildings or whatever in other states of Australia.

MR BEERWORTH: Just thinking about the competitive arena and certainly looking at the next 5 years, how would you feel about mergers of the major banks in this country?

MR FITZPATRICK: I don't think the system should preclude mergers from anybody, and Adelaide Bank is not frightened of mergers or being taken over or whatever. That's a matter for shareholders. I think the issue is to ensure that there is sufficient competition in the marketplace at all levels, and I think it's fairly evident in the last 5 to 10 years that the regional banks are what have given the majors competition.

MR BEERWORTH: There must be an argument if there were a merger in the majors I suppose it would be good for your business.

MR FITZPATRICK: That hasn't escaped us.

CHAIRMAN: Barry, do you have a sort of broader view of the electronic age that's coming on us? I mean, has the bank sort of mapped out a 5 and 10-year view of how it can take advantage of some of the newer technology that's emerging? Do you have a view that you could form a direct bank from your Adelaide base?

MR FITZPATRICK: I think looking at 3 years is pretty reasonable. Looking at 10 years it would be a bit hard. I'm not sure what's going to happen in 10 years' time. All I believe is that small organisations can be very responsive to change and have to adapt very quickly to the changing environment, but with technology the technology to do everything that you want to do is here and has been for quite a while. It's just a matter of opening up some of these gateways like APCA, for example, to ensure that there is some competitive neutrality and allow the telephone to be able to be used extensively for banking operations. So I don't think we need much more new technology. It's here. It's how we use technology now to apply to the customer the products that they want, and how we deliver them.

MRS NICHOLLS: Barry, just continuing with APCA for a moment, I'm remembering back probably not so very many years ago now; the Co-op and Hindmarsh were really quite strong advocates at the time for building societies being given access to the payment system, being able to issue credit cards, being able to offer cheque-writing on your accounts. Of course now Adelaide Bank has been in the payment system for some time. What is your view about the payment system being open more widely to non-bank activities?

MR FITZPATRICK: I think the payment system - we have to ensure that we avoid any systemic risk, so one has to ensure that the regulatory regime is intact and I think the approach taken by the Australian Bankers Association, which we support, is that the payment system should be open to banks. I'm more interested in who administers that process.

MRS NICHOLLS: Barry, is this a case of "I'm on the bus, you can shut the door now"?

MR FITZPATRICK: No, no, I don't think so. That's a very good analogy. Certainly not on the bus - we settle our systems through Chase - but I think it's more or less setting up the rules and firming what is a bank. I think the definition of a bank has to be sorted out. You can look at the US. A bank is not necessarily a bank as we look at it. There are many mutual organisations in the US that are banks, so I think it's the broadly required prudential requirements of what is a bank and what does it do that has to be addressed.

MRS NICHOLLS: How would you see that changing?

MR FITZPATRICK: I think the regulatory regime should allow the ground rules to be set and determine what prudential requirements are necessary and those institutions that meet those necessary requirements, as we were at the Co-op Building Society, pass the exam to get a banking authority. It was an exam, basically. It was a lot of work. You shouldn't just be able to hang out your shingle one day and call yourself a bank.

MRS NICHOLLS: Should organisations that are not financial institutions be permitted to be banks or be in the payment system? For example, we've had representations to us by organisations that say, "I have more capital than all the Australian banks put together. My gearing ratios are not as high and my credit rating is higher. Why can't I be a bank?"

MR FITZPATRICK: I've heard that argument and I think you're going to have to get back to what does a bank do - and it is seen by the customers at large, the people of Australia, as a safe haven for their working deposits. So I think the question has got to be taken further to say if people other than banks were allowed to be banks, not necessarily is their capital better but is their prudential standing just as good, because the primary concern of the Reserve Bank is to protect depositors, to ensure that depositors' money is safe, and they do that by concentrating very heavily on credit and credit assessments and risk management systems within banks.

MR BEERWORTH: Barry, you obviously need to dance very quickly, as you've indicated, because you're bouncing among the elephants' feet in some ways and product innovation is clearly a specialty of yours, quite apart from your customer focus. Are there any other areas in which say securitisation could be used innovatively in this country, because innovational product is something we're very concerned about. Have you ever thought about receivables of other sorts that you might get involved with?

MR FITZPATRICK: Yes, I think it's quite expected in the medium term that credit card receivables could become a commodity and could be securitised. I said earlier I wouldn't think that that would apply to small business assets because each one is different and I think you've got to almost develop this commodity-style approach for securitisation. I think the freeing up of a lot of the regulatory rules state by state, associated with documentation and stamp duty, etcetera, will lead to a fairly robust securitisation market in this country.

CHAIRMAN: Just one last question on GiroPost, Barry. Are you using GiroPost just in South Australia or is it - - -

MR FITZPATRICK: No, we're using it right around Australia for our customers in our retirement villages and our customers in our mortgage securitisation programs to be able to access deposits or withdrawals through the - - -

CHAIRMAN: That's been a happy experience for you?

MR FITZPATRICK: Yes, it has been.

MR BEERWORTH: Is that excessively expensive? I've heard some comment that it is quite expensive.

MR FITZPATRICK: No, it's cheaper than transactions in a branch network and you only pay for transactions as they occur, and the cost of a transaction is a lot cheaper than a transaction in a branch.

MR BEERWORTH: So it's relativity, and it makes sense?

MR FITZPATRICK: Yes.

MR BEERWORTH: Right, yes.

CHAIRMAN: And Mrs Nicholls will be very pleased to hear that. I think we've about covered it, ladies and gentlemen, unless there's anything else you wish to say, Barry, but thank you very much for coming along, to you and your colleagues. Thank you.

MR FITZPATRICK: Thanks very much.

CHAIRMAN: We next have Dennis Dorney from Economic Reform Australia. Mr Dorney, I just might repeat what I said. Please sit down. I'm not sure whether you were here when we opened this morning's proceedings.

MR DORNEY: I was in a different room, the room that was intended to be used prior to this morning.

CHAIRMAN: I'm sorry, I regret if you didn't get any advice of the change of venue. Can I just make it clear that this inquiry has no special legal powers or parliamentary privilege, so participants should not make any comments which reflect adversely on particular persons or organisations. As you can see, we're conducting a fairly informal hearing. We'd be very happy to take your opening remarks and leave as much time for discussion - can I just ask you, for the purposes of voice recognition, if you could commence by stating your name and the organisation you represent, and thank you very much for coming along.

MR DORNEY: Okay, first of all it's Dennis Dorney and I represent ERA, which is an acronym for the Economic Reform Association, Australia branch. Can that be heard?

CHAIRMAN: That's fine.

MR DORNEY: Starting off with our beliefs about why the system should not be further deregulated, our beliefs essentially are that the expectations of the original Campbell Committee report were based on wrong and restricted assumptions, that the assertions in Pocketful of Change that on balance the economy and bank customers have both benefited from deregulation is true only in the context of those assumptions and is not true when the whole impact of banking on the economy is considered. The evidence of the main economic indicators during that time suggests that deregulation has damaged the economy, rather than made it better.

There are serious questions about the behaviours of the banks between 1986 and 1989 and I heard what you said about not making derogatory remarks but I feel I must say that there is evidence that there are concerns that arose during that period, and finally the credit-creating function of the banks is so fundamental to the economy that deregulation is morally reprehensible as well as on actual evidence detrimental to the economy. So they're our beliefs and that leads ultimately to the conclusion that further deregulation should not be countenanced and that the behaviour of the banks since deregulation indicates that, if anything, tighter controls are in fact necessary. So they're the conclusions that we've reached.

I would go on from there, if I'm allowed to, to explain why the expectations of the Campbell Committee seem to be wrong. The Campbell report expected deregulation to improve competition and efficiency in the banking sector. It did also expect to improve stability and that's obviously proven to be totally wrong and I think they admit that that was never achieved. They defined competition and efficiency in a purely mechanistic way more appropriate to factory production or to an internal combustion engine. They expected that efficiency as defined would be in terms of improving cost ratios of production, improving productive use of resources, and improving response to technological change, which is all very fine in a mechanistic fashion.

That is merely measuring efficiency in terms of transaction processing. If that were the only role that the banks had to play, then measuring it that way might be satisfactory, however that is not the banks' major function. The main function of the banks is essentially this: despite every attempt of the banks to promote themselves as being simply private companies answerable only to their shareholders, the banks have a role in society that sets banks apart from any other business, which is the creation of our money supply in credit form.

Other than notes and coin, all moneys - that is, cheques, plastic money, etcetera - comes into existence initially as credit, that is as debt, from which the banks derive direct profit in the form of interest and that new money comes into existence in about the length of time it takes for a teller to process a transaction on his or her computer. Our suggestion is that this frighteningly efficient process so dwarfs productive efficiency - the efficiency which the Campbell report concentrated on - that it makes nonsense of the assumptions of the Campbell report.

The economy depends almost totally on the amount of money in circulation, yet there's no restriction on the banks' right to withdraw money at any time from circulation as far as I can see. The only real restraints on money creation, after Campbell, are the requirement of the banks to retain certain defined assets, the willingness of customers to take out loans, which is beyond the control of the banks anyhow, and the banks' own sense of responsibility. Our feeling, the feeling of the organisation, is that the banks did not show very great responsibility during the period since deregulation.

I did have some slides which I rather hoped that I could show but I see you're not set up to show slides or graphs at all, which seems rather strange from what's an economics discussion, because graphs speak much more cogently than words do and are easier to follow. However, there are some things which need to be questioned and we do question them. From 1984 when deregulation began, to the October 87 crash, the banks created what appears to be about a third more credit - that is M3 money - than was prudent, based on the evidence of the years immediately prior to 84.

Little of it was directed to genuine investment. The rate of GDP growth actually fell during that period. Most of it went to the now notorious captains of industry - I suppose I'm allowed to be derogatory towards those, or am I not - but I would have hoped I would be - and to rampant commercial property speculation. After the crash - that's in 87 - the banks actually increased their rate of credit creation in 88 and raised it again in 89 to a level that seems to be about two and half times the prudent level of money creation. One has to ask the reason for this. Why should the banks do it? And why should that be regarded as being a sensible way to act after a crash has occurred which is about to bring the economy down?

The rate of money creation then remained excessive until 1991 when Australia fell into recession and one would have to ask again why was money creation still excessive 4 years after the crash? From 1984 to 86 the provision for debt and actual bad debt averaged for all banks - and these figures come from the Reserve Bank - rose, yet against the trend of rising bad debts the provision and actual debts from 86 to 87 remained static. What I'm trying to say here is that after deregulation the banks had evidence of rising bad debts, yet for one year from 86 to 87, according to the average figures for all banks, provision did not rise, which requires some questions, and the actual debts they showed in reports did not rise, which needs to be questioned. It seems to be an anomaly.

After 1987 they're still talking about debts. Bad debts rose quite dramatically, and yet provision for debt fell. I think one has to ask why banks are reducing their provision for debt when they've got evidence that debts themselves are getting out of hand. How is it possible for the banks to be allowed to account in this fashion and where was the Reserve Bank's prudential supervision during that time?

Looking at a different issue, the interest margins which are charged for domestic and commercial transactions, from 1984 to 1985 interest margins rose generally but from 85 to 87 domestic margins rose substantially whereas commercial margins fell, even though it was the commercial loans which were creating the bad debts. One has to ask why? Isn't it normal practice that the riskier loans carry the higher margins and clearly the commercial loans were the risky ones, yet in practice the margins were carried by the domestic loans.

Would you agree that domestic consumers were required to subsidise loans or the losses of the commercial property speculators in that time, and how can you then say, or how can the pocket for change say that bank customers on balance benefit from deregulation? The evidence seems to me to be that the mortgage loans of domestic mortgagees carry probably billions of excess costs to cover costs of failed commercial enterprises. That seems to be the evidence of graphs provided by the Reserve Bank.

So finally we would argue that there was irresponsible lending from the banks between 84 and 90, and that the subsequent withdrawal of money from circulation produced the real crash that followed the false boom, and that the banks' accounting during that period is very questionable to say the least, and the banks effectively - and I would personally say possibly deliberately, though I would exclude ERA from making that comment myself - force the home mortgage holder to subsidise lending to sections of the banks.

On that evidence, the deregulation of banks was a mistake. The banks can't be trusted to self-regulate, which is the de facto position in deregulation, and the banks must be placed under closer supervision again, and that is the position of the organisation that I belong to, to a degree. The stronger accusations which are implied are very largely mine.

CHAIRMAN: Thank you, Mr Dorney. I'm sure - - -

MR DORNEY: Dorney.

CHAIRMAN: I'm sorry. You've been a last-minute addition, and I apologise.

MR DORNEY: That's right. I had to sit up till 12 o'clock last night writing this. I'm sorry about that, too.

CHAIRMAN: Okay. I'm sure you're aware of our terms of reference, which are essentially to address the regulatory issues - - -

MR DORNEY: That's right.

CHAIRMAN: - - - governing the Australian financial system. I mean, what would help us if you could be a little bit more specific about what you think this committee should consider.

MR DORNEY: Well, I think that since the Wallis committee appears to have said at various times that it is looking at a further process of deregulation, then you must be starting from the point that deregulation so far is likely to have been beneficial. I think that before you can start from that point you should be looking at the evidence to see if that is true. I have tried to produce evidence that shows that it simply is not true. A few graphs would have made it much clearer than a lot of words.

But certainly the evidence of the supply of M3 money during the period 84 to 91 would indicate that after deregulation the banks were reprehensible in their deregulated position and that they did things which certainly caused the economy damage. I believe they did things they knew would cause the economy damage because they would personally not be badly damaged by it. That's just a personal belief. But if you believe that, you must also believe that deregulation is not the way to go. I can't see how I can put it more clearly than this.

CHAIRMAN: The inquiry is essentially about how we can make the financial system more competitive, more responsive for all Australians, at the same time keeping the system safe. We are actually ruled out of consideration of the Reserve Bank's conduct of monetary policy. I just want to make that point. All I'm trying to draw out from you is the specifics that we can try and take on board.

MR DORNEY: I have tried to make it clear at an earlier point that the mention of efficiency that you are using, the definition of efficiency, is one that's inappropriate to banks because you're regarding banks as if they're purely an industry; that is a money-shuffling industry where money just gets shovelled across counters and the fewer clerks you have doing it per dollar earned, the better. That is efficiency in your terms. I'm simply saying that those terms are wrong terms.

CHAIRMAN: Well, we're looking at it in terms of better outcomes for customers and users.

MR DORNEY: Well, I have just said that as far as the bank customers are concerned, those who have domestic home mortgages have probably been stung to the tunes of billions of dollars by the private banks in an attempt to recoup losses from the commercial sector. Now, if you're trying to do that, you will obviously try to stop that recurring, and yet that recurred as a process of deregulation. Here again I can't be more open and direct than that.

CHAIRMAN: Would you encourage us to provide incentives for more entrants into the system? You've seen the securitisers come into the home mortgage market in recent times.

MR DORNEY: I don't want to stop people coming into the home market, but that is not the real issue. Those people who are not banks can certainly lend money to home mortgagees or people seeking a mortgage, but they are not banks. They do not create money. The issue I'm pointing out is that that kind of competition may be of some minor benefit, but if to do that you further deregulate the bank, then you're making things worse than they were in 1984 when the deregulation that happened then in fact cost the customer billions.

My position is that deregulation has cost the customer billions. The banks do need prudential control of their money creation capacity. I do not care if AMP itself creates loans as long as it's not creating credit out of new money. That's a different issue.

PROF HARPER: Thanks, chairman. Mr Dorney, a couple of things I'm interested in: firstly, your concern about deregulation of the financial system. Of course the term "deregulation" is one that's used widely within the profession, but in actual fact it conceals regulatory changes that go in two directions, and this of course dates right back to the Campbell committee itself which recommended these changes in two directions; in short, the relaxation and in some cases removal of certain types of monetary control - - -

MR DORNEY: Yes.

PROF HARPER: - - - but at the same time the strengthening of prudential controls, and throughout the period that you're describing - for a start as late as 1988 of course the Bank for International Settlements introduced a new system of prudential regulation for banks around the world. What I'm really asking you then in the light of that is this: given that the term "deregulation" covers changes or the removal of some controls and the strengthening of other controls, what particular changes would you like to draw to the committee's attention as having been in your opinion a mistake, and which ones would you like to see reversed or at the very least ameliorated in some way by this committee?

MR DORNEY: Well, it seems to me that the deregulation or the reduction on the need for banks to maintain certain assets, which dropped from I think about 10 per cent to 6 per cent, obviously encouraged the banks to lend more, and the general deregulatory process indicated the banks would have the freedom to do so. In fact after 84 they did do so. I would like to see that process reversed. I would like to see far tighter control over the prudential requirements of the banks. I'd certainly like to see the Reserve Bank show more control in actuality than it appeared to do during that process when things were happening which the Reserve Bank ought to have been preventing from happening.

If you would look at this state in particular, when it was almost certain, judging by things said during the royal commission, that the State Bank of South Australia was deliberately understating its bad debts and its provision for bad debts, it's almost impossible that the Reserve Bank couldn't have known that, and yet this is a state-owned bank and the Reserve Bank appeared to feel no sense of responsibility to tell the people of South Australia, through John Bannon their representative, that things were going amiss.

There obviously has to be tighter control than that. The concern of ERA is essentially that the creation of money remains purely a banking function. That creation should be more tightly monitored than it was during that period. That's our essential position.

PROF HARPER: Portfolio controls?

MR DORNEY: Well, I'm talking simply of - whether you call it portfolio or not - the amount of reserves held and the capacity of the banks to put money into circulation virtually at will if the prudential requirements fall sufficiently, and the capacity to take money out at will. I also feel - and you're going to say it's outside the control of the committee too - that since the banks operate purely in their shareholders' interest, often enough they will take actions that they see will pursue short-term profits which are clearly not in the interests of the economy over a long term.

In the period under discussion they did do things which were not in the long-term of benefit to the economy. I hold the banks totally responsible for the false boom leading up to 1989 and the collapse that followed after it. The position that we hold is that creation of money supply is of such importance, and it's done by the private banks, that the Reserve Bank must have tight control.

I do not care if other people come in and offer money to home loans or home mortgagees if that money itself comes already from money that's in existence. That's probably an advantage. I've got no objection to this. I suspect that other ERA members have got no objection to this. What we do have strong objection to is the cavalier way in which the banks can create money and the purely self-interest way in which they do so for their shareholders' benefit, and we require that there should be controls in place to prevent that happening.

You may be better able to create or suggest what those controls should be, but we are pointing to evidence which suggests the controls just aren't there.

MRS NICHOLLS: Thank you, chairman. Mr Dorney, I'd like to pursue with you this issue of accountability. I feel that I heard you say quite clearly that the measures that we are using for the performance of our banks and regulators are inappropriate.

MR DORNEY: Yes.

MRS NICHOLLS: You don't think that productivity is the right measure?

MR DORNEY: No, it's not.

MRS NICHOLLS: And equally, I felt that I've heard you say that we aren't holding either our banks or our regulators accountable for their performance. Some suggestions have been put to us in other forms about mechanisms that might change the situation. One for example is to have more direct involvement of customers or consumers on boards. Could I ask you please to address, firstly, how exactly would you measure the performance of banks and regulators, and how exactly would you hold them accountable for their performance?

MR DORNEY: Well, I would not regard the major issue as performance being simply dollars shuffled in relation to the number of staff held, and that would be perfectly valid for a private factory or a commercial concern. I regard, since the banks are effectively the sole providers of credit and therefore use more money in the system - and nobody appears to have disputed that this is so - since they are the ones who create money and the health of our economy depends totally upon this fact, if they put too much money in circulation then you get a false boom and potentially inflation and then perhaps high interest rates.

If you take money out to achieve a short-term objective you then turn the country into a long-term recession, the worst for 30 years. Clearly the important thing that banks must be held accountable for is the amount of money they put into the economy and why, and who it goes to. Now, exactly how you set that up is not something that I can say in great detail, but the evidence is quite clear that before 84 money creation was a fairly stable process and that the increase in supply was an increase that appeared to be suitable for the needs of the economy.

If you took inflation out of it, it was virtually a flat line; very slow growth indeed. Since 1984 the money supply has been totally erratic - vast amounts coming in, vast amounts being taken out at different periods. It is this issue which is the main issue that a regulatory process should be required to address, not just paper shuffling.

MRS NICHOLLS: Thank you.

MR BEERWORTH: Thank you, chairman. Mr Dorney, in your comments and certainly in the written submission that we received from Dr Hermann - - -

MR DORNEY: Yes, last night, the but I assume it will be very similar. I hope - - -

MR BEERWORTH: Yes. No, it's the same point. The implication is, or the statement is that the Reserve Bank has really failed in its job by not using the controls which were in its power. Given that institutions ultimately come down to people, it really doesn't matter whether we abolish the Reserve Bank, which I think Dr Hermann suggests was a possibility. You need to put something in its place if you're going to impose controls, and you end up with the same people, people trained in the same way. What's the solution to that problem?

MR DORNEY: Well, you don't necessarily end up with the same people at all because the people on the Reserve Bank at present are people whose perspective is very limited and you could expect them to take a certain line. I don't know what the present composition of the Reserve Bank is. I don't know if Solomon Lew is still a member. His attitudes towards finance have been - - -

CHAIRMAN: I remind you of my earlier comments.

MR DORNEY: Yes, I know. But they have been challenged in a number of places, quite publicly, without I think being sued. I was thinking particularly of various columns in The Australian who questioned Mr Lew's approach to things. But he is a member of the

Reserve Bank and he obviously represents business as he sees it. I believe that Mr Kelty has now quit the Reserve Bank, and you would have thought that he would represent the people. In view of the fact that he was very quick to defend Mr Lew on a certain occasion I'm inclined to suspect that's not the case. Was it Jane Holmes à Court, is that her first name? Is it Jane?

CHAIRMAN: Janet.

MR DORNEY: Janet, thank you. I'm sorry for that. Wife of a person who fell during the period of the 87 crash. I don't know if her views are substantially different from Mr Holmes à Court's.

CHAIRMAN: I think Mr Beerworth might have been referring more to the management of the - - -

MR BEERWORTH: I think ultimately the officials of policy. I appreciate the board has a role, but the bureaucrats if you like, the officials, the public servants are the ones who really guide the detailed policies and the monitoring that you're worried about.

MR DORNEY: Well, it may well be mandarins behind the scene, but if the board seems to exist for self-interested reasons which may well be the same self-interested reasons as the mandarins because they've got the same economic rationalist policy, if you can have some other board to feed back concerns to the mandarins, it should be a much more representative board, and certainly there's nobody from the real public at large out there on that board. The board is very narrow in its focus, and I believe there should be a board to direct concerns to the mandarins, and it's quite obvious that the Reserve Bank failed to do that, so perhaps the composition of the Reserve Bank is wrong. I personally suspect the Reserve Bank failed to do so knowingly.

CHAIRMAN: Thank you. I think we have probably covered it, Mr Dorney.

MR DORNEY: That's fine.

CHAIRMAN: I apologise that you got the wrong directions but there was a last-minute change of venue and I hope you can get an earlier night tonight. Thank you very much.

MR BEERWORTH: During the interval perhaps you might give us your slides and we can certainly circulate them to the committee, Mr Dorney.

MR DORNEY: Well, perhaps I can get a photocopy of the slides and circulate that.

MR BEERWORTH: Thank you.

CHAIRMAN: Thank you very much.

CHAIRMAN: We now have Mr Gerhard Weissmann. Mr Weissmann, thank you for coming along. I'm sure you have the hang of things at this stage. I don't need to repeat my introduction, I'm sure. If you could state your name and I presume you're representing yourself and we would be pleased to hear from you.

MR WEISSMANN: My name is Gerhard Weissmann, I'm a chartered engineer and recently completed a master's degree in environmental studies, so my main interest is between the financial system and the environmental impact. I have made a little paper. Do you want this?

CHAIRMAN: Yes, by all means, please.

MR WEISSMANN: This morning I'd like to concentrate on two aspects of the discussion paper. The first one is the acceptance of the irrational belief that unfettered competition must be encouraged into existence beyond what the free market provides in its normal workings. It is a myth that Australia as a whole would prosper through green efficiency which simply means increased corporate profitability at great public cost to the nation.

The second aspect is I deplore that taxation of institutions and processes is ignored. Your appendix A, terms of reference 4D, excludes the aspect of taxation. But taxation is an alternative political tool to regulation; to discourage rather than regulate undesirable and intolerable practices. It may also raise some funds for more useful government activities.

Now, in detail: the national competition policy, that was the Hilmer report, is based on Paul Keating's statement in One Nation that, "The engine which drives efficiency is free and open competition." Hilmer repeats that mantra as "Competition is a positive form for economic growth and job creation." This is newspeak straight from George Orwell's 1984, a language devised to meet a particular ideological need.

The micro-economic theory lists efficiency as one factor amongst many that contributed to competitiveness of a firm. This logic cannot be inverted one to one. Competitiveness as dog eats dog practice - as it turns out to be practised, is a euphemism for price-cutting wars which has always been an activity that the economic fraternity has abhorred as self-defeating. Price wars were a no-no. It is destructive of good trading practices, of a nation's social fabric and of the equality. We're witnessing now the consequences of that imposition of artificial competition: economic exhaustion, stagnation, depression of rich and poor Australians.

As the need of the national market for say communications was adequately met by one operator like Telecom, imposing another operator into that limited market decreased the efficiency to one half, because the infrastructure was doubled. The resulting competition makes both firms attempt to cut corners, as Optus is with sheltering behind the Telecommunications Act to impose itself on the streetscape at minimal cost - hanging up their cables.

Privatised electricity and water utilities let the installations deteriorate. They impact more ruthlessly on the environment and increase charges due to decreased profitability. Tom the Cheap was an early victim of inappropriate price-cutting. Up to 1983, that's the beginning of the Hawke era, Australia with its population then of circa or around about 15 million people compared with thousands of millions in North America and Europe was served by an oligopoly of a few major banks appropriate to that small population.

Public sector finance was separately sourced from the reserve since infrastructure was deemed to be capital assets. This is as I understood it. Many services operated as government monopolies because they were non-profit making services to the public. The sector was suitably quarantined as appropriate for a small but rich self-reliant nation. This quarantining should be reinstated now by low-interest lending to public utilities by the Reserve Bank or subdivision of that bank set up for that purpose.

The irrational import by Keating of universal competition, even in credit creation by private banks, has to be curbed. Deregulation has done immeasurable damage to Australia. The damage is not assessed or mentioned in the discussion paper. Witness the unserviceable national debt, incredible number of unemployed, soaring amounts needed for social service payments, taxation system on the edge of dysfunction and the effects of the moral destruction of large sections of our younger generation; increasing environmental change becoming apparent with river pollution, salination desertification, sacrifice of forests, excess artesian water draw-down for mining as in Roxby Downs, general destruction of habitats, including that of people, as the extensions to the Sydney Airport show.

Regulation cannot now correct that situation. It is too late. The discussion paper recognises in paragraph 2.10 that regulation did not achieve its objectives. It is ineffective since it is retrospective and invites subversion and evasion; like a toy balloon: squeezing one end, the other one blows out.

Taxation, however, is a legitimate political tool to shape preferences in the open market by reducing the profitability of practices or actions which are agreed to be undesirable in the national interest. For instance, creation of credit by private institutions could be taxed. The means to collect tax by electronic transfers may have to be found. You mentioned options in section 7.118 in your discussion paper and that could be quite useful. I refer to the book The Tobin Tax, a book recently published - I don't know whether it could be put on the record. That book recommends a .1 to a .25 per cent tax on funds - on speculative movements of money in and out of the country. I suggest a transaction tax at .5 per cent even for payments over $5 or else on those that are not for direct purchases of goods or labour. Where money changes hands for things or wages taxation would not be as useful. It could even replace income tax if the income is large enough.

Taxation can be used effectively to modify free choice for operators in a deregulated market without imposing direct regulation, which can be evaded, of course. For various reasons regulations are hard to fit to particular circumstances, costly to administer and difficult to enforce because of legal challenges as the discussion paper recognises. Taxation has not been used at all effectively in this manner although it is well accepted in other areas, for instance parking meters where people will make their choice to move on as intended. These are the two points I have concentrated on in the discussion paper.

CHAIRMAN: Thank you. Bill?

MR BEERWORTH: Thank you, chairman. I was particularly interested in the Tobin tax and how it might operate, Mr Weissmann. Do you think it might inhibit tourism and some industries of that nature which are becoming increasingly important in Australia?

MR WEISSMANN: That may be so, yes, and that is one of the beneficial effects because tourists add to the population; they increase the temporary and very demanding section of the population in Australia. They demand the best, they demand the best spots, they degrade the most interesting areas to the detriment of Australia's nation.

MR BEERWORTH: So there are both economic and environmental issues which you're negative about there.

MR WEISSMANN: Yes, very much so. The negative impacts are not usually recognised because they cannot be translated into direct dollars; for instance tourism bringing in fruit fly in the Riverland here. What's the price on eradication of fruit fly?

CHAIRMAN: Where does the currency fit into this thesis of yours? Do you have any views about how the Australian dollar should be controlled - freely deregulated? Do you start taxing flows into the country?

MR WEISSMANN: Yes.

CHAIRMAN: The dollar may do something very quickly which might make life very expensive for all of us.

MR WEISSMANN: It may - less impact on internal economy - yes, it may make goods very much more expensive to import, and export more difficult, yes. But so be it. The standard of living in Australia used to be much higher than the surrounding world. It's now being dragged down, through deregulation, down to - not quite Third World levels but to very low levels. The people that are squeezed out of the productive processes due to downsizing are suffering substantially. So even The Australian wrote about it. Many people have to sell houses and go into rental accommodation just because they cannot carry mortgages.

MRS NICHOLLS: Thank you, chairman. Mr Weissmann, I was very interested in your comments about the negative effects of competition, particularly price-based competition. That has led me to wanting to ask you about your view on mergers. Now, mergers amongst financial institutions is a topic on which the press has speculated in some detail during our inquiry to date. Could I ask you to comment. Would you see mergers amongst some of the financial institutions as a way of lessening this destructive price competition you referred to, and could you comment more generally on your view about mergers?

MR WEISSMANN: I have no great preference either for or against mergers as long as there is, I suppose, normal competition, as long as it's not forced competition, as under the competition policy it was encouraged - as the competition policy encouraged normal competition in a free market. That's the general idea, that they are free operators in the market and all the assumptions are as closely as possible given, that information is shared and all this.

MRS NICHOLLS: If I could ask on that, how do we know when competition is normal or when it's in that less than desirable condition that you referred to in your remarks? Is it something about prices or - - -

MR WEISSMANN: I think it is probably the social benefits of state monopolies that have been dismantled. I used to work for the Electricity Trust here and this forcing the Electricity Trust into this competitive market seems to me contraindicative to the benefit of having a publicly funded electricity utility here. So that I see as artificially imposed competition, whereas normal competition, electricity - between gas and all this fuel - as a fuel merchant was accepted under a free market regime.

MRS NICHOLLS: Chairman, if I may, just to follow a point - - -

CHAIRMAN: Yes.

MRS NICHOLLS: We have seen with mortgage securitisation quite a marked effect on the prices of housing loans in Australia, and certainly representations have been made to us that one of the effects of this vigorous price competition in recent months has been the removal of some or the erosion of margins; that will mean that cross-subsidies to other products may have to be dismantled. Just so I can understand your model better, is that an example of good competition or is that an example of bad competition?

MR WEISSMANN: If the responsibility that goes with providing mortgages is properly addressed, as banks used to cross-subsidise, as you say, part of the mortgage market, and if that handing down to separate operators of mortgages - that's what you call securitisation, isn't it?

MRS NICHOLLS: Yes. People who are not banks, yes.

MR WEISSMANN: Yes. If the responsibility in that sector were addressed again by taxation, that the banks unload unprofitable or less profitable operations and were made to accept a tax on this unloading of responsibility, then I would say - and they can live with that tax, yes, then that's normal competition. But if it's just simply taking the breaks away, then it's not desirable. So to my mind taxation can be applied to make undesirable processes unprofitable and then the operators will make their choice and say, "Look, there's nothing in it, so there's no point in doing it."

MRS NICHOLLS: Thank you.

CHAIRMAN: Ian?

PROF HARPER: Yes, thank you, chairman. Mr Weissmann, the focus of this inquiry is on how the regulation of the Australian financial system could be improved, so as to improve the efficiency and not compromise its stability. At the same time the inquiry, as you know, has been asked by the Treasurer not to make recommendations on questions of tax. Given in your submission your concern that it seems too late for regulation to have done anything about the matters that you raise, I simply ask what specific things do you think this committee can do to address the issue that you've brought to our attention, given that we can't make recommendations on tax and given that our focus is strictly regulation which in your view seems to be, at this point, too little too late.

MR WEISSMANN: Yes, quite so. You may suggest that taxation needs looking at as a means parallel to regulation or even taking over from regulation. Regulation has, as you know, its difficulties in parameter setting, benchmark setting and enforcement to establish that somebody has stepped beyond the regulation. Then you have to prove it, then you have litigation processes - are you right in applying regulation? Regulation is a very awkward tool, and just concentrating on regulation to my mind is so limiting the inquiry that really I would suggest to look at other means and I think taxation is a means other countries have gone to.

So again I have - this is in German, I can't help you; but it is by Bartzecker, some relation of the German president. He says that taxation really is a much more elegant, a much less effort-involving tool, and it produces some income to do something about it to the authorities. So really to my mind it's a much more elegant mechanism, and it could be suggested that excluding it from the terms of reference was a mistake and maybe it should be included.

CHAIRMAN: Thank you very much, Mr Weissmann. We've appreciated your attendance.

MR WEISSMANN: Okay.

CHAIRMAN: Ladies and gentlemen, that completes the hearing this morning. We thank you very much for your attendance and we shall be pondering everything that's been said, as we work to complete this task of ours. Thank you very much.

CHAIRMAN: Can you hear us? It's Geoff Casey, is it?

MR CASEY: That's correct.

CHAIRMAN: My name is Stan Wallis, Geoff. You have Mr Bill Beerworth, Prof Ian Harper, Mrs Linda Nicholls and Greg Smith, who's the secretary of the inquiry, all around this speaker phone, and we've had a good morning here in Adelaide and we'd be pleased to talk to you about some of the issues that you've raised. Would you like to just tell us a little bit about your view of the world?

MR CASEY: Well, as I've outlined briefly in my letter, and I'm sorry it was a bit scratchy, we're a family-based mining group up here, we're only a small operator, and the finance side of things is one of the most difficult areas. The mining side is quite okay, but when you're starting a new project or something like that, securing finances for it is exceedingly difficult at times.

One of the biggest problems is that the normal sort of retail banks don't have any expertise in the mining field, and they don't sort of feel inclined to - this is from our experience anyway - just accept the reports and recommendations and things like that that are submitted by consultants that we use, and they tend to want to steer clear of mining projects, unless of course you're a public company, which puts you into a different sort of arena.

But they often refer you to the merchant banks, who are traditionally the financiers of the mining industry. The problem is that the amount of money that we're looking for is not big enough to be of interest to the merchant banks. They start at about 5 or 10 million dollars and that's usually only if they can see that further down the track you're going to want more money that's, you know, in the sort of 20, 30, 50 hundred million dollar sort of bracket.

Now, the merchant banks have told me that they don't get involved with smaller projects because the establishment costs are too great because they put in their own geologists and things like that to assess the project, and by the time they've finished doing that they might have spent as much as what you want to borrow anyway, so the small mining sector is sort of between a rock and a hard place almost.

CHAIRMAN: Are there any institutions that have done it better than others over the years? I mean, can you point to any successful instances or any models that we can think about?

MR CASEY: Not really. I mean, small miners do get finance from - I'm not saying that retail banks sort of really have never financed a small miner, because that's not quite true, because they do provide finance for equipment, like if you want a front-end loader or a truck they can come into things like that, because they're pieces of equipment that they can sort of understand and they can see that if anything goes wrong, well, they can sell it. They seem to be preoccupied with the aspect of if anything goes wrong, which I suppose is fair enough because they've got to protect their investment.

CHAIRMAN: Sure.

MR CASEY: But when you start getting into specialised pieces of mining equipment like parts of treatment plants and things like that, they usually want - if they do finance it, it's usually because you've got other finances with the bank. I mean, I have financed specialised equipment like this, but I had - just as a quick example - about $80,000 worth of equipment I received finance for from one of the banks here in Darwin, but backing that up there was about $1½ million worth of real estate and another project that was under way as well, so it was sort of just included as a very small part of a bigger package.

CHAIRMAN: Geoff, I think Linda Nicholls wants to ask you a question.

MRS NICHOLLS: Thanks, chairman. Geoff, I was wondering if you've had any positive experience from some of the smaller banks that might have foreign shareholders. I'm thinking for example like a BankWest, where Bank of Scotland is more than a 50 per cent shareholder, and that shareholder has considerable experience in lending to mining projects because of their proximity to the North Sea. Is there any difference from an institution like that?

MR CASEY: Well, we're a bit limited in our access to some of these other banks.

MRS NICHOLLS: It's kind of a long drive to Perth, huh?

MR CASEY: Well, this is right, yeah. You know, we're basically limited to the banks that have got offices in Darwin.

CHAIRMAN: Who are they, Geoff?

MR CASEY: Well, we've got the majors here, like Westpac, ANZ, National Australia Bank - who have I missed?

CHAIRMAN: Commonwealth.

MRS NICHOLLS: Commonwealth.

MR CASEY: Commonwealth, yeah. I try not to think about them. I've had a rather bad experience with them. Yeah, Commonwealth Bank. Yeah, I think that's it.

CHAIRMAN: Anyone else?

PROF HARPER: And no regional banks?

MR CASEY: Beg your pardon?

PROF HARPER: No regional?

CHAIRMAN: No regional?

MR CASEY: No, no - oh, State Bank, sorry. Bank SA.

MR BEERWORTH: Bank SA, right. Geoff, how much money are you trying to - - -

CHAIRMAN: This is Bill Beerworth..

MR CASEY: All right.

MR BEERWORTH: How much money do you need to raise, Geoff?

MR CASEY: Well, between - well, we usually look between 500 and say about - 500,000 and say about $1.5 million is sort of the range that would suit most small miners.

MR BEERWORTH: What's happened to the firms that build that specialised processing equipment, like say Minproc Engineers? They used to specialise in not only designing equipment but advancing funds and so on, and that's the way it's traditionally been done in that area.

MR CASEY: Well, my area is in alluvial mining - - -

MR BEERWORTH: Right.

MR CASEY: - - - and there's not a lot of suppliers of alluvial equipment around now, like - what was their name? Inverell Foundries used to be the major supplier like that, but I think they've been wound up at present, but like the equipment that I mentioned was two Nelson concentrators. Now, the parent company of them or the designer and that is Canadian based, a chap by the name of Byron Nelson, and they work through a Sydney - like an agent sort of thing, who imports the bowl, which is the core sort of component, from Canada, because it's covered by all the patents, and the rest of the machine is assembled here in Australia, but they're only a fairly small outfit themselves and they don't offer any finance facilities and things like that. Otherwise a lot of our equipment we actually fabricate ourselves.

CHAIRMAN: Can you be a little bit more specific about what you believe an inquiry like this could do for you and similar organisations, Geoff?

MR CASEY: Well, it could come to an education of the financial institutions or suggesting to the financial institutions that they might educate some of their people, because when I've had the opportunity to get a bank manager down on site and he can see what's going on and understand the process a little bit more, I've found that the pathway was smoothed better, but his problem was that he didn't actually run his own bank. I mean, he was a bank manager, but he had to pass any proposals with his recommendations to head office, as it were, here in Darwin, and get it approved there. It was like a central approving depot, if you like.

CHAIRMAN: Okay.

MRS NICHOLLS: Geoff - sorry, Linda Nicholls again. Is there an issue about getting better access for people in areas like the Northern Territory, to those financial institutions who are very unlikely to ever have a branch network, let alone a branch network that came to the Northern Territory. So I'm thinking for example about some of the newer providers of financial services who might not be banks, even though they are still facilitating lending, who are active in Sydney or Sydney and Melbourne, but have not moved out on a national basis yet. Is access do you think an issue?

MR CASEY: With modern communications I would say in one respect it's not really, but finding a list of who's available - I recently found a list of all of the financial institutions in Australia which I got through the Reserve Bank, and that was - actually I got that by accident almost because the information I was seeking was in a Reserve Bank bulletin, and that other information was in there as well, so it was a spin-off.

What I've found is that on the occasions that I've contacted institutions that aren't represented here in the Territory, that seems to be a bit of a stumbling block for them, and I think it's probably a mentality problem more than a real problem, because I mean, like I say, modern communications, we can pick up a phone, talk to anybody, send faxes, you know, there's e-mail, there's a whole host of communications methods available to us today that haven't been, say, 20 years ago, but I think that in some areas of the bank industry or the finance industry, the mentality of 20 years ago still exists in respect of distance.

CHAIRMAN: Is the issue often the question of how much debt and how much equity?

MR CASEY: Well, that's a question that's put, but I think that's just a - you know, I would expect that to be asked, because I mean if you're carrying too big a debt load you can't afford anything further. One thing that's been put to me - earlier I mentioned that I didn't want to think about the Commonwealth Bank because I've got a rather major court case going with the Commonwealth Bank, which is me attacking them rather than them attacking me, over a real estate development deal that went sour, but the root of that was personalities and, you know, you can't really legislate anything there that's going to affect that situation. It's just an unfortunate situation that happens.

Oftentimes, if you mention that you've got litigation - I mean, they're going to find out anyway so you may as well be up-front and, you know, say, "Well, this is going on." If there's any mention of litigation with another financial institution, immediately the shutters go up. That's what I've found here in Darwin anyway. Some of the merchant banks I've spoken to, whilst they couldn't help me because what I was seeking was too small an amount of money - - -

CHAIRMAN: Linda's got one more question, Geoff, and I think we might then have covered it pretty well from our point of view.

MRS NICHOLLS: Geoff, the view has been put to us that if in Australia we had positive credit reporting - that is, greater public access to information about those individuals and companies who have been borrowers for a period of time, who have had a good history of making their interest and principal repayments on time - this would actually make more credit more easily available throughout the country. Do you have a view about that?

MR CASEY: That actually sounds like a good move to me because, as it stands, the credit reporting system that we've got and the most that the institutions dwell on is all negative, like the CRAA which I think is, to put it rather simply, a blot on the landscape for the reason that they report things which they haven't fully researched, so they don't know - - -

MRS NICHOLLS: They don't often have the context.

MR CASEY: Yes, and also they don't make any effort to ensure the reporting is accurate. For myself - I'm using a personal example again, if you don't mind - my wife has nothing to do with my business operations and yet she has found that on her CRAA file every transaction or every inquiry that I've made in respect of finance has been reported against her file, even down to the extent of making a verbal approach to a financial institution to just feel their attitude to a particular project or an idea you may have that you just bounce off. I've found that on more than the odd occasion that is reported on the CRAA, so it creates a false picture, which is negative, of people's credit ratings and things like that.

MRS NICHOLLS: Thank you for that, Geoff.

CHAIRMAN: Geoff, unless there's anything else you want to say, I think we've got a pretty clear idea of where you're coming from. I'm not sure that we can run too hard with it but if it - maybe we have got another question but if we can throw some light on the issue, we'll endeavour to do so, but I think Bill Beerworth has one for you.

MR BEERWORTH: Just one thought. Of course the nature of what you're doing entails very high risk and I'm sure you've read books like Trevor Sykes' Blue Sky (indistinct)

MR CASEY: Hello?

CHAIRMAN: Can you hear us?

MR CASEY: Yes, yes, you just faded out then for a sec.

CHAIRMAN: Sorry.

MR BEERWORTH: I was going to say what you do of course, from a banker's or a lender's point of view, does involve very high risk at the end of the day and you're well aware of that of course but are there any models that you could point us towards? As an example, I was talking to some miners in Colorado and then later in Canada on alluvial mining some months ago and they were expressing exactly the same concerns, particularly on alluvial mining, the difficulty of getting any funding for it, because it's not nicely set out in a block in the ground as far as lenders are concerned. Do you think it's a universal problem or unique to Australia or is there anything you think we can particularly do about it here?

MR CASEY: From what I've heard - I've heard the same sort of thing as what you're raising there from people overseas, although the model I would point to - but I suppose I've got to accept also that the company operating the Argyle diamond mine is a very large public company. A major part of their operation is in fact an alluvial operation treating about 3,000,000 tons of alluvial diamond material a year and the unit value of their ore is actually less than what I'm working, so when the merchant banks say, "You can't make any money out of alluvials," I say, "Well, what are they doing over at Argyle?"

I think probably from the financial institutions' point of view, particularly here in the Territory because this is the area that I can sort of speak with a bit of authority about, there has been a succession of company ventures that have gone into alluvials and they have cost shareholders and finance houses - they have cost money, this is true, but when you look at the reasons for their failure it's always come down to poor management. I don't quite know how you get around the problem, to be quite frank.

CHAIRMAN: Okay, thank you very much, Geoff, for taking the trouble to bring those issues before us. As I say, we'll ponder on it a bit and see whether we can take it anywhere.

MR CASEY: Mr Wallis, if you could bear with me for a little.

CHAIRMAN: Sure, we've just got some time constraints here, but go on.

MR CASEY: I'm sorry. No, I'll be just quick. There's a few points that I thought might be of use, going through your terms of reference and things like that, without focusing just on small miners. The mention of government sort of underwriting, as was referred to somewhere here - a system that exists in the states - that could be a very useful system to all sectors of industry, small business trying to start up - because starting things seems to be the biggest problem, and keeping it going for the first year or two. That system there - there's a mention here at 5.132 about the quality of information and not having appropriate corporate governance structures. I think that's probably true.

Here in the Territory - and this may be a model that might be of some use - we've got small business courses incorporated into our final year of high school curriculum - or not in the actual curriculum, they're electives - and there's short courses that are run by some of the business organisations and the government up here, so there's a fair bit of information available in that respect up here which may be a useful model to sort of draw on. Another thing is that the Australian banking system doesn't seem to recognise contracts as an asset, even though they do fall within the guidelines of the definition of an asset according to the Australian accounting standards.

CHAIRMAN: Mr Beerworth is not agreeing with you.

MR BEERWORTH: I was just thinking of firms like Elton on the mining side, Geoff. Certainly Elton's contracts are brought into account as direct assets by the banks in their lending but that just happens to be one I'm aware of.

MR CASEY: I've had situations where I've put in for contracts and I've approached the local banks about securing finance for the necessary equipment and I wanted to do it as a separate entity to my own operations and I was told, "Well, this company doesn't have any assets to provide security." I said, "Well, what about the contract?" As it was, it was a multimillion dollar contract over a period of 5 years.

MR BEERWORTH: Geoff, you and I both have the same problem; we're small businessmen. The trick, as we both know, is to get from being small to being large, where people will take you seriously and include relative intangibles like contracts and not discount them totally.

MR CASEY: That's right. Getting bigger, going from anything beyond a 10 or 20-man operation, seems to be just as hard as getting started in the first place. There seems to be like a glass wall almost, you know. They talk about the glass ceiling. I think in this case it's down on the ground.

CHAIRMAN: Mr Beerworth has got about 10 or 12. That's his limit.

MR BEERWORTH: Maybe we can link up somehow, Geoff.

CHAIRMAN: How about it, Geoff? Are we there?

MR CASEY: The other thing I was going to mention was there was a reference here to the stock exchange and things like that. I was wondering whether it'd be a feasible idea that either the exchange or brokers would be able to sell private company shares. I suppose it's a step down again from a second board situation where people that had a business going that wanted to attract equity by selling shares in their company - I suppose to some extent there'd need to be a little bit of private contact and negotiations, and the mention in there about the Securities Commission's reporting requirements allowing small companies to become invisible - well, I think that if private companies wanted to sort of step up into this realm where they were able to sell their shares to raise capital, they would have to then meet a higher standard of accounting but for a small company that's just chugging along quietly on its own, particularly in this day and age of criminal activity and things like that, I think there's a bit of apprehension in providing too much information like that because of possible repercussions - from some people; some people just don't give a damn.

CHAIRMAN: Okay, it's flagged.

MR CASEY: I think that if that sort of situation could perhaps occur, that might be something useful. It may only be like a contact system. I'm not quite sure how it would work but it's the beginning of an idea, I suppose.

CHAIRMAN: Okay, we've got - - -

MR CASEY: Another thing you mentioned there about information being distributed to small businesses, a good model that I'd like to suggest is the - probably other banks do it but the ANZ has got a little magazine they call In Business and it does little features on companies that are doing different things in different areas and it's also got articles periodically on finance that are available. Bear in mind it's a propaganda magazine for the ANZ, of course, but it's got positive, useful aspects to it. In this recent one it's got a three-page break-up on lease finance - the different sorts of leases and the advantages, etcetera, of that.

CHAIRMAN: Geoff, we're going to have to call it a day but can I suggest those points that you're making - if you want to send us a very simple statement of half a dozen points, it's far easier for us to sort of take them on board in that form.

MR CASEY: That's true, yes.

CHAIRMAN: I think you put them down clearly and concisely, then we have to deal with them, but we've appreciated the opportunity to talk to you.

MR CASEY: Okay.

CHAIRMAN: I think most of us would sooner be up in Darwin this morning than down here but thank you very much and we wish you well. I know the issues you're dealing with but I hope you get there.

MR CASEY: Well, it's just a matter of determination.

CHAIRMAN: Absolutely. Okay, thank you very much.

AT 11.25 AM THE INQUIRY WAS ADJOURNED UNTIL
FRIDAY, 13 DECEMBER 1996