FINANCIAL SYSTEM INQUIRY

MR S. WALLIS, Chairman
MR W. BEERWORTH, Member
PROF J. CARMICHAEL, Member
MR G. SMITH, Secretary

TRANSCRIPT OF PROCEEDINGS

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CHAIRMAN: Ladies and gentlemen, thank you very much for coming along today. My name is Stan Wallis. I'm chairman of the Financial System Inquiry. I have with me Prof Jeff Carmichael, who's one of the members of the committee, plus Mr Greg Smith, who is the secretary to the inquiry. Mr Beerworth is travelling up from Sydney and should be here, I would hope, any minute.

As most of you know, the Federal Treasurer, the Honourable Peter Costello, 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. We are required as a committee to report to the Treasurer by 31 March next year.

To assist in the task we have received and examined many many submissions, approaching 270 I think as of today, and of course in the last week or two we have released the discussion paper which was the result of all those submissions and the result of many briefings, both in this country and overseas, which the committee participated in. Copies of this document and the terms of reference are certainly available for viewing should anyone wish to examine them.

I must 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 the proposals for regulating the financial system. The inquiry is unable to consider particular complaints about individual financial institutions.

Finally, the inquiry has no special legal powers or parliamentary privilege and for that reason I ask participants to avoid making adverse comments about particular individuals or organisations. The procedures that we've adopted in this hearing so far are largely informal. We will ask those making submissions to come to the table and to make an opening statement and then the committee will ask questions as appropriate.

We have a very tight timetable today so I would ask everyone just to bear that in mind. Our first participants this morning are Stephen Maitland and Kerry Prior from the Queensland Office of Financial Supervision and I would ask those gentlemen to come forward, please.

I don't think I need go through the caution again about the fact that the committee has no legal powers or privilege.

What I'd ask you to do just at the outset for purposes of voice recognition is just to simply state your name and the organisation that you represent and then I will leave it to you to introduce your statement. Gentlemen?

MR PRIOR: Kerry Prior, Queensland Office of Financial Supervision.

MR MAITLAND: Stephen Maitland, chief executive officer, Queensland Office of Financial Supervision.

CHAIRMAN: Over to you.

MR MAITLAND: Thank you very much. Good morning. Just by way of an opening remark we'd like to make it clear that our submission to your inquiry is presented in the form that directly answers the terms of reference and that it's submitted two concepts of principles that we believe should apply to the financial system from our perspective. We deliberately avoided proposing future structures or systems, believing this to be the proper preserve of the committee after considering the principles and concepts that may be observed.

The first thing we'd like to highlight are factors that we identified that appear to be generally more supported in other submissions and we'd like to take this opportunity to reinforce our views of their importance. The first is that we believe all deposit-taking institutions or DTIs should be subject to prudential supervision. The second is that all DTIs should be grouped as one for supervision.

We believe that supervision should be tailored to the institution. We believe that institutional and not product supervision is preferred. We believe that access to the payment system should be available to all deposit-taking institutions. We believe that both at federal and state level discriminatory legislation should be dismantled where it discriminates against NBFIs as against banks, and we also are firm believers in the direct payment of supervisory costs.

The second area we'd like to highlight is that our submission made some points which weren't generally picked up by other submissions but again we'd like to reinforce them here as we believe very strongly in them. The first of those is that we believe that DTIs should have formal lender-of-last-resort facilities. The second is that DTIs should have depositor preference on liquidation, as currently exists under the Banking Act. We believe that legislation should be capable of speedy amendment. We believe very strongly that the supervisor must be resourced adequately and we also are in favour of

incorporation including mutual ownership under the Corporations Law for all DTIs.

The third issue we'd like to comment on verbally to you is some issues that have emerged since the inquiry started and comment on them. The first is an issue that greater disclosure could perhaps replace perception of government protection of deposit-taking institutions. While this theory has merit, we believe it may not reflect reality. The first flaw that we see is a belief that a government, at any level, will be able to walk away from the failure of a mainstream financial institution where ordinary people's savings are lost. One of the core expectations of a government by people operating in the financial markets is that there is some way safe to deposit their money.

The second flaw we see is the lack of appreciation, the needs and sophistication of large numbers of people. There is and will continue to be a need for ordinary people to have a place to safely put their money without having to make elaborate investigations of its safety and security. This not only applies to large numbers of children, the elderly, the ill-educated, but to most adults. The ability to read and analyse complex financial statements and disclosure documents should not and could not become a prerequisite of finding a safe haven for one's savings.

It would appear to be difficult to get away from the concept of a safe haven, whether it's called a bank or a DTI, as a place to deposit savings with safety and without having to make special inquiry. If this is the case, the safe haven will require special control or supervision.

The second issue we'd like to look at is the local level of supervision that is preferred and required. We don't believe it is in the interests of the present nor of the future if smaller financial institutions are not allowed to establish and to develop. By their nature they will be less sophisticated and may require a more intrusive form of supervision and will be more subject to localised economic and other conditions. These factors lead us to the conclusion that the supervisor must have the capacity to provide supervision at a local level.

Speed of take-up of technology: we believe there may be traps in assessing the speed of the take-up of technology by users of the financial system. There is no doubt that at a corporate level the take-up is high as it is for a relatively small and sophisticated section of the personal market. However, the capacity or the wish for very large

numbers of households to embrace all forms of technological interface with a financial system is not in our view proven and may occur over far longer time-frames than is often suggested. While this may not appear to be significant in aggregate dollar terms, it is very significant in the numbers of people involved and thus in social terms.

Our next point we've entitled, "Dollar values versus numbers of people." In a similar vein to the comments in the take-up of technology, we believe the committee should be wary of basing assumptions or analysing issues in trends on the basis of dollar values alone. The numbers of people involved are as important. We sense that many submissions to the inquiry have been made with a focus solely on the big end of town and without adequate recognition of the effects on large numbers of people.

For example, it's true that banks have a lion's share of the financial sector's assets and when you're banking all the major corporates you'll have that. However, the insignificant in gross asset terms, NBFIs, have extremely high relative proportions of people as customers and members. For example, one in three Queenslanders are a building society or credit union member, and that's men, women and children. As significant is the diversity of location of these people as compared with the location and concentration of the large assets. Observations, recommendations and solutions that satisfy the apparent needs of the large dollar values may have quite adverse effects on large numbers of people.

Our final point is in regard to deposit insurance. The concept of replacing the implicit RBA guarantee of depositors with the formal deposit insurance framework has been suggested by some. We do not view this as being a satisfactory alternative for the following reasons. A deposit insurance scheme could require a complete new and additional organisation to be formed and to operate, including the examination and supervision of entities to protect the insurer's interests, and in particular if the insurer is not the supervisor. This is hardly conducive in our view to a more efficient and less complex system.

The second reason is the capping of claim amounts that as a feature of nearly all deposit insurance schemes, results in depositors' actions that cause distortions and inefficiencies in the financial system. Our third point is the depositor is likely to expect, at least implicitly, government underwriting of the deposit insurer, thus the moral hazard currently expressed through the RBA is merely

transferred to the insurer and can experience a view - as deposit insurance bodies in the past 10 years should provide ample evidence of these factors. That's the conclusion of my remarks to you, Mr Chairman.

CHAIRMAN: Thank you, Stephen. I wonder if I could just start by asking you the general question that there was certainly a fair degree of emphasis in some submissions to grouping the non-bank financial institutions into a national scheme. It's just hard to perhaps conclude from what we were reading as to what you are really saying, although perhaps your opening remarks clarified it, as I read it, that all the DTIs should be grouped in some way. I just wonder if you could address that point specifically.

MR MAITLAND: In our initial submission there are at least three areas where we mentioned that we believe DTIs should be grouped. We see no real difference between a bank, a building society and a credit union in their concept. They do the same things. They accept money, generally short-term; they lend money long-term. They're classic deposit-taking institutions. I think if you look at those institutions in today's environment in Australia, their relative quality is very close as well and for that reason we believe there's a compelling logic to group them together as one and to have them supervised as one.

CHAIRMAN: In a national scheme?

MR PRIOR: A single national supervisor.

MR MAITLAND: A single national supervisor full-on. We're not going to be hung up on names and titles. We're going to call them community banks or whatever if they're not a big B bank, but certainly grouped together with the same standards applying to them, but we also made the point that supervision under those standards may need to be tailored to the type of institution.

PROF CARMICHAEL: Steve, within that framework, what would be the most important feature of maintaining the individuality of those institutions so they don't just all become one institution, if you believe there is, which I think you implied there is this character individuality. Is it the mutuality that you need to retain or what?

MR MAITLAND: We're not sure it is. We think that's much more a marketing exercise than a prudential matter and if identities wish to characterise themselves, or indeed remain mutuals and keep that listing characteristic, well, that avenue should be available to them. If they want to characterise themselves as community banks or constrained in

market to distinct geographic or industrial areas, that's the way they would set that differential, if you like, rather than through a legal distinction.

MR PRIOR: I think we're seeing that happen now in particular areas where the banks have foregone the local situation. We're seeing the institutions that we supervise now moving in quite a defined way and picking up the slack and doing business in those areas. So I think it is a question of the kind of culture that they seek to impart.

PROF CARMICHAEL: So you don't think there would need to be anything special in the supervisory arrangements to preserve that? It's just a matter of the way the market evolves.

MR PRIOR: Other than I think that the supervisory arrangements there are responsive to the kind of special problems that they might have, given the type of business that they conduct in those areas.

MR MAITLAND: Again there - if I can say to reinforce a point - they are subject to the smaller institutions' localised economic effects, so that if a credit union is operating in a sugar area and sugar takes a downturn, well, there are particular supervisory problems with that which wouldn't be experienced by a major national bank, for example, or an international bank which has a spread.

CHAIRMAN: Could you say a little bit more about this issue of institutional focus as opposed to the product focus. I mean, again in your introductory remarks you made a very clear statement about it, which perhaps I didn't quite read into your submissions.

MR MAITLAND: Sure. The current phrase is that the institutions fail, products don't fail, and we believe the holistic approach to supervision is important. There is the potential, if you focus merely on products, that other things are happening institutionally which could bring it undone which are not product-oriented - the risk management systems within institutions, treasury operations, for example - and you really, I don't think, can provide that surety of supervision without looking at the whole entity. If your focus is merely on products, you don't have that focus.

CHAIRMAN: Do you recognise it's an issue for this committee as we tend to look at the same products with very similar characteristics from different institutions?

MR MAITLAND: Yes.

CHAIRMAN: Dealing with that matrix is quite a challenge for us.

MR MAITLAND: It is. As I said, the product doesn't make the institution go broke. The institution goes broke itself and we look at an institute that's going broke not institutions that are going on. That's our downside, our worst fear.

PROF CARMICHAEL: I wonder whether in that distinction there isn't sometimes a little bit of circulatory in that you've started here with saying DTIs. Essentially it's the product that defines the institution but it's the institution that gets regulated.

MR MAITLAND: The DTI to us has - well, deposit and deposit-taking is there. It is also a lender. It is an intermediary. It's probably better called an intermediary than a DTI. It takes deposits and it lends. It's that matching activity, that social matching activity, that is the key and the deposit-taking is a focus of that because that's where the bulk of the people are involved in buying and selling.

PROF CARMICHAEL: Still if we pursue that, there are a whole lot of institutions out there that are not currently regulated as DTIs are that do that function. Would you want them brought into the same regulatory net?

MR MAITLAND: There are very few who take - I can't think of any that take deposits on demand.

PROF CARMICHAEL: That's the DTI function.

MR MAITLAND: That's right.

PROF CARMICHAEL: You moved away from that, I thought, to the lending function.

MR MAITLAND: People lend but then there's not the immediate connection between that and a deposit.

CHAIRMAN: You mean mortgage originators or something?

MR MAITLAND: Yes.

PROF CARMICHAEL: No, well, I don't see them as lending on someone else's - putting it through to someone else's balance sheet - but finance companies do lending. They provide that financial function but they don't take deposits. It seems to me that what you are focusing on, I thought, was the deposit-taking function as defining the institutions that you then want to regulate on an institutional basis.

MR MAITLAND: Yes.

PROF CARMICHAEL: Okay, but the supervision or the regulation is then based on the institution once they fit that category.

MR MAITLAND: That's right, because the institution's other activities can refer right back through to the depositor.

PROF CARMICHAEL: Would you want to see that extended to other - anyone that came in looking like they were selling a deposit? I mean, there are a lot of things out there in the community that smell like deposits and look like deposits but they are not labelled deposits. I mean, you could even think of say the new cards that are going out with stored value on them as being a deposit of type. Would you want to see those brought into the same box?

MR PRIOR: Only to the extent I would have thought that they are a product of an institution that requires some fund regulation.

CHAIRMAN: Coming back to this process of a uniform nationally-based scheme of supervision, do you have any views about how that might be effected and, if it was some opting-in process; how one might deal with that in terms of those that go in and those that don't?

MR MAITLAND: The "those" being the institutions?

CHAIRMAN: Yes, being the DTIs that choose to perhaps elect to go to a - there are other ways of doing it of course.

MR MAITLAND: Yes, it's not an issue that we've put a lot of thought into. As we said, we prefer to look at the concepts of supervision rather than the way it might actually happen in a mechanical sense. That might be - - -

CHAIRMAN: Sure.

MR MAITLAND: That's your job. But my reaction would be that I don't think it should be an optional area and that really comes back to the consumer. The consumer should be quite clear that things that take deposits are of that type, and type A and type B would just be confusing to them. So I think the one-in-all then would be the preferred approach.

MR PRIOR: I think that might pick up the other point that Stephen made a little later which was that I don't think we can assume too much knowledge in the minds of the people who are using these institutions. I think it's the old story about annual reports of companies.

MR SMITH: Does that extend to also having a common licence for all of these three institutions? Did you have in mind that there are three licences under the one supervisory authority?

MR MAITLAND: I think we'd say one licence.

MR SMITH: So in effect everyone becomes a bank.

MR MAITLAND: Well, every DTI becomes a bank. A different licence implies different conditions, otherwise why have different licences if you're just going to have a different name on it? And what

would those different conditions be? That would then differentiate between DTIs which is against the thrust of our proposal. We believe that they all could be treated equal and thus one licence would be appropriate. In our view, from our perspective, it's the level of supervision that is applied which would perhaps be different. It may be based on a number of issues: size, risk and so on for the one licence type of body.

PROF CARMICHAEL: Although from what you're saying you wouldn't be hung up on the name. It's in a sense a DTI licence and they could call themselves different labels for - quite different labels under there.

CHAIRMAN: I was interested in your comments, Steve, about the technology time-frame. Your comment was that it might come later but there's an awful lot of people around the world saying that it's coming sooner. Now, maybe that's exactly what will happen, it will move at different paces even within a country such as Australia. But we are seeing two quite distinct segments. I mean there are groupings of the population that clearly want the old ways but there is a whole raft of - particularly people in the younger generation category who are far more at home with the newer technology. How do you see that impacting in your business, in your area?

MR MAITLAND: This is a very anecdotal area, isn't it (indistinct) research in. As we move around - it's interesting, we do see some pockets and Australians are well-known for taking up technology quickly. But surprisingly you still see quite a lot of pockets of, not resistance but slighter acceptance, and I'm seeing a lot of that in younger people as well. It's not a universal trait that everyone under 18 is computer literate nor wants to do their banking that way for example. Remoteness doesn't necessarily have a part in it; there are a lot of metropolitan sophisticates who aren't in that game. Their expression was that there's a sort of thundering herd of technology and we're not sure it's quite so thundering as - - -

CHAIRMAN: Just that based on some of the material that has been put to this committee, for the cost of a conventional transaction you can count in dollars; the cost of that electronic transaction you count in cents. So if you want to deliver lower-cost outcomes to the population at large and in particular the people who perhaps need the lower-cost outcomes, we have to find, we have to be thinking about ways of how that newer technology is delivered.

MR PRIOR: I think I have heard the comment also amongst our institutions that some of them have created services now that have created an expectation amongst customers at a cost which is very substantial and probably non-sustainable over a time in a way that it can be argued that it hasn't really advanced the services being provided. I'm thinking about access to ATMs and so forth and all the costs that that implies. But I struggle with the telephone myself, so I'm (indistinct)

MR SMITH: But is there a regulatory implication of what you're saying about the dollars versus people point? I wasn't quite sure what that was leading in towards?

MR MAITLAND: In the nature of prudential supervision and systemic risk and so on.

MR PRIOR: I suspect it was a philosophical statement really. That's the way I see it. I think all we're saying is that the dollars are one thing and the people that are involved is another. And the figure I think that Stephen mentioned is a telling one; a number of people in this state, a percentage of people, are members of these organisations, and in dollar terms they're relatively insignificant but in their lifestyles, in the way they see the world they're quite significant, of concern. I think we're just pleading that that be recognised in broad terms.

MR MAITLAND: We might just pick up on the technology side too. If supervisors are adequately resourced in terms of being able to engage the best sort of people and have access to technology, I don't think they need to lead in any way. They can keep pace with the changes as and when they occur, and if technology does have an impact on supervisory aspects of their work, provided they're resourced properly they can keep on top of those things without having to set the pace as it were.

PROF CARMICHAEL: Stephen, on a different tack: payment system. You suggested that all DTIs should have access to the payment system. Are you referring there to access in their own names rather than through a vehicle like they have at the moment, through their special services providers?

MR MAITLAND: There are probably some technical reasons which make it better for them to have access through the special service providers in terms of the number of participants actually in the scheme and its management. However, I would prefer to see that arrived at through, if you like, economic efficiencies rather than prescription. So if someone did want to have direct - - -

PROF CARMICHAEL: A bigger one (indistinct)

MR MAITLAND: - - - access they could, you know, in the way - - -

PROF CARMICHAEL: And to all levels of the payment system?

MR MAITLAND: All appropriate - - -

PROF CARMICHAEL: Well, economically - - -

MR MAITLAND: All appropriate levels, yes.

PROF CARMICHAEL: Yes, okay.

CHAIRMAN: If one could overcome - it's a hypothetical question - the perceived difficulties with deposit insurance, would you see that as having some applicability to your membership rates, given that you're interested in the people rather than the dollars.

MR MAITLAND: Yes. If I can answer that from two points of view. I find it very hard to answer for a whole range of people. I think that the Australian public, given that it might be an erroneous impression at the moment, is happier with the Reserve Bank standing behind banks for example than have some formalised deposit insurance scheme. There might be a suspicion that the insurer might not quite be big enough or whatever.

From the supervisory point of view we would far prefer the existing system where there is - the bank system, which we're looking to extend to others - where it gives a lot of flexibility for the supervisor to manage our problems. The deposit insurance scheme we think would be seen as well, that's the solution, and that's the only solution to a problem - is to pay out on the insurance. And subject to probably confusing levels of caps and individual account balances and all those sort of complications with an insurance scheme, and I think perhaps the mystery of a lender-of-last-resort arrangement would work better and be better accepted, because it is simpler, by the public.

PROF CARMICHAEL: Interestingly as you look around the world there are of course as many different varieties of deposit insurance as there are Campbell soups on the shelves.

MR MAITLAND: Sure.

PROF CARMICHAEL: Like you, I tend to look at the US and say that's a disaster, which it is, but there are also other schemes that work reasonably well. One of the features of those schemes that surprised me a little bit but when I thought about it it was logical, and that was that it does tend to support the smaller institutions. If the deposit insurance scheme runs to a cap, then say credit unions tend to be a very natural base of that kind of security whereas banks of course have got deposits

ranging over big, small, medium. And a number of countries overseas put to us that one of the benefits of their deposit insurance scheme is that it does underwrite the diversity of institutions in the deposit-taking area.

MR MAITLAND: Well, I can see that view.

CHAIRMAN: Bill, you've come in halfway.

MR BEERWORTH: I have slipped through, chairman, I think it appropriate - - -

CHAIRMAN: Okay, then, Bill. Greg?

MR SMITH: I wouldn't mind just exploring a little bit more your references to the lender-of-last-resort facility. In your preferred model of the Reserve Bank's role, is there any change that you had in mind there or is it the one - the system as it actually is today that you've got in mind?

MR MAITLAND: We've actually gone a step further than and thought that that should be a little bit more explicit than it is at the moment. It's quite a vague concept. Explicit, intentionally so.

MR SMITH: In what way?

MR MAITLAND: Well, the straight-up statement that the Reserve Bank will stand behind banks which are suffering a liquidity problem. Again you have to temper that a little so that you don't have profit of managing. But we believe that it can be made more explicit.

MR SMITH: Does that - I want to quite - persist a little on the critical point there, whether or not that applies to any bank or whether it only applies to a solvent bank - it might be having a liquidity difficulty but it's still solvent - or whether you are really saying guarantee? And if you're saying guarantee what are you guaranteeing?

MR MAITLAND: Yes. We're really looking at the liquidity.

MR SMITH: Of solvent banks.

MR MAITLAND: Yes.

PROF CARMICHAEL: Stephen, you made the comment about the legislative changes under the FI scheme being sort of slow to be generous. You're not the only ones that have made that comment; that's come from a number of sources.

MR MAITLAND: Yes.

PROF CARMICHAEL: What are the options in trying to tidy that up? What might be the range of ways you might handle it?

MR MAITLAND: It depends if you start off with an assumption that the FI scheme as you know it would continue. I suppose what we're suggesting in ours is the fact that it wouldn't.

PROF CARMICHAEL: Solve - - -

MR MAITLAND: Yes, some - that solves that problem.

PROF CARMICHAEL: One national legislation, yes.

MR MAITLAND: I don't know, it's probably insoluble in its present form from a legal aspect.

PROF CARMICHAEL: Because of the number of jurisdictions that have to agree.

MR MAITLAND: I think so.

MR PRIOR: It has been proven that it's a start-up problem; it's a problem for (indistinct) it's as simple as that.

CHAIRMAN: I suspect we've covered a fair number of the issues, gentlemen. Is there anything else that you would like to add in conclusion - to be reasonably clear?

MR MAITLAND: No, other than to thank you for the opportunity and to wish you well in your inquiry.

CHAIRMAN: Thank you very much, Stephen. Thanks, Kerry.

MR PRIOR: Thank you.

CHAIRMAN: Our next participant this morning, ladies and gentlemen is Evelyn Meier. Evelyn, I'm sure you heard me make my opening comments but I might just repeat them for the benefit of those who have come in late. This inquiry does have no legal powers, special legal powers or parliamentary privilege, so participants should not make any comments which reflect adversely on particular persons or organisations. We would like you to just simply state your name, the organisation that you're involved with, and then the floor is yours. Make a brief opening statement and we will see where we go to. Thank you.

MS MEIER: My name is Evelyn Meier and I am appearing in a private capacity, so I do not represent any institution or any political interests. I am currently conducting a PhD thesis at the University of Queensland. The thesis looks at the Australian financial system and the role of the state in a comparative context.

My views have been influenced by the work in the banking industry in several overseas countries, an upbringing in Switzerland and a tertiary education in the USA. So there's a bit of a mix here. I have been in Australia for the last 2 years and I'm a resident. I'm intending to stay so whatever you decide here will affect me and my children. My main interest in the FS inquiry is whether greater competition will emerge both in the banking sector and the capital market with the effect of reducing the cost of capital for business. That's my main focus.

The political announcement of regulation - who regulates what and how - is of secondary importance as long as the regulatory framework enables the efficient allocation of capital, competition, innovation and implementation thereof by maintaining confidence in the financial system. I decided to use World Bank data to provide a snapshot of the Australian financial system in an international context. It shows in which area the Australian financial system excels and where it lags behind. The point here was just to have a starting point for assessing the Australian financial system.

The aim of the submission was to determine the development level of the Australian financial system in terms of financial system size, size of the banking and non-bank financial institution sector and the stock market performance and this is set in comparison with major European and Asian countries. The findings show a comparatively strong banking system in terms of size, a less strong system with regards to providing domestic credit to the business sector,

and an under-performing equity market in terms of liquidity and global capital market integration.

These observations are somewhat at odds with a system that can be defined as a market instead of a bank-based system. This distinction, which you are aware of, of a financial system relies on the importance of the two main sources of capital for businesses, banks and/or the capital market. Australian companies use predominantly the capital market as a source of funding. For example, the Australian debt-equity ratio has been the lowest of the major OECD countries in the eighties and is still today one of the - has the lowest debt-equity ratio. This is substantially lower than the one of the USA, Canada or the UK, and of course the Germanic countries have a higher debt ratio.

What are the implications of these findings? The major two effects of an inefficient capital market are (1) company growth could be impeded by a higher cost of capital. Number (2), the international competitiveness of Australia's capital market is suboptimal as larger companies go overseas depriving the capital market of further debt, and this is supported in some of the findings which you have reported in your report. For example, the ratio of company-raising capital domestically versus overseas is 5:1. So that's 6 billion being raised overseas versus 1 billion locally, and I do believe that has a negative impact on the Australian equity market.

CHAIRMAN: And the 1 billion is?

MS MEIER: 1 billion of company-raising is domestic versus 6.1 billion overseas; exact 1.2 billion versus 6.1 billion. That's pointed out in section 5.113 on page 139 in your report. Recommendation: what I recommend is a strong government commitment to strengthen the capital market and an elimination of the factors contributing to misprising which is a measurement of not-perfect cap as a global market integration. This is also in line with some of the recommendations made by IPSA on your section 5.112 of your report.

With regard to domestic banks I strongly support that they shall be exposed to greater foreign competition which hopefully could result in lowering the margins on business lending. Furthermore research should be conducted into why the corporate debt market in Australia is so small. I worked at a limitation of my study, of the submission; it incorporates information only with regard to the secondary market for equities. It does not account for the over-the-counter trades, and hence it does not cover the whole financial

market. It is only looking at the equity side of the financial market. Furthermore I am not a financial market specialist, so do not grill me on technical details.

So the section covers - the sections that are covered actually in the discussion paper, which my submission relates to, are for example in your chapter 5, where you look at the development of efficient and liquid financial markets; the approach of the inquiry and its intent to examine the regulatory framework and its impact on the international competitiveness of Australian financial markets, which is also in chapter 5. And in chapter 9 you cover the policies which restrict Australia's competitiveness in the international financial markets. So a lot of the details which I do not provide in the submission are actually supplied in your discussion paper.

However, before opening the floor for questions, I just would like to say a few words and place the Wallis inquiry into a historical perspective. Being European I cannot refrain from doing that. It's just so nice. This is the fifth inquiry relating to banking and monetary issues in Australia. It's (indistinct) that there are economic cycles in all those inquiry cycles. The previous four were held at astonishingly similar intervals, 45, 47 and 44 years, except the last one; the cycle was short, it's only 17 years since the last financial inquiry.

The first inquiry was in response to an economic crisis, and it was called the Committee on Monetary Confusion, and was appointing New South Wales to inquire into the causes of the recession 1841-1843. The second inquiry was during the boom period. It was called for by the Victorian government in 1887 to inquire into the workings of the business of banking in Victoria. That was the first royal commission. The third one came in the wake of the depression in the thirties, the 1935 royal commission. It was, and I quote there:

> To inquire into the monetary and banking system and to report whether any and, if so, what alterations are desirable in the interests of the people of Australia as a whole -

and of course many of its recommendations became the basis for wartime and post-war legislations relating to the control of banking.

The fourth inquiry, the Campbell inquiry, was in a period where the regulatory system had outgrown its time. The fifth one, the Wallis inquiry, was a response to what? I'm still not quite sure about that. Was it a response to pressure from industry for rationalisation? A dissatisfaction with the regulatory framework? Time will tell.

It was announced at a time of relative economic and political calm, ideal to assess the present system and to formulate a visionary regulatory framework for the next millennium. Thank you.

CHAIRMAN: Thanks, Evelyn. Well, would you like to catch up?

MR BEERWORTH: Thank you. Do you think that the low debt-equity ratio in Australia might reflect managerial conservatism, as opposed to the inability to obtain debt reasonably?

MS MEIER: If you look at how much has been raised overseas, then I would say no. So much more money has been raised overseas than domestically I don't think it could only be due to preference.

MR BEERWORTH: Well, then, let me jump to your last suggestion which is that we should somehow make Australian banks more accessible to competition from foreign banks. If people can very easily raise funds overseas, corporately in particular, why should we not think that foreign banks are competing very strongly with local banks?

MS MEIER: I think what I'm looking at is a sector of small companies. I'm not looking at larger companies.

MR BEERWORTH: No, that's a different issue. You haven't raised that. I agree with that. I think there are two markets. One is for major corporations which can go offshore - - -

MS MEIER: Which can go overseas very easily, yes.

MR BEERWORTH: - - - and one is for Australian corporations, but even there let's keep on the foreign banks. Foreign banks have very strong access to Australia; there's almost no limitation. If a foreign bank wanted to get a banking licence it probably could at this stage; many of the foreign banks don't want an Australian banking licence. How is it that we do, in your view, given your background - how do we encourage the foreign banks to come and compete harder in the Australian context?

MS MEIER: You could - I mean, one thing, yes, of course - the limitation in the retail sector in which there is an issue of name recognition for even small to medium-sized companies. I mean, there might be a hesitation for banking with a foreign bank if you do not have otherwise any contact.

MR BEERWORTH: Well, let me take a specific example. BT Australia is a foreign bank. It has a banking licence which it doesn't use in the way that you would like it to use it. How can we persuade BT, which is a very large foreign bank, very successful in Australia, but not doing the

very sorts of things you would like it to do - how do we encourage BT to do it, or rather, why doesn't BT do it now?

MS MEIER: I have no answer to that question.

MR BEERWORTH: It's a general question.

MS MEIER: Yes, I would have no answer.

MR BEERWORTH: Because there's certainly a problem obviously for medium to smaller companies borrowing in this country relative to larger companies being able to go offshore very easily.

MS MEIER: That's correct, yes. So I don't know how BT's approach is to the small to medium company sector. I wouldn't know.

MR BEERWORTH: And I don't mean to pick on BT. Please don't misunderstand.

MS MEIER: Yes. Any foreign bank, yes.

MR BEERWORTH: There are many other foreign banks that have licences but don't lend into that small corporate market.

CHAIRMAN: Evelyn, if you had to leave us with two or three very significant things in your mind that we could effect in terms of change to address your concerns, what would they be?

MS MEIER: I think one would be the whole aspect of prospectus requirements.

CHAIRMAN: What, in terms of simplification?

MS MEIER: Simplification and also when one looks at the cost which has been pointed out in the report, they seem to be substantial for a company to have - to list on the Australian Stock Exchange. There is this whole confusion about taxation which again was very well illuminated in your report. I think there is just that - - -

CHAIRMAN: Confusion?

MS MEIER: Yes, there is a lot of different tax rules based on different state levels.

CHAIRMAN: Sure.

MS MEIER: So you can try to minimise your costs by going around and really try to find where is the lowest tax regime.

CHAIRMAN: Well, I remind everyone that this committee has no mandate to make any recommendations about tax - - -

MS MEIER: I'm aware of that.

CHAIRMAN: - - - but we are certainly making observations.

PROF CARMICHAEL: Evelyn, just a question on your material here. I had a lot of trouble trying to work out what it all meant. I didn't know how you had adjusted for exchange rates, how you had adjusted for the

business cycle in some of these growth figures, and you have got indexes that sort of aggregate across three or four different measures and for most of them I sort of thought you grab a batch of eight countries and Australia sits number 3 or 4. On most measures that didn't seem to me to say very much. But the one that did stand out - and that's a long way of getting to it - was your figure 4, which is the mispricing one. I wonder whether you would mind just telling us a bit about that so I can understand how you have measured the mispricing, because that's the only one where Australia really seems to have a message in here.

CHAIRMAN: Explain for the audience just what we're addressing.

MR BEERWORTH: What is mispricing, yes.

MS MEIER: Yes. Well, first of all, what we are addressing in regards to what I have done - these are, as I say, data which have been compiled by researchers at the World Bank and the issue was really to provide a picture, and this is data from 1988 to 1993. It's an aggregate data. They have all been adjusted for different inflation and they have been translated with regards to currencies, exchange rates and - - -

PROF CARMICHAEL: They are all in a common currency, are they?

MS MEIER: They're all in common currency.

PROF CARMICHAEL: Some of these moves could be totally dominated by exchange rate movements?

MS MEIER: No, they have been all adjusted, and they have also been adjusted - all these measures are adjusted for (indistinct) because as you know it's very hard to provide any comparative figures that make some more sense, because of the issues which you have raised.

PROF CARMICHAEL: Okay. This mispricing one, what do we read into that? What does it mean? What is your measure of mispricing?

MS MEIER: What they call mispricing is at a level of capital market integration. Where are there some variations? Where are there some cost inefficiencies? There have been several aspects of - there is a conglomerate index and they did look at the capital as a pricing model for domestic prices, adjusted it with an international component, and they also looked at the arbitrage pricing model.

PROF CARMICHAEL: Okay, so do I read into that graph that Australia has a permanent risk premium? Is that the implication, on average?

MS MEIER: It seems to be that the prices for domestic equity here seem to be higher than if you would go overseas.

PROF CARMICHAEL: Okay.

MS MEIER: And that is some of the factors that might also explain that it might be cheaper, given the market, for Australian companies to go overseas to raise capital. Some feed into that the equity market here is not very liquid.

PROF CARMICHAEL: Given that you see that same sort of premium in our interest rates and given that a lot of people relate that say to a currency risk, would that not seem to be internally consistent; that our debt rates and our equity rates all carry a premium associated with being a volatile currency perhaps?

MS MEIER: Not necessarily because if that would be out of line with international ways then my question is why is - why 32 per cent of the equity holders in Australia are foreigners. That is maybe a perceived - there's a couple of factors which play into it, and a relatively undiversified equity market here because of the resource sectors. We don't have the normal distribution of service companies listed on the stock market, etcetera. Of course this is being addressed now with greater privatisations. So we're seeing the composition of the Australian equity market is in a way an index of resource stocks. So you wouldn't really have to buy individual resource stocks, you can just buy an index fraction of the Australian stock market which then gives you actually an investment into resource stocks - because I think it's about 40 per cent versus 20 internationally.

PROF CARMICHAEL: Yes. My question is simpler than that. It's is it necessarily mispricing to have a risk premium on Australia, given the history that we have had both in debt and apparently in equity? It may well be that the world's assessment of us - and in fact the comment that there are 33 per cent foreign investors in here is actually consistent with that sort of framework.

MS MEIER: Yes. I wouldn't know. I would have to look more into that.

PROF CARMICHAEL: Okay.

MR SMITH: I guess my question would have been along similar lines, but with a different angle, and that is you made the point yourself about the dominance of resource stocks on the Australian index. Do you control this for compositional differences between countries? Because if you control for compositional differences maybe the difference in the cost of capital is merely reflecting the different volatility

of earnings of our corporates, compared to the volatility of earnings of industrial companies on other forces. Is that a reasonable - - -

MS MEIER: It is more control for it, number one, and how would then this relate to the cost of equity?

MR SMITH: Well, then, possibly the cost of equity isn't as different as it appears at first. After all, the cost of equity is going to be some type of - either the capital asset pricing model or whatever model. It's going to be affected by the underlying risk of the sectors in which you are structuring your index, and if the Australia index is essentially a high-risk index, not because of anything - I mean, Mr Carmichael has made the point about whether or not there is a country risk in Australia, which is one issue, but the other aspect is of course that we do have a very volatile resource sector. I mean, all resource sectors are volatile. So maybe the measure is simply revealing the structural features of the Australian laws rather than any international failing.

MS MEIER: That could very well be, yes, because (indistinct) is relatively high given the composition.

MR SMITH: I was alerted to that also looking at your - I mean, the two countries that had a - on your index, your composite index, the two countries that had a lower score than Australia were Canada and France, which didn't strike me as countries that were, you know, radically underperforming in any particular way, and so I was sort of concerned that maybe your composite indexes don't correlate all that neatly with economic performance.

MR BEERWORTH: A large proportion of Canadian stocks are reserve stocks; just under a third, I think.

MR SMITH: Yes, they're not as high as Australia.

MS MEIER: Not quite, yes.

MR SMITH: But again, not reflected then in economic performance - another country - so the significance of the index to economic performance, which I think is essential to your thesis, I began to wonder whether the correlation was so clear.

MS MEIER: They have not followed that up with any more detailed studies because I think ultimately - but look at the other submissions which were supplied to you. There are similar issues raised from a different angle - and because also what it does incorporate is the cost of transactions for example, which seems to be relatively high here compared with other stock exchanges, and especially the issue is of - Australia cannot afford really to lag further

behind because otherwise of being excluded from international research with regards to other institutional investors there to invest, and of course we are competing now with the Asian sector as well, so I think the main thrust of my submission was to alert to the fact something has to be done.

If we look at also the media reporting and support of the Wallis inquiry, the focus is always banks and what my submission shows is the banking sector performs very well internationally, and also if you look at several other studies with regards to input inefficiencies, and output inefficiencies, Australian banks rank very high. So maybe - you know, they're doing very well, we have to say that. Then maybe the focus has to shift more towards the other areas of financial systems.

CHAIRMAN: We are very mindful of the issues you're raising and certainly a clear focus for the committee and you can see the way we organise a discussion paper is to bring out these issues in terms of the competitiveness and efficiency of the Australian financial market. So your submission is very timely and appropriate to our deliberations. Thank you very much, Evelyn.

CHAIRMAN: The next participant this morning is Fiona Guthrie from the Queensland Consumers Association. Fiona? You have heard my introductions, have you not?

MS GUTHRIE: No, I'm afraid I haven't, I'm sorry.

CHAIRMAN: You haven't. Well, I might just repeat them for the record then, but you need to understand that these are public consultations and the discussions will be recorded and transcripts made publicly available. We have no special legal powers or parliamentary privilege so you certainly shouldn't make any comments which reflect adversely in any way. We would ask you to start by, just purely for voice recognition purposes, stating your name and the organisation you represent, and we would be very pleased to hear your remarks.

MS GUTHRIE: Thank you, Mr Wallis. My name is Fiona Guthrie. I'm from the Queensland Consumers Association. I apologise on behalf of Paul O'Shea from Financial Counselling Services whose spot I have taken. Paul wasn't able to appear at the last minute, so I guess that means that I haven't had as much time as I would have liked to prepare either.

By way of an opening I might tell you that this morning it was my daughter's last day at pre-school and I spent the morning cleaning the puzzles and disinfecting them, and I'm telling you that because I'm trying to point out that consumer groups and consumer reps are by and large fairly badly resourced.

My group, the Queensland Consumers Association, is a group who have a number of other smaller groups such as Brisbane Consumers and Rockhampton and Logan, and we're all volunteers. We don't have the resources that industry has, and my point is that essentially you will get a pretty good picture of industry's view of regulation and how it should be developing, but I think it's going to be difficult to get as good a view from the consumer movement for those sort of reasons.

Apart from the Consumer Law Centres and the Legal Aid Offices you're not probably going to get the chance to talk to people in the street. You're shuffling in your seat as I say that.

MR BEERWORTH: I cut sandwiches for three young men this morning and got them breakfast.

MS GUTHRIE: Well, you know what I mean, don't you?

MR BEERWORTH: That's before I left Sydney.

CHAIRMAN: And we actually have spent a lot of time talking to consumer organisations.

MS GUTHRIE: Yes, I appreciate that.

CHAIRMAN: In Australia and overseas - so we have endeavoured from our point of view to get as close as we can to the action.

MS GUTHRIE: Yes, I understand that. I just thought it was worth pointing out because it's a problem that we have across the gamut of issues because we're often asked to comment on issues, and it is very difficult to just get the time to do it, to write a submission and do any scheduling.

CHAIRMAN: What's your involvement in the association?

MS GUTHRIE: I'm an exec member of Queensland Consumers Association and I was elected to the executive of the Consumers Federation of Australia just a couple of months ago, and Mr Prosser has just appointed me to his advisory body in Canberra, so that will be interesting to see how that goes.

The other thing I wanted to say is that I think the consumer movement has probably not been as smart as it should have in some of the ways we have responded to the issues of financial deregulation in the sense of making statements which are not as sensible as they should be; for example, looking at the global level of bank profits and not understanding what they were - that's irrelevant. It's only relevant to the return on issue holders' funds and at the risk of being excommunicated I thought that was worth pointing out, and I think there are problems on both sides.

But clearly business and consumer groups have got to speak closely because they exist because we exist, and we're two sides of the same coin. So given that we're two sides of the same coin, it means that we have got to get the balance right between the two groups. So often our interests are the same, but there are times when our interests are different.

The next point I wanted to make was just quickly, as a consumer rep I often feel that I can't possibly speak for every consumer - that would just be not only arrogant but it's impossible to do that. But I can tell you - and this won't be a surprise to you - that the view of the people on the street about the financial industry is that they're very sceptical about the big banks in particular. They see them still as unresponsive; as not on their side, I suppose. Now, that

perception has not come out of nowhere. That has developed over the years. I think 30 years ago - I remember my parents talking about their bank manager with almost reverence, and that doesn't happen any more.

I think the other view - and this won't be a surprise to you either - is that we look to governments to provide regulation and we certainly know that there is a view in the community that the government provides a guarantee for bank deposits, and of course that's not the case. But that's certainly the way the community views it, and even that extends to building societies and Rothwells, and people are just amazed that, you know, the link between risk and return is not really understood very well in the community.

CHAIRMAN: Do you think we should clarify that?

MS GUTHRIE: I think it would be really difficult to clarify. I mean, the education campaign to overcome that would be absolutely enormous. I'm not sure that you should. I mean, I don't know that there isn't a role. It's almost fundamental that we have to have some confidence in the banking industry. I think it's a really difficult issue, and I know that's one that you've been grappling with. But how you would clarify that I don't know. People are not particularly interested in those sort of things unless they're about to lose money. Often I find with consumer education, "What's the point of doing another pamphlet or another video if it's not relevant to me?" It's just basic marketing.

So given this sort of symbiotic relationship between industry and consumers, which we have got to obviously realise, I was a bit surprised to see in the report the focus on the Consumer Credit Code. We were quite concerned that there are moves to water that down when it has just been introduced. I guess I would be saying to you please let it run its course and let it go through its review and see how it pans out rather than listen to very strong industry voices jumping up and down about it now. I've read those parts of the report and I haven't had time to get through it all, but I did think their arguments were - I thought they could be defended fairly easily.

The other point I wanted to make is that we have consistently maintained, as a consumer movement, that access to banking is really important. Now, I appreciate that that's not costless, that providing services to people in remote areas and to low-income people with lots of transactions is not costless, but on the other hand we have always maintained that access to banking is a bit like access to

affordable and secure housing. It's one of those things that you need to function in society.

I haven't even talked about capital asset pricing yet, and I'm not going to. The last thing I was going to say is just a couple of case studies about how regulation has helped, and these are things that I'm aware of and have come to me through my voluntary involvement with the financial counselling movement or my contact with legal centres.

There was a case I heard about yesterday where there's a number of people living in a mobile home park at Burpengary which is a northern suburb of Brisbane, and none of them drive and they're pensioners, and in the past they have been able to get a ride off to the bank to withdraw the money to pay their rent to the mobile home owner - caravan park owner. Now they're now longer able to do that and they're looking at having to pay a bank debit of $5 for every transaction. Now, that's not significant probably to you and it's probably not significant to me but it's significant when you're a pensioner. They're the sort of things I suppose that are trying to reinforce this idea about - if we have a completely unfettered market those sort of people would possibly be paying even more.

We see a lot in financial counselling - very, very young people going bankrupt. It's a tragedy. They go into the car dealership and they're sold finance that they don't need through smart sales tactics, through grabbing the highest income slip they've recently had and working out their repayments on that and a couple of months later they lose their job for some reason - they have an accident - and they're bankrupt. It's not uncommon.

Regulation has helped us in some ways, trying to stamp out those practices, certainly through the linked credit provider provisions of the old Credit Act and now the Credit Code and - this is not within your terms of reference but within Queensland, one of the reasons we've been trying to push for a cooling-off period in those sort of transactions.

The last one is one that came to my attention again through financial counsellors, where car dealers and financiers are trying avoid regulation - and this is why we need it; to try and stamp out these practices - by saying, "You can buy a car interest-free; it won't cost you anything." The car's only worth $2000 but all the documentation shows is it's worth five or something like that, so they're

trying to avoid it that way. So you have equal monthly repayments so it looks as if you're not paying any interest but of course it's a shonk, and we've got some chance of trying to turn those things over and stop that happening when we've got some regulation in place.

The current flavour, I guess, at the moment is a deregulatory environment, that somehow market forces are always going to deliver fair outcomes. Market forces deliver competition. They don't always deliver justice. That's one of our fundamental concerns. I think we should not lose sight of the fact that a lot of consumer protection regulation was in response to rorts, to rip-offs and to problems and it's probably been quite effective in stamping them out.

We look at it and see those things are no longer around and say, "Why do we need deregulation?" We're forgetting why it started in the first place. That's where I'm finishing and the last thing I was going to say was I hope you have a nice time in Brisbane.

CHAIRMAN: Thank you very much. You've made some very relevant comments about the system and the ordinary consumer. I guess what you're saying is there has been progress.

MS GUTHRIE: Yes.

CHAIRMAN: We don't want to see anything go backwards, but do you have some specifics for us that we can get our minds around in terms of the way forward?

MS GUTHRIE: Yes. I'm acutely conscious that I have broken the first commandment for policy development, which is to come and talk about problems and not really suggest to you some solutions. Mr Wallis, I apologise for that.

CHAIRMAN: That's okay. This is a very informal discussion.

MS GUTHRIE: Yes, but I know that and I was aware of that and I think it's a good question. It would seem to me that in terms of regulation the finance sector is subject to myriad different forms and it would just be very sensible and commonsense to try and bring them under one sort of umbrella.

CHAIRMAN: So you would like to see a national approach to that?

MS GUTHRIE: I think a national approach is very sensible. I don't have any problems with the banks' arguments about that in terms of the Credit Code. That's a personal view. I don't know whether the consumer movement has - - -

CHAIRMAN: You would support a move towards a nationally focused system of consumer regulation?

MS GUTHRIE: I think that's got a lot of benefits for consumers and obviously for industry.

CHAIRMAN: Okay.

MR BEERWORTH: I don't think on that score you should be concerned that we want to take things backwards. I think most people have very much in common these days with their views about the objectives of consumer credit legislation in particular. I think the main debate is whether or not it ought to be federalised or if it's worth trying to federalise it.

MS GUTHRIE: Good, okay.

MR BEERWORTH: Well, that is a debate, but the states of course have been involved for 13 years, putting a code out, so to take your point, there's a lot to be said for just letting it sit for a while and see what comes up.

MS GUTHRIE: Yes.

MR BEERWORTH: But we're obviously interested, as Mr Wallis says, in getting community views on this one.

MS GUTHRIE: Yes, good, I'm pleased to hear you say that.

PROF CARMICHAEL: Some of the messages that have been coming through to us though, Fiona, on the Uniform Credit Code are, number one, that it is so complex that the banks, for example, are having to put together mortgage documentation that's sort of an inch and a half thick. Now, I'm not going to read a document an inch and a half thick. I wonder how somebody who has no background at all in finance is going to handle that sort of a document.

The uncertainties in it have tended to push to a level where it's not achieving what it was intended to achieve. Now, there may be ways that that can be simplified, for example, without losing the plot. We certainly don't get the message that any of the institutions want to avoid their responsibilities. What's driving the heavy documentation is around the edges, all the penalties that don't seem to be, for example, related to the breach - that they have to make sure they're protected in a court of law. So you end up with lawyers getting rich and big fat documents. That's the main complaint we tend to hear with that.

MS GUTHRIE: I agree with that.

CHAIRMAN: It was said to us by one of the major mortgage providers, housing contractors - those 60 pages - by the time you do copies, 300 pages for a simple house mortgage.

MS GUTHRIE: That seems to me a finetuning sort of aspect rather than a fundamental criticism of legislation.

MR BEERWORTH: It's a very important one. It goes beyond - - -

MS GUTHRIE: But it is and I think it's true. I mean, you've got to be able to produce stuff that people can understand. I tend to think the penalties argument is a bit specious in the sense of ultimately that's a discretion of the courts, and large civil penalties - - -

CHAIRMAN: Yes, sure.

MS GUTHRIE: They have acted as very effective deterrents.

CHAIRMAN: But have the penalties perhaps been out of all proportion to the cost?

MS GUTHRIE: Yes, yes, I mean - - -

CHAIRMAN: You don't accept the banks have an argument in that respect?

MS GUTHRIE: Look, I can't - I'm not an expert on the code.

CHAIRMAN: Their basic proposition is that the penalties that can be awarded could be 10 times the cost that's involved in whatever the transgression is, and some of those transgressions are administrative - you know, it's very difficult - - -

MR BEERWORTH: They're technical or inadvertent, some of them.

MS GUTHRIE: Yes. Well, I would have thought that - I think there's a great deterrent effect in having penalties that really bite, so that people comply, because we know that there's a tendency not to comply otherwise.

CHAIRMAN: It focuses the mind.

MS GUTHRIE: That certainly does, but secondly, because it's up to the court and they have discretion over the penalties that they award, if they think that the breach is technical, then surely they'll award a smaller penalty which fits the crime, so to speak, but if it's serious - - -

CHAIRMAN: I wished I shared your confidence. If you're a big bank, you're a good target.

MS GUTHRIE: If you're a big bank you're a good target, yes, but some of the cases - the banks have had fairly serious and repeated breaches of the - - -

CHAIRMAN: Can I ask a very generalised question? As we've gone around in this country and overseas, one does certainly detect

from the consumer movements that all this extra information that's being pushed out is actually not helping. It's not achieving the end result that a lot of people were hopeful it would. From your constituency do you think all this vast amount of information that's now available - insurance and housing contracts - is it helping? For my own part I'll read a four-page document. I don't read 60 pages.

MS GUTHRIE: I'll answer that in two ways, I think. I think it helps if you have a dispute, so that you have things clearly spelled out. That's when people need to know that they're there and they think, "Gosh, I wish I got that in the first place." Secondly, I'm a big believer - if you can avoid it - in using a big stick if you can; that really if you want to get people to change their behaviour you try and not use the law. You try and do it through education and by culture of compliance and through different methods. So there's room there for certainly having that information but - - -

CHAIRMAN: Do you think we've made progress in terms of the basic purpose of that information disclosure, to make the consumer - - -

MS GUTHRIE: I think we could get smarter about how we market some of this stuff. For example, one of the big insurance companies has just released what they call their service guarantee. It's actually a marketing tool. It's what I'd call a consumer charter that sets out how they should behave. You know, if I was a big bank I'd be saying, "Look what we're doing for you. We're making sure you understand. Here's your big mortgage document but here's the main points" - something like that and really say - - -

CHAIRMAN: Have you had any exposure to the banking ombudsman system?

MS GUTHRIE: No, I haven't. I haven't personally, no. The consumer movement is fairly happy generally with the way that scheme seems to be working though.

MR SMITH: Do you, in your experience, find that the areas that cause the most trouble are the areas where dispute resolution schemes are not in place?

MS GUTHRIE: Yes. For example the finance companies - the Avcos and the HFCs - by and large for a number of reasons they're dealing with, as you know, higher risks so they have higher defaults.

CHAIRMAN: But the banking schemes are working reasonably well?

MS GUTHRIE: The banking schemes seem to be working pretty well. I think to their credit, for example, the insurance industry is starting to come on board with trying to improve the way they're operating as well. I have concerns about, for example, the way financial planners have developed over the years and the way that scheme might be working but, you know, access to dispute resolution is just vital and one entry criterion. I think that's one of the things other people are going to push, but there's a plethora of schemes and that's just confusing for anybody.

CHAIRMAN: They're very good points.

PROF CARMICHAEL: I was just going to make one comment, Fiona. On your access to banking services in rural areas and to low-income people, we don't sort of take a position against that at all. The question that we raised in the discussion paper was who pays? And when people are hungry we don't ask the government to force Arnotts to give them free biscuits; it's provided through the government process, and if you want to have an efficient sector, whether it's banking or biscuit manufacturing or whatever, you tend to let the sector run and then pick up the social needs through the social system, which includes the budget. We just made the comment in the discussion paper that it's better to put those, in a sense, where they belong, not to argue that they don't have a place.

MS GUTHRIE: Make a more transparent process.

PROF CARMICHAEL: That's right.

MS GUTHRIE: I mean, you're right, and in some ways you're wrong, I think, because it doesn't get done. No-one's going to do it.

MR BEERWORTH: But I think it accounts for his comment where you've said that the market might be efficient but that doesn't give you justice. I think that's right. I think Jeff just says that it's better to try and do them in different segments if you can.

CHAIRMAN: Fiona, I think you've made your points extremely well for a last-minute presentation. Thank you.

MS GUTHRIE: Thank you for the time.

CHAIRMAN: Thank you very much.

MS GUTHRIE: Paul would have talked to you a lot more about the Credit Code, so you'll just have to pretend you got more about the Credit Code.

CHAIRMAN: Well, I can assure you Mr Beerworth did make the sandwiches then.

MR BEERWORTH: We'll pretend we got more about the Credit Code.

MS GUTHRIE: Okay, thank you.

CHAIRMAN: Thank you very much.

CHAIRMAN: Our next participant is Austin Donnelly from the Australian Investors Association. Austin, thank you for joining us this morning.

MR DONNELLY: My pleasure.

CHAIRMAN: I'm sure you've heard all my earlier remarks, so if you'd care to start off by simply stating your name and the background to your organisation, we'd be very pleased to hear from you.

MR DONNELLY: My name is Austin Donnelly and the submission I made was actually on my behalf and of the association. The association was founded by me 5 years ago and my submission is also based on my 42 years' investment experience. On the principle of first things first our comments are directed to bread-and-butter issues as distinct from the big ticket items to which the discussion paper and most recent media attention has been focused.

In making a point at the peace conference after the end of World War I, the Australian Prime Minister, William Morris Hughes, said, "I speak for 60,000 Australian dead." Today I speak for far more than 60,000 Australians who are financially dead or seriously injured. They are the victims of what must be the greatest regulatory failure of the century, namely the failure of the ASC, the ISC and their predecessors to enforce the law relating to the disclosure of material information about investments.

Before commenting on some specific issues, may I compliment the committee and staff on their achievement in considering such a large number of submissions in the production of their discussion paper in such a relatively short period. As there are frequent references in the discussion paper to the need for disclosure, it is extremely surprising and disappointing that in the 450 pages I could not find one reference to the submission on this subject by the voice of the investing public, the AIA, yet there are frequent references to the views of organisations, many of whose members are the beneficiaries of the present culture of concealment.

What makes this submission even more surprising is the fact that the AIA submission included an example of how material information about risk is being adequately disclosed, namely the extract from the prospectus of one of the funds of the Vanguard investment group, which is the second-largest mutual fund manager in the United States, with 274 billion under management. See page 19 of the AIA submission. As for the Treasury concern on costs, better disclosure

generally does not involve extra costs. In most cases, as the Vanguard example referred to above shows, it is simply a matter of including a few paragraphs of factual material.

For the regulators in their surveillance activities it is a matter of a little less attention to matters of form such as registers, compliance manuals, etcetera, and a little more attention to the disclosure of the unattractive truths to which the court referred in the Thannhauser v Westpac case, which I discuss in exhibit 1. To put it in good old Australian parlance, investors are not getting a fair go from the regulators. Unfortunately the regulators have drifted unwittingly into being an advocate for industry interests. I say "unwittingly" rather like the business executive who said, "Ours is a non-profit organisation. We didn't plan it that way. That's just how it worked out."

One proof of that situation is a letter from the ASC which stated that because the unlisted property trusts were popular at the time, no action would be taken on a complaint by an investor who lost about 70 per cent of his capital because a prominent adviser did not disclose material information about risk, and their failure in recent years to take action on a very large number of similar cases.

The bulk of the AIA submission, in my submission, relates to the urgent need for proper enforcement of the law but it also includes some suggestions for changing the law to achieve these objects:

(1) more democratic election of company directors by cumulative voting;
(2) ensuring that auditors of listed companies are truly independent;
(3) giving the regulators power to issue, cease and desist orders; and
(4) ensuring adequate representation of consumers on the committee advising the Attorney-General on Corporations Law.

There is insufficient time to discuss these matters but I would be happy to answer any questions on them from committee members. I now turn to exhibits 1 to 7, which spell out details of important matters relating to the subject I'm addressing. Exhibit 1 under the heading What the Courts Have Said About Disclosing the Full Extent of Risk, in the Thannhauser v Westpac Banking Corporation, the judgment in a claim for recovery of losses on foreign currency borrowing due to non-disclosure of the full extent of risk includes this wording:

What he -

referring to the bank executive -

> What he said was calculated to keep from the prospective borrower's mind these unattractive truths. The point could have been easily illustrated by taking examples of the results which could have been obtained by 5-year borrowers since the Swiss float such as those worked out by Mr Donnelly.

The example referred to in the judgment was my illustration tendered in evidence to indicate the worst result on the basis of past experience, which could occur on a 5-year borrowing. It showed that for each dollar borrowed the borrower, as a result of currency changes, had to pay back 5 years later almost $2.50. In exhibit 2 we look at another currency case, Chiarabaglio v Westpac Banking Corporation in which the judgment includes this wording:

> I am satisfied that the presentation led to a reasonable perception on the part of the audience that whereas fluctuations would occur, they would basically be of an even nature along a horizontal axis.

It goes on:

> No picture was given of the type of sharp decline without recovery to a lower level of valuation of the Australian dollar against the yen, such as had occurred in the not-distant past. A reasonably competent adviser would and should have pointed these matters out. Again, in my view, the introduction of serious risk into the picture would have turned Mr Chiarabaglio away from any interest in the suggested offshore borrowing.

The third exhibit refers to the Rogers v Whitaker Full Court of the High Court case in November 1992. Though this case related to a medical matter, the wording of the judgment in relation to risk and generally accepted practices in a profession or industry are relevant in other areas including investment advice. The following points are significant:

(1) In relation to the disclosure of risk, even if the probability of the adverse event occurring is very low, there is a duty to disclose it.

(2) Having acted in a profession or a business in accordance with generally accepted practices in that profession or industry is not necessarily a good defence to a claim in relation to meeting a duty of care.

In connection with the latter point, it is extremely disappointing that it has been ignored by the ASC:

(1) in refusing an AIA request to amend a practice note; and

(2) in not taking action against a large number of advisers who have consistently failed to disclose unattractive results.

From those judgments it's quite common that specific details of the full extent of the risk must be shown. In exhibit 4, I quote a few examples, and namely that's:

> In relation to shares and equity trusts there is a need for prospectuses and recommendations of advisers to disclose unattractive truths such as capital losses up to 40 per cent or more, with recovery taking up to 10 years, a wide variation in prices and periods of up to 15 years in which there has been no sustained net gain.

Exhibit 5 gives an illustration of a sample of the failure of an adviser to disclose material information. Set out below is a copy of the whole of the comment on share market investments in a recent report to an investor by a large advisory organisation which, like the vast majority of advisers, depends on commission for its income, and I quote:

> We recommend equity trusts and direct shares because of the long-term benefits of investments in shares. Shares provide high returns and significant tax advantages from dividend imputation. They are one of only two assets which provide protection against inflation through growth in income and capital. Equity trusts and direct shares provide investors with a diversified conservative portfolio of blue-chip Australian companies. An attractive feature of Australian shares is franked income which receives favourable tax treatment.

It is clear that the above comment is basically sales talk for equity trusts on which the advisers earn about eight times as much commission as on fixed interest investments. In particular:

(1) It is similar to the practice criticised in the court in Thannhauser v Westpac of keeping from the mind of the client unattractive truths.

(2) It fails to disclose material information on a number of matters referred to in exhibit 4.

(3) There is a complete absence of any reference to risk.

The above wording, which would be part of the standard wording of the organisation which has a large number of advisers - some hundreds, I believe - working for it, and similar sales talk in reports of most of the 36,000 people now legally able to offer advice, means that sales talk of that type, rather than advice, is constantly being given to a large number of people.

It demonstrated that there was no truth, no truth at all, in claims by the industry and the ASC that standards have improved. Exhibit 6 refers to action by investors to recover losses due to non-disclosure. In many cases in which I have been involved, either as an expert witness or as a negotiator, there has been a 100 per cent success rate in achieving satisfactory out-of-court settlements. The parties against whom the claims were made who agreed to settlement include banks, financial institutions and some prominent advisers in various states. In very case the basic issue was the failure of the adviser to disclose material information about were described in Thannhauser v Westpac Banking Corporation as unattractive truths.

It is very significant that many of the parties who agreed to settlement were financially strong institutions with ample funds to finance legal expenses. The fact that none of them were prepared to go to court indicates that after initially claiming they were not responsible for losses because their non-disclosure was common practice once their minds were concentrated by pending court action, they saw the validity of the need for disclosure.

Finally in exhibit 7, the position of various parties on the disclosure of the type of information I have been discussing, could be summed up as follows: the parties who believe that it must be disclosed are (1) federal parliament which made the law; (2) the Full Court of the High Court of Australia; (3) the Federal Court of Australia; (4) the voice of the investing public, the AIA; (5) the Australian Consumers Association; (6) other consumer organisations on the National Investor Liaising Committee; (7) tens of thousands of victims of concealment; (8) professional advisers who do not derive commission income and (9) a number of other advisers, banks and institutions who agreed to the need for disclosure by out-of-court settlements.

On the other hand the parties who are in favour of concealment are: (1) the beneficiaries of the concealment, namely many advisers and fund managers who have not yet faced the moment of truth, ie those whose clients have not yet been concentrated by imminent court hearings and actions by investors for recovery of losses due to non-disclosure. The only other party in that side of the debate are the regulators who have the responsibility of enforcing the law. Surely it must be time for the regulators to come in from the cold.

Finally in conclusion, Mr Chairman, personally it gives me no great joy to have to put so much time and effort into the

unceasing battle the AIA and I have fought to get a fair go for investors. Edmund Burke's statement about 200 years ago that for evil to triumph all it needed is for good people to remain silent is just as true today; indeed even more so when the financial rewards for remaining silent are so great. While a number of other issues raised in the discussion paper are important, nothing is more essential to the integrity of capital markets than the essential requirement for the investing public to have reliable information on material matters including the unattractive truths.

No civilised society should tolerate the present situation in which a culture of concealment, officially sanctioned and encouraged by the regulators, enriches investment industry people and impoverishes the investing public; indeed, it makes them the powerless vassals in a latter-day financial feudal system. The remedy is neither complex nor costly; it is just a matter of will. All that is needed is for the government of the day to ensure by a ministerial direction to the regulators, if necessary, that the regulators enforce the law. Because of its overriding importance in the operation of capital markets and the allocation of resources as well as from the viewpoint of adequate consumer protection, the AIA and the investing public hope that this will be one of the first and most emphatic recommendations of the Financial Systems Inquiry. Thank you, Mr Chairman, for the opportunity to present these views, and best wishes for your further efforts.

CHAIRMAN: Thank you, very much, Mr Donnelly. Could you say a little bit about how you see prospectus development has gone in the last 4 or 5 years. Have we made any progress?

MR DONNELLY: I don't think so. I would say that in my view of the hundred of prospectuses out there right now, particularly relating to the - well, most of them relate to mainly equity funds as distinct from new issues - I would doubt very much whether there is one of them which complies with the law. In my view there is not one. I'm not a lawyer but I have had this confirmed by lawyers.

CHAIRMAN: Can you be a bit more specific?

MR DONNELLY: Well, the law states you must disclose material information. Now, I don't think there is any argument that material information relating to the share market includes in addition to all the good things about the share market, good long-term return prospects of capital gain, tax benefits and so on.

In addition to them, the fact that there are slumps which can cause losses of - in the case of the leaders in the 1974 slump

a loss of 75 per cent, and the rest of the market 45 per cent, and up to 10 years for recovery of those slumps, but there have been periods of 15 years for the All Ordinaries Index and 23 years for the All Mining Index in which there has been no net-sustained gain.

The fact that there is a very wide variation in results over 5-year periods, you can have a capital gain - all of those facts - nobody I think can reasonably deny that they are not material because, as the courts have confirmed in considering risk, you must know what's the worst possible result if things - if - - -

CHAIRMAN: If I'm a corporate issuing a prospectus these days, there seems to be very stringent requirements in terms of disclosing historical information. You're looking for something further, are you, from - - -

MR DONNELLY: If you have a look at any of the prospectuses for - if I could for the present concentrate on the equity funds which is a far greater - in total investments - - -

CHAIRMAN: All right, I was actually trying to get to that point.

MR DONNELLY: Okay.

CHAIRMAN: So that's really what we're dealing with, is it?

MR DONNELLY: Well, if you wish I can make a comment on the other type of effect. I believe in the other type of effect there has been some improvement but still some way to go. There is some disclosure of risk there but not sufficient about market risk. In the equity funds and in the investment bonds and so on, all those managed funds, in most of them there is not one word about risk.

If those prospectuses were right, and if the advisers normally echoed just what's in the prospectus - because they're mostly the advisers - unfortunately 99.5, and I kid you not - 99.5 per cent derive all or most of their income from commissions, done on the principle of, "He who pays the piper calls the tune," with due respect to a number of financial advisers who are good people. The plain fact of the matter is they tend to see themselves, at least subconsciously, as the marketing arm of the fund managers, of selling financial products rather than giving objective advice, as that example showed. So they just trot out all the good things.

One of the Macquarie equity people recently took some steps in the right direction by disclosing graphs and talking about risk but in my view, if action was taken under the Trade Practices Act,

against any one of the most prestigious institutions in Australia in issuing these prospectuses, they would be in real trouble.

CHAIRMAN: Should we do something about the way commissions are paid and advisers are remunerated?

MR DONNELLY: Yes, I think one thing that could be done - right now they have to disclose the information but I believe they should disclose what I call the relative commission. Disclosing the fact that we get 4 per cent commission on your investments is fine up to a point, or even if they disclose the amount.

Let me give you an example. Suppose a couple had $300,000 on retirement - and you don't have to be the manager of the biggest company in Australia to retire on that today - and I might say this problem is far worse in Australia because to the best of my knowledge Australia is the only country in the world - well, our sort of world - where most people retire on lump sums. In nearly every other country they retire on pensions and so it's a bigger problem.

If you have $300,000 to invest you approach an investor and if he does the job properly, if he's working on a fee basis and doesn't have any conflict of interest - the basis I worked on until I went into semi-retirement a couple of years ago which now means I work 50 hours a week instead of 70, most with the AIA. If you worked on a professional basis you know you're only going to get paid X dollars for 5 hours' work. If you do the 5 hours' work you can be objective.

If you are getting a commission the alternative is this: if you suggest that for retired people with no other income, or there could be at least - well, the judgment may vary but at least a considerable case for considerable portion of their investment being put into the low-risk area where they get a definite income and they know their return and so on with a smaller portion of the equity area.

If you do that on the fixed interest component of the investment you will get one-half of 1 per cent, so on 300,000 you will get $1500 commission. If you just suggest equity funds of various types, you get 4 per cent commission which is $12,000 which is not bad remuneration for a few hours' work. If these people are poetic, as I have said, I think they could probably say, "I think that I shall never see a QC earn as much as me," because I know lots of QCs who have to work a whole day to earn $12,000.

But if they go further and inveigle the client into going into negative gearing, then would you believe the 300,000 - and

they borrow another 900,000 and invest $1.2 million - they then get three times $12,000 - what's that, four times 12,000 - 48,000, so 48,000 for negative gearing, 12,000 for mostly equity investments and for the less risky investment, the conservative investment, $1500.

I believe that sort of commission should be - instead of in addition to disclosing commission, they should say, "The investments we have recommended to you, we will get, say, $12,000 commission. Had we recommended other investments we would have got 1500." I think that would probably mean more to the average person than not so - - -

PROF CARMICHAEL: Should we even go further? Isn't the combination of fees and commissions inherently a conflict of interest? Shouldn't it be just purely fee-based?

MR DONNELLY: I think so. Yes, in the objectives of the memorandum of the Australian Investors Association - has one of its objectives the fact that anybody showing their - putting up their shingle as an investment adviser should meet three requirements. One is that they should work on a fee basis of any commission received being passed on to the client; secondly, that they should have some qualifications in commerce or accounting or allied field, and business, finance etcetera. Thirdly, that they have had some adequate experience. Of those, the first one is by far the most important. That's - again I guess I didn't put it in the submissions because I thought it perhaps a little bit - we would certainly be in favour of that but I thought it may be a little bit beyond the realms of practical politics, so to speak. I would strongly support it.

MR BEERWORTH: Mr Donnelly, most of your submission is a very strong indictment of the regulators, particularly the ASC and the ISC. What's their response to you? You have obviously taken particular cases to them?

MR DONNELLY: Yes, well - - -

CHAIRMAN: What's their response?

MR DONNELLY: The response is extremely cordial and nothing is done. To their great credit, despite all the criticism from me, they still talk to me and they still - - -

CHAIRMAN: Why do you think that is?

MR DONNELLY: Well, I think the - I believe political science have a term called "regulatory capture" where there is a tendency for - is that right? I believe that in various industry there is a tendency for

regulators, even with the best will in the world, because they're dealing with the people in the industry they are regulating on a day-by-day basis and they sort of get to know them - they're nice people and they tend to subconsciously drift into sort of sitting on their side of the fence. What has happened here of course is that they have done that - and of course until the Investors Association can - that started 5 years ago - I was waging a one-man crusade for about - many, many years until somebody said to me, "Austin, if you walk in front of the proverbial bus one of these days there will be a lot of joy in certain sections of the investment industry."

I had hoped I wouldn't walk in front of the bus but I wasn't getting any younger, so I then formed the Investors Association and our friends had a recent conference and in my submission I made the point that the ASC particularly have done some good things, and one of them is they have set up a national investor liaison committee to advise them. How good it's going to be, I don't know, but at least they have set it up and I have attended a couple of meetings.

CHAIRMAN: Does this lead us to conclude that you would prefer to see some separate organisation representing the interests of the consumer and the investors away from the existing structure?

MR DONNELLY: Well, one of the cases where there should be an ombudsman - that could be well desirable. What we were trying to do is if the present system - we made a - - -

CHAIRMAN: I'm only picking up your point about regulatory capture, that's all.

MR DONNELLY: Well, there's certainly - maybe an ombudsman type of structure would be fine but if you set up another one, if you set up another regulator, well, that regulator might be, with due respect, subject to regulatory capture anyway, so maybe the ombudsman. The voice of the investor hasn't been heard and I know that there have been very very great forces arranged against us. My articles have been taken out of papers under advertising pressure. I have been taken off, in some states, the ABC because of pressure from people who didn't like what I was saying.

MR BEERWORTH: The second issue that interests me is this: you said that there has been a 100 per cent success rate whenever somebody does bring a claim against a miscreant of some sort. I take it then that no change is required to the civil law which is obviously working quite well in itself?

MR DONNELLY: Yes, but the point is that people shouldn't have to do that, you see. If the law was being enforced it wouldn't be ready and a lot of people hesitate to take legal action because, for good reason, the costs involved. I have been there to help them. I have even now tried to negotiate in some cases to get the thing going before we even have to go to law.

MR BEERWORTH: That brings me to my third point. You said that the solution is for the minister to give a direction to those responsible to enforce their law. That of course in legal terms is a nonsense because those people are already obliged by the law itself to enforce the law. That's the number 1 thing the law does. Those people would have to be dismissed and replaced. Do you really think the situation is that bad that - - -

MR DONNELLY: Well, I think it is. I have put that to the attorney-general - and by the way I might say I had to edit this out to get down to 10 minutes, but I had planned to say that the comments of the Treasury in the discussion paper differ from the views of the Treasurer because before the election we wrote to each of the political parties and Mr Peter Costello, then Shadow Treasurer and now Treasurer, wrote back to say that he shared our concern about the problems which I have discussed this morning and that in government the Coalition would do something about it. We are hoping they will but we have said to him and I have said to the previous attorney-general, "If this is so bad, you must issue an order." Under the act the attorney-general has the power to issue a direction. He used it politely because he doesn't want to be seen to be putting political pressure on.

MR BEERWORTH: He can only give general directions and specific to the - - -

MR DONNELLY: Well, it seems to me that if he gave a general direction - the AFC seem to have a hang-up, they say, "We don't like to be prescriptive," and they say, "Well, we tell them if we have got to disclose these certain things," and I have said, "You don't have to prescribe the wording but you should tell them, tell the advisers, that you must disclose the factors which I have mentioned," but they say, "No, we don't like to do that." Unfortunately in their surveillance, for example, we have been amazed when we have complained to them of the cases I have sort of mentioned, and then they come back and they say, "Oh, no, we're not going to take any action."

They also had a fear that because the action - these abuses were so widespread, that if they took action against one, they would have to take action against a hell of a lot and they would wreck the industry. That argument, in my view, isn't valid because there's various actions they could take. They can suspend or revoke and even if they suspended one or two licences for a week, it would establish the principle. Even if they said, "Look, unless you do these things - unless you disclose this information, we're going to take action," I think that gets somewhere.

CHAIRMAN: Putting aside the nature of remuneration, do you think greater disclosure along the lines you're talking about would make significant difference to investor behaviour?

MR DONNELLY: I think it would, I think it would because from my experience over many, many years when I was giving advice, if I was talking to pensioners, for example, I would say on the various classes of investments, I would give them the benefits of equities and capital gain and so on. I would point out that fixed-interest investments are safe and secure provided you select them carefully and so on and follow a few principles, but they don't give you any prospects of capital gain. I will say, "Now, it's a matter for each person to decide how much of your capital you want to put into each area." I would say to them, "I believe that if you are retired and have got no income from other sources, you can't afford to put a large amount in the capital area and you have to - however much you would like to enjoy the capital gain prospects, you've got to because you need income and you can't risk your capital. If you're earning a salary and you lose capital, it's disappointing, but you can build it up, they can't, and in many years of experience I've never found that concept hard to get across.

CHAIRMAN: A great majority of financial advisers would lead people to imbalance - an imbalance towards equity in that situation?

MR DONNELLY: Yes, yes, indeed, because - and not only equity, because in advising clients and those who are in the radio and newspaper - if you ever look at any of the newspaper comments, you never see or very seldom see an adviser suggest that people should buy shares. They suggest they go into equity trust because in equity he gets 4 per cent commission, and if they go into shares he gets little or no commission, and it's outstanding that - I just find it hard to believe that in effect despite the efforts of people in the Financial Planning Association, a number of them good people from whom I'd buy a used

car any day of the week and if I lent them money I'd expect them to pay it back, but in this area they've got - the culture of concealment by the regulators accepting just what the industry likes to disclose has been so venerated that a lot of them will do anything to earn commission. A lot of others who are basically honest people, they just go along with what happens to be conventional practice, but whichever way they do it, whether they're doing it because they'll really sell anything for a commission or they do it just because they've been sucked in by the conventional wisdom - but to the person who loses 70 per cent of his capital it's equally serious.

MR BEERWORTH: Do you think this is mainly limited to that part of the prospectus industry that does deal with funds? Certainly in many prospectuses I've seen you sometimes get three pages on risks - which deal with risks - - -

MR DONNELLY: Yes. Well, in that area there's been some improvement on the risk, and the only suggestion I'd make there is that they ought to include in there market risk because very often market risk is the risk of a bigger market decline.

MR BEERWORTH: But it's very commonly included, very commonly included.

MR DONNELLY: Not in - not in - I haven't seen anything very specific. They might say it's affected by market fluctuations, but if they went a little bit more specific along the lines of the two or three paragraphs of - a person going into a new share issue is entitled to be told the risks of the industry, and currency risks, and all the other things, which by and large I believe are well covered, but he also should be - he or she should be told, "If you go into the market there's a risk that a slump might occur tomorrow and you may be down 30, 40 per cent, and you may take 10 years to recover," however good the company is and however well it's managed, but by and large they're better, and I think there's been improvement there. There's been a significant deterioration in the funds area because under the old regime they had to put in performance for at least the last 5 years, and so at least you got some figures you could look at, but that's gone by the board.

CHAIRMAN: Well, Mr Donnelly, I think your points are very well made and very clear, and we will certainly be thinking about them. Thank you very much.

MR DONNELLY: Thank you.

CHAIRMAN: We now have the National Credit Union Association represented by Philip Elliott and Derek Weatherley. Gentlemen? Good morning. If you could just commence, please, by stating your names and the organisation you represent, and it's over to you.

MR ELLIOTT: Philip Elliott, National Credit Union Association.

MR WEATHERLEY: Derek Weatherley, National Credit Union Association.

MR ELLIOTT: We've identified six major issues which we'd like to present for further consideration. They fall under the broad categories of prudential supervision and consumer protection. Six items are supervision of deposit-taking institutions, a single deposit-taking institution supervisor, the Uniform Credit Code, deposit protection, barriers to new entrants in the area of credit unions, and the topic of mutual banks. We would now address each of those matters in turn.

We've noted with considerable concern the proposal by Treasury for a system that is best described as caveat emptor. It implies limited or no supervision, and based on more detailed disclosure. We consider such a concept to be untenable and beyond all reasonable bounds, and we will explain our reasons for that shortly. We also understand there's very little precedent in this regard in developed economies similar to ours.

We strongly support sound prudential supervision because we believe the public in general has a real expectation of government to provide adequate oversighting of all major institutional aspects in our lives, and people's life savings in our opinion fall into that category. We see the same principles applying to health, welfare, law and order, as to the safety of institutions which hold the financial security and dreams of the public.

The concept of caveat emptor in fact implies that Mr and Mrs Average Australian have an accounting or commerce degree and can on an ongoing basis analyse the complex financial statements of sophisticated financial institutions. To suggest that even well-educated people would have the capacity to assess for themselves the risk profile of most banks, many building societies and dozens of credit unions is just not acceptable.

In many respects from an industry viewpoint we would prefer that there was no supervision. However, as corporate citizens we have responsibilities, and particularly from the mutual

financial sector we represent we believe it would be completely imprudent not to have an effective yet non-intrusive supervision system.

The next issue is that of a single deposit-taking institution supervisor, and we believe the arguments are now compelling for a single federal supervisor for deposit-taking institutions. If we're to have an efficient, effective and competitively mutual range of financial institutions competing, particularly in the household sector, then one federal deposit-taking institution supervisor is the only way to ensure, particularly over the longer term, that a level playing field exists between the players, and we stress these comments, aware of the fact that credit unions in this country represent only some $16 billion in total assets. However, they represent some 3.3 million Australians, and when you add building society statistics to that, you're getting towards a third of the Australian adult population.

So picking up the point that Mr Maitland emphasised this morning, the dollar asset size is a very small segment within the Australian financial system. However, in terms of citizens of this country, it is a very very large number. You may also be aware that credit unions contend that they have been significantly disadvantaged on many fronts for many many years, and now believe that events have compounded to a degree where there's no sustainable argument to prevent similar prudential treatment and therefore similar supervision of all deposit-taking institutions.

The question as to who that supervisor should be is one which we have an open mind on. Whether it be the Reserve Bank, a rejigged segment of the Reserve Bank, or a completely new organisation is of no great concern, provided it is appropriately empowered to undertake its very important role. Perhaps the time has arrived to remove any incorporation and supervision divisions amongst DTIs, provided they can meet the prudential requirements without any arbitrary minimum size. Mutual banks as a concept opens up a range of options in this regard, and we'll address that matter later in this presentation to you.

I'd like to move now to the Uniform Credit Code, just a few brief comments. We submit that the Uniform Credit Code has taken the issue of consumer disclosure and protection way too far. We believe it's now demonstrated beyond doubt that the issues attempted to be covered by the legislation generate a complexity that is causing inefficiencies in financial institutions, and resulting in consumers being

mesmerised by the volume of documentation - and we're certainly pleased to hear some of the comments that tend to support that view here this morning - and the documentation consumers are left with, and the cost of which they would be horrified if they learned of it, and it's surprising Greenpeace hasn't been in to try and protect the forests.

We contend that in the interests of the efficiency of the financial sector that adequate and proper consumer protection must be provided for with commensurate disclosure. However, we believe the essential element here is to keep documentation simple, so that consumers have a reasonable chance of understanding the fundamentals of their contract, while the legislation ensures that unscrupulous practices, which have largely been removed from the marketplace over the large decade or two, have been addressed.

Perhaps the Trade Practices Act could provide the lead here, where unacceptable practices are addressed in the statute but do not form the basis of day-to-day contracts. We know it's a complex issue, it won't be resolved easily, but we believe the problems are such that it does need to be addressed. It's causing enormous difficulties within the financial sector on both sides of the counter.

The next item is that of deposit protection. Presently a consumer would have to be extremely well informed to understand what levels of depositor protection, if any, apply to banks, building societies, credit unions, and any other financial institutions. As your discussion paper points out, there are some major misconceptions afoot, and it is time that consumers were properly informed as to the real position. That in itself indicates to us that there's time for change.

There's no question in our mind that a majority of Australians believe their deposits with banks are guaranteed. We understand that the authorities have been totally reluctant to clearly enunciate the position regarding banks to the community at large because of a fear of what may result. This should be considered untenable, and it's a position that we don't believe should be allowed to exist.

At the other end of the spectrum, that is from the banks, apart from the prudential standards and supervision, there is no protection afforded building society depositors, and in between building societies and banks, like credit unions with their contingency funds, so we've got a real mixture. These funds and their predecessors have effectively quarantined credit union members against loss, with losses of

depositors with credit unions being so insignificant as to be irrelevant. So for the purposes of the broader argument, credit union contingency funds have assisted credit union members to ensure that their deposits have been completely safe.

On the matter of deposit insurance, we'd make a number of points. It should largely remove or has the potential to remove the moral hazard for governments, which we know is a concern. It would or should remove the need for any government guarantees of banks or other institutions, and thus assist in rectifying the false impression successive administrations have permitted to exist within Australia.

It should remove a preferred status rating of any one DTI group over another, and it should meet the community expectations of the authorities. In particular, with the introduction of retirement savings accounts by banks, credit unions and building societies in mid-1997, the key issue of the safety of those funds could be adequately addressed via deposit insurance.

The inquiry's comments in relation to deposit insurance in many countries have been noted with interest. It certainly appears that Australia is the exception in relation to developed economies on the matter of deposit insurance and/or government guarantees. The inquiry discussion paper accurately stated that our submission opposed the retention of contingency funds with credit unions, and it's important that our position be made clear on that issue.

Our reasons are as follows: there is no such cost impost on building societies or banks, therefore credit unions were being disadvantaged competitively. From a perception viewpoint, the general public had little or no knowledge of the existence of these funds and what their function was, whilst the majority of the population believed the banks were guaranteed. Again credit unions were being disadvantaged.

Thirdly, the era to which these funds belong had passed. Credit unions have about fourteen-fold the dollar value in reserves, essentially retained profits, that the contingency funds ever held at their peak when credit union reserves were quite low, so we have moved into a completely different era.

A system of deposit insurance across all deposit-taking institutions - and our position would be that it applies to all or it's not introduced at all. We think it must be applicable to all

institutions and on an equitable basis, and this should help in terms of a level playing field particularly, and also assist in removing a preferred status of DTI category being conferred by government either by its action or inaction. It would appear that there is sufficient precedent around the world to demonstrate that these schemes can be properly constructed to work effectively and in the interests of the consumer without inviting management of such organisations to embark on reckless risk-taking due to the existence of the insurance scheme.

A brief comment now in relation to barriers to new entrants in the area of credit unions: the effect of the current legislation, the Financial Institutions Code, is tantamount to a prohibition on new credit unions being formed, and is also being very severe on small credit unions. Testimony to this is the demise of over 70 credit unions since the scheme started in 1992, while only one credit union has been formed in that period, and it's got quite exceptional and unique circumstances applicable to it.

It is submitted that not one credit union operating today would have been able to achieve registration if the FI Code had applied in the past. Even those credit unions which today have risk-weighted reserves of 25 per cent are comprising almost exclusively retained earnings. None of them in our opinion would have gotten off the ground. The capital adequacy requirement, 8 per cent risk-weighted, and the non-share capital nature of credit unions as mutual organisations combined to produce a catch 22 formula for registration.

We need to add to that the fact that a group interested in forming a credit union must convince their state supervisor of their success potential, while the elements for demonstrating same are not recorded anywhere. We believe this matter needs to be addressed so that new credit unions can be formed, especially as more and more people could utilise their facility - probably best exemplified by the departure of banks from many rural areas, where a number of inquiries from people arising in relation to the formation of credit unions - but we see a difficult path for them.

Mutual banks is the next topic, and as representatives of mutual organisations we're very pleased to note the discussion paper acknowledging the very successful role of mutual banks in the finance sector overseas. To us this is at odds with the long-standing opinions of successive regulators in this country.

The North American and European experience and success of mutual banks should not be ignored, and we strongly recommend that the inquiry contention at paragraph 7.156 in relation to mutual banks be contained in the final report to government. We will expand on our comments in a subsequent submission on this issue, which we believe has enormous strategic benefit for financial service delivery in Australia into the future.

A couple of footnotes under that topic of credit unions generally, and mutual banks: the first one is the retention of mutuality. It's an issue that you discussed with Mr Maitland this morning. Our view is that irrespective of the outcomes of the inquiry in relation to supervision, legislation form, mutual banks or not, credit unions must continue to be provided for, firstly because of their commitment to the household sector, and secondly with their mutual bases completely intact. The credit union industry is unified on that point and feels very strongly about it, and it is a major feature of the distinction of credit unions from most other financial institutions.

This may however necessitate provisions for permanent shares as well, which are presently prohibited, particularly if there is no relief provided to the inequitable taxation treatment that credit unions presently experience, which leads to that point. Whilst we acknowledge the terms of reference of the inquiry exclude recommendations on taxation, we point out that being prohibited from issuing permanent shares effectively prevents credit unions paying dividends.

This resultant inability to distribute tax credits by way of franking credits, as banks can do for their shareholders, seriously penalises credit unions and particularly their members, and by an amount equivalent to 64¢ in each dollar of tax paid by financial institutions relative to post-tax profits. Every dollar members earn from their credit union is taxed, while bank owners can enjoy up to the full post-tax profit as dividends franked up to 36¢.

We thank you for the opportunity to present our opinions to the inquiry members, and we'd certainly welcome any questions on those matters.

CHAIRMAN: Thanks, Philip. Gentlemen.

PROF CARMICHAEL: Yes. Philip, on your depositor protection argument, how would you actually structure the scheme if you were putting something together?

MR ELLIOTT: If I was the architect?

PROF CARMICHAEL: Yes.

MR ELLIOTT: I'd probably have to analyse a lot of the schemes that are in operation, but broadly speaking we would see all deposit-taking institutions required to contribute to the fund firstly, and that would naturally enough be based on actuarial studies, and it would have to have a very close relationship with the supervisor because if you're charged with the responsibility of basically underwriting the financial safety of these organisations, then I believe it's essential that you have an important role in the supervision of their performance, because the two are totally correlated.

Beyond that, the technicalities of it, we haven't as yet undertaken any studies, but we can say that the operation of contingency funds in a number of the states in Australia by credit unions over periods of up to 20, 25 years gives us a fairly micro view of how it might work, and without necessarily realising it at the time they've performed that depositor protection role, the structure I guess is in simplistic terms. The organisations contribute funds, presumably on an expenditure basis, not the capital-type funds that we've had in these contingency funds. Those premiums build up, and hopefully there's sufficient funds there to cover any problems that might occur.

We would hope that something like the S and L debacle in the US, which appeared to be a combination of extreme factors, not the least of which was inadequate supervision and control - that they wouldn't exist in any similar environment in Australia, so that we wouldn't have that sort of experience, not even the potential for that sort of experience here.

PROF CARMICHAEL: And if there weren't a depositor protection scheme you'd still favour getting rid of the contingency fund?

MR ELLIOTT: Yes, essentially because we have three different versions of depositor protection across the three major deposit-taking institutions, to the extent with building societies nothing exists other than their prudential requirements and the supervision, and we believe it's time to get all three major sectors in the DTI sector onto an even keel.

MR BEERWORTH: Your recommendation that you should move to federal supervision, does that spring from a belief that the banks are in a preferred status position, or from the fact that you don't think state regulation is effective or appropriate?

MR ELLIOTT: It's both of those factors. There's probably eight or nine major factors that we might list in terms of the reasons for it, but certainly the preferred status of banks is one issue that causes us concern. We find that there is a range of difficulties that we don't believe would exist at a federal level that we experience now. One of those was touched on this morning, one that's of great concern to us, and that is the delay in any amendments to the legislation.

It's now quite certain that there will be a 2-year period that will have passed by January 97, and no effective progress will have occurred in relation to amendments to the FI scheme. That's just far too long, and the comments this morning explained that that's the way of a uniform scheme like this - there are just so many players involved, and the processes that amendments have to go through are just too numerous, and it's almost impossible to rectify.

If we weren't moved to a federal level, we'd be strongly pressing the authorities under the FI scheme to in fact appoint on whatever representative basis from the states six people who had the job, so that one group addressed the issue, whereas at the moment there's probably about 15 different groups that all have a chop at it, and by the time you take it through that range of organisations, there's precious little left at the end.

MR BEERWORTH: If we were to recommend that all deposit-taking institutions come under federal supervision, common to the banks perhaps, are there any of the DTIs who are likely to oppose that move or who would prefer to stay under state supervision?

MR ELLIOTT: You mean individual?

MR BEERWORTH: Yes, any particular segments, do you think?

MR ELLIOTT: Look, in probably a group as diverse as credit unions and building societies, there probably would be some, but I think the great majority of both building societies and particularly credit unions would support that move.

CHAIRMAN: There might be some carrot that might be capable of being provided?

MR ELLIOTT: Well, we believe that a number of deficiencies that exist in the current system would be removed by a move to a federal level, and believe that they should be sufficient inducement for people to see that on balance as a better position than the one that exists now.

CHAIRMAN: We have heard two sort of views expressed about the Credit Code this morning, from consumer representatives and your

view. I mean, do you accept the argument in any sense that maybe the financial institutions have made too much of a meal of it in terms of disclosure and amount of information, and it could've been tackled a lot more simply?

MR ELLIOTT: Unfortunately not. I've been living with it since the mid-eighties in Victoria, when the government changed the position there to bring credit unions under the Victorian Credit Code, and it's not too different to the Uniform Code in many respects. It is a nightmare. From the credit union viewpoint - and we told the authorities this on a number of occasions - in our opinion it would add at least 1 per cent to the cost of loans, and we're talking in a range of 12 to 14 per cent, so percentagewise it's a massive increase.

The credit union I was working in at that stage - we had a reduction in the throughput in our loans of 25 per cent. We eventually got that back up, but we added about 20 per cent more staff numbers to the loans area. The administration of it from the financial institutions viewpoint is horrendous and very expensive. Certainly a lot of solicitors have invoiced larger amounts in relation to it, and I believe that the stick which the consumer advocate said is a good idea to have - in principle I can't argue with it, it's just the size of this stick. It's about 50 foot long, and we've got a very small peanut shell that we're trying to crack.

The horrors of that - and we now know - we've had enough experience with credit unions, where their borrowing members are just horrified at what they're being served up, and they're trying to push it back over the counter, saying, you know, "I'm not going to read this." I think all of us agree if you get something more than four pages - I'd never read a 20-page document, and I should know better than to be in that position, but, you know, you can only handle so much.

Our view is that so much of this protection ought to be parked over here in the legislation rather than dumped on the institution, because no financial institution these days I believe - certainly with any morals - opposes the principles. Credit unions have never opposed the principles of truth in lending and what the Consumer Credit Code is about, it's the way the code has been made so complex, and we've had experiences over the last 4 years where solicitors, groups of solicitors, will sit down and three of them will have five different opinions on one clause. That's the reason for the opposition and the difficulty with it.

MR SMITH: Well, I wanted to go back to the depositor protection issue a little. I just wasn't sure what you meant when you said that it must apply to all or not at all in terms of - would you contemplate that it might have a different premium for different institutions?

MR ELLIOTT: Yes. We believe that in terms of equity, risk must drive premium, so that an organisation - it might be 25 per cent risk-weighted capital - may be paying a much lesser premium than one that might be at 8 or 9 per cent. Yes, so we believe that firstly it should be across all like institutions, firstly, and secondly, that the structure of the scheme must reflect reality, and that is risk versus premium.

MR SMITH: And just on that one, your idea that something has to be done to enable new entry: I mean, is there a problem there with the interaction to presumably what would be high risk new entrants with potentially high premium deposit insurance? Did you have any particular ideas as to how we would make it possible to get this new entry and not get that new problem?

MR ELLIOTT: Yes. Well, as I said in the presentation, it really is a catch 22. Without being able to issue permanent shares, the only capital credit unions can raise is from retained earnings. It's a bit hard to produce retained earnings before you start trading. It really is an embargo on incorporation, unless you get someone who provides a big bank roll and that's going to satisfy the authorities in that particular state.

We believe in fact that those capital requirements ought to be dispensed with for new entrants, because we're talking very small monetary value as a new credit union gets going, and I would imagine that the industry itself would be prepared to arrange something to ensure that if that had to be wound up or merged somewhere, that that problem could be addressed. It's certainly not a major concern for the financial system, let alone the credit union industry with $16 billion in assets, to deal with some difficulties that may occur in very very small new credit unions, but the likelihood is that they may achieve success rather than failure.

PROF CARMICHAEL: Can I push that one a little bit further because I was also interested in that aspect. My understanding was that there was scope say within the FI scheme for new entrants to come in to get special treatment while they got started, and it was my understanding that there hadn't been people knocking on the door wanting to start up.

Are you suggesting that there has been a pent-up supply of new entrants there that hasn't been accommodated?

MR ELLIOTT: Yes. Probably there are two things applying here. One is that a number of groups may have been reluctant to proceed because they became aware of the fundamental requirements - I have had discussions with representatives of groups that have spoken to state supervisors and have been largely discouraged because of the requirements that they must meet. Unfortunately that reference you made to the FI scheme where the requirements may be relaxed is completely at the discretion of the state supervisor, and there is no written guide anywhere, it is what the supervisor decides based on the ability to vary those requirements. So that level of uncertainty makes it almost complete - yes. If there was the - we believe that there should be a very dramatic relaxation of the requirements, particularly for an organisation starting up like this, and we believe the legislation needs to be quite specific rather than totally ambiguous in terms of whatever the state authority determines.

CHAIRMAN: Thank you very much, gentlemen. We appreciate your words and submission. Thank you.

MR ELLIOTT: Thank you.

CHAIRMAN: We now have Mr John Cumming from Austand. I'm not sure whether you're on your own, John, or with someone.

MR CUMMING: No, I'm on my own.

CHAIRMAN: Okay, well, take the middle chair there, and if you could just announce yourself, and if you are representing any organisation.

MR CUMMING: Yes, my name is John Cumming. I represent and I speak on behalf of Austand, which is a very active team of people throughout Australia who are researching and providing us with information that is keeping us well and truly informed about some of the horrible things that are happening in our country. I've spent a lot of time in the advertising business. I built one of the biggest advertising organisations in Australia, a research organisation and a PR company. I retired about 5 years ago and came to Noosa where I was going to quietly settle down and paint, which I'd got going nicely, but I could not stand seeing what was going on in Australia.

I should just give you a little bit of information, Mr Chairman, which may help you in this difficult task you've got in front of you. It may tip the scales the right way in the final analysis. Australians are magnificent people, they are wonderful people, and I hate to see them being pushed into the background. We are capable of doing far more than Americans do. I know that, as I was an infantry officer during the war, and I worked closely with them, and I knew what our troops did compared with what they did. We are the wealthiest country in the world - - -

CHAIRMAN: By some measures.

MR CUMMING: - - - according to the World Bank, and yet we are very very poor and getting poorer day by day and very rapidly. Now, that means and necessitates really urgent action. In our early stages of Austand we had to establish ourselves what foreign ownership was. We realised that that was the major problem. ABS had stopped publishing figures in the segments, the market segments, although this has been denied, and we had to have some sort of figures. Well, with our research background we were able to do it very quickly and very accurately. We established 90 per cent, and we checked that carefully all the way along the line, also with ABS, and they said, "You can be pretty safe with that figure."

We found later on that there was around about $200 billion going out of this country tax free. We thought we'd hit the

target and we knew exactly what was going on, but we hadn't. That $200 billion sounds like a lot of money, but when you realise that the country is turning over 27 trillion currently it's about - even half of that, you wouldn't make 1 per cent. So beyond that we had missed a very good target but fortunately we were alerted to it by Clyde Cameron, the politician, and he pointed out that what really happened was that in the double taxation agreement that was signed in November 1953 - you will remember this, Mr Chairman - a lot of my friends at the time - a lot of people running companies, big companies, were selling out to foreigners, and they had to because they couldn't compete with companies that were not paying tax, foreign companies not paying tax - they had no hope.

They disappeared, and that's how we have such a high foreign ownership. This was orchestrated. We are terrible managers in Australia. The management that's run our country for the last 200 years is nothing but appalling - there's no doubt about that, and I think it's fair that I can say that about our politicians. I think they're fair game. But it can be said also that we have been manoeuvred. We at Austand call it the great Australian swindle.

Now, with that background you might look twice at some of the things that people put up to you. You know only too well that in South America the Americans got themselves organised there with banks, banks, banks, banks, and they set a rate and they got the thing all organised and then they got together with the government, the people borrowed heavily because it was a fixed rate - it was going to be a fixed rate for some years - and the government changed its mind and the banks ended up with all the profits.

Now, that could easily happen if we Australians do the wrong thing. There's no earthly reason why we should be running with foreign banks, none. We've just lost our own bank which we must have - I mean, a country like Australia not having its own bank is rather peculiar, to say the least of it. It is ridiculous.

CHAIRMAN: You're referring to?

MR CUMMING: The Commonwealth Bank.

CHAIRMAN: Which is now owned by all of Australia.

MR CUMMING: Now?

CHAIRMAN: Now owned by many Australians.

MR CUMMING: Are you sure?

CHAIRMAN: Well, I'm just putting the question to you.

MR CUMMING: Yes, well, I'm not too sure, but if you're sure we'd like to get - - -

CHAIRMAN: No, I'm asking you.

MR CUMMING: Well, I would think that the word privatisation has been produced by some very clever people. It's not privatisation. When those shares go on the market they're snapped up by foreigners at the rate of knots. You must know that. They go whoosh, they're already booked, and so I think it's fair to say that we don't have any longer - we don't even have control of it any longer. I hope I'm wrong. I hope. But it is essential - and I think you would agree entirely that we hold onto that bank if we can - and if you're right - because it is impossible to think that we don't have our own bank.

Now, I think you'd take that into your calculations and it may make it - a big difference.

CHAIRMAN: I'm happy, Mr Cumming, for you to talk on but maybe the best value is actually some questions in the interests of time, and please don't let me - - -

MR CUMMING: Well, I'm getting too - - -

CHAIRMAN: I don't want you to leave yourself with no time for us to ask you some questions. That's all.

MR CUMMING: All right. Okay. Devaluation - I want to get to that, but I just want to say that the other thing that is of significance is that the service industries in Australia have disappeared. We used to have some marvellous advertising people, which I'm familiar with, we used to have wonderful accountants, we used to have wonderful people in all directions, and they have all been replaced by foreigners or amalgamated with foreigners, and there we go.

I envisaged as a younger fellow that we would have a wonderful team of accountants, researchers, promotional people and so on to sell to South-East Asia. What happened to it? Someone is leaning on us. As far as deregulation is concerned - you asked the question - we did the honest thing, we went along with it, and we reduced our tariffs, we did all the things that were asked of us. What did the other people do? Backed off on it. And that wiped out a tremendous amount of industry in Australia. I don't need to tell you that.

CHAIRMAN: It's a bit outside our terms of reference.

MR CUMMING: Yes, I know that, but it all does come together somewhere along the line. As far as the financial management, we will be giving you a report on the 13th which will I think help you materially

on the question of how you can control things and what should be done there, and perhaps you'd - I'll leave it at that.

CHAIRMAN: Okay. I mean, it's a very clear message you're putting that there's too high a degree of foreign ownership in the Australian economy and it's having many many negative outcomes.

MR CUMMING: Great to hear you say that.

CHAIRMAN: Can I just put a simple question to you: do you have any view about Australian companies moving offshore?

MR CUMMING: Yes. I can't blame them. How can you blame any man who's commercially inclined not putting his money into whatever and getting it back, and this is an enormous amount - - -

CHAIRMAN: You have no objection to Australian companies heading off and - - -

MR CUMMING: Not Australian companies. Individuals I think is more the pace. But, yes, I do - I do - but you can't blame them doing that when they're being hammered from the other side. I mean, if you look at the taxation situation from the other side to Australians for Australian companies, it is hopeless.

CHAIRMAN: Yes, okay.

MR BEERWORTH: Your figures of 200 billion a year out of 90 per cent of Australian industry and business being owned by foreigners seem to come from Mr Clyde Cameron, the former minister. Is that correct? Is that the position?

MR CUMMING: He said - well, two former ministers endorsed them - Jim Cairns and Clyde Holding - at least Clyde Cameron - they were pretty close to them at the time, but it originally came from SBS, the information - from ABS. It was a hundred - it was 80 to a hundred billion dollars in 1986 and we simply projected it with the subsequent assets sold, and it came to about 200 billion.

PROF CARMICHAEL: Well, John, with respect, the numbers don't seem to stack up. Total foreign equity investment in Australia is about 200 billion. The stock market capitalisation alone - that's only part of it - is 375 billion and you're only giving 90 per cent - - -

MR CUMMING: Where are you getting your figures from?

PROF CARMICHAEL: From ABS numbers.

MR CUMMING: Yes, I thought so.

PROF CARMICHAEL: And I did a sample last night just to check. I pulled out the share register of a company that I'm a director of - it's a publicly listed company - and I thought, "Gee, maybe I've missed the point here,"

and I just went and looked at anything that looked like it could even possibly be foreign I called it foreign, and I got to 17 per cent, and the others were clearly identifiable as Australian. You can't get 90 per cent.

MR CUMMING: Go and stand on the street corner if you know - between the foreign company and an Australian company. Buy a book called Lucky - Be Damned which I wrote. It lists it. It was published in 1990, I think, and that lists the breakdown of the market segments, and you'll read it there.

CHAIRMAN: John, we are trying to take in your basic proposition and, like Prof Carmichael - I mean, I've worked for and been involved in a number of Australian companies, and I've got a pretty fair idea of their ownership. Now, you're onto something else that I've never seen, because it's just not there in terms of the equity ownership of Australian corporations large and small - it's not there. I mean, you can track that ownership back through the Australian institutions and through the policyholders of - in those Australian institutions, and/or the individual shareholders.

MR CUMMING: Well, I can only suggest that you have a look at the figures that we've got in that book.

CHAIRMAN: All right, well, if you can give us something that we can get our teeth into, we will, but I can assure you a lot of the Australian corporations I am involved with - just 15 to 20 would be tops.

MR BEERWORTH: I didn't think the Australian economy was 27 trillion, either. I thought we were below 2 trillion, but - - -

MR CUMMING: Well, I can assure you we could sit here all day discussing that and, you know - - -

CHAIRMAN: Well, we have - we're trying to take opinions in all the time, but we also need some factual basis on which we can proceed. Our tax expert might like to ask you a question in that area. He's the double tax man.

MR CUMMING: Well, just to save you any embarrassment, you saw the statement made by the Australian Taxation Office in Canberra to the question, "What are foreigners paying in tax?" and his answer was - and he was 2IC to the tax operation in Canberra - "Little or nothing at all."

MR SMITH: I was luckily born in the year that the double tax agreement was introduced and I can't be held responsible for that one, but that particular bill - you refer to it as a bill. It's an act. It actually

deals with the distribution of income, it doesn't deal with the taxation of company profits.

MR CUMMING: Yes, I'm aware of that.

MR SMITH: And all companies in Australia, whether foreign owned or Australian owned, are subject to exactly the same company tax law.

MR CUMMING: I'm aware of that.

MR SMITH: So it doesn't - - -

MR CUMMING: But they'd be dumb to pay out their tax in Australia, wouldn't they?

MR SMITH: It wasn't mentioned in your submission, that's why - so I just wanted to quickly clarify that.

MR CUMMING: Well, it's - I'm afraid it's a shortcut, but that's basically what the situation is.

MR SMITH: Yes, but they pay the same tax under the same tax law.

MR CUMMING: Well, they don't pay it because it would be stupid for them to pay it. They would be paying a lot more than they would pay in Venezuela or whatever.

MR SMITH: Why do you think they're not paying any tax?

MR CUMMING: Well, because Mr Canelli in Canberra says they're not. That helps.

MR SMITH: Yes. I think that we can be confident that they're paying tax. I'm not saying for a moment that there's no tax avoidance, but I think that's something shared between all taxpayers or all classes of taxpayers.

MR CUMMING: Well, I can assure you that's how all the Australian companies were wiped out, and it is a tragedy, and all I'm mentioning it for is because if you fellows make some decision to let more and more moneylenders bend our arm, you know, you will never live it down. You will hate yourselves, too.

CHAIRMAN: Thanks very much, Mr Cumming, appreciated that. Thank you.

CHAIRMAN: We now have Raymond Thyer. I think you may have just come in. Please sit down. I should just repeat perhaps what I've said early in the morning: that all of these proceedings are being recorded and transcripts will be publicly available. We have no special powers, no parliamentary privilege, so you certainly should not make any comments which reflect adversely on any particular persons or organisations. We ask you simply to start for the purposes of voice recognition by stating your name and whether you represent any particular organisations. It's yours, Raymond.

MR THYER: Thank you. My name is Raymond Thyer, and I am here as a member of the public. I have written words on these pages that I would like to read for the sake of expediency. This in my opinion briefs or makes it more concise and in keeping with the aims and objectives as I understand is the aim of this committee.

CHAIRMAN: Yes.

MR THYER: So with your permission I'd like to read the words that I've written on these pages. When I think of banks I am reminded of those memorable words, "What a horrible web we weave when first we practise to deceive." Do banks deserve deregulation or do they deserve stricter controls and complete regulation? The answer surely is stricter controls and complete regulation.

Once banks were the most wonderful and perfect places, and one could have complete faith and trust in one bank's manager too. One could enter banks free of charge to deposit or withdraw one's money from a human teller, and banks were good and kind and they rewarded their customers who stayed with them, and many had since childhood. They gave one a mortgage and loaned one another's money at a higher rate of interest than they paid, and when children became old banks offered not to pay them fair and just payments of interest of their life's savings until the government deemed it so.

One was certain that one's money was always safe in one's bank for there was never any doubt about that, and then one day it all began to change and deregulation came, and with it came new large bank fees and charges and they called them user-pay fees. Now one has to pay to talk to a human teller or one could use the teller machine in the window. It would not cost so much and was so easy to use too. Also came account fees to keep one's bank account open, and more fees for one who dared to write more than a few cheques, and one

must keep a minimum in one's account for their whole life for never, never to be withdrawn.

Yes, deregulation proved to be a winner for banks and not for the people of Australia. Banks seem to be a law unto themselves. They take 5 days to pay out proceeds of cheques, while they debit accounts on day one of the same cheques, and they are very quick to debit people's accounts with the latest in interest charges, yet strangely take months to pass on a reduction in interest rates.

Banks became big and powerful and the voices of the little people didn't seem to matter. Deregulation benefits everyone, banks would have us believe, but norm was not so perfect. Foreign currency loans that were the flavour of the banks began to lose their sweetness, and men and women were called upon by their wonderful banks and summonsed with demands that they pay more, very much more money to their wonderful benevolent banks, and when it was found men and women couldn't answer the call they were shut out of their homes, farms, factories and their business, and cast out along with their children and told never to return.

More people too had difficulties and problems with their wonderful banks, and a new course was decided upon. There would be simple resolutions to all the banks' problems. There would be a new and voluntary code of conduct for the banks, drawn up by banks for banks to follow, and better yet, there would be a person installed to listen to all grievances, and banks would pay for everything, and if there were more deregulation there would be no discrimination.

There would be more competition and greater benefits for all for there was no discrimination, was there? It was just unfortunate that people's individual volume of money couldn't compete with that of big business, or even a small business couldn't compete either and didn't deserve the same benefits given by banks to big business. No, there was no discrimination there at all. That was just a business decision after all.

All seemed peaceful and calm. Hadn't the little people been put in their right categories, and what about the new voluntary code of conduct? Better to have that to hide behind for banks, and all the while banks' pockets grew larger and larger still, and their ambitions swelled towards even greater things yet, and for more deregulation, but this time with less and less disclosures to the people. Surely banks' conduct and practices were unimpeachable.

The hell, the denigration, the mental stress that comes with eviction of one and of one's wife and children of one's family home at the hands of banks has been the cause of some people seeking respite in alcohol and even suicide. I have but the clothes I wear and just a few more, but I have a truly wonderful wife, a marvellous daughter and two loyal sons, and every night when I lay down to sleep I do not sleep easily as the torment never diminishes. There has been no money for gifts for any birthdays or for the last five Christmases and none again for this Christmas because of what banks have done to us.

There is much left to be desired in the conduct and practices of banks in Australia, and insomuch as the current voluntary code of conduct written for banks by banks is deficient, this inquiry seems the best opportunity to bring justice into the state of anarchy that surely has come with deregulation, and to reverse the relentless ambitions of banks in Australia for more deregulation.

If I were Prime Minister of Australia I would say, "No more deregulation," and impose on them more and stricter still regulations, and say unto all banks, "From this day forth there will be greater regulations of all banks in Australia." Deregulation so far has been deregulation abused, and many people in Australia have suffered because of it. There is no such thing as, "As safe as a bank." Instead there is nothing; no security for one's money, for what little there is equals nothing at all.

I would say unto all banks, "From today forth all banks in Australia will provide free insurance to all depositors and shareholders for all moneys held by all banks, and there shall be no more discrimination in benefits given by banks in Australia between people; people in business and big business. There shall be one rate of interest charged by banks, charged on mortgages, loans and lending on banks' credit cards, and all should be the same rate as charged on home mortgages, and all benefits should be the same for everyone, and there should be fierce reduction in interest rates. There should be more and not less disclosure by banks, for not enough is disclosed to the people now."

It is not good enough for banks to hide behind caveat emptor for many but a few exist who really understand the Latin words for "buyer beware", for not all have spent years of intensive study to gain the knowledge of solicitors, and there should be new and stricter regulations and legislation enacted, and quickly, to provide all the

peoples of Australia for a fair go and to administer control of all banks in Australia. These matters I commend to you and your committee, along with those others that I have already submitted. Thank you for the opportunity of appearing today.

CHAIRMAN: Thank you very much. I said at the outset we have no ability to deal with individual claimants on the system, but I take it you've been a pretty unhappy customer of the banks. Is that what's - - -

MR THYER: That is exactly right, yes.

CHAIRMAN: We of course are dealing with the regulatory framework, and it doesn't necessarily assume that there has to be less regulation, and we are looking at a complete range of options. I've taken note of your various points. I mean, some of them would be pretty difficult to take on board. It would be difficult to have perhaps no differential rate of interest. I mean, if you were a borrower offering a lot of security, how would that compare with someone who might have a very risky proposition? You feel the banks should charge the same rate of interest, irrespective of - - -

MR THYER: With all due respect, I feel that if one approaches a bank for finance for a particular purpose, if that be likened to venture capital, then obviously that is to be treated as a category of finance rather than a category of people. It's not a category of finance that I feel applies today. I feel that it's more a discrimination between the financial wealth of peoples and of persons in small business, and I was one of those in small business until banks did what they did unto myself and my family.

CHAIRMAN: What was your business?

MR THYER: My business was an importer and supplier of dry-cell batteries to governments in Australia. Sorry, I'll rephrase that, to governments in Australia and to business and commerce in Australia, and for 19 years I ran a very, I consider, successful business, but for me to say any more now than that I have to be very careful.

CHAIRMAN: All your ills hark back to the banks.

MR THYER: I beg your pardon?

CHAIRMAN: You blame the banks for the totality of what happened to you?

MR THYER: I blame one bank.

CHAIRMAN: One bank.

MR THYER: But I particularly feel - irrespective of my present circumstances I feel that approaches to other banks have suggested to

me that banks are treating all circumstances and peoples the same and do discriminate very heavily between peoples in business, peoples not in business and peoples in big business.

CHAIRMAN: You don't think banks have got to respond more in the general sense to the marketplace now with a range of products and the way services are delivered in a far more personalised sense - and I'm talking across a range of products - for houses, for other forms? I mean, some people would argue there's a much greater range of services being provided by the banks in fairly competitive forms. I mean, the number of mortgage products has gone up by a factor of many many times in the last 10 years.

MR THYER: Exactly, but I feel the discrimination is very large in all banks. I feel that the rates charged as to attract business in housing mortgage is very very competitive. Where this competitive and cost of moneys and funds to banks - I'm not an expert on this, but I'm only suggesting what I assume to be the matter - that if all costs of funds were the same, then there is a horrible amount of discrimination between the rates charged to peoples in business for their working capitals, their cost of machinery and stock and so on.

CHAIRMAN: So you feel the small business sector perhaps has been the one that's fared badly in this process? Is that perhaps the point we should take on board?

MR THYER: Yes, I do, and also I feel that the people in Australia at large are horribly discriminated in terms of bank lendings, be that for - as I say, the competitive nature that exists more or less controls the housing mortgage rates but it doesn't exist to the same extent in credit cards and other personal lending for personal loans, motor cars, vehicles and so forth. My experience has been that I have definitely suffered in small business in terms of borrowings and the cost of borrowings from banks, as opposed to what is granted to big business, and bear in mind that the big business then becomes more a direct competitor in the marketplace.

So that basically is what I'm saying, but in terms of the discrimination, it's very large in - if I may refer to this again - yes, to small business. That's correct, yes. I'm sorry.

MR BEERWORTH: Just one point: I think part of your experience has obviously come about through foreclosure and enforcing proceedings of the banks. Banks have never changed very much of course through

deregulation. They've always been very tough once you fall onto the enforcement side of life. Deregulation hasn't affected that very much.

MR THYER: Sorry, I can disagree with you very very thoroughly in this matter, because my circumstances are very shortly to become a trial by jury in the Supreme Court. This will bring forth exactly the subject matter you're talking about. I can't comment on that, I'm sorry.

PROF CARMICHAEL: Only a general comment to say that your concern about finance to small and medium-sized enterprises is one that's shared by a lot of people.

MR THYER: Yes. I was looking here before. The thought that I had in mind was the discrimination in - I don't know; I would presume that your committee would look at the discrimination that applies in lending rates applicable to credit cards.

CHAIRMAN: It's been mentioned.

MR THYER: I'm talking about banks issuing credit cards and this is - I'd better be careful what I say. This is a totally, totally larger amount of rates of interest than would one see visibly in the newspapers of the day and on television that's available on housing mortgages.

CHAIRMAN: Thank you very much, Ray. We appreciate your comments.

MR THYER: Thank you very much.

CHAIRMAN: Thank you.

MR THYER: Thank you, gentlemen.

CHAIRMAN: We now, ladies and gentlemen, have Richard Sanders and Brian O'Halloran, according to my bit of paper, from the Australian Company for Economic Justice.

MR SANDERS: Coalition.

CHAIRMAN: Coalition, is it? Sorry, the abbreviations were - we talked earlier, Richard. It says "Australian Company" here too.

MR SANDERS: Sure. I think it's probably just an abbreviation that went slightly wrong.

CHAIRMAN: Okay, Richard, you're on your own? Yes.

MR SANDERS: Thank you.

CHAIRMAN: You know the drill here this morning?

MR SANDERS: I know the drill, sir, yes.

CHAIRMAN: If you'll just state your name we'll get under way.

MR SANDERS: Richard Sanders. I represent the Australian Coalition for Economic Justice which a coalition consisting of about 40 organisations who represent small business, academics, churches, social justice, unions, the environment, farmers and others, and we represent a broad diversity of ordinary Australians who are extremely concerned at the economic direction our country has taken. We're concerned at the very limited public debates surrounding this inquiry.

CHAIRMAN: Well, it's not short of media attention I have to tell you.

MR SANDERS: Yes. The problem is the public is not engaged in this debate.

CHAIRMAN: But it's been communicated fairly widely, hasn't it though?

MR SANDERS: Well, I would agree that it has had some coverage but the problem is - I think what the inquiry is not doing is attempting to actually demystify to some extent some of the realms of finance, some of the fundamentals in particular which I think are topics that the Australian public to some extent are fairly aware of in some ways, particularly if there is some discussion and debate on this. So I think there is a shortcoming there, and I will probably refer to some of that demystification as I go on.

We're also concerned at what we perceive as the limited consideration of the public and national interest in the discussion paper. The inquiry appears to be primarily for the benefit of bankers and the shareholders of financial institutions. There seems to be an implicit assumption that the interests of bankers, financiers and the

shareholders are coincident with the public interest, and we would refute that. The reality of globalisation and deregulation is a huge syphoning of wealth out of this country, which I suppose is one of our major concerns.

For the wealthy who have a stake in the system, who have significant shareholdings or whatever in the financial system - a significant place in the financial system - it doesn't really matter where they live in the world or who owns the companies or whatever because they get their cut by virtue of the fact that they are shareholders or players in this game. But for the ordinary person who has either a small stake - I mean there are a lot of people who have got a small stake in the Commonwealth Bank say for example but in real terms it's insignificant - or no stake at all in the system, their wellbeing ultimately depends on the wellbeing of the country as a whole, and I would submit that the country as a whole is not benefiting from deregulation to date and will not be benefiting from what appears to be the almost predetermined agenda that there will be further deregulation, and it is clear that the major institutions are pushing that very hard.

Your terms of reference charges the inquiry with making recommendations on the regulatory arrangements consistent with financial stability, prudence, integrity and fairness. It's in that context that the principal issue I want to raise is that of the regulation of credit creations and the implications for financial stability arising out of that. On my reading of the discussion paper there appears to be no real discussion of credit creation per se. What is talked about, and indeed the whole financial system is defined in terms of intermediation which is a completely different matter, of which you would be completely aware.

So I find it strange that this particular issue receives no consideration. It has been a concern over the years as an academic that there has been almost a hiding of the fact that the principal role of banks is credit creation and the fundamental objective of central banks, such as the Reserve Bank, is to actually regulate and control the rate at which credit is created and the rate at which the money supply grows.

The closest the discussion paper comes to this matter I suppose is to talk about systemic risk, which of course is what we're talking about, but again there is no real detail, and I suppose this is part of - though I think the demystification process could have definitely been helped, and I know talking to a lot of people around the

country who do have some sort of understanding - there has been a reasonable amount of comment by people like Santamaria on credit creation and alternative schemes for actually getting the country up and running again in terms of public credit through the public sector as opposed to the private sector. So people are sort of wondering about these things and are wondering why these kinds of issues aren't subject to consideration by this inquiry.

CHAIRMAN: I don't want to really interrupt but our terms of reference are very clear. Really we have no role at all in monetary policy; that's clearly spelt out in reference 4A of the terms of reference. I can appreciate where you're coming from but I just want you to understand from our point of view.

MR SANDERS: Yes, I understand.

CHAIRMAN: We are not in the Reserve Bank and money supply monetary policy.

MR SANDERS: I'm not stating that for those reasons. I'm stating it for the reason of regulatory controls over credit creation which is the concern that I wish to move towards. Again, within your discussion paper the thrust is that all of the financial institutions are sort of converging in the products they provide, and there is no real distinction between banks and non-banks; I mean the fact that banks have this additional privilege over other institutions of actually being able to expand the money supply through the credit creation process.

In fact on reading part of your discussion paper I was of the opinion that - there was almost something niggling in my mind saying that there are no other institutions who are not banks that seem to be able to be creating credit, and I really don't fully understand the situation there but it does cause me concern. The reason this causes me concern is that the financial system is inherently unsustainable and I say this from the perspective of being an ecological economist who studies the relationship between the real physical economy and the more intangible economy in terms of the financial dimension.

The nature of the financial system is one in which the money supply as a whole is essentially interest-bearing debt to banks, and therefore the money supply grows exponentially at essentially the going interest rate. What you find, if you look at money supply in Australia from 1901 to the present, it's an exponential function running almost on rails at 6 per cent compounding. So you have this

growth in the money supply in an exponential way. Now, this money supply is not wealth in itself but it's a claim on wealth, and wealth ultimately has a tangible dimension. What this means is that you have to basically transform the material dimension of the world from the environment and having environmental impacts at an accelerating and an exponential rate to keep up with the growth of credit or the money supply, to the extent that the claims on wealth, the money supply, doesn't - it grows faster than the physical economy or the physical wealth dimension - you tend to have inflation.

CHAIRMAN: Where you would help us, Richard, is - you know our terms of reference, I'm sure you've read them. We are dealing with the regulatory options, the control of the system. I mean, if you could address specifics that we could get our minds around, that would be helpful.

MR SANDERS: The problem that I have, you see, is I can't make the assumption that you have this preliminary understanding of the interrelationship of the physical - - -

CHAIRMAN: Let's assume we've picked up very quickly what you're getting at.

MR SANDERS: Okay.

CHAIRMAN: Let's try and get the specifics.

MR SANDERS: The reason I'm making this point is that the financial system is inherently unsustainable and the expansion of credit has to be brought under control.

CHAIRMAN: I heard you say that.

MR SANDERS: Now, if we're not going to increase the control over the creation of credit and slow down the creation of credit, then the financial system ultimately has to collapse because the exponential growth cannot go on forever; this is an impossibility in the world. So we're moving into a situation of an increasingly insecure financial system, and the last thing we want to have happen is for the system is to collapse. If it's not to collapse, then the credit creation must be strictly controlled.

Another problem with the credit creation that I foresee is when we move into the era of electronic money. At the moment you have some kind of almost a tangible reserve base, whether it's legal tender or other assets, but as you move into electronic money it seems to me that it becomes increasingly difficult to actually control who electronically is actually creating credit, which to an extent can in fact be

counterfeiting of money. If you're creating credit without the authority or the basis to do it or if you're not a bank for example, then you're actually counterfeiting money.

CHAIRMAN: We had some strong views put to us about this subject.

MR SANDERS: So this again - it seems to me therefore that in this whole area of credit creation there needs to be very much tighter regulation.

CHAIRMAN: What would you like us to do about that? A new era of cybermoney and cybercash and whatever?

MR SANDERS: I would suggest that this thesis that is being presented by the financial institutions and commentators and so on that technology is driving us inevitably towards further deregulation of the system is in fact not really the way to look at it. The way to look at it is to say the new technologies and the ways of getting around the regulation are actually an argument to strengthen up the regulatory system in some way to prevent this happening.

CHAIRMAN: But given that we may not be able to stop the electronic revolution and - - -

MR SANDERS: But you can regulate it.

CHAIRMAN: Who should have access and participate in these new forms of currency and cash and ways of settlement?

MR SANDERS: Well, to my way of thinking the only institutions that should be allowed to create credit - well, ultimately my view is that credit creation and expansion of the money supply should be solely in the hands of the government through the Reserve Bank. That is what I would believe to be the theoretical ideal system. I recognise the political difficulties, but I think in terms of the exponential growth of the money supply we really have to start seriously looking at that option if we're really serious about a sustainable future, and I don't only mean that from - - -

CHAIRMAN: Well, you have made that point.

MR SANDERS: So if it isn't going to be the Reserve Bank, then it can only be the chartered banks who have been granted that privilege to create credit. Nobody else should have the privilege of creating credit, and if any organisation - I don't know if for example, you have a store card from one of the chain stores for example, if they are actually creating credit when they give you credit. I haven't really come to grips with that issue.

CHAIRMAN: Is buying travellers' cheques creating credit?

MR SANDERS: I don't know. But if it is, then it is my view that it should not be allowed to be done. Now, there is no reason why - if a chain store for example wants to extend you credit, they don't borrow credit from a credit provider and then on-lend; in other words intermediate, which is the role. So as far as I'm concerned only banks should have the privilege of credit creation. Everybody else should be limited to an intermediation of credit that has been created either by the banks or preferably by the Reserve Bank.

CHAIRMAN: I would like some of my colleagues to perhaps ask you a question or two, because we are going to run out of time.

PROF CARMICHAEL: Okay, one very quick one. I was reminded of Malthus when you were talking about the system may collapse.

MR SANDERS: Yes.

PROF CARMICHAEL: We must read the same comics. You mentioned 6 per cent growth since 1900. Given that it's been going on like this in this unsustainable way for a century, how come it hasn't collapsed already?

MR SANDERS: Well, you see, the rate at which the growth is occurring, the rate of change of growth in the initial stages is relatively low. I'm trying to think of my mathematics now; I'm not much of a mathematical expert. But the rate of growth, the exponential curve is fairly flat in the initial instance. You know, you look from 1901 up to say about 1950, 1960, it's almost a flat line, it's hardly rising at all. Physical wealth is able to grow in that kind of a manner because you're talking about a function that is virtually linear. But as that function starts to stand up and go vertical, then it's impossible for the growth to continue.

I mean just to illustrate the absurdity of the system, if you started with 6 per cent compounding interest in the year dot on a debt of 1¢, by 1993 it would grow to the mass of the universe of gold, which I mean is an absurdity, what it represents. So that demonstrates the impossibility of a financial system that's based on that premise. So what I'm suggesting is that we've now reached the stage, as we move into the next millennium, where we really have to be reconsidering the way in which financial systems work, and the only way - and I mean even Milton Friedman was arguing this back in 48 in the American Economic Review, that we should be moving to essentially a hundred per cent reserve wherein the government is the creator of the money supply.

MR BEERWORTH: Richard, I don't think you should be too concerned about the fact that we didn't comment specifically on credit creation. We're well aware of course how credit is created.

MR SANDERS: Yes.

MR BEERWORTH: We weren't setting out to write a textbook on banking or on economics, but I think we all did cover credit creation in economics. The prudential chapters of course presuppose that the Reserve Bank as the central bank does precisely what you're worried about. It does keep a close eye on credit creation in accordance with the needs and requirements of the economy. So whilst we didn't talk about it at large in our discussion paper, which would have had to have been 2000 pages long, we are aware of the issue and of course we are very much aware of the fact the Reserve Bank is there every day pitching for us on ensuring that credit creation doesn't run amok.

CHAIRMAN: We've just about exhausted the time allocation, Richard. Is there any final point you want to leave with us?

MR SANDERS: I just want to make briefly a few points on the diversity of the system to further argue in terms of changing the system of credit creation. One of the strange realities is that because the whole money supply essentially exists as debt, if we were to all repay our debts, the money supply would cease to exist, which is an interesting sort of thought. The obverse of that is that in order for us as a nation to become increasingly wealthy we actually have to become increasingly indebted as a whole, and it seems to me that again, as we move into the new millennium, we really need to be thinking of a monetary system which is created free of debt as opposed to - and while that may be beyond your - I don't know if it is within or without your terms of reference but I think that it is something that, in terms of the contextualising of the issues that you are concerned with, is worthy of consideration.

CHAIRMAN: Well, we've been accused of going outside our terms of reference already so who knows where it will end up. But thank you very much.

MR SANDERS: Thank you.

CHAIRMAN: All right, we now have Alan Skyring.

MR SKYRING: Good morning.

CHAIRMAN: Okay, you're clear on what we can do and what we can't do this morning? You're being recorded, there's no privilege, so please don't get into personalities.

MR SKYRING: All right, I won't be doing that.

CHAIRMAN: We would like just a very brief opening statement and try and leave us some time to ask you some questions because that's really where the value in these sessions is.

MR SKYRING: All right, my name is Alan Skyring. I'm a mechanical engineer in private practice and it's on account of difficulties that I came across in this area back in the 1970s that got me interested in this subject.

CHAIRMAN: Okay.

MR SKYRING: In essence what I'd like to do is I would like to follow up on the comments of the last two speakers. I hope I can give you something solid to work on which will address the problems which (indistinct)

CHAIRMAN: Okay, so that's Raymond and Richard Sanders and yourself.

MR SKYRING: Yes, these last two. Now, there was a handout which I did, which I presume you've got.

CHAIRMAN: Are you giving us some joint presentation, the three of you?

MR SKYRING: No, no, I've just come in out of the blue.

CHAIRMAN: Okay.

MR SKYRING: I've been particularly taken by what they've said. These matters I've gone into go right to the heart of those things (indistinct) I've done here. That's actually part of a somewhat larger submission and there's only a couple of points that I'd like to speak to here now.

CHAIRMAN: Okay.

MR SKYRING: I think that sort of goes to the heart of the matter. If I can just draw your attention on page 1 to the start of the second paragraph, matters immediately requiring attention. This bears heavily on your comments of what you say you can't do in your charter. Might I comment that if in fact your charter is so limited, the question arises as to whether you shouldn't be torpedoed here and now.

CHAIRMAN: I can assure you our charter is pretty wide. We're having great difficulty coping with the terms of reference that we have.

MR SKYRING: Okay.

MR .....: We can keep floating, Mr Skyring.

MR SKYRING: The reason I say that is that by doing that we can address the question in a way which would not be otherwise possible, which I will come to at the end of this effort now. Taking up the previous matters, there's a strong interaction effect, from my studies, as I've said, between legal tender money, interest, banking and taxation. Unless you address all these things together you're not going to come anywhere near getting to what the real cause of the problems are, as I see it.

There's been much talk these days on these modern methods of making electronic payments, which is just the latest variation of a development that has been going on for centuries. I'm rather minded to think that the comment that was made earlier that it's an artifice of the financial institutions to get around government control has got a lot to be said for it because if you follow it through, okay, you've got electronic now - this part of the century. Go back into last century, it was cheques. Go back a couple of centuries before that, it was bank notes and all of them were done to get around crown control.

The ultimate crown money of course - and it's bona fide legal tender, a form of payment you're obliged to accept - is gold and silver coin; has been for centuries. If you look at the statutes in this country to this day, it still is, and it seems to me it's high time that was enforced because if you did this there's an awful lot of things you could spring.

MR BEERWORTH: But what the statute does is make sure that you can't demand gold or silver; you must take paper.

MR SKYRING: But therein lies the problem because if you look at - - -

MR BEERWORTH: I'm sorry, I misunderstood what you said.

MR SKYRING: If you look at the statutes - and this has been a subject that I've been boxing on through the courts for 15 years in an endeavour to try to pin this down and to get literally some law and order into the scheme of things. As at federation our only legal tender is gold and silver coin and it still is. The Currency Act is framed that way and what has been my interest was that having taken great interest - I sort of really came on-line on this subject at the time Gough got tipped out in 1975. It always interested me how that was done. It was a

$4,500,000,000 loan, as I recollect it, for a gas pipeline system and the way that got chopped around in the legislature at the time was just unbelievable.

As an engineer interested in major civil infrastructures and development, that seemed to me to be a massive miscarriage of process that somebody really ought to have done something about. They say life begins at 40. Well, that was 5 days before my fortieth birthday but it started me and I've been in that fight ever since and it still continues to this day. By 1985 I'd taken on one of the banks myself, on the interesting matter which brings me to that opening comment made between legal tender money, interest, banking and taxation, in that how was I going to pay my income tax lawfully?

At the time I was doing a job. My credit was good. I got a cheque from my employer and, having got a word from some lawyers on how I wanted to do this, I presented this to the teller at the bank, asking that that be paid in strict legal tender in terms of the Currency Act because I had some obligations that I had to meet lawfully. They couldn't do it so I sued them. When that hit the courts the first thing that happened was I got struck out, and that has been the basis of the argument ever since and it continues to this day.

It seems to me that this is the con which has to be addressed, and it is a con. If you go right back to where it began - from what I can see of it, this was in the 1630s. The first bank note as we now know it was passed in but in those days there was literally the king's money to back it. That got separated in 1694 - the crown (indistinct)

CHAIRMAN: Tell us a little bit about why. I mean, you want to take us back to the gold standard or what?

MR SKYRING: No, what happened - it's the gold standard - - -

CHAIRMAN: See if you can explain it to us.

MR SKYRING: Okay, I'll speak to it here briefly now but in my major submission there's a lot of historical background plus the full text of my recent legal actions in which this is all spelt out.

PROF CARMICHAEL: You need to put it pretty simply to us.

MR SKYRING: Okay. The point I'm about is the point that was made by the previous speaker. Creation of money in any form, as I understand it, is the sovereign right of the crown. So the question I ask - that's supposed to be how it is.

CHAIRMAN: The government runs money supply.

MR SKYRING: Exactly, and the reason for it is to maintain value. This goes right back to the dim days of history when kings was kings and one of the things they found out was that you had to have that in order to get things under way, so that's how we got our currency way back in the - - -

CHAIRMAN: Tell us about the future.

MR SKYRING: Okay, if you look at the physical form of currency, for instance in terms of this in the notions of complex numbers - the higher maths - you have the - - -

CHAIRMAN: I'm surrounded by all these people.

MR SKYRING: Okay, if we translate that into the material and spiritual dimension, which is literally what it is. The physical form of money, be it the gold coinage or your paper or whatever, that's one leg of it but the other dimension is this ideas thing which has got to do with credit and all the bookkeeping function and all the rest of it that goes with it. As I see it, where the problem is - and this goes back to the founding of the Bank of England, which is where - there's a point in history, in our culture anyway, where things got off the rails, and until that's fixed up from there - - -

CHAIRMAN: Tell us what we can do.

MR SKYRING: Okay, what's got to happen, as I see it, is that firstly all money creation in the dematerialised form of credit, which is what I regard as - that's the book entry stuff - that has to be taken out of the hands of private outfits. There's no if's, but's or maybe's about that. The question arises in respect to the form of banks. I believe it is quite improper that we have joint stock companies operating in this area, in this manner.

CHAIRMAN: All banks to be government owned?

MR SKYRING: I don' think there is any other credible option. I think it has to be that because you are dealing with the sovereign right of the crown. The reason for this is that your whole control mechanism then, rather than the indirect effort that we've got at the moment - the Reserve sort of operating through these private outfits - literally becomes then in the legislature itself. Coupled with this we have to have a properly drawn set of national accounts. As I understand the show, and I have great difficulty in this area - - -

CHAIRMAN: You're not alone.

MR SKYRING: A properly drawn set of accounts involves a balance sheet which spells out the assets of the nation, what they're

worth and, more importantly, who holds title to them. Under the present deal you'll find that if you do that accounting properly the banks have got most of it through mortgages, and that's something they shouldn't have. People ought to have their own property.

CHAIRMAN: They're pretty worried about losing their market share of property. I have to tell you, Mr Skyring, they're not feeling very confident.

MR SKYRING: Stuff their market share. It's a question as to whether they should be in the business in the first place anyway.

CHAIRMAN: Okay.

MR SKYRING: That's basically what I'm about. The set-up would be that rather than have the practice in the legislature at the moment where we have a budget that talks about what we're going to pay in taxes, what that ought to be directed is in what direction is the national effort to be directed? What are we going to do? On the basis that there are only so many of us, even with all modern aids and with a given scale of values for work, we could only do so much work and maintain the value of money. That's the ultimate high-level deal which has to be achieved. To get that, firstly you've got have a departisan legislature.

CHAIRMAN: I think we've got your first two points very clearly.

MR SKYRING: Right, okay. Now, the question is how then might one go about this? If I just mention briefly, in the paper itself my presentation is the first bit where I just give you a background, then there's about three pages where I give the historical background as to how I got into what I did and why I think what I do, and there's all the back-up documentation that'll give you all the detail on that. So I won't take you up here with them. Starting about halfway down page 5 I get into the detailed effort as to how it all might be done. I won't go through that here now but that's the - - -

CHAIRMAN: There isn't really time and I'm conscious that if you talk to us, these gentlemen are not going to ask you a question. You haven't got much time left.

MR SKYRING: Quite. Now, the point that I want to come to is how can one unspring the present set-up and get on to this little lot? It's all got to do - again coming back with this legal tender question - the function of legislation.

CHAIRMAN: Okay, we've got that.

MR SKYRING: Are our representatives in that legislature properly there because the way I see it, your presence here - now, the inference

is that you are properly constituted legally. It is of the nature of these things that this has to be.

CHAIRMAN: Sure.

MR SKYRING: It is that that I question.

CHAIRMAN: Right, you - - -

MR SKYRING: No, no, no, let me - - -

CHAIRMAN: You can make representations, but not to us.

MR SKYRING: No, but the point I would make is for you to take up higher because, okay, you get your authority from the Treasurer. I've had a scheme - an effort in the system since 1990, basically challenging the legality of the last three federal elections on the interesting point as to whether in fact anybody is properly nominated. This goes to the heart of the matter concerning your legal tender question because if in fact - because of this screwed up values, what we've actually got operating here is two legal systems.

We've got the Magna Carta-based common law and we've got the law merchant. In fact what's actually happening when you get into the legal system - this is what I've found out from my efforts of the last 15 years - the format is the common law based on Magna Carta.

CHAIRMAN: Is this set out in this document?

MR SKYRING: Yes.

CHAIRMAN: Okay, why don't you leave that with us?

MR SKYRING: Okay.

CHAIRMAN: If you're challenging our fundamental legality of our inquiry, we'll have a look at it.

MR SKYRING: That's the essential point that I would seek to do because that'll - - -

MR BEERWORTH: There's nothing to challenge. I'll acknowledge we are an informal committee. We're not set up under any statute. The chairman said at the outset we have no such privilege.

MR SKYRING: But no, the point - - -

MR BEERWORTH: We're just an informal committee.

MR SKYRING: Okay, yes, but this is part of the problem because you're being set up in effect under the auspices of government, which you are, there's a certain expectation within the community that you will be able to - - -

CHAIRMAN: We're here today listening to the community.

MR SKYRING: Okay.

CHAIRMAN: We're going right around Australia.

MR SKYRING: Right, and that's all fair enough but the point I'm trying to get at is this concept of ultimate legality which comes back to this matter of the currency. The present monetary system everybody thinks, genuinely believes, is proper and correct, which is why the banks take the actions that they do. It is my view that it's based on a monumental con - quite wrong.

CHAIRMAN: Alan, I'm going to have to bring it to a close because I've let you go over time and I think we've got your views very clearly, and I thank you for all the very considerable effort you've put into that document. Thank you very much.

MR SKYRING: Okay, you're welcome. Good on you, thank you.

MR BEERWORTH: I don't have the attachments to your affidavit, by the way.

CHAIRMAN: I've got them all here.

MR BEERWORTH: That's very good.

MR SKYRING: Thanks very much. That's the formal submission. There's a fair bit of it. There's only one set there.

CHAIRMAN: Thank you very much.

MR SKYRING: Good on you, thank you.

CHAIRMAN: Thanks, Alan.

CHAIRMAN: We now have Simon Cleary from the Legal Aid Office, Consumer Credit, and do we have someone else with you, Simon? Steven O'Reilly from Queensland Law Society. Randal Dennings, sorry. Simon Cleary and Randal Dennings, ladies and gentlemen. You know the drill. If you wouldn't mind just outlining your names for the record and who you represent. Thank you.

MR CLEARY: Simon Cleary from the Legal Aid Office of Queensland and I'm a solicitor with the Consumer Protection Unit at the Legal Aid Office, which is a specialist unit there.

MR DENNINGS: Randal Dennings is my name. I'm a partner of the law firm of Clayton Utz, in this case representing the Queensland Law Society.

CHAIRMAN: Okay, thank you. Simon?

MR CLEARY: Thank you. I've prepared an outline of submissions which I handed to Shauna as I came in. They expand a little bit on some of the particular points that I'd just like to raise here. The reason why we requested the opportunity of making a presentation was, having read some of the discussion paper in respect of the consumer protection matters, some of the points outlined there are of some concern. We wanted to address some of those.

The Consumer Protection Unit for whom I work gives advice and represents a large number of consumers in disputes with, in particular, financial institutions. The majority of those are in dispute with consumer credit providers, but also one of the insurance companies and other financial institutions who are involved, for example in deposit accounts. The Consumer Credit Code in relation to the work that we do against consumer credit providers is a fundamental document and the reason why it is so fundamental is that it acts to ensure that there is a truth in lending philosophy that underpins the dealing of all credit providers.

That particular philosophy is fundamental to the whole code. In relation to a way of enforcing that particular philosophy the civil penalty is one of probably three mechanisms which are used. The other two are criminal penalties as well as licensing or negative licensing systems. The civil penalty seems, in the discussion paper, to have been under some attack from some of the banks and I want to address some of that. The civil penalty is the most effective mechanism that we've seen in encouraging this culture of compliance and

encouraging credit providers to comply with the disclosure provisions of the code.

The criminal penalty is less effective because of the resources that are required through government agencies to enforce it. The negative licensing system operates in the same way. It requires government agencies to devote resources to enforce that. The civil penalty doesn't require the same government resource levels. The civil penalty, under the act, has been crucial to this culture of compliance and under the code it's envisioned that it also will be. Under the act there were a number of criticisms of the penalty and a lot of those criticisms went to cost and went to the difficulty in complying with some of the requirements of disclosure.

There were arguments that the requirements were trivial, of a trivial nature, and that for that reason the whole mechanism failed. Under the code many of those arguments have already been addressed; many of the arguments of the credit providers have been addressed. The civil penalty mechanism is no longer automatic, as it was under the act. It's been capped so that the size of the penalty is capped at $500,000 nationwide. In the past the size of the penalty had no such cap.

Thirdly, where a credit provider has committed nationwide breaches, in the past it was necessary for the credit provider to bring applications in each jurisdiction. That's now changed. There's only the need to bring application in one jurisdiction and the determination of that particular occasion is then registered in all the other jurisdictions, so those arguments about unnecessary legal costs and unnecessary legal applications have been met to a very significant degree by this mechanism.

Fourthly, the number of breaches of the code which attract a civil penalty have been significantly reduced and this in turn has met some of the arguments of the industry that trivial requirements of disclosure require them to bring the necessary applications, so there aren't as many disclosure requirements that occur with a breach. Fifthly, the code itself contains room for variances, so that if there are trivial misdisclosures of an annual percentage rate, for instance, then if that misdisclosure fits within a particular variance, then there's no need to bring an application for a civil penalty.

CHAIRMAN: How do you mean no need?

MR CLEARY: If the misdisclosure, for instance, and then the percentage rate falls within the variance which is allowed by the code, then there is no breach of the code, so therefore no need to bring an application. Sixthly, the Uniform Consumer Credit management committee which has been set up as something of an overseeing body is in the process now of publishing guidelines and those guidelines will go a long way to guiding industry about what practice, what documentation is or is not allowable, hence industry won't be in the position where it was in the past of travelling blind, if you like. We're now going to be guided by this uniform committee.

A seventh point is that a court itself when it's determining the size of the penalty on any application has the discretion to take into account a whole range of factors such as inadvertence compared with deliberate misdisclosure or non-disclosure of key requirements. I guess in a nutshell they're some of the issues in relation to a civil penalty. I was also concerned that there were some comments about the contract reopening provisions as well and that the ABIO submissions seemed to be indicating that that was contrary to disclosure and the philosophy of truth in lending.

We would certainly oppose that sort of position quite strongly. We see, day in and day out, cases of borrowers who have quite simply been ripped off. Examples of that are legion and they're cases where they haven't been given the ability to make a free and informed decision. That ability has been taken away from them by the circumstances in which the contract was entered into. For example, somebody goes to a used car yard to buy a car and is sold a credit product at the same time.

The agent or the dealer of the car makes misrepresentations about the costs of the credit, doesn't provide the person with the documentation in order for them to make the decision, doesn't allow them time to read through the documentation and the borrower signs a document which is legally binding without having been given the opportunity to make a free decision. Fundamentally the contract reopening provisions are there to meet that type of a situation. For credit providers who carry out good banking practice or good business practices, the contract reopening provisions are of absolutely no consequence at all.

They're fundamentally the two areas I wanted to raise and of course I'm open for any questions at all that you might have.

CHAIRMAN: You'll be putting in a supplementary submission?

MR CLEARY: That's right, I've handed something to Shauna.

CHAIRMAN: Okay, thank you.

MR DENNINGS: I'm representing the Queensland Law Society, who has made a submission to you, picking up the submissions of the Law Council of Australia and also picking up some other points as well.

What I would like to do today is to really focus on one issue which doesn't seem to have been given a lot of airing recently and that particularly looks to the issue of self-rectification onto the code. I really want to say three points and if I may, hand up an outline of submission.

The three points that I want to make are balance, cost and competition. From reading the material produced by the inquiry it becomes evident that several submissions have been received by you which look at the high degree of cost and I would say fear in the mind of credit providers when considering the impact of the Uniform Consumer Credit Code.

CHAIRMAN: A degree of agitation.

MR DENNINGS: And agitation. The suggestion that was made by the Queensland Law Society, and indeed others, some time ago would be that there should be a self-rectification procedure available under the code. In fact it was included in earlier drafts of the code and then taken out later on. In my view and the view of the majority of the Queensland Law Society's committee of security and finance, self-rectification is a good answer to a lot of the issues that have formed the basis of the submissions made to you, and I suggest this for the three issues that I have discussed.

(1) Balance. It permits the interests of consumers to be protected yet at the same time removes a degree of risk that is inherent in the notion of civil penalty. It removes the degree of risk since credit providers would be in certain instances given the capacity to self-rectify without going to the courts but on the basis that, firstly, you notify the debtor that a problem has occurred, and secondly, you must also notify the consumer affairs agency of the relevant state. So that if that agency forms the view that the breach occurred intentionally or recklessly, then it can take action or indeed it could permit the debtor to

take action to recover any loss or damage it sustained and impose civil penalty, but the condition that the credit provider would have before it could self-rectify is that any loss or compensation must be fixed up with the debtor and, further, that it must fix up not just that one debtor but anyone else that it's got within its portfolio. So, as I said, balance is the first reason.

The second is cost. I've practised in this area for a little over a decade and have found, even under the new code with less key requirements, etcetera, that it is a very difficult task and a complex task indeed to draft contracts that can clearly be said to comply with no risk, and in fact I go so far as to say it's not possible. The cost if you get it wrong is significant, not only in court time, not only in tribunal time, not only in legal costs or other advisers' time and cost, but also in the administrative time that it takes out of the financial institution in getting all the evidence together, as well as the market damage that it's done and the loss of strategic direction it's affected. Having been involved in those cases, the cost is immense.

The ability to self-rectify minimises that cost in minor matters. As I said, if it's intentional or reckless, well, then rightly there should be a major inquiry into the matter, but if it's a minor - and keep in mind that the vast majority of cases that have been before the Credit Acts, and I suggest also come under the code, would involve on balance minor matters relating to disclosure - on balance.

The last point is competition. Many of the clients for whom we have acted in the past - I am speaking personally now - have been competing in the retail marketplace. With the advent of the Consumer Credit Code they are no longer competing in the marketplace because they can't afford it. Can they not afford compliance costs? So here you are.

CHAIRMAN: Some examples?

MR DENNINGS: Many - retail financiers, the small corner shop out west that used to have a slate system where people could buy their goods and services on tick. They can no longer do that because it will be regulated credit. Now, the cost isn't in setting up the compliance system; the cost is that they can't afford the prudential risk or systemic risk that would follow from it. What that leads to or could lead to in my view is a clearance of the market, so that only those that have a capacity to heed the risk costs can take that on board.

Now, in the outline that I've handed up I've included at the back page, back two pages, the submission that the Law Society made on self-rectification. I've also included in the outline a degree of dealing with some of the issues that Simon raised and I'm happy to answer questions on that.

CHAIRMAN: Thank you. Bill?

MR BEERWORTH: Chairman, the submission seems reasonable and, Simon, I wonder if we could have your reaction to the society's proposal.

MR CLEARY: Certainly. I think that fundamentally, and again from an in-principle perspective, it changes the direction of compliance, and it changes the direction from compliance at the point of disclosure to the implementation of compliance systems by credit providers which will allow them to quickly pick up errors once errors have been committed, if that shift is a fundamental one.

It's focusing not on prevention of the problem but on the cure and it's the prevention which the legislation is trying to deal with at its very very heart, and a system must be put into place which allows borrowers the opportunity to make an informed decision as to the credit product that they're about to buy. In order to make that informed decision they must have accurate disclosure of the terms and conditions of that contract.

MR BEERWORTH: Is that reasonable, as Randal says, to permit some power of - or to cure inadvertent mistakes and errors if there was a consistent pattern of behaviour? Clearly what he has in mind is that a tribunal can make appropriate orders. Doesn't it seem fair to allow the curing of minor mistakes or relatively light mistakes?

MR CLEARY: I guess Randal's point - that the majority of applications under the Credit Act were of a minor nature. I guess that to some degree turns on what your perspective of minor is and I don't entirely agree with that interpretation of things. It's a fundamental concern to us who are advising and representing consumers that - situations such as occurred in the State Bank case, which was a particular civil penalty application where the State Bank committed a range of errors, probably the most significant of which was the overcharging to the tune of millions and millions of dollars a number of consumers, a situation where - and in that case it was inadvertent. I don't think there's any argument at all that the bank was deliberately trying to - - -

MR BEERWORTH: It was an error, a genuine error.

MR CLEARY: It was a genuine error. It was done inadvertently. Nevertheless it was inadvertent and any situation where a mistake of that magnitude, albeit inadvertently, might be able to be dealt with without an open court or tribunal hearing and an open and public airing of the issue, I think would be - - -

MR BEERWORTH: But again, to be fair to Randal, I took him to say that where you had negligence to that degree, you wouldn't fall into the exception. That seems perfectly reasonable.

MR CLEARY: I don't know the detail of the proposition.

MR BEERWORTH: I am sorry, let's put the general proposition. If you and Randal could agree on the words, is it reasonable to have some curative mechanism of that nature where you had genuine error or minor discrepancies, to save the whole thing going to a tribunal and wasting a great deal of time and money?

MR CLEARY: I think the dangers would be too great. I think the dangers of shifting the focus of the type of legislation - - -

MR BEERWORTH: So you think it's an absolute rule, an ironclad rule, and everyone gets caught up in it whether it's an innocent error or otherwise?

MR CLEARY: I think that the way the code has been drafted now is that in situations where there are smaller errors and innocent errors, there is room for the court and the tribunal to take that into account and the setting up of the Uniform Consumer Management Committee which I would envision would be dealing with this type of problem at the request of credit providers and can raise as a potential issue a particular drafting suggestion - that the management committee will be in a place to propose guidelines.

MR DENNINGS: No, I don't agree with that, with respect. I don't think that the management committee is a function of SCOCA. It is setting up consultative bodies for whom it can consult but it certainly won't be in a position to be able to determine the sorts of issues that we're discussing here. In my view it's unfortunate, a missed opportunity, and something that we have an opportunity to fix up, that the ironclad rule that if there's a mistake, the only person who is enriched by it is the lawyer. It's a bad rule. It seems to me there's got to be an opportunity where people, like credit providers who have made a mistake, can rectify it by themselves.

PROF CARMICHAEL: I think my position on this is that if you're dealing with a very simple piece of legislation, I would agree with Simon's

position. It should be on getting it right in the first place, but this is an incredibly complex piece of legislation and we've seen in the past these situations where a whole industry stands to be wiped out almost overnight because of some incredibly trivial little slip of the pen putting down an acronym instead of a full name. We're trying to move away from that with the new Uniform Credit Code to fix up some of that and yet some of the mechanisms seem to have been left in there from the old processing. It just would seem to have been logical to go a bit further.

MR CLEARY: I think that example of having a credit provider go down because of a particular breach wouldn't occur under the code. One of the things that a court or tribunal must have compounded is the prudential standing.

PROF CARMICHAEL: If something like that is picked up, it should be easy to just fix it with in a sense a stroke of a pen if it's an inadvertent and inconsequential omission, rather than having to go through a legal process.

MR CLEARY: I guess I wonder how long and detailed that legal process would be if it was that simple and that clear an example and that from our point of view the dangers associated with putting in place a self-rectification situation would be too great. They would outweigh those possible benefits.

MR BEERWORTH: Even though the consumer gets the benefit and it's disclosed to the consumer?

MR CLEARY: In terms of broader consumer benefit, in terms of individual cases, I'm not sure that that's right.

MR BEERWORTH: As I read his drafting, the consumer would be fully refunded any overcharges or anything like that of course.

MR CLEARY: With a system of self-rectification I think there'd be dangers though of credit providers actually sweeping cases underneath the carpet. The systems of self-rectification I've seen wouldn't deal with that adequately. It would be a temptation to a credit provider to deal with it informally rather than to bring an application.

CHAIRMAN: You may not have heard Philip Elliott earlier refer to a number of - adding as much as 100 basis points to the cost of a loan as a result of the UCCC. Do you have any view about that?

MR DENNINGS: Yes, the costs that I have heard quoted by industry sources for the Credit Act and the Credit Code I consider to be conservative.

MR CLEARY: As far as the consumer movement generally goes, and I'm certainly not speaking for the movement now, it's always been very difficult to get access to cost from industry and it's been very difficult to analyse that and some of the fears that I've heard, I guess I would question those figures.

MR DENNINGS: Perhaps if I might just address one issue that came out of what Simon said, if I may?

CHAIRMAN: Sure.

MR DENNINGS: And that's on the issue of changing the focus of inquiry. I've personally been involved with setting up compliance systems with credit and the Credit Code, and regardless of what system you've got where you've got a civil penalty system, where you've got a civil penalty system with a self-rectification system plugged in the end, anyone who's going to rely upon a line of defence after settlement is crazy because you just expose yourself so greatly to the idea of recklessness and to the media damage that would follow definitely from that, so I'm not sure about that.

The other point is that the reason why people in my view aren't getting into the industry arises from fear, and that fear translates for the current phase of playing it safe. If we're wanting to have innovation and global competition, then we should be having people who know where the game lines are, and if things change then they should be able to be in a position - or if they are wrong - without complementing the ethic of compliance, they should be in a position to turn quickly.

CHAIRMAN: That's fair comment.

MR CLEARY: Just one comment, and it's more of a general comment, that the industry of credit provision is certainly dominated by a number of credit providers but they're not the sole players. There are a number of smaller credit providers and they're the ones that more often than not are engaged in the unscrupulous behaviour. They're credit providers who aren't incorporated, for instance, credit providers such as City Finance Loans and Cash Solutions. There is a particular credit provider operating around the Gold Coast, purely a Queensland operation but providing money at rates of 60-odd percentage.

In this whole debate I guess on one hand we can look at the banks and the large finance companies and other credit providers, but the role of those smaller credit providers who can do untold damage on human beings' lives shouldn't be lost.

CHAIRMAN: We appreciate that. Are there any other questions, gentlemen?

MR BEERWORTH: Has the society produced a detailed criticism of the new legislation - or is it too early for that, I suppose?

MR DENNINGS: No, we have produced that and that's been submitted to the council, the management committee, but in that we've simply flagged - amongst those issues they've simply flagged a concern once more on that.

CHAIRMAN: Thank you very much, gentlemen. That, ladies and gentlemen, brings this morning's proceedings to a conclusion and I would thank everyone who has contributed and thank everyone for their attendance. It's been most helpful to the committee. Thank you.

AT 1.25 PM THE INQUIRY WAS ADJOURNED UNTIL
WEDNESDAY, 11 DECEMBER 1996