FINANCIAL SYSTEM INQUIRY

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MR W. BEERWORTH, Member
MRS L. NICHOLLS, Member
MR G. SMITH, Secretary

TRANSCRIPT OF PROCEEDINGS

AT PERTH ON WEDNESDAY, 11 DECEMBER 1996, AT 10.03 AM

Continued from 10/12/96 in Brisbane

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CHAIRMAN: Ladies and gentlemen, good morning. It's very pleasing to see you all here. My name is Stan Wallis; I'm the chairman of the Financial System Inquiry. I have with me today Mr Bill Beerworth, Mrs Linda Nicholls and Greg Smith. Greg is the secretary to the inquiry.

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

To assist in our task the inquiry has received and examined over 250 submissions; I think we're through about 270 as of this morning. We have also published this discussion paper in the last week or so which essentially outlines the options as we see them and, as the very submissions have laid them out, the options for regulating the financial system. We do have here this morning copies of the terms of reference and copies of the discussion paper if anyone would wish to look at those.

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 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 this reason I would ask all participants to avoid making adverse comments about any particular individuals or organisations.

We have participated in public consultations in Sydney and Brisbane; this is our third day of hearings or consultations and we will be moving around the rest of the country over the next few days. We are conducting the hearings in a very informal way: we simply ask the participants to come up to the table, make a statement and then the questions and discussion generally flow. Our first participant today is Dr Hilda Turnbull and I think, Dr Turnbull, you are by yourself or - - -

DR TURNBULL: Yes.

CHAIRMAN: Yes, I wasn't sure, but if you could join us, please. We would ask each participant at the outset to simply state their name and the organisation they represent, if any, largely for voice recognition

purposes. We would be very pleased to hear your remarks, Dr Turnbull, and I'm sure the committee will have some questions. Thank you.

DR TURNBULL: Thank you. My name is Dr Hilda Turnbull. I'm the member of parliament for the seat of Collie in the Western Australian Legislative Assembly, and today I'm making a representation on behalf of the National Party of Western Australia. I'd just firstly like to ask, is there a time limit?

CHAIRMAN: I think all participants should have been advised of the allocation of time. We have scheduled 20 minutes for your presentation.

DR TURNBULL: Thank you very much.

CHAIRMAN: So I suggest you confine your remarks to 5 to 10 minutes, if you can - - -

DR TURNBULL: Yes, that's right.

CHAIRMAN: - - - if you want to have some useful interchange.

DR TURNBULL: That's right. That is what I expected. Thank you very much.

CHAIRMAN: Sorry if that hadn't been made clear.

DR TURNBULL: That's okay. Now, today I'm following up on a submission that we made to your inquiry and I'd like to start first by just reading an item from the terms of reference in the appendix, page 347. It says that:

> The inquiry will make recommendations on the nature of regulatory arrangements which will best ensure an efficient response and competitive and flexible financial system. The purpose for this is to underpin stronger economic performance consistent with financial stability, prudence, integrity and fairness.

Now, in the discussion paper - we have read the discussion paper and we have looked at it very carefully, and we don't really see it addressing the issue which I'm going to raise today. It doesn't address it specifically. But our contention is that our proposition does fit within the terms of your reference, and it particularly affects your reference when it comes to specifics.

Where you've got specifics 1(c), "The economic effects of deregulation on growth, employment and savings"; point 2(d), "Consumer needs and demands"; point 3(d), "Establish a consistent regulatory framework which will be similar across financial functions, products or services" - and one of our contentions is that we are discussing the issue of a financial product and the regulation of that

product. Finally point 4(a) where you are addressing the objectives or procedures of the Reserve Bank in its conduct of monetary policy.

So my remarks today follow on the submission that we made, and I'd just like to clearly spell it out, that the Wallis inquiry does deal with all aspects of the financial services as I said. It does address depositor regulation, service delivery, information transfer and prudential regulations. But as I've already mentioned, it doesn't address the issue which we want to address, which is the protection of the borrower in relation to overservicing.

Your discussion paper does deal with the issues of protecting the borrower in relation to supply of information and consumer awareness, but as I want to argue this morning, following what I read out from the terms of your reference, we feel that the issue of the overservicing of the borrower is very, very important, and that it should and can fit within the terms of your reference.

Like any service organisation lenders are constantly making their products more attractive and innovative. At a time of low economic activity the market becomes saturated. Competition for customers is fierce, particularly in the area of residential mortgage-backed securities as the Reserve Bank gives capital concessions for this type of lending; that is to banks. Due to the competition lenders have taken to bundling the debts and rewriting the debt over greater maximum periods, and so allowing the customers the ability to repay the loan.

On the books this debt looks good as it does have an asset backing and there does appear to be a demonstrated ability to repay. But this is very likely to cause a major headache for the borrower in the long term as many of the assets bundled will lose their effective usefulness long before the money borrowed on them has been repaid.

From the financial institutions' point of view the problem they face when they try to invoke a higher quality credit portfolio by ensuring that the loans are repaid over an asset's useful life, is a risk of losing their customers and therefore losing their profits. Further problems will be highlighted if an upturn in the interest rates occurs where not only the affordability of these loans is decreased but the asset replacement will also need to occur, thus increasing the risk of default or personal bankruptcy - and I want particularly here to draw attention to an item which was in the Western Australian newspaper, 10 December, and it follows on, "A release of the Reserve Bank's

figures on debt" and I will turn to that when I finish - that this problem of the changing of the interest rate, whereas at the moment it's low and then it could be changed to higher, is a very great problem to the borrower.

We contend that to solve the problem a consistent approach to personal lending for all lenders should be put in place; that is, all lenders should have to use the same method of calculation for debt servicing, particularly in relation to debt service ratios and to the maximum length of time over which a debt can be structured - the repayments can be structured.

Maximum debt service limits should be determined by the lending bodies so that they are consistent from lender to lender. If a customer transfers a debt from one institution to another, the repayment of that debt should also include a letter to say what the purpose of the loan was originally for and what are the remaining terms of times for the loan. The new institution should then only write the same type of facility over the balance of the remaining term, and that of course excludes items if the asset was to be sold.

Effectively, this will stop the customers jumping banks to refinance debt and so focus on debt reduction. It will stop unscrupulous lenders bundling and refinancing or, in other terms, "lending" people into trouble. Lenders therefore would be required to deliver a product on price and efficiency, something this inquiry I'm sure is trying to achieve. It will also, I believe, have a tendency to make the customer market more fierce, as the personal market will be limited in its ability to repay, not to the lender's ability to move money, that is, to create more sales. It would then redirect a lender's resources to the business area, where rates are considerably higher than in the personal area. So you can see that this change in the focus - - -

CHAIRMAN: Are you saying rates are higher in the business area?

DR TURNBULL: Yes. So this change in the methods of personal lending would actually be not only of benefit to the borrower, it would also be of great benefit to Australia as a nation. It would focus on business lending, not on personal consumption. It would give the Reserve Bank another mechanism for controlling consumption without having to move the interest rates, which is one of the ways - the major way in which the Reserve Bank currently operates.

Of course, when you move the interest rates, you have a great impact on the people who already have loans, whether they are personal loans or whether they are business loans. So if the Reserve Bank had the ability to set a level for the personal debt servicing issues that all the lenders would follow, then the Reserve Bank would have more control over how much is spent and how much is saved, and I think that we would all agree, from the many articles that have been written and the great concern which is being expressed at the moment, that the increase in personal debt is one of the greatest problems that Australia has to face.

There's one set of figures which was produced from the Bureau of Statistics report, household expenditures 1993-94, and which apparently is even worse when you analyse the latest ones. This set of figures shows that in Australia, if you cover all household types, couples, couples with dependent children, of one, two, three or more children, etcetera, and you take the average wage compared with the total requirements for living, income tax, mortgage repayments, superannuation, the total of that, there is only one sector in the whole of Australia's households which is not on the average spending more or committed to more than they actually have coming in, and that is a very small percentage of all the households of Australia on average. It's only 3.2 per cent of all households. All the remainder have a negative each week over their average income, over their average expenditure, and the figures from the bureau does show that it is only the top 20 percentile who actually are in front of their income when it comes to the end of the week. Even when you take the fourth quintile, you still have an average expenditure of $1200 a week, and an average income of 1158.

So this issue is a huge problem to Australia. I contend that it does fit within your inquiry's realm. It is an issue which I feel that you should be addressing, and it is a method of management which is not going to affect regulation very greatly. Your inquiry guidelines do say that you can address the issues of regulation.

So to conclude, I'd like to say that what we're proposing is that you recommend that it be a regulatory requirement that there be a debt service ratio and a maximum debt term limit for personal debt, and how this would be applied we're not sure, but in the very very harsh competitive world of banking and financial institutions at the moment, we don't really see that this can be a voluntary code by the

financial institutions. We feel that this does have to be a regulatory requirement. We also state that we feel that this would be of benefit to the Reserve Bank in managing our situation in Australia.

CHAIRMAN: Thanks, Dr Turnbull. Bill, do you want to head off?

MR BEERWORTH: Thank you, Mr Chairman. Dr Turnbull, you mentioned that you were appearing on behalf of the National Party. Is that just Western Australia or is this national policy or is it - - -

DR TURNBULL: No, it's just Western Australia at the moment.

MR BEERWORTH: Right. One thing I didn't quite understand. You're concerned of course about imposing a maximum debt limit, but only on personal borrowings.

DR TURNBULL: Yes.

MR BEERWORTH: Are you concerned about the position of personal borrowers who over-extend themselves? Are you concerned about excessive credit generally, or are you concerned about the institutions which may be impaired by excessive lending and the need to enforce debt?

DR TURNBULL: I'm concerned particularly with the tragedy that occurs in the individuals' households.

MR BEERWORTH: The personal - - -

DR TURNBULL: But we're also very very concerned from the state of the nation in the ever-increasing debt for Australia. Now, when you take into account the personal debt component of that, it's nonproductive. I know it's consumer, and it helps to keep the economy moving around, but in terms of a debt, it's a debt which has no benefit to Australia in that it's not productive.

Now, I think that an example of where you see it is - if I can just quote this article - is that:

> The Australians are continuing to take advantage of the low inflation environment and to binge on debt.
>
> The Reserve Bank figures released yesterday show that credit growth is still running at above 10 per cent compared with a year ago, and of that the consumer credit is a very large component. On the personal debt situation, that is also still at more than 10 per cent, and it has reached $50 billion for the year ending 31 October, so in terms of Australia's national debt, a $50 billion component is an important component of the nation's debt.

CHAIRMAN: The driver of your submission is to protect the individual?

DR TURNBULL: Yes.

CHAIRMAN: That's a point we need to appreciate.

DR TURNBULL: Yes.

MR BEERWORTH: I suppose one concern I might have, Dr Turnbull, would be that if we imposed really what used to be called quota restrictions, and we used to have restrictions of various sorts of that nature by the Reserve Bank on the banking system, what tended to happen of course is that when banks were limited effectively on the amount that they could lend and the type of lending they could make, they only lent to the most qualified borrowers, and the people who missed out in being able to borrow tended to be the poorer segments of society, and also they had to borrow at higher interest rates.

If we imposed direct quotas, which I think this would tend to do, you would I think lose competition in interest rates for personal lending to a degree, and I suspect that the poor might tend to suffer at the ability of those with higher collateral, but that's just an observation.

DR TURNBULL: I think the poor are suffering now. I think the poor are suffering in that their debt levels are too high. Those poor who are not suffering from high debt levels are doing their own financial management in a very prudential way. Those poor who are overcommitted are suffering anyway, because their debt level is just increasing and increasing, and then they have to refinance and they run into this issue of bundling, and the bundling then means that they have - as the Commonwealth Bank says, you put your car on top of your house and your boat on top of your car and your fridge on top of your boat, and what the heck? By the time the fridge is worn out, you've still only paid the interest payment. So it is really a very false issue, and I have discussed this with people whose incomes are not very high, and it is a very very severe social issue.

In fact from my point of view in that I'm a doctor of more than 25 years' experience, I would say that debt and the inability to deal with debt is one of the biggest reasons for family breakdown and social disruption in our society.

CHAIRMAN: Thank you, Dr Turnbull.

MRS NICHOLLS: Thank you, chairman. Dr Turnbull, I would like to take the discussion in a slightly different direction. In our consultations in other cities we have had views put to us by financial advisers and planners talking about how the advice industry is changing and how

increasingly it may be difficult to separate financial advice from the sales of financial products.

Now, one view that some financial planners have put to us is the requirement that now exists on planners, that is that they must be cognisant of an individual's entire situation when offering advice, recognising their needs and acting in their best interest, is an onus that needs to be extended more widely to include those who sell both investment and loan products.

You have been talking about - suggesting that the imposition of fixed ratios would be desirable. Could I ask you to comment on the suggestion that there be an onus on people promoting products to take into account an individual's entire circumstances.

DR TURNBULL: Yes, I agree with that entirely, and that is the ideal world and any responsible bank or any responsible lending institution would say that they do that, but when it comes to the actual practice and when it comes particularly to a very, very returns-driven financial environment, such as the one we're in at the moment where the banks do and the lending institutions do have a fair bit of money to lend, then you have got an imperative on the salespersons to get the very maximum return, and unfortunately regardless of what the ethics are or what principles they espouse, they are inclined to cut that, or they are inclined to push the product. What you're saying is that there shouldn't be this pushing of the product on the borrower - but there is.

MRS NICHOLLS: You would be aware that currently the onus that is - the legal onus of financial planning that rests with advisers is not extended at law to salespeople.

DR TURNBULL: That's right, yes. I have actually had a lot of experience with financial planners in that I helped to set up their organisation in Western Australia about 10 or 15 years ago when they first came in to - well, this is the financial counselling system which is out there to give free advice particularly to the sort of people that we're talking about, the sort of people who could overextend themselves. I agree with you entirely on that statement.

MRS NICHOLLS: Thank you.

CHAIRMAN: Could I ask you just another variation, Dr Turnbull, and you may have thought through it? If a system such as yours was introduced do you have a concern that there would be another sort of marketing lending that would be dominated by more unscrupulous

people outside the regulatory framework who would actually perhaps tend to exploit some of these people even more fully?

DR TURNBULL: Yes, I do. I do have that concern for sure, and in national policy terms you don't quite know whether it would be better to have the $50 billion debt where you can partially measure it and you can partially see it, or whether it would be better to have that driven into the loan sharks and perhaps the money launderers. But I think that in terms of national policy, really, it would be better to have that debt out in the open. It would be better for the consumers, the vast majority of consumers, to be educated into what their responsibilities are.

If there was a responsibility, if there was a regulatory requirement then people like the Commonwealth Bank wouldn't be able to go out and advertise. There would have to be this truth in advertising, and I can assure you it's not just the Commonwealth Bank that advertises in this fashion either. I just should say "the banks". Sorry about that. There would have to be some truth in their advertising that there is a limit on how much you can bundle your debts and over how long a time you can stretch that out.

CHAIRMAN: We're drawing near the end of the time, ladies and gentlemen. Did you want to cover anything, Greg, or not?

MR SMITH: I would just like to ask one question actually: does your proposal mean the abolition of revolving credit?

DR TURNBULL: No, it doesn't, it just says that you should - that the terms and conditions of the previous loans are known or have to be known to the lender which is being approached to refinance or to bundle.

MR SMITH: Yes, so you don't want to apply a debt service ratio to the fact that I might have used my Visa card this morning to pay for my hotel room, because that's essentially an extension of credit of an amount of money and there's no asset - - -

DR TURNBULL: Backing it.

MR SMITH: - - - in relation to that credit, and if I do that six or eight times I can borrow a couple of thousand dollars - - -

DR TURNBULL: No, we hadn't extrapolated it that far, no. We were looking at the long-term type of debt which households get into, and I know they use their credit card to increase this debt for sure, and that is one of the big problems in Australia at the moment of course; that a person can go in and take out a fixed loan and then they can use a credit card from another institution to decrease their capacity to pay

their fixed loan - yes, I agree with that. But, no, we were looking at this as being on the fixed loans items and not on the credit cards.

MR SMITH: Okay.

CHAIRMAN: Dr Turnbull, thank you very much. Your submission is very clear to us and we understand precisely what you're putting. Thank you very much.

DR TURNBULL: Thank you.

MRS NICHOLLS: Thank you, Dr Turnbull.

CHAIRMAN: The next participant, ladies and gentlemen, is Mr Michael Hovane from the Consumer Credit Legal Service. Mr Hovane?

MR HOVANE: Thank you, and one of the other solicitors from our service, Andrew Moore, with me.

CHAIRMAN: I will just make a comment if you wouldn't mind just having a seat. Given that the two gentlemen have just joined us, I should repeat my earlier remarks that these are public consultations and the proceedings will be recorded and transcripts made available. We have no legal powers or parliamentary privilege, so you should not venture into the area of making any adverse criticism or comments which reflect on particular organisations or people. We would simply like you to start by both - for voice recognition purposes - stating your name and the organisation you represent, and we would be very pleased to hear from you with a brief opening statement. We have about 25 minutes to cover your submissions. Thank you.

MR HOVANE: Thank you. Michael Hovane from Consumer Credit Legal Service.

MR MOORE: Andrew Moore from Consumer Credit Legal Service.

CHAIRMAN: Yes.

MR HOVANE: Thank you. We don't have a written submission but effectively our verbal submission this morning is primarily focused on the code and the need to retain the Credit Code and I suppose echoes some of the sentiments of the submissions that have already been made to the Financial Services Inquiry.

Perhaps if I just start by way of introduction of our organisation so that the inquiry has some understanding of our service, what it does, where it comes from and what its experience and its credentials are to comment upon to the Financial Services Inquiry.

Consumer Credit Legal Service is a community legal centre specialising in credit banking and financial services issues, and our role in Western Australia is very similar to that of our counterpart, Specialist Consumer Credit Services in New South Wales and Victoria, perhaps with the exception that in Western Australia CCLS - which is the abbreviation for us - is the only organisation in this state which provides legal advice, assistance and representation to the public in these areas.

CCLS has in the past had extensive experience in representing consumers under the previous Credit Act, particularly large numbers of consumers in civil penalty applications. Further, we have been involved in the development of the code and have a good working knowledge of the civil penalties regime under the code, and have been responsible for the delivery of training to financial counsellors, solicitors and paralegals from Legal Aid, Aboriginal Legal Service and to the professional legal body in this state.

So the comments we'll make perhaps come from the basis of our extensive working knowledge of the Credit Act and the Credit Code, and experience with how the civil penalties regime actually operates in practice in order to try to inform the inquiry of what the actual effect of the code might be as opposed to what it might be anticipated or speculated to be.

While a prominent emphasis will be effectively on the Credit Code, we also just wish to make a short question in relation to the regulatory regime that might be recommended as a result of the inquiry. CCLS itself has no particular preference, either philosophically or practically, as to whether there are a number of regulators in the system or whether there may be a mega-regulator as has been proposed. But certainly we would strongly submit that there does need to be a separate and independent regulator that has control of the consumer protection function.

Effectively other than that perhaps the format is not particularly important from our point of view. The reason you need to have a separate entity for consumer protection is, firstly, if you have that function under a mega-regulator, there is the very real risk that consumer protection will be subsumed as a matter of secondary importance or subservient to other financial or commercial or prudential considerations.

The other major reason is that if you have a separate and independent entity then that entity is far less prone to industry capture, which is otherwise a very real risk if you have the consumer protection responsibility under one regulatory body. In relation to the code, perhaps as a preliminary point I make the point that the code is not new, as you're probably all well aware having heard about the code. It's the end product of some 20 years of negotiations between government, industry and the consumer body.

I perhaps make the point that the issue of the allegedly prohibitive costs of the implementation of it and the regime were certainly not items that were strongly put forward when the code passed through the states of Australia, and in fact a number of industry bodies made much of the significant cost savings that would go to industry as a result of uniformity, and I make that point because with the greatest of respect, without wanting to be too cynical, there is perhaps a suspicion that this is simply an opportunity that's been grasped by some industry groups to get away with what they can, given that the inquiry has come under way and to perhaps undermine what has effectively been a process to achieve a balanced code.

In that sense I suppose, rather than putting forward figures because I don't have the benefit of figures that might have been put forward by various industry groups as to the costs of implementing the code or compliance or civil penalties regime, but I would ask that the inquiry seek details as to those costs and scrutinise them very carefully in order to determine whether in fact those costs are due to the implementation of the code or would have had to have been incurred in any event.

CHAIRMAN: It was said in Brisbane yesterday a hundred basis points to the cost of credit.

MR HOVANE: Right. But our submission would be that many parts of the credit industry obviously have been largely unregulated, and this has in fact led to poor and marginal lending practices and compliance systems, and in fact a portion of the cost is probably attributable to simply bringing lenders up to a responsible and acceptable banking and business conducts and lending practices, so that a large amount of the expense was required in any event. The Credit Code and the Banking Code are simply the catalysts for that change, rather than necessarily the cause to which they are attributable.

I suppose I make the other point which is probably very obvious to the inquiry, that even on figures that I've certainly seen provided by some lenders, that the code is now here. It has been implemented, and on costings that have been provided, the largest portion of the cost is to establish documentation and compliance systems which are now in place. Those moneys have already been spent, so that it may be an attractive argument that you see a large amount of money in that respect, but those moneys have already been spent so those costs will be passed - it's a one-off thing.

They'll be passed on to consumers in any event, and really all the inquiry should be focusing on, if it does look at the issue, is the ongoing annual cost of compliance, and perhaps in that regard I'd address sort of the two reasons for what's alleged to be excessive cost, and they are on the one hand the disclosure requirements and on the other hand the civil penalties regime, or penalties that may supposedly result as a result of having the civil penalties in place.

The other thing perhaps the inquiry might pay some regard to is, if we did go backwards and actually abolish the civil penalties regime, what is the cost of actually doing that? There must be some cost, some change in systems, and again there may have been no costings provided in respect of that, and it must be borne in mind there may be some additional cost incurred of that, and again unless that's actually addressed it could be easily glossed over and ignored.

In relation to disclosure, I wish to make the point that disclosure is not just a consumer protection mechanism. The purpose of disclosure is to facilitate informed choice, and informed choice is not just about consumer protection. It is equally about competition. Informed choice is the basis of competition, and unless you have informed choice and consumers having the necessary information to make informed choice, you cannot have a marketplace that operates efficiently. Consumers need to have the information to make choices between different products, so it's not just a consumer protection mechanism. It's as much about competition.

The point has probably been made to the inquiry but we hammer it home again: is that allegedly disclosure is overly prescriptive, and if you look at the change from the Credit Act to the Credit Code the requirements for disclosure or those disclosure requirements that trigger a civil penalty have been drastically reduced, and we would submit what we are left with is only the minimum necessary information in order for consumers to make informed choice.

There are many disclosure requirements which have been jettisoned from the previous Credit Act in terms of triggering a civil penalty. For example, one could look at, under the Credit Act, the requirement to disclose a commission payable in relation to a loan. That's a disclosure requirement but it no longer triggers a civil penalty, and yet under the previous Credit Act decisions in the Commercial Tribunals and in the Courts of Appeal indicated it was quite a serious

matter. So what I'm saying is, we're really only left with the very core information necessary for the operation of a free market.

In relation to the issue of civil penalties, I'd perhaps ask the inquiry to be cautious in assessing any estimate of costs that will accrue or flow from civil penalties. We haven't as yet had obviously any civil penalties cases under the Credit Code, so that any estimates of the potential expense are purely in the realm of the speculative, and I suppose we would strongly submit it's premature to make an assessment at this stage of what the potential cost might be.

But in making some sort of estimate of what the potential cost might be, it's perhaps helpful to look at what occurred under the previous act and what the changes are and how that might effectively reduce costs under the Credit Code. There have been a lot of allegations, and I'm not sure exactly how detailed those allegations have been, about the high cost of civil penalties under the Credit Act.

Our submission would be, it facilitates the inquiry to look very closely at those allegations and actually look at the individual cases where a high cost was incurred by way of a penalty to a lender, and one might think of the State Bank of New South Wales case or other cases such as the Westpac cases. These are not cases that involved purely technical breaches of the law. The only cases where there were actually large penalties were cases where there was not just a blatant disregard for technicalities, but there was substantial and systemic overcharging, illegal fees and practices such as insurance forcing, false and misleading interest rates leading to actual or potential loss to borrowers.

CHAIRMAN: I think the main point that's been put to the inquiry is that there are instances where for technical-type breaches the penalty can be, you know, out of all proportion to the loss that's involved. That's the broad proposition that's been put by some institutions. I'm not saying whether we're picking up on it or not but - - -

MR HOVANE: Sure. I think in order to assess whether that's actually true you need to scrutinise the actual cases. Our submission would be that Commercial Tribunals across the country have actually moved towards a view that for purely technical breaches actually very little penalty applies. In fact it's our intention to provide the inquiry with a list of cases subsequent to today of a range of more recent cases around the country, even under the Credit Act, where purely technical

breaches - and this shows the attitudes of the courts - have resulted in full reinstatement of interest and very little penalty.

CHAIRMAN: Sure.

MR HOVANE: Now, the point I make is that even under the act, really there has been very little penalty for purely technical breaches, so that the only cost incurred has been the cost of having to go to court to have interest reinstated, and that obviously is a cost, but here's the big difference between the two regimes. Under the Credit Code - and this is the fundamental difference in the civil penalties regimes under the two systems, and it's one that really needs to be appreciated - there is no automatic loss of the right to interest.

That means there's no necessity to have to go to court to remedy errors, and it's certainly our strong belief that under the Credit Code there will be neither no incentive nor no necessity for lenders to have to go to the courts to remedy purely technical breaches because unless a borrower can establish actual or potential loss or detriment they are not going to receive a penalty. The courts are not going to give a penalty. So the question remains: what then will be the cost of purely technical breaches. It's certainly our belief that there will be none.

CHAIRMAN: What you say, in the interests of time - I mean we understand exactly what you're talking about, but if there are some positive points that you want to put to us that we can deal with in terms of the regulatory framework, that's what we're most interested in today.

MR HOVANE: Certainly. I don't know whether perhaps the inquiry has anything specifically that it may wish some comments on.

CHAIRMAN: Sure.

MRS NICHOLLS: Thank you, chairman. Earlier in your opening remarks I believe you said that you had virtually sole coverage of Western Australia, and in addition that you do considerable work with Aboriginal groups. Could you offer some comment on what you see as particularly significant issues in financial services for the Aboriginal communities that you're working with?

MR HOVANE: Do you want to make some comments on that?

MR MOORE: I think the major issues that would emerge there would be in connection with remoteness generally of communities in rural Western Australia from legal advice and financial advice - in the financial counselling and legal advice areas - and the lack of access of those people to be able to have an informed choice about credit

products that they're given to assess and decide whether or not they'll take them up or not. And the potential, I suppose, for people in those areas to be sold products that are not necessarily - they're not in a position to assess whether or not they should buy them, particularly some sorts of credit products, some sorts of insurance products, that type of thing, and to be basically in a position where they're not properly advised at the time of taking up those products.

MRS NICHOLLS: How would you see those matters being remedied?

MR HOVANE: It's partially a matter of resources and also of focus, and I suppose because of the regional size, those particularly remote Aboriginal communities are susceptible to all the worst sort of systemic abuses and marginal practices. It's something that regulators have perhaps failed to address because of limited resources to be able to have a presence in those areas. It certainly should be the focus of education but it's a very difficult educational process because it requires quite a grassroots specific delivery that isn't conducive to a uniform approach. But in WA we certainly have a lot of problems that you have in Queensland with that sort of selling of life insurance products that aren't appropriate or systemic credit forcing and insurance forcing sort of on a fairly regular basis; that's difficult to police or regulate.

CHAIRMAN: Bill?

MR BEERWORTH: Thank you, chairman, a couple of points if I may. Michael, you mentioned in your outline that you felt fairly strongly that although there might be a mega-regulator, that any consumer protection authority should be quite separate. By that you meant literally separate, not just a division of the mega-regulator. Is that correct?

MR HOVANE: No, I think the temptation is if it's simply a division and - I mean it may be a matter of semantics as to how you divide it up but unless you're provided with a separate budget, separately resourced then the danger is that resources will simply go to the other section as well.

MR BEERWORTH: And a separate culture I think, as I understand it.

MR HOVANE: A very separate culture, and that again is the danger of industry capture. I suppose we would view the ACCC has having performed that function quite effectively in the past and of the various government regulators it certainly has a great deal of consumer confidence and credibility because of the way in which it has performed its role.

MR BEERWORTH: Given the difficulty of the time involved in coming to a uniform code, which I understand has taken about 13 years, would you be in favour of trying to federalise this aspect of consumer protection, that is consumer credit legislation and codes?

MR HOVANE: Perhaps personally I do see perhaps it doesn't have any philosophical difficulty with it necessarily being federalised, but we perceive many practical considerations and difficulties which may actually make it unworkable and increase the cost, and there are obviously the problems with the jurisdictional or constitutional issue of a federal agency being unable to deal with non-corporate lenders.

There is also again the specific questions of resources and agencies. I mean I'm not sure that the federal government, if it's going to be the regulator, has the resources or the presence in each state to perform that task; whereas in the past state agencies have been very good, certainly in this state, in fulfilling their roles - in providing a regulatory overseeing function in respect of credit. So I suppose the difficulties - are you going to set up then some separate framework? That needs to be accurately resourced?

Our experience in Western Australia is unfortunately that where there is a federal body we're usually at the end of the line; in that resources tend to be very New South Wales-Victoria focused. So if you have a federal body we're usually the poor relations and I have some concerns about it in that respect. Inevitably that's what tends to happen. Even with the Banking Ombudsman scheme, as an example of something else, it has very little presence in Western Australia. Surveys done of clients that we have conducted have shown that many people aren't aware that the scheme actually operates to Western Australian consumers. There's a Melbourne address on the pamphlets. People actually presume it's a Victorian state dispute resolution scheme. These are some of the problems when you have a federal body.

The other problem I think is that problems under the Credit Act aren't uniform across Australia. Even with uniform laws, policies and practices they aren't uniform. If you look at the act - - -

MR BEERWORTH: But that would be the only reason to federalise it; to try and make them absolutely uniform, rather like the securities laws.

MR HOVANE: To make them uniform - I suppose - - -

CHAIRMAN: There is a fair degree of support - which wouldn't surprise you, but it surprised us a little bit - from the consumer groups to

opt for a national code in this area, and we were surprised at the response they gave.

MR BEERWORTH: To have national uniformity.

CHAIRMAN: Yes.

MR HOVANE: I think there are advantages for consumers in that consumers move from state to state. Hopefully if the reciprocating sort of vesting legislation is adequate; it means that someone moving from a state can commence an action in Queensland, where they'd moved into, even though they entered into a contract in Western Australia. So it has considerable advantages and - we deal with clients who enter into contracts over the telephone from another state and then proceedings are commenced against them in a local court in say New South Wales. It's impossible for them to enforce their rights because you're not going to get aid over there, so all those problems arise.

MR BEERWORTH: One may point if I may, chairman. We had an interesting submission from the Queensland Law Society yesterday to the effect that the problem occurring at the moment is that it's totally draconian and that what's needed is some form of steam valve or amelioration.

MR HOVANE: Self-rectification.

MR BEERWORTH: It's a self-rectification concept which certainly on its face seems very reasonable; that if there has been an unintentional and a non-reckless breach, provided notice is given to the consumer within 12 months and provided the consumer is refunded all charges, provided there's also notification to the local consumer authority which can take action if it wishes, that basically that should be self-mending as the name applies. That seems reasonable. Do you have an objection to that sort of approach?

MR HOVANE: I've only seen it very briefly; I think I got a copy of portions of it last night. It appears attractive on the surface. I don't have any great objection to it, but I think the code is not draconian and effectively you're going to have that anyway for technical breaches, and I suppose when you look at what Queensland has proposed, it involves the lender obviously going to the government consumer agency, and they obviously must provide details as to what the breaches are - - -

MR BEERWORTH: Yes.

MR HOVANE: - - - who's effective and such. Now, what's the difference therefore between that process and the process that would operate in any event under the code? Normally what actually happens

in civil penalties cases under the code is exactly that. An application is lodged in the court and a copy goes to the government consumer agency. But that application contains details of the alleged breaches, the number of affected borrowers and the types of errors. So it's exactly the same process.

What I'm saying is I don't see that really there is any additional cost. The main difference is that under - if you go through the courts there is actually a process of notification to borrowers, and that is usually actually not by way of direct notification, it's generally been by way of advertising, that's what tribunals have allowed. So that's the only additional expense. But the advantages of going through that process is that - obviously there are natural justice issues - borrowers then have the right to be heard or put forward their case as to whether there has been any loss or not.

That's very important because our experience here in Western Australia is that often with civil penalty cases so far, they may have been commenced in New South Wales and Victoria and initially a list of the types of errors that the lender believes have occurred is provided. When it gets to Western Australia we're actually picking up in many cases very different errors that have occurred on a systemic basis here even though this is under - the Credit Acts are the same in New South Wales, Victoria and Western Australia - are almost identical and that's because even if you have got uniform laws and policies often they way they're put into practice is the same.

We have a very recent example with a case with a finance company whereby when the application has come to Western Australia we've picked up systemic errors in stamp duty, calculation of interest that weren't in the original application and the only reason they were detected is because there was a separate process of advertising in this state, simply because a separate application was required, the borrowers came in and the errors were detected - quite serious errors.

So I suppose my worry about the self-rectification is it can overlook and miss matters entirely, it assumes uniformity in errors which is not necessarily the case, and it denies borrowers the right to apply. My point is, really you talk about prohibitive costs - what is proposed by Queensland is exactly what happens with civil penalty applications in the courts anyway.

The other point I make is that with civil penalty applications very few of them ever get to trial; in fact virtually none here

in Western Australia. They're all resolved by mediation anyway. So the only additional cost is that advertising process that allows the ability for potentially serious errors to be picked up. So I don't see that there are necessarily huge costs savings or a great difference between self-rectification or what's presently proposed. It may appear superficially attractive but the differences aren't that real and the cost savings that significant.

CHAIRMAN: Michael, I didn't say anything about prohibitive costs; we're just putting forward other people's views.

MR HOVANE: Sure.

CHAIRMAN: Thank you.

MRS NICHOLLS: Thank you, chairman. Michael, I had the opportunity to meet with some consumer groups in the United Kingdom and one of the subjects discussed with them is what are the tools that deliver the most effective enforcement of best practice for consumers. In the UK they made the point that fines in some cases are either too big or too small to actually have the desired effect, and the ultimate threat of sending directors or trustees to gaol may be too heavy-handed to have the most desirable effect when the matters are minor.

A notion they put to us was that disclosure of those who are not exhibiting best practice - outing if you will - was actually a very inexpensive and quite effective method of enforcement. Could I ask you to comment on how you see the most effective enforcement of best practice for consumers.

MR HOVANE: That's quite an interesting idea - outing. I think there's no problem with a range of innovative strategies to deliver compliance. I suppose our experience is very similar to those in the UK in that penalties, criminal penalties in particular, don't work as a method of ensuring compliance What we're really concerned about from a consumer point of view is not punishing bad lenders, it's ensuring that consumers are protected and that there is a culture of compliance.

Civil penalties have certainly been by far the most effective means of ensuring compliance. You can say what you like about the Credit Act but certainly I think it's widely acknowledged that we have ended up with a culture of compliance because it is in place. We have experience under motor vehicle dealers legislation the Hire Purchase Act which, although it has in effect some civil penalties regime for loss of term charges, most of the provisions are in fact criminal, and our experience time and time again is that they're simply not followed,

because those criminal breaches rely upon government consumer agencies to initiate prosecutions; prosecutions are incredibly expensive; government agencies are badly under-resourced - - -

MRS NICHOLLS: Michael, sorry, let me ask you: do you feel that fines have helped consumers avoid those firms who are not undertaking best practice?

MR HOVANE: No, not whatsoever.

MRS NICHOLLS: So how is it that fines help consumers?

MR HOVANE: Sorry, when you say "fines", you're talking about criminal fines or - - -

MRS NICHOLLS: Any sort of fines that are imposed on those who have breaches of best practice.

MR HOVANE: Fines do very little to assist consumers because they don't ensure compliance, and just to give one example: under the Hire Purchase Act in Western Australia, which is a very old piece of legislation, you're not allowed to repossess a vehicle from private property without a court order, but under contracts under the Hire Purchase Act here it's done on a very regular basis and the reason is there's only a criminal penalty for that breach. In fact a discussion just a few weeks ago with a lawyer from a credit provider - wasn't even aware that it was illegal, and it's done on a fairly regular basis by most finance companies.

Conversely, under the Credit Act, if you illegally repossess without a court order the credit provider is not allowed to charge enforcement expenses for doing so. So that's a civil penalty; they lose their right to charge expenses. Experience under the Credit Act is that lenders comply with that. I mean, that's the difference - that perhaps illustrates the difference. Fines have no effect really in ensuring compliance because prosecutions are so rare that the advantages of, I suppose, disregarding the legislation far outweigh the potential risk of a single prosecution.

CHAIRMAN: One the last questions that I thought was put to us in our travels - it would seem we're talking about the code all the time - that the requirements of the code were actually taking providers out, providers of credit out, particularly away from the sort of mainstream and that may well result in less service, less credit available to the consumers. Do you have any experience of that at all?

MR HOVANE: In what sense?

CHAIRMAN: Just the retailer who might have offered credit now cannot do so, or cannot live with the requirements - - -

MR BEERWORTH: Small stores and hotels.

CHAIRMAN: Even, yes - maybe it's not a big issue, but it was just put to us.

MR HOVANE: That's a good point to observe but in Western Australia for instance we have a positive licensing regime, so you haven't really had small lenders in any event. The other thing is you still obviously have your hockshops and pawnbrokers and such and they perhaps cater to a large amount of the lower end of the market, and there are various other loan schemes in place.

CHAIRMAN: Sure.

MR HOVANE: I wouldn't see that really as significantly impacting. Andrew, sorry, is there something you want to say?

MR MOORE: There are also provisions for short-term credit obviously under the code as well which would take in a large number, I would have thought, of the smaller lenders or the short-term lending.

CHAIRMAN: If they're prepared to continue to be a provider.

MR MOORE: Yes.

CHAIRMAN: In accordance with the code. Yes.

MR HOVANE: I think they're exempted from the provisions.

MR MOORE: Yes, if they're prepared to lend for that shorter period of time - - -

MR BEERWORTH: What is a short period?

MR MOORE: As I understand it, it's 60 days, I think, under the code. If they're prepared to lend for that shorter period of time they won't come within the scope of the code.

CHAIRMAN: I think we have come to the end of the allotted time. Thank you both very much.

MR HOVANE: Thank you for your time.

CHAIRMAN: We are next to hear from Mr Wayne Leggett from the Australian Lifewriters Association. Mr Leggett?

MR LEGGETT: Thank you, Mr Chairman.

CHAIRMAN: You are being joined by?

MR LEGGETT: I'm accompanied by Steve Birch who is one of the association's directors for our western region.

CHAIRMAN: Again, if you could just commence by both stating your name and the organisation you represent for the purpose of the record, then we can proceed.

MR LEGGETT: Wayne Leggett, from the Australian Lifewriters Association, and our presentation is made in conjunction with the National Council of Life Agents Associations.

MR BIRCH: Steven Birch from the Australian Lifewriters Association.

CHAIRMAN: Thank you. I suggest you take 5 to 10 minutes and leave us some time to ask you some questions if that's practical.

MR LEGGETT: Certainly. Obviously the inquiry has been given a complete copy of our submission, so I won't reiterate the terms of reference of it, other than to say that although I'm here representing the advisers in the financial services industry, I think by virtue of our situation we can give some feedback in terms of a consumer perspective mainly because of the fact that our members are dealing with the marketplace on a daily basis and therefore we have a golden opportunity to obtain feedback from the public, as it were, and the feedback that we get is that what the consumers are looking for is that the advice they get is appropriate and that any system that is implemented to regulate the giving of advice shows fairness to all parties. So what we're talking about there is that the advice is appropriate.

The bottom line of it all is that the general public's attitude seems to be, "I don't necessarily want to know all the information that is required about this product. I want access to it but I want to know that my adviser knows." So in other words, "If he is registered to give advice and therefore I know that that means he's qualified and met with a certain set of minimum competencies, then he knows what he's talking about and if he does the wrong thing and that opportunity to give advice is revoked then he can no longer trade."

I have prepared a presentation for each one of you which will outline our information on it. There are just some diagrams in

there. The discussion points cover two areas. The first bit is to outline our proposal for an independent stakeholders' registration board for those giving advice in the financial services industry, and what we want to do is make a comparison between the present models under the ASC regimen and the ISC, and if you turn to the diagrams I will take you through those, and they outline it fairly clearly.

The first diagram outlines basically the system as it works for the industry at present under the areas covered by the Insurance and Superannuation Commission. You can see obviously that we start with the various acts of parliament that relate to the Insurance and Superannuation Commission, and they are in fact listed down the right-hand side of the page, so you will get a feel for - under the current circumstances, just on the side of giving advice under the ISC - the extensive range of legislation that advisers in this industry have to be cognisant of.

Obviously underneath there, there are a significant number of areas that relate to the giving of advice, and several different ways in which the consumer has exposure to advice-givers. If you follow the line down there are three general areas in which the consumer has access to the giving of advice. It can come direct from a life office, quite obviously, or it can come via representatives, and they can be either the broker's representatives or they can be agents who represent a life office, or they can be employees of a life office. Obviously all of those three groups have to currently adhere to a code of practice and therefore deal with the consumer.

The second diagram relates to the regime as exists under the ASC regulation and responsibility and we understand that a view has been put forward that a similar regulation system could be imposed for the entire financial services industry, or at least what's presently covered by the ISC. Now, it would look simple by virtue of comparing that diagram to the first one, but the problem that we see is that there are literally hundreds of licensed dealers and their sizes range from a dealership which might have half a dozen authorised representatives to those that have literally hundreds, so there are problems of uniformity and standards and application of those standards.

If we turn to the next diagram, this is what we have prepared as a possible responsibility flow chart in terms of by whom and in what capacity a life product sale can be made. If we had the natural

person giving advice and then they're governed by an agency agreement - the person could have multiple agencies, so they can either hold the agency personally or they can hold it through an associated company, or the responsibility can be held by a life company, or a dealer, or a broker.

Once again under each of those headings, all of those people, depending on where they fit into the picture, all have to comply with the current code of practice in order to complete the - - -

MRS NICHOLLS: Excuse me, Wayne, we're getting a bit confused. What page are we on? We seem to be stapled in a different order.

MR LEGGETT: I'm sorry, this is the responsibility flow chart - by whom and in what capacity a life product sale can be made.

CHAIRMAN: Okay, so it's this one.

MRS NICHOLLS: The one that begins, "This is the situation now"?

MR LEGGETT: That's it, yes. My apologies. So what this is outlining is what the current circumstances are in terms of where people fit into the current code of practice and how they are able to give advice on the sale of life office products. They can either hold an agency personally or through a company, they can be an employee of a life company through a dealer or through a broker. In all instances they have to adhere to the code of practice in order to be able to complete the sales transaction, and they also, as you know, have to provide a customer advice record on interview. But you can see that there are different categories into which all those people fit in.

Now, on the final page is where we've made our suggestion as to an alternative method of registering people and getting them to comply with provision of advice. It wouldn't - - -

CHAIRMAN: What is that page?

MR LEGGETT: This is the final page headed up - the first box is Parliament. Now, we're suggesting that it would require ultimately the implementation of a new act, a new Financial Services Act, which would incorporate life insurance, risk, investment and superannuation, and could perhaps be extended further than that.

CHAIRMAN: Such as?

MR LEGGETT: Well, perhaps into banking products and so on, and there have been some comments made this morning which would perhaps tie in very nicely with this sort of a regime, a regulatory regime. It would require a statutory commission to oversee the act, and the overseeing could be divided into two areas. Obviously you can

separate the prudential standards from the actual regulation of those giving advice, which is where the consumer protection provisions come in.

CHAIRMAN: By prudential standards you mean?

MR LEGGETT: As in what's currently governed by the ISC. So that role could be separate. In other words, the dealing with the life offices and in terms of the product design and implementation.

CHAIRMAN: Yes.

MR LEGGETT: Interestingly enough we've had some very encouraging feedback from our discussions with the ACCC in terms of this particular model and how it fits in with their objectives, so we're quite heartened by that. What we're saying is that if we had regulation of natural persons through this self-regulatory organisation then we could achieve the objectives of consumer protection and natural justice within the industry.

Now, if I could ask you to turn to the first page where I've outlined the dot points, I'll now refer to those particular comments. These are the points as to why we see the benefit of the registration of natural persons. A model such as this would control all those who give advice in the financial services industry, and that could include accountants, solicitors, and the like. In other words, anyone who is giving advice on financial services products can be registered to do so.

Another problem it solves is that it obviates the moral dilemma which exists where the current structure is that those who are entrusted with regulation of the advisers have a pecuniary interest in the transaction. So there have been incidences in the past where they're caught between deciding what's in the best interests of the consumer and what's in their own best interests.

MR BEERWORTH: Which regulator is that that finds itself in that position?

MR LEGGETT: Well, the situation of - particularly with a life office where they have one of their agents, let's say - - -

MR BEERWORTH: The office itself?

MR LEGGETT: Yes. I mean, if he makes an inappropriate sale but there's a profit for the life company, they're torn between the consumer's interests and their own, hence the moral dilemma. If the responsibility exists with the adviser it quarantines the brand name - in other words, the institution itself - from any adverse publicity, because it's the action

of the individual that will be taken to task, and that doesn't necessarily then get related to the particular company.

So it protects them from that adverse exposure, because one of the problems you have at the moment is that something that we've tended to refer to as chequebook ethics - rather than have adverse publicity, an institution will deal with a consumer who has a particular axe to grind and irrespective of the appropriateness or not of their complaint there's a tendency to say, well, rather than have it splashed all over the papers and on television, we will make this go away by just getting out the chequebook. Now, of course the problem there is that that's an inappropriate distribution of resources which ultimately belong to the investors and policyholders.

The next point is that if we implemented a regime such as this it would eliminate the duplication of costs that we currently have with parallel regulation processes, and that would hopefully free finances to fund whatever the costs were of individual registration. It does allow for a complaints procedure to be amalgamated with the registration process itself, and that would obviously implement greater efficiency and economy.

I have referred previously to natural justice. Our view is that the person who gives the advice across the table from the consumer is the one who should accept the responsibility for the appropriateness of that advice, because the other - the way the situation is at the moment, the people who wear the responsibility aren't a party to what actually took place, other than in terms of what's documented, and there's a serious limitation in the process there. Our members and the people we represent are quite comfortable about the fact that if they give the advice, they're prepared to stand as individuals by the appropriateness of that advice.

We have a problem at the moment with individuals where they might hold agencies or be licensed in different areas. There is a duplication of the regulatory requirements, and they might be having to do the same thing with any number of - up to half a dozen different institutions. That obviously provides problems both for the principal concerned in controlling them, and they themselves in terms of who's responsible and how they sign off.

CHAIRMAN: You need to be just a little bit aware of the time if you want us to come back to you, that's all.

MR LEGGETT: Yes, certainly. The justification would be created for the registration scheme having access to things like police records and so on for implementation of ethical standards, people coming into the industry, and the model creates a system whereby it would therefore be extremely difficult for unethical practitioners to either enter the industry or, more importantly, to continue within in, because without registration they have no access to product and therefore they can't trade.

Finally, I'd just like to comment on - I believe that there have been some points of view put forward in terms of the cost of individual registration, and a figure of the order of $600 was quoted, and that was put together when the Multi-Agents Regulatory Group commissioned the Halesworth partnership to investigate it. Our indication is that the figure would be closer to $300, and that information was provided to the Interim Registration Board by Ernst and Young, and that was based on 5000 advisers being registered. So the point is that there are some economies of scale in there by bringing in a wider base of advisers, and that's the total of the submission.

CHAIRMAN: Thanks, Wayne. You obviously put a lot of thought into that, and we certainly appreciate it. Perhaps you could comment - I mean, is there an issue about sort of quality control and all this? I mean, life companies have traditionally wanted to have a fair hand in the nature of the advice and the standard. If you bundle everything up into this new structure, is there going to be an issue there in terms of - - -

MR LEGGETT: You mean a subsequent problem with quality control?

CHAIRMAN: Yes.

MR LEGGETT: In fact the reason we're suggesting this is we believe that this is the most appropriate way of obtaining quality control. The reality is that the vast majority of advisers out there are ethical practitioners, have been in the industry a long time and wish to continue to do so, and what happens is - I mean, we all know that laws only control the law-abiding. What we're saying is if you register the individual and say, "Step out of line, you lose your ability to trade," you by definition then would create a scenario where only those who are working on a best practice basis would be able to continue.

CHAIRMAN: But does the institution lose some control over that process?

MR LEGGETT: The point is at the moment their control is - it's there officially but it's very difficult to police, and they also - as I said, there are some problems in doing so. Defining what's an appropriate product to sell in the particular circumstance is very nebulous. Now, at the end of the day, what could happen under a registration system like this is that the individual is held accountable for whatever advice and products they recommend to a client, and irrespective of the legality of the product, if it's inappropriate and the individual is found to have been conducting inappropriate practice, then they lose their ability to continue trading, and we believe that that's the most effective way of controlling the appropriateness of advice.

MR BEERWORTH: Thank you, chairman. Thank you, I found it a very interesting submission. One thing that sort of surprised me, both in the written submission and what you had to say, was this. The system you describe, which is basically of registering all providers of financial advice, seems obviously sensible on its face, but you seem to draw back from including in that securities advisers, those who advise on equity, etcetera, those presently licensed under the ASC law, and I couldn't quite understand why that was - - -

MR LEGGETT: No, not at all. You see, the reality is that most of the advisers that are currently covered under the ISC regime are also controlled by the ASC.

MR BEERWORTH: So you would have universal regulation of all financial advisers?

MR LEGGETT: What we would like to see is one set of rules, irrespective of the type of advice you're giving. If you're advising on financial services, you're registered to do so, and you comply with one set of rules.

MR BEERWORTH: Right.

MR LEGGETT: Because there are horrendous difficulties at the moment with the different sets of compliance, how you represent yourself to a client, because the legal requirements are to make a representation of who you are who's behind you to a client before you have established what services that client requires, therefore you don't know which hat to put on, and obviously if you were governed by one set of rules, you hold yourself out to be an adviser and then you refer specifically to the type of advice that client requires.

MR BEERWORTH: You seem to exclude nonetheless the product developer, life insurance companies, as it were, and you put the onus

directly onto the adviser. Under the securities law of course, the onus is directly on the provider of the product, the equities house, and they in fact give out the licences to the authorised representatives.

MR LEGGETT: The area we're focusing on is the giving of advice. What we're saying is that there are three parties to the transaction. There's a manufacturer, there's the distributor, the retailer if you like, and there's the consumer, and we're saying that it's inappropriate - the analogy, if you like, is that if the pharmaceutical companies were to control what prescriptions a GP makes to his patient, because he has no way of knowing what the particular patient's circumstances are, but in the current circumstances we have it's the provider of the product that is saying, "This is or isn't appropriate for you to offer that particular client." They're not a party to the discussions and they have no basis for that.

MR BEERWORTH: Thank you.

MRS NICHOLLS: Thank you, chairman. Wayne, I'd like to draw you to a fairly muddy area in this discussion. We have had views put to us on how you can delineate, if indeed you can, between offering advice and making a sale. Now, on the one hand we have had representations of consumers who say, "I don't want a financial plan I just wanted to buy death cover."

MR LEGGETT: Mm.

MRS NICHOLLS: On the other hand, we have had representations from consumers who said, "Well, I went along to the bank, and I know I was just getting a term deposit but, you know, they told me it was a really good investment that I made." How do you see us, or do you see us, trying to determine what is a sale, what is advice, and how would you see your advice program getting broad community coverage to pick up all those who offer advice, even if it isn't confined to insurance, investment and superannuation, as your group is now?

MR LEGGETT: What we see as being the terms of reference, if you like, for registration is that if you give advice that relates to the purchase or otherwise of a financial product, then that would be covered by the registration scheme that we're talking about.

MRS NICHOLLS: Sorry, so a real estate agent that offers advice on a loan to go with the property you're buying?

MR LEGGETT: Well, ideally, even the property itself. I mean, if you think about the possibilities of it, if someone is advising people on an investment of any description or access to a lending product - I was very interested in some of the comments that were made earlier about

loan products and so on, because one thing that's always been incongruous to me is that in our industry when we're advising on financial products that are covered by the ASC or the ISC, we have to comply with a very sound basis for our recommendations, researched and documented, yet when my clients go to a bank to take out a lending product, for argument's sake, it's basically a case of if they're prepared to pay the price at which the bank offers it, they can take it, and then they come to me and say, "Well, this is what I've done," and I'm in the position of saying to them, "There are umpteen different better ways you could've set yourself up with the bank than what you've actually got here," but as I understand it, there's no onus on the bank to do that.

MRS NICHOLLS: Sorry. So does your proposal bring - just for clarification - bring bank officers into this?

MR BEERWORTH: It doesn't at the moment.

MR LEGGETT: Well, what we would like to see is that anyone who advises on financial product, which is defined as anything that someone ultimately purchases, be it a loan, an investment, an insurance policy, an annuity, whatever, and perhaps even extended to discussions of alternative investments, real estate and so on, that those people should be registered. I mean, the situation is that if I call a plumber into my house to repair a blocked drain, he has to be licensed, but someone can go to you and tell you how to invest your life savings or how to protect your family - they're not required to be licensed. It just doesn't make any sense.

CHAIRMAN: What's the answer to the question about the bank officer who's selling a credit product?

MR BEERWORTH: Selling a credit product.

MR LEGGETT: Well, I mean, ideally we would like to see them brought in under that regime as well, because what you have at the moment is a situation where if those people aren't registered in terms of their ability to give advice on that particular product - the advice may be appropriate - now, you can make delineation between those who are employed, because if you go into a bank and there's the bank's logo over the door, it's reasonably safe to assume that the employee has the bank standing behind him for his advice - reasonably assume, perhaps.

But when a client is dealing with an adviser, it is very difficult to know and in fact it is very difficult to determine, for the different areas in which we deal with clients, who should be responsible

for each particular transaction, because there are so many different things involved.

MRS NICHOLLS: Thank you.

MR SMITH: I just wanted to know - it's a very technical question but you may have done some work that I would have to do, so I thought I'd ask you whether you had done it. If we shift the whole onus from the corporational level to the individual, to the actual natural person providing the advice, have you checked whether or not that's constitutionally possible for the Commonwealth to legislate in that field?

MR LEGGETT: I'm very glad you raised that actually, because we've sought legal advice on the ability to do this, and our legal opinion is that the capacity to impose individual registration on a voluntary basis already exists within the ISC regulations. The regulations say that the ISC can require that, for argument's sake, in this instance the life companies can only accept business from an adviser who complies with a certain requirement, eg regulation, therefore it could be imposed immediately.

Ultimately, as I have said in our submission, we would like to see an appropriate act that governs it and regulation to go with it, but it could be imposed as simply as bringing that on board. But of course one requirement for the self-regulatory organisation, the body controlling the registration, would have to be Treasury indemnities because otherwise they stand liable for prosecution if they take someone's registration away from them; similar to what is carried on in a number of different areas, and I believe the ISC has used in other areas themselves.

MR SMITH: Yes, well, there's an insurance power under the constitution for the Commonwealth, but when you're talking about extending this to a whole range including managed funds where insurance is not involved, had you sought advice in that broader - - -

MR LEGGETT: Not on the broader spectrum in terms of that, but certainly in terms of what currently fits in under the - the ISC regime, that's available there to already implement.

CHAIRMAN: Thank you very much.

MR LEGGETT: Thank you.

MRS NICHOLLS: Thank you, Wayne and Steven.

CHAIRMAN: Ladies and gentlemen, we're now going to hear from Gertrud Thompson, I believe. If you could for the record, please, just state your name and whether you in fact represent any organisation or whether you're speaking for yourself, and we'd be very pleased to hear from you. Thank you.

DR THOMPSON: I'm Gertrud Thompson, and I represent myself. Thank you for coming to Perth to give us the opportunity to talk to you. My comments will be directed toward the subject of international financial regulation. The concept of international regulation occurs on a number of occasions in your FSI discussion paper, albeit in a very limited way.

Chapter 8, which deals with consumer protection, has an important discussion in section 8.162 under the heading Examples Of The Type Of Measures That Might Be Taken are listed - "(1) promotion of international industry codes of conduct or ethics; (2) development of international industry dispute resolution arrangements; and (3) the establishment of international agreements or protocols as a basis for harmonising regulatory arrangements in as many jurisdictions as possible." But then in section 8.163 it states, "The inquiry has not formed a firm view whether it can or should make recommendations on these specific matters."

This expression of hesitancy causes concern, especially as this committee must be aware that seven financial groups have already found it essential to set up their own international regulatory bodies. For example, mentioned are chapter 8 section 8.155, the International Organisation of the Securities Commissions, and in chapter 9 section 9.13 the International Society for Standardisation and the Society for Worldwide Inter-Bank Financial Telecommunications, and some others.

I would therefore like to suggest that the subject of international financial regulation be taken on board by you. Further, I would propose that an international financial regulatory authority be established, a mega-regulator. Its first task would be the collection of taxes from tax avoiders who use tax havens for their deposits. This would not only recover the cost of the regulator but the money may be used to pay the United Nations Organisation, which could become the enforcing arm.

The next legislation would address and outlaw the existence of incognito numbered accounts. These accounts are a major

source of corruption worldwide. We know that billions of dollars have been deposited in these accounts since the 1930s, and in the last 15 years Australians have made their contributions with various scams. Once this legislation is in place and the period of grace for claiming the account has expired, unclaimed money mainly arising from illegal activities could be used to repay national debts. Non-cooperation from the government of the tax haven could result in sanctions.

Another major instability in the international market is the use of the futures market for currency speculation. The resultant losses have been causing great suffering to people in countries like Mexico and Russia, but I would like to point out that the Australian dollar could also be vulnerable. Legislation on the international futures market specially operating from tax havens is urgent and should be discussed in your report.

Once established the international financial regulatory authority would be able to legislate on future international financial problems as they arise. For example, commerce over the Internet is one such problem already under discussion. The FSI discussion paper states that, "It is of importance for Australia to be a major player in the international market." It compares our position with Singapore and Hong Kong, but if we are to be a leading player we must have ideas and courage.

Leadership is about ideas and courage. Therefore your investigations should encourage the Australian government to take a stand on creating the international financial regulatory authority in the international arena, otherwise the ever-increasing foreign debt and a deteriorating financial position with social problems, as referred to by Dr Turnbull, and more racial divisiveness will cause this FSI report to be found wanting.

So far Australia is not host to a single UN international agency, and the report could suggest that the international financial regulatory authority reside in Australia, as it is ideally situated away from the centre of world commerce and hopefully less corruptible. Then Australia would be in the forefront of international trade. Thank you.

MRS NICHOLLS: Thank you, chairman. Dr Thompson, could I ask you to elaborate your submission in the context of Australia's role in Asia?

DR THOMPSON: I am not an economist. I was a physicist and a traveller, and as such I ran across the tax havens and saw what was happening. I think it is an international problem of course. Everybody is in the same - most countries except maybe Japan are in the same position with the huge international debts which they have to finance, and they are therefore in the hands of the tax havens because they have to borrow the money from them.

This has made our democratic government, as far as I can see, a puppet of the tax havens and also that of others, right? Our position in Asia or any other position would improve enormously because the tax havens are cancer on the commerce. They are not truly a creative item and that, because a lot of people with a lot of money are involved, they don't want to have it changed obviously.

MRS NICHOLLS: A follow-on question: for Australia to be effective in carrying out the policy direction that you're advocating, which other countries would we need to have aligned with us on this, or do you feel that Australia could go it alone?

DR THOMPSON: No, not at all. I mean, the first people of course to try and get interested in this would be President Clinton who is in a very strong position because it's the beginning of a second term, and that's the strongest position an American president can be in because he won't be re-elected anyway, so now he can really act, if he wants to act - and naturally the OECD, because they're having enormous problems with this problem of tax havens because many of them are located in the OECD, like Luxembourg and Andorra and the Channel Islands and so on. So I am sure that the governments of the OECD - and the OECD reports are the only reports that have been against these tax havens, would in fact be happy with - maybe. I have tried to - I have written to many politicians. I have never had a satisfactory reply from any one of them, so I can't - - -

CHAIRMAN: There's an implicit assumption that tax havens are costing the Australian economy, I guess, to put it simply. Have you got any real substantive evidence that major Australian corporations, major chunks of the wealth of this country, are in fact avoiding tax in tax havens?

DR THOMPSON: Well, you see, I'm only - - -

CHAIRMAN: Forgetting the international issue.

DR THOMPSON: Yes, yes, I know.

CHAIRMAN: I'm just trying to put it to you in the Australian context.

DR THOMPSON: Yes, yes. I have only got what is known as public information, okay? I have no private information. The first part of the public information - that I read the newspapers, especially the English newspapers - is the enormous amount of tax avoidance on Mr Murdoch's part. So here is one item that - sorry?

CHAIRMAN: 80 per cent of his activities are outside this country.

DR THOMPSON: That's right. But I can't give you the information of how much Australian tax avoidance is.

CHAIRMAN: There's no suggestion, I might add, that the Murdoch - - -

DR THOMPSON: No, no, no - yes, yes.

CHAIRMAN: - - - organisation is in any way avoiding tax.

DR THOMPSON: The other very interesting part which I found very amusing is that - in my travels of course, I went for 4 years travelling around the world.

CHAIRMAN: I'm looking forward to it actually.

DR THOMPSON: Very good. With a backpack. I will send you my booklet, How to Travel Cheaply. Anyway what I found, for example, was I met people who were in the export business in South Africa, and they were the first to tell me about the scam of how you never report the correct amount of what was imported or exported but you always leave 10 per cent off. Well, 10 per cent is quite a lot on every turnaround. But somewhere who read the paper here in Australia said to me, "Trudi", he said, "You think it's only 10 per cent?" They didn't say, "This isn't true", they think the figure's even bigger. And always when they take this money of course it ends up in a tax haven. I cannot tell you that exactly but I think it's huge, because the tax avoidance is enormous.

CHAIRMAN: Do you mind if I ask the Treasury official to ask the next question?

MR SMITH: I'm just interested in understanding your particular approach to the issue. Are you looking at actually closing down tax havens in terms of their financial activities?

DR THOMPSON: Not necessarily, no. I think that once - well, first of all the international regulatory authority which would be an authority of well-understanding people - with a financial understanding, and hopefully one from each continent, Africa, South America and so on -

would of course have a far better understanding than I have of how to handle the matter. But as I say, two important items stand out. First of all is the tax avoidance people which would then have to pay tax on an international scale, not to each individual country, but to this authority which could then help finance the United Nations and finance the authority. But secondly the closing of the incognito accounts. These are the accounts without someone's name on it, right - with a number - of which there's a great deal, and of course we have heard a lot about the gold and the Nazi accounts recently but there are also a lot of other accounts like that. In fact - I don't mention names because I've been asked to, but there is in fact one case here in Western Australia - most amusing because the person is dead and the numbers aren't known to the family.

So I think that these are the outstanding things. But there are lots of things coming up, you see. There's the question of the financial market across the Internet. I mean there are a lot of unknown things that will be coming up.

CHAIRMAN: You'll appreciate a lot of our comments were actually directed at - - -

DR THOMPSON: That's right.

CHAIRMAN: - - - protecting retail consumers in that global - - -

DR THOMPSON: Exactly.

CHAIRMAN: - - - market that may evolve, which is not quite tax haven country.

DR THOMPSON: No. I mean once this authority is in place and it has dealt with the tax haven issue - that will be then finished - new issues will come up and this authority will be there in place to deal with international issues that come up, because we are in a totally deregulated situation and international issues will continue to be coming up which we can't even foresee, and which the Campbell report didn't foresee because - well, how could it have foreseen it in 81 what was going to happen. But we can foresee it and that's why I think it's essential that we deal with it.

MR BEERWORTH: Dr Thompson, how would this new authority, which I think would have a major role in imposing tax on international commerce, how would that authority link with the World Bank and the International Monetary Fund and other international financial agencies?

DR THOMPSON: Well, you see, I can't answer that question. I knew the late Dr Schlesinger from a family point of view. I don't know what

the present bankers are thinking. I don't have any more contact with economic professors; I am actually a second cousin or third cousin of Raymond Goldsmith, whom you may have encountered in your studies, but he's also dead now, so I have no-one to talk to, and I really don't know.

I want this authority established so these people can get together and have a central focus where to discuss this question because its also a question of immorality.

CHAIRMAN: You don't think there would always be some part of the world, even if we got it 95 per cent stitched up, that would affect - - -

DR THOMPSON: Always, always.

CHAIRMAN: Isn't that the dilemma?

DR THOMPSON: Always. I mean, whatever regulation you people make - - -

CHAIRMAN: So how practical is this really?

DR THOMPSON: Well, this is truly the problem with all regulations. You make a regulation and - - -

CHAIRMAN: Well, I'm just posing it to you.

DR THOMPSON: - - - and the smart cookies would be sitting there and saying, "How can I get around it?"

CHAIRMAN: Someone will find a rock and do it, won't they?

DR THOMPSON: Right, right. But at least we have a regulator and the public and everybody will be aware of the scam. And since, hopefully, 90 per cent of all people are honest, or maybe even 95 per cent of people are honest - - -

CHAIRMAN: Say 99. I mean - - -

DR THOMPSON: Yes - it will mean that actually - say for example you own your residence in Jersey or Guernsey or - they might also get fed up with this. They might say, "Why should we be in this scam for these 10 per cent of people who are making money out of us." In fact once I think the authority says, "This has to stop", the people in these places will want to stop it. Not everybody of course. And one of them will probably be opening up in Greenland or something - I mean no question. But I would like you to take it on board.

CHAIRMAN: Okay.

DR THOMPSON: That's what I think is important.

CHAIRMAN: Right. Well, I think it's a very clear message to us and thank you very much.

DR THOMPSON: Thank you.

MRS NICHOLLS: Thank you, Dr Thompson.

CHAIRMAN: Our last participant today is Mr John McKay. John, if you could come forward. You've been here all morning, have you not?

MR McKAY: I have, sir, yes.

CHAIRMAN: So I don't need to repeat any of my earlier remarks; you can sense how it all works. As I say, the best thing is if you can give us time to ask you some questions but it's how you wish to play it. If you wouldn't mind just repeating your name for the record?

MR McKAY: Sure. John McKay is my name, I'm here representing myself. Mr Chairman, members of the committee, ladies and gentlemen: a trans-disciplinary approach to social dynamics. John Kavanagh entitled his article The Great Money Revolution and mentioned evolution. Money has evolved over archaeological time from gathering to barter to money. The first great revolution of money occurred when a commodity was stamped at a mint for weight and fineness. Aristotle referred to money as a symbol, it's principal use being exchange.

Another great money revolution occurred when the goldsmiths wrote false receipts for gold not stored in their vaults. The practice was institutionalised by the Bank of England. In agricultural science, structure and function of plants usually correlate. The structure of money over time has changed. It was a commodity-backed symbol for exchange, now it symbolically backs production and limits exchange. Aquinas insisted that money should serve economics and politics, not be their master. He warned of greed when money was used in its secondary role. He condemned outright usury in the technical sense. This is summarised in the Latin pun, "Mutum teum meum." He reaffirms that morality relates to individual human actions.

Moral values have practically no place within the science of economics. The morality of modern banking is not well researched. Modern economics purvey false and pseudo-satisfiers of fundamental human needs. Evidence is mounting that economic rationalism is destroying the social fabric of nations.

The first history of the federal reserve system reveals the enormous power of the money creators over economics. Gustav Thebon lamented the lack of living and responsible leaders. John Howard showed moral courage in meeting the Dalai Lama. Did that courage desert him at the IMF meeting? Costello established this FSI, Wallis, Mr Wallis, collates the recommendations but Howard is responsible for rejecting any or all of them.

Organic evolutionary theories range from mechanistic and materialistic to the vitalistic and spiritual. Social organisations rely upon the social norms of trust, cooperation and honesty. If materialism permeates these norms, then who is to say which acts are criminal? Hodson and Bland have shown that our present debt money system is exponential and unsustainable. Taxation must therefore rise to cover interest bills on national debts. Wallis has shown a degree of moral courage in raising the taxation issue.

Those who recommend and enforce change upon others need to be aware of many factors. (1) Graham Towers showed that governments do have power over bank operations. (2) The Maastricht Treaty seeks absolute power for the money creators. (3) Money can become useless and extinct. (4) Science demonstrates a creative power behind the big bang.

The Australian and American constitutions allow their governments to create the nation's money as non-debt. This, as the base of a financial system, would allow Howard to give "good government to all Australian people" and "is essential to the wellbeing of all Australians."

The human body evolved through cooperation and its organs do not operate at high efficiencies. Human families must deteriorate if competition and efficiency levels exceed the threshold of individual pain, endurance, submission and tolerance. Thank you.

CHAIRMAN: Would you be able, Mr McKay, to be a little bit more specific to this inquiry as to what you would like us to take on board from your points you have just made, given that we are an inquiry with terms of reference? We have some strict limitations but we're endeavouring to get out of everyone's viewpoint issues that are relevant.

MR McKAY: I mentioned your name as having some moral courage in looking at the taxation. I don't have the reference but I think it hit the headlines in the Australian a few days back. I guess what I would like to see happen is for your committee to have the moral courage to go over and beyond the terms of reference and recommend that our government also have the moral courage to take back from the banks that power to create money which rightfully throughout most of time has belonged to governments and does not rightfully belong to banks. Banks could then do their little duty of borrowing money and loaning money and all those other things.

CHAIRMAN: So strict governments control the money supply?

MR McKAY: No, not control, issuance. And there is a difference.

CHAIRMAN: Okay.

MR BEERWORTH: Just on that same point, if I may, Mr McKay. In your written submission you posed a number of broader questions to which I confess we haven't really addressed ourselves and I wonder if you might like to comment briefly. You say we should address issues such as the true objective of politics, the true purpose of economics and the true structure and function of money. You've covered money, I think. Did you want to comment at all on politics and economics for us?

MR McKAY: Well, my understanding of a democracy is that people - or to quote a famous American - "government of the people by the people". I don't remember the rest but I think you know what I'm saying. As I see it now worldwide, banks really control governments and governments therefore do not act in the best interests of people. Refer Max Mieff's book on fundamental human needs; how he has examined and in various countries held workshop and found that most economics only supply false and pseudo-satisfiers of fundamental human needs. This in turn leads to social dislocation, violence, drug-taking and all the rest of it.

MR BEERWORTH: Thank you, Mr McKay.

MRS NICHOLLS: Thank you, chairman. Mr McKay, we have had a view put to us that the increased use of technology in financial services is having a depersonalising effect on the way services are delivered to some segments of the community. I'm inferring from your remarks that you might feel that technology is perhaps going further than that in having a dehumanising effect on some parts of the economy. Could I ask you to comment in the context of financial services which aspects of technology give you the most concern.

MR McKAY: I haven't examined the aspects of technology. I've looked more at the philosophical points, and I see that depersonalising and dehumanising can be taken in two contexts, the two philosophies that I mentioned - in the materialistic or the spiritual. If you take a totally materialistic view then persons just become machines to be at the service of technology, at the service of economics, at the service of politics. If you take the other view, then people are for real; have worth and should be number 1 in the scheme of things. So they should be

served by technology, should be served by economics and should be served by politics.

MRS NICHOLLS: Thank you.

CHAIRMAN: Thanks very much, Mr McKay, we appreciated your attendance.

MR McKAY: Thank you, Mr Wallis.

CHAIRMAN: Ladies and gentlemen, that concludes this morning's session. I would just again thank you all for your attendance and particularly those who contributed. Thank you.

AT 11.51 AM THE INQUIRY WAS ADJOURNED UNTIL
THURSDAY, 12 DECEMBER 1996