Citizens Electoral Council of Australia

Postal Address: PO Box 376, Coburg Vic 3058
Phone: 1800 636 432 Fax: 03 9354 0166
Home Page: www.cecaust.com.au **Email:** cec@cecaust.com.au
Authorised by R. Barwick, 595 Sydney Road, Coburg, Victoria 3058. Printed by Citizens Media Group Pty Ltd., 595 Sydney Road, Coburg, Victoria 3058.

Independent Political Party

1 February 2018

ASIC report more proof Australia needs Glass-Steagall banking separation

A report by Australia's investments watchdog ASIC (Australian Securities & Investments Commission) reveals that the vertically-integrated structure of banks makes it easier for them to fleece their customers. The vertical integration of banking, also known as universal banking, turns banks into supermarkets for all kinds of financial services—deposits and loans (commercial banking), investments, insurance, stock broking, financial advice, etc. ASIC's report provides yet another reason Australia needs to break up its banks with a Glass-Steagall separation of commercial banking from all other financial services.

The ASIC report, "Financial advice: Vertically integrated institutions and conflicts of interest", released 24 January, reviewed the financial advice provided by Australia's five biggest financial institutions: CBA, ANZ, NAB, Westpac and AMP. This has been a scandal-ridden sector of the financial system for more than a decade. The complicity of banks in such financial debacles as Storm Financial, the Timbercorp and Great Southern managed investment schemes, Opes Prime, and many others, has left thousands of Australian families ruined.

The report's findings were entirely predictable. Nearly 70 per cent of the funds that banks advised their customers to invest went into in-house products sold by the same bank. This was despite the fact that nearly 80 per cent of the investment products that bank staff were authorised to sell were from other institutions. In other words, bank staff had a clear bias in pushing their bank's products. Anyone who has queued at a bank simply to cash a cheque or such-like only to have the teller recommend insurance or some other product has experienced this bias.

For its report ASIC tested the advice bank staffed provided to customers to see whether it satisfied the requirement that banks give advice in the "best interests" of the client. The report found that in 75 per cent of the cases ASIC reviewed, the advice did not satisfy the "best interests" requirement. Moreover, in 10 per cent of the cases ASIC found the advice "was likely to leave the customer in a significantly worse financial position". Given that the five biggest financial institutions have well over 80 per cent of the Australian population as clients, this 10 per cent figure represents a huge number of potential bank victims.

Old problem

ASIC's report is not surprising. Under the neoliberal law of the financial jungle, predatory banks will prey on their customers—if they are allowed to. The question is, why have they been allowed to?

This problem was addressed and solved 85 years ago in the USA. In 1933 hearings of the US Senate banking committee, legal counsel Ferdinand Pecora exposed that the biggest Wall Street banks, most notably National City Bank, the forerunner of today's Citigroup, had aggressively targeted their depositors with dodgy investment advice. National City had unleashed an army of bond salesmen on to their customers, who were talked into buying bonds of all sorts, including the debts of failing banana republics. Often, the bonds National City sold to their unsuspecting customers raised funds that were used to ensure loans were repaid to National City—the bank was simply transferring losses it should have worn for bad loan decisions on to its unsuspecting customers.

The Pecora hearings led to the new Franklin Roosevelt administration passing a raft of laws to protect consumers from financial predators. Foremost among them was the *Glass-Steagall Act* 1933, which walled off deposit-taking commercial banks from securities trading, insurance and other financial services. Banks no longer had investment arms into which they could lure customers. As well as consumers, Glass-Steagall protected essential banking services from risky financial speculation, until corrupt, deregulation-crazed Wall Street bankers and Washington politicians succeeded in having it repealed in 1999.

Australian MPs: Break up the banks!

Now, more than eight decades after the Pecora hearings and the passage of the *Glass-Steagall Act*, ASIC has similarly discovered that "Conflicts of interest are inherent in vertically integrated firms". In response to ASIC's report, some of the leading bank critics in Parliament have again raised ending vertical integration, which means breaking up the banks. "Nationals Senator John Williams said it may be time that was addressed", Crikey.com.au reported 25 January. *The Australian* of the same day reported Greens Senator Peter Whish-Wilson saying, "This needs to be one of the core issues the Royal Commission has to look at and the commissioner shouldn't be afraid of recommending breaking up existing vertical integration within the big banks." In December the Nationals and Greens had agreed to have vertical integration included in the terms of reference for a banking inquiry, but at the banks' behest Prime Minister Malcolm Turnbull jumped in at the last minute to take control of the process, announcing a royal commission with terms of reference that excluded everything the Nationals and Greens had agreed on, including vertical integration.

ASIC's report is the latest example of an Australian banking problem, to which the solution is Glass-Steagall. In early January, Small Business Ombudsman Kate Carnell called for banks to be classed as essential services, which Glass-Steagall does in principle. And for a number of years Carnell and other voices in the business community, including former ANZ Bank director John Dahlsen, have criticised the banks for starving small businesses of credit while they speculate in the overvalued housing market, mortgage securitisation and related derivatives contracts, which Glass-Steagall would address by stopping banks from diverting credit into speculation, leaving credit available for productive businesses.

Warning to MPs: More than 1,000 submissions to Senate inquiry prove Australians despise 'bail-in'

Reflecting the overwhelming public opposition among Australians to losing their savings to prop up failing banks, the Senate Economics Legislation Committee revealed on 25 January that its inquiry into the APRA "bail-in" bill has received more than 1,000 submissions from the public. The vast majority of the submissions objected to the bail-in provisions of the bill, which would empower the bank regulator APRA (Australian Prudential Regulation Authority) to convert into worthless shares, or write off, the savings of unsuspecting mum-and-dad investors, and possibly depositors, in order to cover the gambling losses of banks and keep them afloat.

This is a stunning response—the average number of submissions to a Senate Economics Committee inquiry is 30! The submissions came from Australians who learned about the bill not from the media, which has largely blacked out any reporting of it, but from the Citizens Electoral Council. Once informed, a large number were motivated to write to the committee to express their objection. Unlike most politicians who reply to their constituents with identical form letters written by their superiors, the people who made submissions went to the effort to write their own letters.

In the face of this many submissions, which were made before the 18 December deadline, it is clear that the committee's subsequent decision not to hold a public hearing is a cover up. A hearing would allow a public examination of the content of the submissions, including the all-important issue of whether the conversion or write-off provisions could extend to deposits, and concerns about APRA's secrecy and complicity with the banks, which former APRA employees have raised.

The government, which controls the committee, does not want these issues aired. From the beginning, Malcolm Turnbull and Scott Morrison have tried to minimise publicity for this bill—and the media has accommodated them. For the same reason, Turnbull rigged the terms of reference for the banking royal commission to exclude any examination of APRA and its policies. However, the scale of the public response to the Senate committee sounds a warning to MPs: Australians who are informed emphatically oppose bail-in, so be prepared for an electoral backlash if you agree to pass this bill.

Bail-in extends to deposits

It is undeniable that the APRA bill clears the way for the bail-in of hybrid securities, which APRA allowed the banks to sell to hundreds of thousands of unsuspecting self-funded retirees and self-managed super funds. That alone is grounds to oppose the bill, but even more concerning is that the bill as written empowers APRA to extend a bank bail-in to deposits. Both the government and APRA deny this. For instance, APRA's submission to the Senate committee states, with forcefully underlined words, that the bill "does not include a statutory power for APRA to write-down or convert the interests of other creditors in resolution, including depositors of a failing ADI (often referred to as a 'bail-in' power). … APRA also notes, and fully agrees with, the statement in the FSI [2014 Financial System Inquiry] Final Report that, in Australia, deposits should not be included within any such framework, and should not be subject to bail-in."

As Shakespeare would say, "Methinks APRA doth protest too much." Firstly, APRA does the bidding of the global banking regulation apparatus centred in the Bank for International Settlements in Switzerland, which since 2009 has overseen the implementation of a global bail-in regime that in every other jurisdiction applies to deposits. Secondly, the reassurances of APRA and the government are meaningless—the wording of the bill is what matters.

On 23 January the CEC lodged a supplementary submission to provide the committee with legal analysis that the bill is worded to ensure that APRA does indeed have the scope to extend a bail-in to deposits. Following is the summary of the CEC's submission, which outlines the legal analysis:

1. Summary of supplementary submission

In summary, this Supplementary Submission has been considered necessary as a consequence of communications by Members of Parliament to constituents which seek to allay constituents' concerns as to the Bill's provisions concerning "bail-in"—the conversion and write-off provisions—and in particular their extension to deposits. The communications contend that the Bill does not provide any authority for the Australian Prudential Regulatory Authority ("APRA") to bail-in deposits in the event of an ADI bank getting into financial difficulties.

This contention has also been repeated by various Authorities.

Bail-in of deposits has caused considerable hardship overseas where it has been employed and is of increasing concern to the Australian community.

This Supplementary Submission is accordingly being lodged to draw to the Committee's attention the relevant provisions in the Bill relating to bail-in (whether explicit or implicit) and the concerns of this organisation and the community generally as to the nature and extent of those provisions.

As elaborated in this Supplementary Submission:

- by all definitions financial "instruments" includes deposits;
- the Bill clearly states that its conversion or write-off (bail-in) provisions apply to Additional Tier 1 and Tier 2 capital or "any other instrument";
- if the Bill only intended to refer to instruments which include conversion or write-off terms, all such instruments come under the definition of Additional Tier 1 and Tier 2 capital, and the additional clause "or any other instrument" is therefore unnecessary, but sufficiently broad language to give APRA scope to extend a bail-in to deposits;
- the author/s of the Bill's Explanatory Memorandum foreshadow a future scenario under which this Bill will allow APRA to determine through its prudential standards that instruments not currently considered to be capital, such as deposits, could be reclassified as capital for the purpose of conversion or write-off—bail-in.

It therefore remains our contention that the Bill does provide APRA with power to bail in deposits and for this and the reasons appearing in our primary Submission of 18 December 2017 that the Bill should be rejected.

The CEC is continuing the fight to defeat the APRA bail-in bill—join us!