

Review of Australia's Consumer Policy Framework

Submission to the Productivity
Commission

May 2007



INTRODUCTION

Australia and New Zealand Banking Group Limited ('ANZ') is pleased to provide comments on the Productivity Commission *Consumer Policy Framework—Issues Paper*, released in January 2007.

ANZ is one of the largest providers of banking and financial services to all parts of Australia and operates within a regulatory framework the objectives of which are to protect consumers and improve consumer welfare. ANZ is subject to:

- Fair trading laws across a range of jurisdictions including the Commonwealth and States and Territories;
- Industry specific laws such as the Uniform Consumer Credit Code; and
- Self-regulatory measures such as the Code of Banking Practice and the EFT Code of Conduct.

ANZ therefore considers itself well placed to comment on Australia's consumer policy framework.

The subject of the inquiry is broad ranging, and this submission covers those themes raised in the Issues Paper in which ANZ has a particular interest.

1. JURISDICTIONAL HARMONISATION

ANZ operates across all Australian jurisdictions and is required to comply with a range of State and Territory as well as Commonwealth regulation. This includes consumer protection laws under the Commonwealth *Trade Practices Act 1974* and individual State and Territory Fair Trading Acts.

State and Territory fair trading legislation is necessarily different from Commonwealth legislation due to the limitations of Commonwealth power under the Australian Constitution. However, based on the 1983 Commonwealth, State and Territory Consumer Affairs Ministers' agreement, individual State and Territory legislation was originally intended to be uniform across all jurisdictions with the State and Territory legislation to be modeled on the consumer protection provisions of Part V of the *Trade Practices Act 1974*.

Despite the intention for a uniform set of fair trading laws across the country, there have been legislative developments in various States and Territories in recent years that have created some inconsistencies. It appears that State and Territory governments are increasingly using fair trading legislation as a means to drive consumer protection initiatives which do not necessarily have national support.

An example of this is the introduction of new obligations for credit card limit increase offers in the Australian Capital Territory. Details of this example are provided in the shaded box below.

Inconsistency in State and Territory laws is at odds with the existence of national markets in financial services. Consumers today shop for goods and services largely without regard to State and Territory borders and they have gained from this through lower costs, greater efficiency and increased choice.

The shift to a national market for financial services has been facilitated through greater use of internet banking and the availability of online applications for financial products such as credit cards, home loans and transaction accounts. For example ING Direct, as well as BankWest, have competed vigorously in the market for high yield deposit accounts although they do not have a significant physical presence through a branch network.

ACT Credit Card Limit Increase Amendments

In 2002 the ACT introduced obligations on credit card providers to ask existing customers for new information on income and expenditure to assess manually whether a credit limit increase could be granted, rather than relying on the automated behavioural scoring tool developed and used by banks (see section 28A of the *Fair Trading Act 1992* (ACT)).

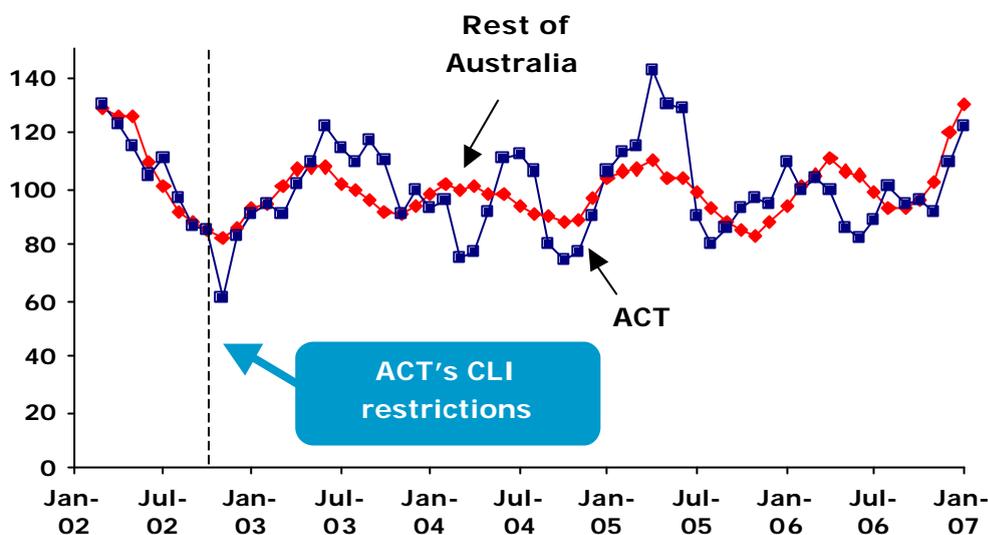
ANZ's analysis of its credit card customer base has shown consistently that behavioural scoring is a significantly more reliable assessment method than manual assessment of a customer's financial information. The major weakness of manual assessment is that it relies on the accuracy and currency of information provided by customers as opposed to a behavioural history.

In April 2005, ANZ conducted a trial in which customers applying for a credit limit increase in the ACT were asked to complete statements of financial position. The study found that 24% of forms could not be processed due to errors and omissions in financial details. Around 12% contained obvious data errors while a further 12% of forms appeared to contain incorrect income details when viewed in conjunction with the living expenses stated. In other words, almost half of the statements of financial position contained errors, making them less reliable than behavioural scoring.

The ACT's amendment put it out of step with other jurisdictions. It added a further step to the process of granting a customer a credit card limit increase and for a relatively small segment of ANZ's customers. This has added cost and reduced efficiency but for not discernable customer benefit.

Chart 1 below shows credit card delinquency rates for the ACT compared with the rest of Australia. While data for the ACT is more volatile than the rest of Australia due to the small population, the Chart shows that credit card delinquency rates in ACT have moved identically to the rest of Australia. This suggests that the ACT's credit limit increase restrictions have had no observable impact on ACT residents' credit performance.

Chart 1 Delinquency rates of ANZ credit card customers in ACT and the rest of Australia



Note: Delinquency rates show the percentage of customers 90 or more days past due in the last 12 months. Data for ACT and Rest of Australia has been indexed to give an average of 100 for 6 months prior to November 2002. It should also be noted that delinquency rates shift over time as credit policy and economic conditions change.

Source: ANZ Credit Cards Australia

ANZ believes that the objective of effective and efficient consumer protection legislation, as was intended under the original agreement, is not met where a patchwork of inconsistent State and Territory laws is allowed to develop. Inconsistencies between jurisdictions are contrary to the development of a national market, such as in financial services, and this has the potential to impact on companies operating in these markets.

The Impact of Inconsistent Legislation

Fair trading laws are designed to protect consumers, through businesses complying with those laws, or in those instances where they do not, through the application of corrective action. A lack of uniformity of fair trading laws affects the way organisations that serve national markets, such as ANZ, work within these laws and ensure compliance.

ANZ's experience is that differences in laws can lead to a number of compliance issues. Firstly compliance registers and compliance monitoring arrangements become complex. They must not only reflect the differences in substantive laws across jurisdictions, but also the circumstances in which the laws of one jurisdiction can apply over the laws of another.

For example, inclusion of fair trading obligations in ANZ's compliance register is currently cumbersome, as multiple pieces of legislation are required to be cross-referenced to the same obligation. This creates a situation where staff are

required to monitor and update multiple pieces of legislation for a single obligation.

Secondly, a lack of uniformity can increase the length and complexity of compliance training used to communicate the compliance requirements of the various legislative regimes to ANZ head office staff, branch staff, call centre staff, finance brokers, financial planners and financial advisers.

It is important that any ANZ communication or training to an audience, potentially as large as over 13 000 staff in ANZ's Personal Division, be clear and concise so that it is retained by the target audience. The material must also be meaningful to staff with a clear rationale. The requirement to factor multiple legislative regimes into compliance training can complicate these objectives.

This increased complexity not only increases ANZ's communication and training costs but can also increase the risk of compliance breaches because:

- The compliance requirements of one jurisdiction may be confused with another by staff serving the national market;
- Compliance requirements may never be fully understood because the training material is necessarily complex; and
- Changes to one state or territory's legislation may be more likely to be overlooked when it is only one part of a patchwork of State and Territory legislation.

Thirdly, the complexity of complying with multiple legislative requirements generally increases reliance on professional advisers which in turn increases the operational costs of an organisation. These costs are then passed on to consumers.

Another implication of inconsistent legislation is that an organisation such as ANZ may at times apply the most onerous State or Territory law in a particular area as a 'fail safe', as this avoids the complexity and risk associated with complying with multiple legislative requirements.

ANZ notes that, in response to its Consumer Credit Review, the Victorian Government is currently seeking to introduce changes independently from other jurisdictions. On one hand, the Victorian Government's response to the review recognised that credit is a national market and that issues surrounding the small amounts lending market should be progressed nationally. On the other hand, its response to the recommendation that credit providers should allow customers to positively elect their credit limit increase was that the Government would amend the *Fair Trading Act 1999* (Vic) with no indication that it would consult with other jurisdictions to achieve consistency.

ANZ supports the recommended reform that would allow credit card holders to nominate a credit limit increase that they believe is appropriate for their circumstances and said as much in its submission to the Victorian Consumer Credit Review (May 2006). However, for this initiative to be effective, in what the Victorian Government itself has described as a national market, it needs to be implemented in all States and Territories, rather than allowing a patchwork approach to regulation of consumer credit to develop.

Ways to Harmonise Across Jurisdictions

ANZ recommends that a more effective mechanism be implemented for coordinating the policy development and application of fair trading across jurisdictions. Although the intention in the 1983 agreement was to enact uniform fair trading legislation, this goal has proved to be elusive and as a result, there are substantial differences in State and Territory Fair Trading Acts.

One way harmonisation could be achieved would be to revisit that agreement to include some positive obligations on States and Territories to ensure consistency in consumer protection laws. One such mechanism could be Commonwealth 'incentive payments' to States and Territories similar to those that applied under the National Competition Policy (NCP). Under the NCP process the Commonwealth set aside \$3.5 billion in competition payments to be made to States and Territories as incentives for these governments to undertake often politically difficult reforms.

A similar style of incentive regime could be used to encourage States and Territories to harmonise fair trading laws and to work together to ensure this consistency continues with national agreement on any changes.

Another way of achieving harmonisation would be to adopt a 'template model', as exists in the Australian Uniform Credit Laws Agreement 1993. If adopted for consumer protection laws, this would require States and Territories to enact laws to adopt a template Fair Trading Act (along with any amendments) and for any changes to this template legislation to be approved by a majority of the Ministerial Council of Consumer Affairs.

An alternative to this would be for States and Territories to, similar to the 1983 agreement, mirror those relevant provisions of the TPA, but be limited to only those provisions. This would mean that the decision to, and manner in which to address new issues surrounding consumer protection would be the responsibility of the Commonwealth. This however, would ultimately result in States and Territories referring their right to fair trading law policy to the Commonwealth.

2. GENERIC VERSUS INDUSTRY SPECIFIC REGULATION

ANZ is subject to a combination of generic consumer legislation, such as the *Trade Practices Act 1974* and individual State and Territory Fair Trading Acts, and also industry specific regulation such as the Uniform Consumer Credit Code.

Improving the effectiveness of generic regulation

Generic regulation is generally the most appropriate consumer policy tool as it confines the cost of regulation to those businesses that breach the provisions. However, because generic regulation is generally adversarial in nature with an *ad hoc* enforcement process, the precise application of regulation is at times uncertain—especially in those circumstances where new legislation has not been ‘tested’. This results in a situation where the regulatory outcome may be unknown and has the potential to be costly.

For example, some regulators adopt an approach where they are unwilling to provide guidance to industry on the correct interpretation of regulation and instead use the court process to do this. This results in a situation where a company may inadvertently fail to comply with regulation and as a result face costly legal proceedings, or alternatively adopt an unnecessarily conservative ‘fail safe’ approach to compliance.

One way of addressing this would be to accompany generic regulation with greater industry assistance from the appropriate regulator. This assistance could take the form of non-binding guidance notes, compliance education programs or simply establishing effective and open communication channels for advice.

A good example of this can be seen with the introduction of the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* (AML/CTF Act) which is administered by the Australian Transaction Reports and Analysis Centre (AUSTRAC).

AUSTRAC Implementation of AML/CTF Act

AUSTRAC has indicated to industry that it will be implementing the AML/CTF Act over a period of two years and during this time it will be actively assisting businesses in meeting their requirements through awareness raising, ongoing education, advisory visits and compliance monitoring.

AUSTRAC has also indicated that during this period civil pecuniary penalties will only be initiated where a reporting entity has failed to take reasonable steps towards compliance with its obligations.

This approach by the regulator shows a desire to ensure compliance through education and assistance rather than potentially adversarial enforcement.

The need for industry specific regulation

ANZ believes that industry specific legislation can be useful in correcting market failures that cannot be addressed by generic legislation. However, if used excessively industry specific legislation has the potential to hinder innovation in that market and lead to an overly prescriptive and complex regulatory environment which can result in increased compliance and administration costs.

Industry specific legislation should therefore be seen as a last resort solution to market failure and it should complement rather than replace generic legislation.

Care also needs to be taken to ensure that industry specific legislation appropriately targets the market segment where the market failure exists and does not unnecessarily apply to other functioning markets. An example of this was seen in measures proposed by state governments to address excessive pricing in the small amount loan market.

Regulating the Small Amount Loan Market

The small amount loan market has been characterised by excessive pricing caused by a lack of competition. Governments therefore examined industry specific regulation to attempt to address the market failure.

The New South Wales Government developed an appropriate legislative response by implementing an interest rate cap of 48 per cent per annum (factoring in both interest charges and fees). This cap was effective at regulating clearly egregious lending practices while at the same time providing a legislative 'safety net' as the short-term small amount credit market develops. Most importantly, the legislative intervention was put in place where the market failure is present and not across the entire mainstream credit sector.

By contrast the Victorian Government's Consumer Credit Review considered implementing a regime whereby all consumer credit fees and charges would be reviewable on the grounds of 'unreasonableness'. This approach would have involved legislative intervention in the mainstream market when the clear market failure was in the non-mainstream sector. The Victorian Government has not gone forward with this proposal.

3. SELF-REGULATION

Self-regulation can, in certain circumstances, be an effective alternative to government regulation and offers a more flexible and less costly option for both business and consumers.

ANZ has adopted the banking industry's self-regulation tool, the Code of Banking Practice (CoBP), which sets out the industry's key commitments and obligations to customers on standards of practice, disclosure and principles of conduct for banking services. The CoBP applies to personal and small business banking customers and is contractually binding on those banks that adopt it. The current version of the CoBP was developed in consultation with consumer advocates, business groups, ASIC and other stakeholders and incorporates periodic review as well as independent monitoring.

As noted in the *Industry Self-Regulation in Consumer Markets—August 2000* report, prepared by the Taskforce on Industry Self-Regulation, the circumstances where self-regulation is likely to be most effective will depend on the nature and extent of market failure, the market structure, industry and consumer interests. The CoBP is a highly effective self-regulatory tool because of the nature of the industry which is characterised by:

- A small number of large and mature firms;
- A highly competitive environment;
- Representation by an active industry association, the Australian Bankers' Association (ABA); and
- A strong sense of the value of reputation and corporate responsibility, including not only to its customers but to the community as a whole.

Further, nearly all banks that provide services to retail customers subscribe to the CoBP.

The CoBP success is also supported by the industry's dispute resolution scheme, through the Banking and Financial Services Ombudsman (BFSO), and, as previously noted a compliance monitoring scheme, the Code Compliance Monitoring Committee (CCMC).

The BFSO provides an accessible alternative to other dispute resolution remedies (such as court proceedings) for individuals and small businesses that use financial services. While the BFSO is funded by industry, it is an incorporated entity with Directors comprising three industry Directors, three public interest Directors and an independent Chairman. The BFSO is able to provide an independent and prompt resolution, at no cost to the consumer, which is binding on banks if the disputant accepts the decisions. If the disputant does not accept the decision they are able to proceed with any other remedies, such as court action.

The CCMC is responsible for monitoring bank compliance with the CoBP. The CCMC has been set up as an independent body with consumer, small business and banking industry representatives. It has the power to investigate complaints from anyone who thinks a bank has breached the CoBP and make a decision on whether that breach occurred. If the breach is serious, or a bank fails to remedy a breach, the CCMC can publicly name the bank in its annual report. Consistent with the fact that banks have a strong sense of reputation, the ability to 'name and shame' is an effective deterrent against breaches of the Code.

One aspect of self-regulation that can impact on its effectiveness is the need to seek industry agreement for the regulation to be widely adopted and accepted. Difficulty in reaching industry agreement can lead to delays in finalising self-regulation or certain aspects being applied at a level lower than the current practice of some industry players.

To address this issue, it is important to ensure that self-regulation design and review is done in conjunction with government and consumer advocates. These third parties can add an independent and legitimate viewpoint on areas of industry disagreement.

However, ANZ would also note that self-regulation results in industry incurring the full cost of design, implementation and administration of regulation and these costs are likely to be passed on to consumers.

4. POLICY TOOLS

Meeting the objectives of consumer policy does not always require government intervention in the marketplace. In some instances the market can complement government policy, or even remove the need for intervention.

One example of this is ANZ's work in financial literacy. Consumers of financial products have the potential to be disadvantaged and vulnerable due to a lack of financial literacy. A lack of financial literacy diminishes a consumer's ability to make informed and confident decisions regarding their budgeting, spending and saving as well as their use of financial products and services, from every day banking through to borrowing, investing and superannuation. It also leaves people vulnerable to being scammed.

Customers with good levels of financial literacy tend to hold more financial products, avoid buying products and services that are not suitable to them and are able to plan for their futures and accumulate assets over their lifetimes. Consumers with good levels of financial literacy also tend to promote competition in financial markets.

To determine the extent to which financial literacy was a problem in Australia, ANZ commissioned research into adult financial literacy in Australia in 2003. This primary, independent research aimed to better understand the nature, cause and

consequences of low levels of financial literacy. In 2005, ANZ repeated its research and also examined the issue of financial difficulty. In 2004, ANZ also commissioned research into size and nature of financial exclusion in Australia.

One of the most significant findings of these surveys was the strong link between socio-economic status and levels of financial literacy. While ANZ cannot solve this problem alone, it has focused on helping some of the most vulnerable people by developing deep partnerships with community organisations.

These partnerships have been used to implement a number of innovative programs to improve financial literacy and financial inclusion, such as MoneyMinded, Saver Plus and Progress Loans.

MoneyMinded

ANZ supported the development of MoneyMinded, a comprehensive financial education program, to improve financial literacy and help people make better and more informed decisions about their money.

ANZ has initiated the development of two MoneyMinded programs. Firstly workshops delivered by community educators and financial counselors working with people facing financial hardship to help them develop their financial management skills and capabilities. And more recently, the introduction of an online program available to anyone interested in improving their money management skills.

The development of MoneyMinded was initiated and funded by ANZ with essential contributions from community sector and education experts, including the national financial counseling peak body, the Australian Financial Counselling and Credit Reform Association.

An important feature of MoneyMinded is that it provides unbiased consumer education and does not contain any ANZ branding or promotion of our financial products and services.

An evaluation by RMIT University found that 15 279 people participated in MoneyMinded for the year to 30 September 2006, exceeding ANZ's target. Focus group research showed that the most significant impact of MoneyMinded was increased confidence in dealing with financial issues, including creditors and banks.

Saver Plus

Saver Plus is a financial literacy and matched savings program developed to help families on low incomes set and achieve a savings goal, and establish a long-term savings habit. Saver Plus provides financial education training, offering personal coaching support and matching every dollar saved with an additional \$1 (up to \$1000 in matched funds) towards primary, secondary and adult vocational education costs.

Saver Plus was developed by ANZ in partnership with the Brotherhood of St Laurence. The program has been extended through partnerships with Berry Street Victoria, The Smith Family, the Benevolent Society and most recently, the Victorian State Government (Department for Victorian Communities).

More than 660 families participated in the Saver Plus pilot program between 2003 and 2005, together saving more than \$617,000 and were rewarded with matched savings totaling \$1.1 million by ANZ.

With new funding (ANZ has pledged \$3 million to match participants' savings) ANZ and its community partners have set a target to deliver Saver Plus to 5400 individuals and families on low incomes by 2009. The Victorian Government will contribute \$1.35 million over the three years to extend Saver Plus to a further 1800 Victorians on low incomes.

Progress Loans

In May 2006 ANZ and the Brotherhood of St Laurence launched Progress Loans, a pilot program which provides small affordable loans of between \$500 and \$3000 to people on low incomes for essential household items such as whitegoods, furniture, computers, cars, car repairs and hot water systems.

Progress Loans was developed in response to ANZ's research into financial exclusion which showed that some Australians struggle to access appropriate, low-cost, fair and safe financial services from mainstream providers.

Results from the pilot are encouraging, with 57 loans totaling \$70,387 approved by 30 September 2006, a 70 per cent approval rate and no loans in arrears.

ANZ's research and innovative solutions, in partnership with other organisations, to the issues of financial literacy and financial exclusion demonstrates how some consumer issues can, and are, being addressed by the market. Improving financial literacy in our community is not only a core social responsibility for our business but it is also essential to its long-term success.

ANZ shares its financial literacy and inclusion resources widely amongst industry, government, regulators and community stakeholders. ANZ's CEO, John McFarlane, is a Board member of the Australian Government's Financial Literacy

Foundation. ANZ has also supported a number of international experts in financial literacy and inclusion to visit Australia to share best practice and inform our thinking around these issues with our staff and our stakeholders.

5. CONCLUDING COMMENTS

This is the first substantial review of the consumer policy framework since 1984. The objective of consumer policy, i.e. the protection of consumers to improve their welfare in the most effective and efficient way, has not changed since then. Technology and consumer behaviour and preferences on the other hand have changed, such that, in the case of financial services, markets have become increasingly national rather than regional or state-based in nature. ANZ believes that the regulatory framework needs to reflect this.

State and Territory laws should be harmonised, and an effective mechanism for ensuring ongoing uniformity needs to be put in place. Where possible, regulation should be generic in nature with industry specific regulation reserved for instances of clear market failure that can really only be addressed in this targeted way.

Also since the last review, a growing number of companies have responded to community expectations about their responsibilities to their customers and the wider community. Governments and regulators might usefully give consideration to how to support and encourage the spread of positive initiatives and the way in which this may complement or, in a limited number of instances, obviate the need for intervention and regulation.

ANZ would be pleased to provide any further information about this submission as required, and can be contacted as follows:

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