Organisation for Economic Co-operation and Development

DAF/COMP/WP2/WD(2017)3

Unclassified **English - Or. English**

15 November 2017

DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS
COMPETITION COMMITTEE

Working Party No. 2 on Competition and Regulation

Co-operation between Competition Agencies and Regulators in the Financial Sector - Note by Australia

4 December 2017

This document reproduces a written contribution from Australia submitted for Item 3 of the 64th meeting of the Working Part No. 2 on Competition and Regulation on 4 December 2017.

More documents related to this discussion can be found at:

www.oecd.org/daf/competition/cooperation-between-competition-agencies-and-regulators-in-the-financial-sector.htm

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Australia

1. Overview of the financial system

1. The Australian financial system is often characterised as the interactions between financial institutions and its regulators, financial markets and their participants, and the payments system under which it operates.

2. The first consists of financial institutions including banks, credit unions, and building societies engaged in obtaining financial assets and incurring liabilities. The financial regulators including the Reserve Bank of Australia (RBA), Australian Prudential Regulation Authority (APRA), Australian Securities and Investment Commission (ASIC), and Australian Competition and Consumer Commission (ACCC) have responsibility in ensuring stability, efficiency, competition and competitive neutrality of the financial system. The second consists of market participants to either raise funds (such as by issuing financial assets) or invest savings (by buying financial assets). The major markets in the Australian financial system include the share market, bond market, and money market. The last consists of the payment system which supports trade and commerce in the economy. Cash including notes and coins are one means of payment. Other means including cheques and electronic transfer facilities add to the variety of liquidity in transaction needs. The interaction between the three components enables funds for domestic and foreign investment or consumption to be made available from savings in other parts of the national or international economy.

3. The Council of Financial Regulators (CFR) is the coordinating body for Australia’s main financial regulatory agencies. Its membership comprises of the RBA, which chairs the council, APRA, ASIC and the Commonwealth Treasury. Other agencies, including the ACCC and the Productivity Commission (PC), can be invited to CFR meetings. The CFR is a non-statutory body with no legal functions or powers separate from those of its individual statutory member agencies. The role of the CFR is to contribute to the efficiency and effectiveness of financial regulation and to promote stability of the Australian financial system. This is achieved through meeting in person on a quarterly basis (or more often as circumstance requires) sharing information and views on the financial sector’s conditions and risks, discussing regulatory reforms and if the need arises, coordinating responses to potential threats to financial stability. Furthermore, the CFR is expected to advise the Australian Government on the adequacy of Australia’s financial system regulatory arrangements and discusses the development and application of various international regulatory reforms in Australia.

4. Financial regulators play an important role in ensuring financial stability, sufficient competition and integrity and consumer protection across the financial system. The current financial regulatory framework came into effect in response to the recommendation of the Financial System Inquiry 1996 (Wallis Committee). Under the new structure, a single prudential supervisor, APRA, was established to take responsibility for the supervision of banks, life and general insurers, and superannuation funds. ASIC has responsibility for market integrity, investors and consumer protection across the financial system. The RBA has responsibility for monetary policy and financial stability including stability in the payments system. The ACCC has the role of

maintaining and promoting competition, protecting the interests of consumers and promoting fair trade in markets.

2. Measures introduced in response to the Global Financial Crisis

5. During the Global Financial Crisis (GFC), the Commonwealth Government, RBA, and regulatory agencies (such as APRA) took a number of steps to support the stability of Australia's financial system. Two key measures which were aimed at preventing a run by depositors and the close out of contracts by (often overseas) creditors were the introduction of:

- The Financial Claims Scheme (FCS), which guaranteed deposits of up to AUD$1 million per account holder, per authorised deposit-taking institution (ADI) (broadly banks, credit unions and building societies) in the event that an ADI failed; [1] and
- The wholesale funding guarantee, which, for a fee, allowed eligible ADIs to offer government-guaranteed deposits greater than $1 million, and government-guaranteed wholesale funding with maturity out to five years (less in the case of foreign-bank branches licensed in Australia).

6. Both of these measures were announced on 12 October 2008 during a period of heightened uncertainty about the stability of the global financial system, the virtual closure of parts of the global capital markets, and governments in a number of other countries announcing strengthened depositor protections and wholesale debt guarantees of their own – all increasing pressure on Australia to do the same.

7. The wholesale guarantee scheme formally commenced on 28 November 2008 and enabled eligible ADIs to access a government guarantee for large deposits and wholesale liabilities. In exchange for the guarantee, which bestowed the government's AAA rating on this debt, ADIs paid a monthly fee based on their credit rating and the value of the debt/wholesale deposits guaranteed.

8. The scheme shared many features with wholesale debt guarantee arrangements announced in other countries although, on balance, it was more flexible and generally at the more supportive end of the international range. This was by design: the emphasis was on supporting financial stability by seeking to deliver arrangements that decisively addressed potential investor concerns without the need for further interventions. Specifically:

- **Size of the scheme:** the government did not limit the total value of liabilities covered, in contrast to most other schemes.
- **Term of the guaranteed debt:** the Australian scheme covered issuance at different maturities up to a maximum of five years (less for foreign bank branches). ADIs could issue debt up to this maximum at any point while the scheme remained open to new issuance. In comparison, many other overseas schemes nominated a maximum maturity date – often three years – beyond which debt would not be guaranteed. These dates were later extended in some cases, arguably reducing the credibility of government announcements.

[1] The FCS is now a permanent feature of Australia's regulatory regime but capped at AUD 250,000 per account holder, per ADI.

- **Closure date:** no closure date was announced when the scheme was introduced, rather it was declared open 'until conditions normalise'. Most other governments set a closure date when announcing their schemes, with many subsequently extending these dates.
- **Fees:** for highly rated borrowers (AA- and above), the fee charged under the Australian scheme was ultimately relatively low compared with those in other countries. The difference in fees between highly rated and lower-rated borrowers in Australia was, in contrast, high by international comparison. Monthly fees were charged on the balance of outstanding guaranteed liabilities, which was in contrast to many other countries where fees were charged upfront for the life of the security/scheme and were non-refundable.

9. The scheme closed to new issuance from the end of March 2010, following advice from the CFR that funding conditions had 'normalised'. At its peak, the Australian Government guaranteed more than $150 billion in debt over the life of the scheme. The final guaranteed bond matured in early-2015.

2.1. The Financial Sector Legislation Amendment (Prudential Refinements and Other Measures) Act 2010

10. The *Financial Sector Legislation Amendment (Prudential Refinements and Other Measures) Act 2010* (the Act) received Royal Assent on 29 June 2010. The Act was introduced following a review of Australia's prudential regulatory framework by APRA and the Commonwealth Treasury and was designed to strengthen APRA's ability to effectively fulfil its mandate.

11. The Act included five key areas of reform:

1. It strengthened APRA's powers to prevent prudential regulatory concerns arising and to address them should they arise. This included:
    - empowering APRA to investigate financial institutions during winding up and access a wider range of records held by institutions to support its prudential supervision;
    - strengthening Australia's 'fit and proper' persons framework, allowing APRA to set standards for 'fit and proper' persons in legislative instruments (as opposed to guidelines) and preventing such persons from refusing to provide information to a regulator or court on the grounds that doing so may expose them to disqualification;
    - clarifying the extent of APRA's directions powers, including in relation to APRA's ability to direct a foreign bank branch in regards to inappropriate intra-entity transactions; and
    - strengthening APRA's crisis management powers to: clarify APRA's ability to direct a distressed ADI or insurer to recapitalise; increase the effectiveness of the statutory and judicial management regime (particularly in relation to information gathering); and allow for the compulsory transfer of a general insurance business (in addition to ADIs and life insurers) in appropriate circumstances;
2. It amended the FCS to facilitate APRA's administration of the scheme and improve the scheme's operation through enhanced information gathering powers and its extension to policy holders with general insurers;

3. It amended the *Financial Sector (Collection of Data) Act 2001* to promote the harmonisation and flexibility of the data collection and publishing regime (such as removing the requirement for APRA to consult on data collection forms where the delay may have a detrimental effect on financial system stability), and APRA's role as the central repository for the collection of financial data;
4. It amended the financial sector levies framework (which is used to recover APRA's costs) to improve the methodologies governing the determination of levies; and
5. It repealed five redundant acts related to the validation of past financial sector levy determinations.

2.2. Implicit guarantees in the Australian financial system

12. Australia's four major banks benefit from a market perception that they are too-big-to-fail and would therefore receive government support in a crisis. This is reflected in the fact that the three major credit rating agencies (Moody's, Standard & Poors and Fitch) each provide the major banks with a two-notch credit rating uplift, which effectively lowers their funding costs relative to other ADIs.

13. Estimates of the value of this implicit guarantee vary, but most literature suggests that it is larger during periods of financial stress when public support is more likely to be needed.

- In 2012, the IMF estimated that the major banks' funding cost advantage rose from 80 basis points pre-GFC to 120 basis points during the GFC.
- In 2013, the RBA estimated that the implicit guarantee was around 100 basis points during the GFC, but had fallen to around 10 basis points by the start of 2014 (with this difference not being statistically significant).

2.3. Australia's 'Four Pillars policy'

14. The 1996 Financial System Inquiry (the Wallis Inquiry) made 115 recommendations to the Australian Government. Only one was rejected: the recommendation that there should be no outright ban on mergers among financial institutions but that all merger proposals should be considered on their merits through the usual channels. In response to this recommendation, the Treasurer announced that 'for the time being' he would not authorise mergers among any of Australia's four major banks. This was the start of Australia's 'four pillars' policy.

15. On 2 June 2008, Deputy Prime Minister and Treasurer, the Hon. Wayne Swan MP, made a statement to the House of Representatives announcing that he would maintain the 'four pillars' policy for the banking sector.[2] At the time of the announcement, the Deputy Prime Minister argued that:

"The Four Pillars policy has endured, in one form or another, through four successive Prime Ministerships and seven successive Treasurerships over nearly two decades, and has served Australia well in that period.

[2] While the 'four pillars' policy was implemented in 1997, it was preceded by a broader 'six pillars' policy that was introduced by the Australian Government in 1990 and prevented any mergers between the four major banks and the two major life insurance companies at the time.

The strength and soundness of the Australian banking system over the past year further demonstrates the soundness of the Four Pillars policy.

The Government considers that Australia is best served by a stable banking system that can continue to draw on the strength and risk management skills of four major banks, rather than a lesser number."

2.4. Merger assessments during the GFC

16. The ACCC enforces the merger provisions of the *Competition and Consumer Act 2010* (CCA), which involves monitoring and reviewing mergers that potentially have anticompetitive effects, including in financial markets. The merger test applied[3] is whether the merger would be likely to result in a substantial lessening of competition in any relevant market/s. The ACCC will identify the areas of overlap between the merger parties as a starting point for considering the relevant market/s where competition concerns may arise. The analysis focuses on whether the merger is likely to increase or enhance the merged firm's market power, taking into account actual or potential constraints on the merged firm post acquisition. The financial sector is characterised by a broad range of products and services and the various relevant markets often display differing competitive dynamics. Therefore it is difficult to reach generalised conclusions about competitive conditions without regard to the specifics of the market or conduct in question.

17. In 2008 the ACCC decided not to oppose two banking mergers. The first decision, Westpac Banking Corporation's (Westpac) acquisition of St George Banking Limited (St George), was made on 13 August 2008, while the second, Commonwealth Bank of Australia's (CBA) acquisition of BankWest, occurred after the collapse of the Lehman Brothers on 15 September 2008. Since then, government and non-government stakeholders have commented on the impact this consolidation in the banking sector may have had on overall competition in Australia's financial system.[4] Whereas global events following the GFC had a direct impact on the ACCC's assessment of CBA's acquisition of BankWest, they did not factor into the decision not to oppose Westpac's acquisition of St George.[5]

[3] Section 50 of the CCA

[4] For example, Senator Nick Xenophon 31 May 2011 at Budget Estimates before the Senate Economics Legislation Committee of the Australian Parliament, Official Committee Hansard, p 142; and http://www.theaustralian.com.au/business/opinion/samuels-mixed-messages-on-bank-mergers/news-story/77fdd8a0bcbd8012cfb75a61c859171e?nk=9cb720096d5de56e863f9be21ddc6856-1508465874.

[5] In 2011, the former Chairman of the ACCC Graeme Samuel AO, publicly commented that while he agreed that competition in the banking sector was less intense than it was at the time of the ACCC's decision, this was not "as a result of those mergers". The former Chairman instead stated that the reduction in competition could more accurately be attributed to "the hibernation of the nonbank financial intermediaries, the NBFIs, in the home mortgage market, which [the ACCC] think[s] has been the major impact on competition in the residential mortgage market". Further, that along with foreign banks, "many of them have withdrawn their lending bases in Australia to recapitalise for substantial losses that they incurred back in their home bases as a result of the GFC." Comments made on 31 May 2011 at Budget Estimates before the Senate Economics Legislation Committee of the Australian Parliament, Official Committee Hansard, p 143.

2.4.1. Westpac Banking Corporation's acquisition of St George Bank Limited

18. On 13 August 2008, the ACCC announced its decision not to oppose the proposed acquisition of St George by Westpac. At the time, Westpac was the third largest retail bank in Australia by market capitalisation, valued at approximately $45 billion.[6] St George was the Australia's fifth largest retail bank by market capitalisation, valued at around $16 billion. The merger parties overlapped in the areas of personal banking, business banking, corporate and institutional banking, wealth management and insurance.

19. The ACCC considered that credit conditions at the time of the assessment had the effect of raising barriers to entry for lenders. In particular, the closure of securitisation markets and the increase in the cost of credit meant that many non-bank players had exited lending markets and some other players ceased writing new loans in the interim. Similarly, the ACCC also found that the relative increase in costs of funds had made it more difficult for the smaller financial institutions (with less favourable credit ratings) to compete in the short term.

20. In relation to retail banking markets, the ACCC considered that the proposed acquisition was unlikely to result in a substantial lessening of competition. The ACCC found that:

> *"[b]arriers to national entry are high and appear to be even more significant for branch-centric products. However, the level of aggregation arising from this transaction is relatively limited and a number of competitors — the other three majors, regional banks, credit unions and building societies, and other niche players — will pose a constraint on the merged entity post-acquisition. Further, while St George is competitive in terms of price and customer service, it does not appear to be unique or a market leader in either attribute."*[7]

21. The then Commonwealth Treasurer, the Hon. Wayne Swan MP, approved the acquisition[8] but placed conditions on Westpac. Under the conditions, Westpac was:

> *"required to maintain the existing number of Westpac and St George branches and ATMs, including in non-urban areas; retain all Westpac and St George retail banking brands including Bank SA, maintain dedicated management teams for St George and Westpac retail banking distribution and retain a corporate presence in Kogarah. The conditions will also require the removal of foreign ATM fees for Westpac customers using St George ATMs and vice-versa."*[9]

22. Although the ACCC's merger review occurred before the GFC, the Treasurer's approval happened shortly following. The conditions the Treasurer placed on the merger may have been influenced by global events at this time.

[6] ACCC Public Competition Assessment, *Westpac Banking Corporation – proposed acquisition of St George Bank Limited*, p 2: http://registers.accc.gov.au/content/index.phtml/itemId/839278/fromItemId/751043

[7] ACCC Public Competition Assessment, *Westpac Banking Corporation – proposed acquisition of St George Bank Limited*, p 15: http://registers.accc.gov.au/content/index.phtml/itemId/839278/fromItemId/751043

[8] *Financial Sector (Shareholdings) Act 1998*, s 14.

[9] Wayne Swan, media release, 23 October 2008, http://ministers.treasury.gov.au/DisplayDocs.aspx?doc=pressreleases/2008/116.htm&pageID=003&min=wms&Year=&DocType=0

2.4.2. Commonwealth Bank of Australia's acquisition of BankWest

23. On 10 December 2008, the ACCC announced its decision not to oppose the proposed acquisition of BankWest by the CBA. ACCC's review occurred in the post-GFC environment during which the Australian Government initiated a number of policy responses in relation to the financial sector.

24. At the time, CBA was the largest retail bank in Australia by market capitalisation and valued at approximately $42 billion, with a national market share of 18.8% in home loans markets.[10] CBA operated the largest branch and ATM network throughout Australia. BankWest was a retail bank primarily based in Western Australia, and held a national market share of 2.8% in home loan markets. BankWest's parent company was HBOS, a major UK-based bank. Lloyds, another leading UK bank, had announced in September 2008 a proposal to acquire HBOS, an acquisition that was expected to proceed at the time the ACCC was undertaking its assessment. At the time of CBA's announcement, HBOS was experiencing considerable funding pressures and had stated that the proposed acquisition of BankWest by CBA would result in an immediate and substantial funding benefit. This aspect added an additional timing pressure on the ACCC's assessment process.

25. The ACCC took into account a number of retail banking markets for the purposes of assessing the matter. Based on market inquiries, the ACCC formed the view that BankWest had been a vigorous and effective competitor in retail banking markets.

26. It was arguable that the acquisition would be anticompetitive and encourage concentration in the banking sector, given that BankWest was a regional bank that was a vigorous and effective competitor to the major banks in retail banking markets.[11] However, the ACCC did not oppose the acquisition on the following grounds:

> *"after extensive market inquiries and analysis, the ACCC considered that, due to global financial conditions, in the event that the merger did not proceed, it was unlikely that BankWest would continue to be as aggressive in its pricing, product offering and expansion plans. On this basis, it was found that the likely state of competition if the merger occurred would not be substantially lower than the state of competition if the merger did not occur.*
>
> *In the absence of the global financial crisis, and the funding difficulties faced by BankWest's overseas parent company, the ACCC's conclusion may have been different."*[12]

27. The ACCC formed the view that the relevant counterfactual in the matter was that HBOS/Lloyds would continue to operate BankWest business. The ACCC received evidence from the merger parties and APRA and the RBA, which suggested that on this

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[10] ACCC Public Competition Assessment, *Commonwealth Bank of Australia – proposed acquisition of BankWest and St Andrew's Australia, p 2:* http://registers.accc.gov.au/content/item.phtml?itemId=852911&nodeId=fa54b9e99a99bcd0a07cbc76ba7601df&fn=Commonwealth+Bank+of+Australia+-+proposed+acquisition+of+Bankwest+and+St+Andrew%27s+Australia+-+10+December+2008+-+banking

[11] ACCC submission to Australian Senate Economics Committee: Inquiry into aspects of banking mergers, January 2009

[12] Ibid, p. 8

scenario, BankWest would not be in a position to provide strong and sustainable competition.

28. Given a counterfactual under which BankWest would no longer be the competitive force it once was, the ACCC considered the proposed acquisition was unlikely to substantially lessen competition in the relevant national retail banking markets (including home loans and saving/term products). Given BankWest's relatively modest market share in these markets, and the number of other significant competitors, the ACCC found that it was unlikely that the acquisition of such a small competitor, no longer offering market leading prices, would substantially lessen competition.

3. Financial System Inquiry

29. The Australian Government established the Financial System Inquiry (FSI) in 2013. This implemented the incoming Australian Government's commitment to a 'root and branch' examination of the nation's financial system.

30. The FSI was considered to be timely given changes in the landscape of the financial system - a similar inquiry was previously conducted in 1997 (the Wallis Inquiry) and it had been 32 years since the first major investigation into Australia's financial system (the Campbell Inquiry). The findings of both of these inquiries led to major reforms.

31. The FSI's Terms of Reference required reporting on the consequences of developments in the Australian financial system since the 1997 Wallis Inquiry and the GFC, including implications for domestic competition and international competitiveness.

32. It also required a refresh of the philosophy, principles and objectives underpinning the development of a well-functioning financial system, including balancing competition, innovation, efficiency, stability and consumer protection.

33. Competition and competitive markets were at the heart of the FSI's philosophy for the financial system. The FSI saw them as the primary means of supporting the system's efficiency. Although it considered competition was generally adequate, the FSI found that the high concentration and increasing vertical integration in some parts of the Australian financial system had the potential to limit the benefits of competition in the future and should be proactively monitored over time.

34. The FSI's approach to encouraging competition was to seek to remove impediments to its development. It made recommendations to amend the regulatory system, including: narrowing the differences in risk weights in mortgage lending; considering a competitive mechanism to allocate members to more efficient superannuation funds; and ensuring regulators are more sensitive to the effects of their decisions on competition, international competitiveness and the free flow of capital.

35. The Australian Government is implementing a comprehensive response to the FSI, which includes a large number of measures to encourage competition in the financial system. For example, the Australian Government:

- has tasked the Productivity Commission with conducting inquiries into the state of competition in the financial system, and into data availability and use;

- has committed to reviewing the Statements of Expectations[13] so they are clear that regulators should explain in their annual report how they have balanced competition with other elements of their mandate, which is under development;
- is addressing barriers to cross-border trade in managed investment schemes through the establishment of the Asia Region Funds Passport, which is under development; and
- has committed to introducing an explicit reference of competition in ASIC's mandate, which is under development.

4. Competition themed policy measures

4.1. Introduced and implemented

4.1.1. ASIC regulatory sandbox measures

36. ASIC introduced a regulatory sandbox in December 2016 to eligible businesses to test certain products and services for 12 months without needing to obtain an Australian financial services (AFS) licence or credit licence.

37. Businesses do not need to apply to obtain the benefit of the FinTech licensing exemption. If a person meets the eligibility requirements and follows certain conditions (including client and exposure limits, disclosure requirements, and adequate compensation and dispute resolution arrangements), they are legally entitled to rely on the exemption for 12 months. However, they must provide ASIC with written notice of their intention to rely on the relief, and provide certain information to ASIC (including the person's contact details and a description of the services the person proposes to provide during the testing period).

38. As part of the 2017-18 Budget, the Australian Government announced it will introduce legislation to enhance ASIC's regulatory sandbox to facilitate more innovation, promote greater competition and increase choice for Australian consumers. This world-leading regulatory sandbox will allow businesses to test for a period of 24 months a wide range of new financial products and services, allowing businesses to evaluate the commercial viability of new concepts without a licence but subject to meeting minimum consumer protection obligations.

4.1.2. Crowd-sourced funding regime

39. On 29 September 2017, the Australian Government's crowd-sourced equity funding (CSEF) framework for *public* companies commenced. CSEF allows businesses to obtain capital from a large number of investors through an online platform, where each investor typically contributes a small amount of money in return for an equity stake in the business. Eligible unlisted *public* companies, with assets and annual turnover of less than $25 million, will be eligible to raise up to $5 million in funds per year via CSEF.

40. The CSEF framework has a number of protections for investors. Issuers will be required to prepare offer documents, to ensure investors can make informed decisions.

[13] ASIC: http://asic.gov.au/about-asic/what-we-do/our-role/statements-of-expectations-and-intent/statement-of-expectations-april-2014/; APRA: http://www.apra.gov.au/AboutAPRA/Documents/140417-SOE-APRA-Statement-of-Expectations.pdf

Retail investors will be permitted to invest up to $10,000 per issuer per 12-month period and will have the right to a five day cooling-off period. Further, CSEF intermediaries will require a financial services licence as they hold a central ‘gatekeeper role’, checking that offer documents contain the required information and displaying a risk warning on the platform. ASIC has finalised regulatory guidance and is accepting licence applications from potential intermediaries.

41. The Australian Government introduced legislation to extend CSEF to *proprietary* companies on 14 September 2017. This extension will use many of the existing features of the public company framework, such as the obligations of intermediaries and the process of making crowdfunding offers. Acknowledging *proprietary* companies that access CSEF will no longer be closely held by shareholders, these companies will be subject to obligations designed to increase shareholder engagement and mitigate the occurrence of fraud. The additional obligations include: a minimum of two directors; financial reporting in accordance with accounting standards; audit requirements when raising $3 million or more; and restrictions on related party transactions.

42. Equity crowdfunding will enable companies to obtain the capital they need to turn good ideas into commercial successes while providing Australian investors with a larger pool of choice. Unlocking a new source of funding supports the Australian Government’s commitment to foster innovative economic activity and support the development of the Australian FinTech sector.

4.2. Policy measures in development

4.2.1. Open Banking Initiative

43. The Treasurer announced in his 2017-18 Budget speech that Australia will introduce an open banking regime in 2018. To inform the regime’s implementation, an independent review has been established and will report to the Treasurer by the end of 2017, including on an appropriate timeframe for the regime’s commencement.

4.2.2. Other policy measures

44. The First Report of the House of Representatives Standing Committee on Economics’ Review of the Four Major Banks, released in November 2016, recommended that (Recommendation 6):

- the Australian Government review the 15 per cent threshold for substantial shareholders in ADIs imposed by the *Financial Sector (Shareholdings) Act 1998* (FSSA) to determine if it poses barriers to entry;
- the CFR review the licensing requirements for ADIs to determine whether they present an undue barrier to entry and whether the adoption of a formal ‘two-phase’ licensing process for prospective applicants would improve competition; and
- APRA improve the transparency of its process in assessing and granting a banking licence.

45. In its response (released 9 May 2017), the Australian Government agreed with this recommendation, noting:

- the 15 per cent ownership cap would be relaxed either through ministerial discretion or legislative change;

- APRA would review its approach to ADI licensing arrangements in 2017 and would also review its relevant guidance on licensing; and
- though not recommended by the Review of the Four Major Banks, the Australian Government would remove the prohibition on the use of the word ‘bank’ by ADIs with less than $50 million in capital, as a measure to further enhance competition and innovation in the banking sector.

4.2.3. FSSA 15 per cent ownership threshold

46. The Australian Government is currently consulting on options to reform the FSSA and, at this stage, legislation to implement this measure is likely to be introduced in 2018.

4.2.4. Two-phased licensing of ADIs

47. Coming out of its review of ADI licensing arrangements, APRA has proposed a two-phased approach to the licensing of ADIs, in line with Recommendation 6 of the Review of the Four Major Banks. APRA is currently consulting on this proposal through a discussion paper until 30 November 2017.

48. Under the proposal as it currently stands, new entrants will be able to apply for a ‘restricted ADI licence’ which will allow them to begin limited operations while they are developing the resources and capabilities necessary to meet the requirements of the prudential framework. This will increase competition in the banking sector by reducing barriers to new entrants, including those with innovative or otherwise non-traditional business models or those leveraging greater use of technology.

49. The Restricted ADI licence will be subject to certain eligibility requirements and a maximum period after which the new entrant is expected to transition to an ADI and fully comply with the prudential framework (or exit the industry).

4.2.5. Use of the word ‘bank’

50. Legislation was introduced into Parliament on 19 October 2017 (submissions were due by 14 August 2017). The draft legislation removes the $50 million capital restriction, so that all ADIs will be able to use the term ‘bank’, but still allows APRA the discretion to limit the use of the term for ADIs in exceptional circumstances.

51. The measure will boost competition and innovation in the financial sector by allowing all ADIs to benefit from the reputational advantages of the term, and by encouraging new entities to enter the market for which use of the term is essential to their business model.

4.2.6. ASIC MoneySmart

52. ASIC's MoneySmart website is an established communication channel for providing information, guidance and tools to build the financial capability of Australians. ASIC's MoneySmart website reached over 7 million people in 2016/17. ASIC continues to grow and improve this service, including by enhancing existing and building new online tools, maintaining engaging content and promoting messages to consumers (with a focus on managing money day-to-day, planning for the future and making informed decisions). There is an ongoing commitment to work with other government agencies and departments to cross-promote key messages and new tools and apps as they become available, including promoting access to data and tools that encourage consumers to compare financial products.

5. Increased focus on role of competition in Australia's financial system

53. Since the release of the FSI Final Report, the Australian Government and regulators have increased their focus on the role of competition in the various markets that comprise Australia's financial system.

5.1. Greater engagement between the ACCC and the CFR

54. In October 2016 the CFR began to assess the state of competition in banking and markets in which banks operate. The purpose of this exercise was to identify measures that could increase competition and make recommendations to the Australian Government regarding initiatives that would improve competition and consumer outcomes. The ACCC was necessarily involved in this process from the outset.

5.2. Competition Policy Review

55. On 4 December 2013 the then Prime Minister and the then Minister for Small Business announced a review of competition policy. The review was conducted due to the changing Australian economy. It was intended to be comprehensive. In addition to the law, the review looked at the broader competition framework, including policy objectives and institutional arrangements, "to increase productivity and efficiency in markets, drive benefits to ease cost of living pressures and raise living standards for all Australians".[14]

56. In 2012, the former Australian Government introduced in Part IV Division 1A of the *Competition and Consumer Act 2010* (CCA), which contained banking sector specific anti-competitive disclosure of information provisions, including disclosure of pricing provisions. These provisions were introduced in response to public concern about price signalling regarding interest rate movements by Australia's four major banks.

57. The provisions in Division 1A prohibited the following types of conduct in relation to particular types of banking services:

- the private disclosure of pricing information to a competitor, where it is not in the ordinary course of business;
- the public or private disclosure of information relating to price, capacity or commercial strategy for the purpose of substantially lessening competition in a market.

58. The provisions have not been used. The prohibitions have not been extended to other types of goods and services, although this power was available to the Minister.

59. In its first submission to the Review Panel, the ACCC recommended that the anti-competitive disclosure of information provisions should apply across the economy. The ACCC highlighted that this would be consistent with the universality principle that anti-competitive conduct should be prohibited regardless of the sector of the economy in which it occurs. The ACCC advised that anti-competitive disclosures can be just as harmful as hard core cartels and are recognised in this way by international best practice. In making this point, the ACCC referred to European law, where the focus of the prohibition is on whether the object or effect of the anti-competitive disclosure is to

14 Minister for Small Business the Hon. Bruce Billson MP, http://bfb.ministers.treasury.gov.au/media-release/014-2013/, 4 December 2013

prevent, restrict or distort competition, whether the disclosure is part of a fully formed agreement or reflects a "concerted practice". The Review Panel's Draft Report recommended that Division 1A be repealed. The Review Panel recommended extending the scope of the CCA's prohibition on anti-competitive contracts, arrangements and understandings to explicitly include a prohibition on concerted practices that substantially lessen competition. The ACCC supported this draft recommendation, and worked with the Review Panel and the Treasury to develop this legislation to be consistent with international approaches.

60. In March 2015, the Panel of the review issued its final report. Included in the range of recommendations made by the review Panel was that the Australian Government should repeal banking sector specific anti-competitive disclosure of information provisions.

61. The Review Panel ultimately agreed with the ACCC and recommended the repeal and replacement of Part IV Division 1A with a prohibition on concerted practices that have the purpose, effect or likely effect of substantially lessening competition.

62. In October 2017, the Australian Parliament passed legislation to this effect.

5.2.1. House of Representatives Standing Committee on Economics: Review of the Four Major Banks

63. On 13 September 2016, the Treasurer formally requested the Australian House of Representatives Standing Committee on Economics (the Committee) to hold public hearings at least annually with Australia's four major banks. The Committee was asked to look into the performance and conduct of the major banks, and has since released two Reports and has recently completed its third Inquiry. In addition to the hearings, the Committee also receives evidence on financial sector issues from Australia's three financial system regulators (the RBA, APRA and ASIC) and the ACCC, in the course of its separate but related review of those regulators' activities more generally.

64. Although the Terms of Reference for the annual reviews does not explicitly refer to competition, the Committee's 2016 report (the First Report) focussed on competition issues, including consumer empowerment. The 2016 report found that Australia's four major banks' "market dominance, coupled with a number of structural features of Australia's financial system, has left them with significant market power."[15] Further, that "continued claims of misconduct suggest that the culture of these institutions is often not one that has consumers at its centre."[16]

65. The Committee made a number of policy recommendations including:

- that the ACCC establish a team to monitor and report to the Government on the state of competition in the banking sector. In response, the Government provided the ACCC with funding in the 2017 Budget to establish the Financial Services Unit (FSU), to undertake regular in-depth inquiries into specific financial system competition issues. More detail on the FSU is provided below.
- Deposit Product Providers be required to provide open access to customer data and small business data. The Government agreed with this recommendation and committed to introducing Open Banking in Australia. The Commonwealth

[15] *Review of the Four Major Banks: First Report*, at [1.5]

[16] *Review of the Four Major Banks: First Report*, at [1.6]

Treasury is currently reviewing how to best implement and regulate Open Banking; and

- the Government and regulators review regulatory barriers to entry, to determine where regulatory barriers could be reduced.

66. Specifically, the Committee recommended amendment of the below policies, with a view to decreasing barriers to entry and expansion in the banking sector:

- the 15 per cent threshold for substantial shareholders in ADIs imposed under legislation;
- the licensing requirements for ADIs to determine whether they present an undue barrier to entry and whether the adoption of a formal "two-phase" licensing process for prospective applicants would improve competition; and
- the prudential regulator work towards improving transparency of its processes in assessing and granting a banking license.

67. As discussed above, the Australian Government agreed with these recommendations and work is already underway towards implementation.

5.2.2. Creation of the ACCC Financial Services Unit

68. As part of the 2017-18 Budget, the Australian Government provided the ACCC with additional funding of $13.2 million over four years to establish the FSU to undertake regular inquiries into competition issues across the financial system. An additional $1.2 million has been provided in 2017-18 for the first task of the FSU to undertake a price inquiry into residential mortgage products.

69. Alongside the ACCC's role in promoting competition in financial services through our enforcement, mergers and adjudication work, the FSU will monitor competition in Australia's financial services sector by assessing competition issues, undertaking market studies, and reporting regularly on emerging issues and trends in the sector.

70. The Productivity Commission's Inquiry into Competition in the Australian financial system is likely to identify additional competition issues in financial services markets that may warrant referral to the FSU.

5.2.3. Productivity Commission review of the competitiveness and efficiency of the Australian superannuation system

71. In 2016, in response to a recommendation of the FSI, the Australian Government tasked the Productivity Commission to begin a three-stage process to assess the competitiveness and efficiency of the superannuation system. This commenced an extensive three-stage review process, due to the size and uniqueness of Australia's superannuation system. Australians have over $2 trillion of assets in superannuation funds, comprising about 20 per cent of total household assets.

72. The Productivity Commission is currently in the final stage of its review. In this third stage it will conduct a system-wide assessment that examines all components of the superannuation system, with a key focus on outcomes for members.

5.2.4. Productivity Commission Inquiry into Competition in the Australian financial system

73. On 8 May 2017, the Australian Government tasked the Productivity Commission to hold an inquiry into competition in the Australian financial system. The Productivity Commission commenced the inquiry on 1 July 2017 and is due to provide its final report to the Government by 1 July 2018. The inquiry is broad ranging, and will take a holistic view of the financial system in Australia. It will consider competition issues in the following key segments of the financial system:

- financial market infrastructure, including payments system, online banking, securities and derivatives;
- funds management and financial planning, including financial advice, funds and wealth management, asset management, portfolio and platform administration, and custodian services;
- investment banking, including equity issuance and structuring, debt issuance and securitisation, non-exchange traded securities, market-making/trading, corporate advice, and risk management;
- business banking, including credit, equipment finance, trade finance, supply chain finance, agribusiness finance, transactions, merchant services, foreign exchange services, and the corporate money market;
- personal banking, including credit such as home loans and credit cards, transactions, and personal savings; and
- insurance, only to the extent that these issues affect competition between banks and other financial service providers.

74. This list demonstrates the comprehensive nature of the inquiry. The matters under consideration are within the remit of the three financial regulators, APRA, the RBA and ASIC. Additionally, the inquiry's scope means certain aspects fall within the purview of a number of industry and sector regulators, for example the Australian Small Business and Family Enterprise Ombudsman. The Commonwealth Treasury will have responsibility for policy development in relation to any findings and recommendations the Australian Government may decide to implement.

75. The ACCC is working closely with the Productivity Commission in the course of the Inquiry. The ACCC expects the Productivity Commission's report to identify specific areas or markets where competition issues warrant further and formal inquiry or potential action by the competition regulator.

6. Antitrust cases in the financial sector

76. In this section we identify two specific ways in which the regulatory set-up can affect the ACCC's antitrust cases in the financial sector:

1. **Competition issues subject to an antitrust case may be a symptom of the regulatory set-up**: In the course of a case, it may be determined the competition issue being investigated is a symptom of the regulatory environment, rather than resulting from any specific anti-competitive behaviour. As such, the appropriate response to the problem would be revisiting the underlying financial regulation or government policy leading to the anti-competitive outcome, rather than taking an enforcement or compliance action against the conduct initially of concern.

2. **Avenues for engagement with overseas regulators can affect the progress of an antitrust case**: Advancing an antitrust case may depend on obtaining information from or cooperating with an overseas competition or financial regulator. As such, it is essential to have a global regulatory framework that facilitates effective cross-jurisdictional engagement.

77. We analyse each of these issues below, and provide ACCC case examples in support.

6.1. Competition issues resulting from the Australian regulatory framework

78. The interaction between financial regulation and competition objectives is a recurring global theme, particularly following the GFC and the resulting focus on financial stability above other objectives in some jurisdictions. The financial sector is subject to various regulatory objectives resulting from its importance to the broader functioning of the economy, and its susceptibility to systemic risk. These objectives may conflict with or otherwise affect competition objectives, and this interplay has become an increasing focus in Australia, as outlined in previous sections of this submission.

79. Regulatory systems can afford competitive advantages to particular market participants, and in some cases, result in competition problems investigated by the ACCC. The ACCC may discontinue a case after finding the source of the problem is the regulatory system. Such cases can assist in identifying areas for potential advocacy or regulatory reform.

80. An example of conduct where the specific regulatory set-up influenced the ACCC's decision not to take enforcement action involved the markets for clearing and settlement (CS) of securities listed on the Australian Securities Exchange. In Australia, the ASX Group has a monopoly in the CS of listed securities. Following an emerging interest from potential competitors in clearing cash equities, the CFR together with the ACCC (the Agencies) reviewed competition in this market in 2012. The Agencies recommended a two-year moratorium on competition in the clearing of cash equities, on the basis of stakeholder concerns regarding the potential regulatory and operational costs associated with multiple clearing service providers, within the context of market conditions and other regulatory reforms at that time. However, the Agencies recognised the benefits of competition and considered the prospect of competition and/or further regulation of the Australian Stock Exchange (ASX) should be revisited at the end of the two years. The Australian Government endorsed the recommendations of the review in February 2013.[17]

81. During and following the start of the moratorium, the ACCC investigated certain competition issues in cash equities markets. The ACCC considered the issues did not warrant enforcement action under the CCA, but would be appropriately addressed by regulatory reform to facilitate a more competitive market structure.

82. These investigations contributed to the ACCC's advocacy for the introduction of competition in the clearing of cash equities in the Agencies' subsequent review in 2015. The 2015 review made a number of recommendations relating to competition in clearing,

[17] As such, competition in clearing cash equities was prevented as a matter of government policy, though it was possible within the existing legislative framework.

all of which were endorsed by the Government in March 2016. This included recommendations to:

- open the market for cash equities clearing to potential competition;
- implement legislative changes to grant Agencies rule-making and arbitration powers, discussed in further detail below; and
- introduce policy measures to ensure competition objectives were balanced with other objectives, such as efficient market functioning and financial stability, and to increase the ASX's accountability while it remained a monopoly.

83. The 2015 review recommended legislative changes to provide for the ACCC to arbitrate disputes where a third party was seeking access to ASX's monopoly cash equity CS services. The 2015 review also recommended legislative changes to grant relevant agencies rule-making powers to impose specific obligations on ASX's cash equity CS facilities to act in accordance with the recommended policy measures. The Conclusions Paper from the review describes the gap to be filled by the proposed rule-making powers:

> *"The powers would be held in reserve and would be expected to be used only in the event of a material deviation from the expectations or where ASX's conduct was generating undesirable outcomes for the market but was not sufficiently severe to trigger intervention by the ACCC under the Competition and Consumer Act 2010 (the CCA). The rule-making powers would be used to address systematic problems, rather than specific issues arising between particular parties."*[18]

84. Following the emerging prospect of potential competitors in the settlement of cash equities, the Agencies commenced a further review of competition in the settlement of cash equities in Australia in early 2017. This review has now concluded and reiterated the government-endorsed policy stance of openness to competition in both clearing and settlement, and the intention to develop legislation to provide Agencies with rule-making and arbitration powers.

6.2. Cross-jurisdictional engagement between competition and financial regulators

85. Cooperation and mutual assistance between regulators across jurisdictions, including information-sharing, is necessary to progress antitrust investigations. Information-sharing can be critical for evidence gathering. It is also useful to learn lessons from other jurisdictions or coordinate approaches to effectively and efficiently respond to anti-competitive conduct engaged in between jurisdictions or on a global scale. To facilitate this, many jurisdictions have introduced information-sharing arrangements or agreements, which facilitate parallel investigations or sharing of information or evidence gathering.

86. Following the financial crisis, the discovery of evidence of collusion in respect of foreign exchange and interest rate benchmarks brought increased attention to the allocation of responsibility between financial regulators and competition authorities. Different jurisdictions allocate responsibility for enforcement of competition law in the financial sector differently. For example, while in Australia the ACCC has competition law powers for financial services, in the UK, these powers reside with the financial regulator, the Financial Conduct Authority (FCA). To the extent jurisdictions diverge in the regulator responsible for competition laws in financial services – i.e. a specialised

[18] *Review of Competition in Clearing Australian Cash Equities: Conclusions*, June 2015: p. 6

financial regulator versus a generalised competition authority – coordination on antitrust cases may be hindered due to a lack of access to relevant information-sharing arrangements, which may only operate within networks of competition agencies or financial regulators.

87. The ACCC is of the view that the global cooperation framework could be improved to allow for improved mutual assistance between competition and financial regulators. This view is supported by its experience in several ways. For example, the ACCC has an immunity and cooperation policy for cartels, which provides cartel participants with the opportunity to receive conditional immunity in exchange for evidence of a contravention of the Cartel Division of the CCA. As part of the policy, the ACCC usually receives a waiver from the immunity applicant to disclose information about their application to a foreign regulator, as part of an effort to coordinate or conduct joint investigations across jurisdictions. However, the ACCC may not be able to receive or share information with a counterpart overseas regulator if that regulator does not also have an immunity policy in place, which permits "waivers". The ACCC has previously been prevented from exchanging information or conducting joint investigations because a financial regulator – rather than the competition authority with a relevant immunity policy in place – was conducting a parallel investigation in a foreign jurisdiction, and the financial regulator did not have an immunity program under which waivers could operate to facilitate cooperation.

88. Another impediment to cooperation and information-sharing is that financial regulators do not generally participate in the same networks and forums as competition regulators. Communities of engagement allow regulators to informally share learnings, develop MOUs or update each other on their respective work. For example, the International Competition Network and the ICN Cartel Working Group have established very strong operational links between competition regulators.

89. The ACCC finds antitrust investigations can be frustrated where information-sharing arrangements or agreements between financial regulators do not extend to competition authorities. For example, in 2002, the International Organisation of Securities Commissions (IOSCO) introduced a multilateral MOU (MMOU) between regulators in securities and derivatives markets to allow them to provide mutual assistance to each other, cooperate and exchange information on matters. While ASIC is a party to the MMOU, the ACCC is not. As part of a foreign exchange case by the ACCC, the ACCC sought access to material produced during a joint investigative activity by ASIC a foreign financial regulator. The ACCC could not participate in the activity itself in order to gather evidence specific to its own investigations, because it did not have a direct arrangement in place with the foreign regulator. It also could not obtain from that regulator some categories of material which the ACCC considered important to its investigation. Instead, ASIC sought the consent of the regulator under the IOSCO MMOU and the ACCC received some material via ASIC pursuant to the ASIC Act.

90. In another case, the ACCC sought material from a foreign financial regulator (also party to the IOSCO MMOU) located in the jurisdiction where the conduct had occurred, and which had already completed its investigation into the conduct. The ACCC considered obtaining material from the regulator would significantly advance its own case by enabling it to gather evidence more efficiently. However, the ACCC was unable to obtain the cooperation of the overseas regulator, and while it eventually obtained some of the material indirectly through ASIC and the banks under investigation, the regulator limited the extent of their disclosure.

91. Australia considers reforms should be considered to the international cooperation and mutual assistance arrangements between competition agencies and financial regulators to enhance the capacity to work together to progress investigations. While financial regulators already have a sophisticated system of sharing information, extending this system to competition authorities through new or revised MOUs, or an alignment in policies, would assist investigative capacity of all agencies. Financial regulators with competition responsibilities could benefit from greater participation in international competition forums. Such measures will allow antitrust cases in the financial sector to be progressed more quickly or effectively, particularly where a case is being investigated simultaneously across jurisdictions.

92. The ACCC supports considering whether appropriate groups including the ICN, IOSCO and the OECD Secretariat might be invited to identify shared objectives and explore methods of enhancing cooperation among competition and financial regulators.