On Sound Commercial Terms:

An Inquiry into Regulatory Impediments in the Financial Services Sector

A draft report for further consultation and input

March 2010

Victorian
Competition & Efficiency
Commission

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About the Victorian Competition and Efficiency Commission

The Victorian Competition and Efficiency Commission, which is supported by a secretariat, provides the Victorian Government with independent advice on business regulation reform and opportunities for improving Victoria's competitive position.

VCEC has three core functions:

- reviewing regulatory impact statements, measurements of the administrative burden of regulation and business impact assessments of significant new legislation
- undertaking inquiries referred to it by the Treasurer, and
- operating Victoria's Competitive Neutrality Unit.

For more information on the Victorian Competition and Efficiency Commission, visit our website at: www.vcec.vic.gov.au

Disclosure of interest

The Commissioners have declared to the Victorian Government all personal interests that could have a bearing on current and future work. Moreover, while the Commissioners confirm their belief that they have no personal conflicts of interest in regard to this inquiry, Matthew Butlin wishes to disclose that he has shares in companies in the resources, manufacturing, financial, energy, transport, retail, telecommunications and engineering sectors.

Opportunity for further comment

You are invited to examine this draft report and provide comment on it within the Commission's public inquiry process. The Commission will be accepting submissions commenting on this report and will be undertaking further consultation before delivering a final report to the Government.

The Commission should receive all submissions by **30 April 2010**.

Submissions may be sent by mail, fax, audio cassette or email.

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Terms of reference

Inquiry into Regulatory Impediments in the Financial Services Sector

I, John Lenders MP, Treasurer, pursuant to section 4 of the *State Owned Enterprises (State Body — Victorian Competition and Efficiency Commission) Order* ('the Order'), hereby direct the Victorian Competition and Efficiency Commission ('the Commission') to conduct an inquiry into reducing regulatory impediments in the financial services sector.

Background

Victoria's financial services sector is large and diverse, employing some 100,000 people in a range of industries, including banking, superannuation and insurance. A stable and vibrant financial services sector underpins economic performance and provides the confidence and stability necessary to attract financial capital and overseas investment.

The financial services sector is also recognised as being an increasingly global business environment and one in which Victoria competes for businesses and endeavours to attract the highly skilled and mobile workforce. In recognition of these opportunities and challenges, Victoria has developed a Financial Services Strategy aimed at supporting the growth of a financial services sector through positioning Victoria as providing an internationally competitive business location with particular strengths and capabilities.

Similar commitment to the sector has been demonstrated nationally, with the Commonwealth and states taking a collaborative approach to establishing a national regulatory framework and the Commonwealth Government establishing the Australian Financial Centre Forum.

A review by the VCEC would be aimed at supporting the competitiveness of the Victorian financial services sector through the identification of regulatory and other impediments and barriers.

Scope of the inquiry

The Commission is to inquire into and report on:

1) the significance and diversity of the financial services sector in Victoria;
2) identification of Commonwealth and State regulations that impact the development of Victoria's financial services sector, including regulations that

might impact adversely upon attraction of foreign business to Victoria's financial services sector;

3) any regulatory or other impediments to ensuring sufficient supplies of skilled labour, including consideration of the need for accreditation to facilitate labour mobility within the sector;
4) options for regulatory and/or operational changes that the Victorian Government can undertake to support development of the Victorian financial services sector; and
5) identification of the economic impacts (including reductions in the regulatory burden on business) of any options identified in this inquiry.

The Commission should take into account any substantive studies or developments undertaken in Victoria and elsewhere — including actions within the Council of Australian Governments, by the Commonwealth and other States, and international best practice — that may help it provide advice on this Reference. The Commission should have regard to the strategic directions set out in *Victoria's Financial Services Strategic Statement* and draw upon other relevant reviews by State and Commonwealth Government.

Inquiry process

In undertaking this inquiry, the Commission is to have regard to the objectives and operating principles of the Commission, as set out in section 3 of the Order. The Commission must also conduct the inquiry in accordance with section 4 of the Order.

The Commission is to consult with key interest groups and affected parties, and may hold public hearings. The Commission should also draw on the knowledge and expertise of relevant Victorian Government departments and agencies.

The Commission is to release an issues paper at the beginning of the inquiry process and produce a draft report, outlining recommendations for consultative purposes. A final report is to be provided to me as soon as possible, but not later than nine months after receipt of this terms of reference.

JOHN LENDERS MP

Treasurer

Received 18 September 2009

Preface

The release of this draft report gives interested participants the opportunity to comment on the Commission's analysis in relation to its inquiry into regulatory impediments in the financial services sector. The Commission will consider comments received prior to developing and presenting the final report to government.

In preparing this draft report, the Commission invited public submissions and consulted widely with a range of businesses, organisations, government departments and individuals. Stakeholder input has greatly assisted the Commission in reporting on the financial services sector in Victoria and in presenting a draft response to the Victorian Government on removing impediments to the future development of the financial services sector in Victoria. The Commission also wishes to acknowledge the assistance and data provided by the Australian Bureau of Statistics, Skills Victoria, the City of Melbourne and the Osborne Group.

The Commission invites written submissions on the draft report. These submissions may address any of the issues covered by the terms of reference. In light of the submissions received, the Commission will hold further consultations as necessary.

At the conclusion of consultation on the draft report, the Commission will prepare a final report to be presented to the Victorian Government by June 2010. The Order in Council establishing the Commission says that the Treasurer should publicly release the final report and that the Victorian Government should publicly release a response to the final report within six months of the Treasurer receiving the report.

The Commission looks forward to receiving feedback on the draft report.

Dr Matthew Butlin	Deborah Cope
Chair	Commissioner

Contents

Appendices

Abbreviations

ABA	Australian Bankers' Association
ABDC	Australian Business Deans Council
ABS	Australian Bureau of Statistics
ACE	Adult Community Education
ACFS	Australian Centre for Financial Studies
ADI	authorised deposit-taking institution
AFCF	Australian Financial Centre Forum
AFMA	Australian Financial Markets Association
AFTS	Australia's Future Tax System
ANZSCO	Australian and New Zealand Standard Classification of Occupations
ANZSIC	Australian and New Zealand Standard Industry Classification
APRA	Australian Prudential Regulation Authority
ASCO	Australian Standard Classification of Occupations
ASFA	Association of Superannuation Funds of Australia
ASIC	Australian Securities and Investments Commission
ASX	Australian Securities Exchange
ATM	automated teller machine
AUSTRAC	Australian Transaction Reports and Analysis Centre
Austrade	Australian Trade Commission
BSX	Bendigo Stock Exchange
CAT	Credit Authorised Transfer
CAT/CAP	CAT with Merchant Data CAPture
CBD	central business district
CBUS	Construction and Building Unions Superannuation

CF-1	Common Fund No. 1
CF-2	Common Fund No. 2
CF-3	Common Fund No. 3
CF-GR	Common Funds Guarantee and Reserve Account
CFA	Chartered Financial Analyst
CLUE	Census of Land Use and Employment
COAG	Council of Australian Governments
CSO	community service obligation
DEEWR	Department of Education, Employment and Workplace Relations
DIC	Department of Immigration and Citizenship
DIIRD	Department of Innovation, Industry and Regional Development
DSE	Department of Sustainability and Environment
EFTPOS	Electronic Funds Transfer at Point of Sale
Finsia	Financial Services Institute of Australasia
G20	Group of Twenty
GSP	gross state product
GST	Goods and Services Tax
GVA	gross value added
HESTA	Health Employees Superannuation Trust Australia
IA	Infrastructure Australia
IBSA	Innovation and Business Skills Australia
ICAA	Institute of Chartered Accountants in Australia
ISCs	Industry Skills Councils
IT	information technology
ITABs	Industry Training Advisory Boards
LIBOR	London Interbank Offered Rate
MAFC	Melbourne APEC Finance Centre

MCFS	Melbourne Centre for Financial Studies
MFSS	Melbourne Financial Services Symposium
NCVER	National Centre of Vocational Education Research
NIA	National Institute of Accountants
NIBA	National Insurance Brokers Association
NQC	National Quality Council
NSX	National Stock Exchange Limited
OECD	Organisation for Economic Co-operation and Development
OH&S	occupational health and safety
PFAB	Public Finance and Accountability Bill
PFC	public financial corporation
PPP	public private partnership
RBA	Reserve Bank of Australia
RPL	Recognition of Prior Learning
RTOs	registered training organisations
SDIA	Securities and Derivatives Industry Association
SIS Act	*Superannuation Industry (Supervision) Act 1993* (Cth)
SMO	Senior Master's (Funds in Court) Office
SMSF	Self Managed Superannuation Fund
SNZ	Statistics New Zealand
TAC	Transport Accident Commission
TAFE	Tertiary and Further Education
TCV	Treasury Corporation of Victoria
UN	United Nations
VECCI	Victorian Employers' Chamber of Commerce and Industry
VET	vocational education and training
VFMC	Victorian Funds Management Corporation
VMIA	Victorian Managed Insurance Authority

VRQA	Victorian Registration and Qualifications Authority
WEF	World Economic Forum
WFE	World Federation of Exchanges

Glossary

Act	A Bill that has been passed by Parliament, received Royal Assent and become law.
banking and finance sector	Includes banks, building societies, credit unions and other financiers. Provides a wide range of deposit-taking, lending, wealth management and business banking services.
banking commercial	Commercial banks undertake traditional banking activities including accepting deposits and providing loans.
banking retail	Retail banks are local bank branches which provide services predominantly to households, including deposit accounts, mortgages, loans, debit and credit cards and certificates of deposit.
banking wholesale	Wholesale banks provide services predominantly to large organisations. Wholesale banking is otherwise known as business to business banking.
building societies	Building societies are similar to credit unions. They are formed to provide traditional banking services to their members. Their main activities are deposit taking and loans.
clusters	A cluster has been defined as a group of interconnected companies, specialised suppliers, service providers, firms in related industries and associated institutions in a particular field (Porter 2000, p. 15).
credit unions	Credit unions are similar to building societies. They are formed as financial cooperatives established by their members. Credit unions provide traditional banking services including deposit taking and loans. They are owned and operated by their members, who share in any profits.
externalities	Situations in which one person's or firm's activities affect others who are not direct parties to the transaction. Consequently, they do not take the impact

on others into account when making production or consumption decisions.

financial asset broking services Businesses mainly engaged in trading financial assets on behalf of others. Primary activities include commodity futures broking or dealing, stockbroking or trading, and trading of mortgages.

financial planning Financial planners help individuals create and implement strategies to achieve their financial goals.

funds management Fund managers invest, manage and monitor client assets.

Future Fund The Future Fund is a financial asset fund established by the *Future Fund Act 2006* (Cth). Its purpose is to meet unfunded superannuation liabilities that will become payable during a period when an ageing population is likely to place significant pressure on Commonwealth finances.

green paper A green paper is a document detailing draft policy intentions designed for consultation with stakeholders.

gross value added Industry gross value added is the term used to describe the unduplicated value of goods and services produced by individual industries. This measure removes the distortion caused by variations in the incidence of commodity taxes and subsidies across the output of individual industries.

industry superannuation funds Industry superannuation funds are funds with members from employers across an industry and have employer organisation and union sponsors.

investment banks Investment banks provide specialist banking services including underwriting, brokerage, and facilitating mergers and acquisitions.

legislation Laws passed by Parliament, or subordinate legislation being statutory rules made under powers delegated by Parliament.

liveability	Liveability reflects the wellbeing of a community and encapsulates the many characteristics that make a location a place where people want to live.
money market	The money market is a financial market segment that is used for short-term borrowing and lending.
money market dealers	Money market dealers trade high liquidity, short-maturity money market securities including certificates of deposit.
mortgage originator	A mortgage originator is the original mortgage lender, and is part of the primary mortgage market.
not-for-profit organisation	An organisation providing services to the community or its members that does not distribute profits to its members or owners.
offshoring	Describes a business's decision to replace domestically supplied service functions with imported services produced offshore.
policy development	The process of formulating the direction of new primary and subordinate legislation, codes of practice, preparation of regulatory impact statements and business impact assessments, as well as policies on funding programs, community information or other activities. It includes consultation on these matters.
public goods	Goods that are non-excludable, in the sense that it is not possible to exclude people from consuming them, and non-rivalrous, in the sense that one person's consumption of the good does not affect another person's capacity to enjoy it. Because individuals can typically access public goods without payment, commercial incentives to provide public goods are weak, and may warrant public funding.
public financial corporation	Public financial corporations are public entities that have responsibility for delivering financial services. Some of these entities deliver services to the Victorian general public. Others service other areas of the Government.

regulation	The imposition of some rules, supported by government authority, intended to influence behaviour and outcomes. The OECD defines the term as 'the instruments by which governments place requirements on enterprises, citizens and government itself, including laws, orders and other rules issued by all levels of government and by bodies to which governments have delegated regulatory powers'.
regulator	A regulator derives from primary or subordinate legislation one or more of the following powers: inspection; regulatory advice to a third party; licensing; accreditation; and standards monitoring and enforcement.
stockbroking	Stockbrokers facilitate transactions between retail and institutional investors (those with capital) and issuers of securities (those seeking capital).
support services	This segment includes services to finance and investment and services to insurance. Businesses in this segment mainly provide nominee, investment management or advisory services, arrange home loans for others, and provide insurance broking services.
transaction costs	These costs include bargaining and decision costs for the owners, managers and users in negotiating a mutually acceptable sharing arrangement. Such costs are likely to be incurred during the identification, negotiation and funding of sharing arrangements.
venture capital	The venture capital sector finances new innovative businesses.
wholesale funds management	An organisation that manages the financial assets of other large organisations.

Key messages

- Victoria's financial services sector makes a major contribution to the state's economy, with most activity being concentrated in Melbourne.
- The sector's relative strengths are regarded as:
  - industry superannuation funds
  - funds management
  - infrastructure development, including financial contracting.
- The financial services sector in Australia is regarded as having growth potential, stemming from:
  - economic growth increasing the demand for financial services
  - demographic, structural and policy changes that are causing shifts in demands for financial services, including for retirement products
  - exploiting opportunities to grow outside Australia
  - changes in the approach to risk and cost management.
- Almost all of the regulation of the financial sector is done by the Commonwealth Government. Its responses to the recently completed Australian Financial Centre Forum review and the Henry taxation inquiry, and to the yet-to-be completed Cooper inquiry into superannuation may remove or reduce significant regulatory barriers to the financial sector, including those parts strongest in Victoria. The Commission's inquiry has been done in that context.
- The Victorian Government has limited influence on key factors affecting location decisions by businesses. The aspects that the Victorian Government can influence are: the few remaining areas of state financial services regulation; the overall quality of the economic and regulatory environment as an underpinning for economic growth; selected operations activities including Public Private Partnerships; ensuring arrangements for skills formation that encourage flexibility, responsiveness; and targeted measures to improve access to information about the sector to organisations and individuals resident overseas.
- State taxes and/or state regulations fall mainly on insurance transactions, the activities of selected public financial corporations and exchanges. There may be scope to adjust these to reduce or remove impediments, but the capacity to do so will be constrained by revenue and other considerations. Such actions seem likely to have modest, positive impact on the Victorian financial sector.
- While access to appropriate skills and labour is regarded as a key strength by the sector, there is little evidence of widespread skill shortages, which appears to be confined to accountants. Better, more comprehensive information on skills is likely to assist businesses, training and education providers, and individuals in improving the efficiency of skill formation. Less costly pathways to accrediting training and education, especially that provided by businesses, is likely to improve labour flexibility and mobility.
- Other areas where the Victorian Government can remove impediments or improve knowledge of Victoria's financial sector are through its advocacy to the Commonwealth regarding its three key reports into taxation, the Australian financial system and superannuation regulation.
- In addition to making a small number of draft recommendations, the Commission seeks some important information that will enable it to assess the impact of the proposed changes.

Overview

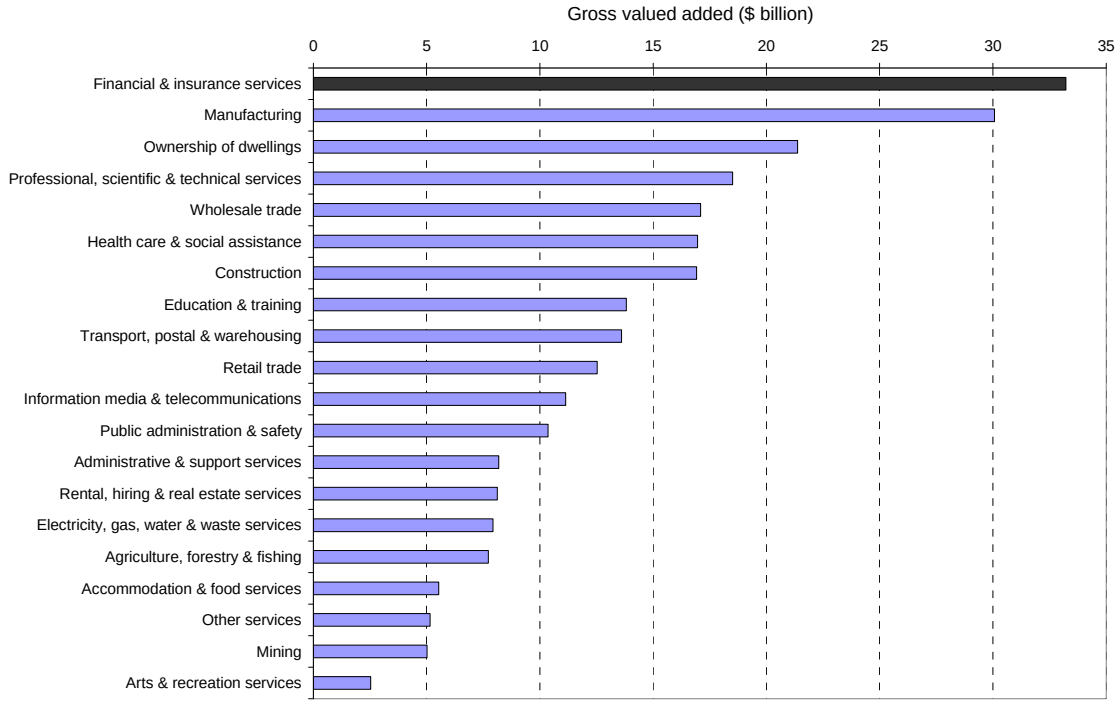
The Victorian Government has directed the Victorian Competition and Efficiency Commission (the Commission) to inquire into regulatory and other impediments to growth in the Victorian financial services sector. This request is part of a broader government strategy to position Victoria as an internationally recognised and competitive financial services hub.

To inform its review, the Commission conducted a public inquiry, which consulted widely with relevant stakeholders, and also drew heavily on other recent reviews and the submissions to those reviews.

The financial services sector in Victoria

The financial services sector makes a significant contribution to the Victorian economy and in 2008-09 it was the largest industry sector in Victoria, measured in terms of output (figure 1). The value of the industry is more than its direct contribution to the Victorian economy — financial services provide an enabling function which underpins much economic and social activity.

Figure 1 **Gross value added, by industry sector, Victoria, 2008-09[a]**



a Current price financial year data.

Source: ABS 2009c.

There are already some major segments such as banking, insurance, funds management, and support services located in Victoria. Many financial services businesses are located in close proximity to each other in metropolitan Melbourne. In particular, there is a significant cluster of businesses in the funds management industry.

The sector's export performance is modest and may be an area of opportunity. Competitive, dynamic Victorian businesses would be expected to identify and take advantage of opportunities to expand their activities. This could result in greater turnover for Victorian firms, more assets under management in Victoria or increases in the sales of support services.

Such growth can also be accompanied by increases in employment opportunities — not only directly — but also in supplying the services that support a growing industry or in new businesses attracted by growing clusters and new opportunities.

Focusing the report: building on strengths

The Commission's approach during the inquiry has been to consider opportunities to remove regulatory and other impediments to development and growth so that:

- Victoria can build on its strengths in the financial services sector
- the financial services sector can take advantage of future opportunities for growth and development.

While the Commission has not yet reached any final conclusions regarding the areas of comparative advantage of the financial services sector in Victoria, it considers they may include:

- some large scale public sector funds managers domiciled in Melbourne, in particular the Future Fund and the Victorian Funds Management Corporation
- the industry superannuation funds that provide services to their members around Australia
- the capacity to define, manage and deliver major infrastructure projects, especially Public Private Partnership projects
- intermediaries whose business has identified specific segments of consumers not adequately served by existing intermediaries. Examples include the ME Bank and the Bendigo and Adelaide Bank, which has developed a network of franchised local banks
- some specialised, efficient and publicly-owned financial services providers, such as the Rural Finance Corporation.

Victoria's strengths in these areas stem from a number of factors including:

- historical and institutional factors
- the general competitiveness of business and regulatory conditions
- access to a critical mass of skilled employees
- the presence of related businesses and clients (clusters of activity)
- local demand for services and access to local customers
- access to appropriate infrastructure
- the overall liveability of the location.

Participants and others have identified a number of potential opportunities for further development of the sector. These opportunities stem from:

- a growing national and state economy and population growth
- demographic, structural and policy changes causing shifts in the demand for financial services. For example, the ageing of the population has lead to an increased interest in retirement products.
- taking advantage of global opportunities to grow the industry beyond the domestic market
- changes in the approach to risk and cost management, including as a result of the global financial crisis.

The Commission's approach is underpinned by the idea that growth is often best built by combining existing strengths with new opportunities. The Commission has then focused its analysis on impediments impacting on the sector by examining:

- the drivers of investment and location
- regulation and taxation
- government operations
- ensuring a supply of skilled labour.

Drivers of investment and location

Victoria is an attractive location for the growth of existing businesses and for attracting new businesses, including from overseas. Future growth opportunities would enable Victoria to build on areas where it already has a strong financial services sector presence.

While the State Government has limited scope to influence many of the factors affecting business location decisions, it is able to remove barriers to growth by influencing the following:

- building the general competitiveness of business and regulatory conditions, including regulatory and tax policies

- supporting access to a critical mass of skilled employees
- reputation factors, such as a centre's profile and reputation, including overseas, in areas like research and network opportunities, and generally creating a positive industry environment
- capitalising on strengths in the Government's own operations
- removing impediments to the development of natural clusters of financial activities.

These issues are discussed in the following sections.

Regulation and taxation

The Commission observed that most of the regulatory arrangements affecting the financial services sector in Victoria are Commonwealth. In addition, there have been a number of recent and current Commonwealth reviews on aspects of the sector and the Commission has not duplicated this work. The Commission considers these reviews have the potential to have a significant, positive impact on the financial sector, depending on the Commonwealth Government's response.

The Commission has concluded, on the basis of the evidence available, that there is little state regulation that impedes the financial services industry. The Commission has sought participant comment on the robustness of this conclusion.

However, there have been some concerns about inconsistency across jurisdictions, particularly in relation to insurance products. The Commission has recommended that the Victorian Government encourage the Council of Australian Governments (COAG) to consider the harmonisation of insurance requirements across jurisdictions when the next round of COAG priorities are being determined.

Also, state regulation appears to confine a lot of service provision to state agencies. While it is recognised that how the State Government chooses to provide such services can have a significant impact on their efficiency and the opportunities available in the sector, the Commission has not received any submissions to suggest that the current balance is controversial.

Concerns have also been raised with the Commission about state stamp duties on insurance. The Commission considers that while concerns about the efficiency of such taxes are valid, they are best addressed in the context of a national response to Australia's Future Tax System review (the Henry review), if possible.

Government operations

The terms of reference requires the Commission to inquire into options for 'operational changes that the Victorian Government can undertake to support development of the Victorian financial services sector'.

The areas of the Victorian Government's current operations, outside direct regulation of the Victorian financial services sector, that may also affect the sector include:

- providing an internationally competitive regulatory environment for business in general, encouraging growth in the Victorian economy
- removing, or advocating the removal, of impediments that adversely impact on the competitiveness of those areas of the sector that have comparative advantage. By so doing, the Victorian Government may contribute to the further development of sub-sectoral clusters within the Victorian financial services sector.
- improving access to information for potential new businesses and customers outside Victoria about the strength, quality and sophistication of the Australian financial system, including that part operating in Victoria, through promotion activities, including overseas missions
- deepening, and capitalising on, the expertise of its own operations in financial activities to deepen the sophistication and capability of the sector.

Ensuring supplies of skilled labour

There are many participants in the financial services labour market and the skills formation system. The skills formation system involves state and national education and training providers, and government and industry skills bodies (which cater for the financial services sector — and other sectors in the economy).

In response to concerns about skill shortages, the Commission examined national and Victorian evidence on skill shortages. The latest available evidence, whilst subject to limitations, indicates skill shortages in Victoria's financial services sector are confined to a small number of occupations — particularly accountants — and are not particularly widespread among businesses. This is supported by the Commission's recent consultations with businesses and other participants in the sector.

Major reform to the skills system in Victoria is being phased in over the next four years. The Commission supports the broad aim of this reform, which seeks to make the system work better by being more responsive and flexible to the needs of businesses and individuals. Good practice dictates that the outcomes of the reform be monitored, evaluated and reported.

The Commission has not found any significant regulatory impediments to the supply of skilled labour to the financial services sector. Nonetheless, there appears to be scope to improve aspects of current arrangements by enhancing skill needs information, updating occupational codes, providing information on nationally recognised courses and qualifications, and establishing a consultation mechanism between industry and the higher education sector.

In relation to accreditation and licensing, the Commission has not found sufficient evidence that suggests major changes are needed.

Implications of the Commission's recommendations

In developing its recommendations the Commission has focused on ideas that would generate sustainable growth. Such growth will result when the market is strongly competitive and barriers are removed so that the industry can take advantage of new ideas, opportunities and innovations in areas in which it has a comparative advantage.

The types of activities the Commission is seeking to reinforce through its recommendations, for example, the development of clusters, have proven in the past to stimulate innovation and growth — the development of the Mercer Global Pension Index is an example.

It is in freeing industry to respond to opportunities where the greatest economic benefits of these recommendations will arise.

Taken together the Commission's recommendations will help remove impediments to Victoria's financial services sector taking advantage of growth opportunities and ensure it has the flexibility to respond to opportunities as they arise.

In its draft report the Commission has made a large number of requests for further information. The Commission is therefore not in a position to fully evaluate its package of proposed reforms. The full package and its implications for that part of the financial services sector located in Victoria will be presented in the Commission's final report.

Draft recommendations and requests for information

The draft recommendations and information requests are listed in the order they appear in the report, and they need to be understood in the context of the discussion in respective chapters.

Chapter 2: The financial services sector in Victoria

Information request: What is the extent of offshoring in the financial services sector in Victoria? Which parts of the sector and which activities have been affected by offshoring?

Chapter 4: Regulation and taxation

Draft recommendation 4.1

That the Victorian Government should support and encourage the Commonwealth to implement recommendations 4.3 and 4.8 from the Australian Financial Centre Forum report. This would involve support for:

- **Recommendation 4.3: The Asia Region Funds Passport**
- **Recommendation 4.8: Removal of regulatory barriers to Islamic finance.**

Information request: The Commission has identified some areas from both the Australian Financial Centre Forum report and Cooper review as areas of particular significance for Victoria — does this list cover the main issues, or are there other additional (or fewer) areas the Victorian Government should focus on?

Information request: Are there any issues associated with the scope of operation, and legislative restrictions on that scope, and the methods of prudential regulation applied to public financial corporations in Victoria?

Information request: Are there any other impediments or operations issues relating to the operation of bodies providing financial services on behalf of the Victorian Government that the Commission should consider in meeting its terms of reference?

Draft recommendation 4.2

That when future Council of Australian Governments (COAG) priorities are being identified, the Victorian Government should encourage the inclusion of harmonisation of regulation covering mandatory insurance requirements on the national COAG agenda.

Draft recommendation 4.3

That the Victorian Government should support and encourage the Commonwealth to implement recommendations 3.1, 3.3 and 3.6 from the Australian Financial Centre Forum report. This would involve support for:

- **Recommendation 3.1: Investment Manager Regime**
- **Recommendation 3.3: Funds management vehicles**
- **Recommendation 3.6: Islamic finance products.**

Information request: As with the regulatory issues, the Commission has identified some areas from the Australian Financial Centre Forum report, Cooper review and Henry review as areas of particular significance for Victoria — are these issues being sufficiently covered by these reviews, and does this list cover the main issues, or are there other additional (or fewer) areas the Victorian Government should focus on?

Draft recommendation 4.4

That, in light of the findings of the review of *Australia's future tax system* (Henry review), the Victorian Government should take a lead role in negotiating national harmonisation of stamp duty on insurance and reducing the reliance on such taxes.

Draft recommendation 4.5

That, in the absence of the conditions necessary for achieving national harmonisation of stamp duty on insurance, the Victorian Government consider reducing the distorting impact of the state tax on insurance by reducing stamp duty to the lowest rate among state jurisdictions as circumstances permit.

Information request: If an exemption to land rich duty were to be extended to all licensed stock exchanges, what would be the likely economic impact?

Information request: Are there any other state-imposed regulatory impediments that are restricting the growth of the financial services sector in Victoria?

Chapter 5: Government operations and other matters

Information request: In what way could the Victorian Government support Victoria's capacity for financial sector research and its reputation as a centre of academic excellence, in particular in relation to 'pre-competitive' or basic research?

Draft recommendation 5.1

That to promote the strengths of Victoria's financial sector in a changing global environment, the Department of Innovation, Industry and Regional Development work with Austrade to ensure that appropriate weighting is given to the financial services sector based in Victoria in national promotional activities.

Information request: How can Victoria best exploit its expertise in PPPs? How would this affect Victoria's financial services sector? What are the benefits? What are the risks? How could the risks be mitigated?

Chapter 6: Skilled labour

Information request: What is the appropriate frequency of the metropolitan and regional skills and labour needs surveys, given the changes under the new skills system?

Draft recommendation 6.1

That the Department of Innovation, Industry and Regional Development prepare and publish, as soon as is practicable, employment and training forecasts for the financial services sector in Victoria. These forecasts should be updated and published at least annually using the latest available information.

Draft recommendation 6.2

That the Victorian Government, through its representatives on national advisory bodies such as the Australian Statistics Advisory Council, report the limitations of the Australian and New Zealand Standard Classification of Occupations in the financial services sector, and advocate that the classifications in that sector be updated to reflect current occupations.

Information request: The Commission seeks further information from industry, employers and higher education providers on the advantages and disadvantages of 'bridge' diplomas, internships, industry placements, cooperative education programs, and provision of specialised courses.

Draft recommendation 6.3

That the Victorian Government request Business Skills Victoria to develop representative business cases for the Financial Services Training Package and Business Services Training Package, including expected benefits, costs and returns and comparison with other training.

Draft recommendation 6.4

Information about nationally recognised qualifications — such as those in the Financial Services Training Package and Business Services Training Package — should be included in:

- **the consolidated industry information service being developed by the Victorian Skills Commission and Industry Training Advisory Bodies**
- **the Victorian Government's public information campaign about the new skills system.**

Information request: What scope is there to improve existing Recognition of Prior Learning (RPL) processes? Is there a need for additional measures to raise awareness about RPL among registered training organisations in relation to financial services skills? If so, what measures are needed?

Information request: Are there any impediments to credit transfer for completed units or subjects in finance, business and commerce between vocational education and training institutions and higher education institutions in Victoria?

Draft recommendation 6.5

That the Victorian Government propose, in the Ministerial Council for Tertiary Education and Employment, the establishment of an industry panel to advise a national higher education committee such as the Australian Business Deans Council on industry needs regarding skill needs, qualifications and associated curriculum development. In the absence of national agreement, the Victorian Government should implement an equivalent arrangement in Victoria.

Information request: Based on submissions, consultations and roundtable discussions for this inquiry, there do not appear to be significant concerns with existing accreditation arrangements. Are there any reasons why this is not a valid conclusion?

Information request: The Commission seeks further information on the advantages and disadvantages of publishing the quality indicators collected under the Australian Quality Training Framework.

Chapter 7: Implications of the Commission's recommendations

Information request: The Commission invites feedback on all the recommendations and other requests for information made in this draft report. In particular, the Commission invites comment on the economic impact of its recommendations and potential impacts in areas where it has made specific information requests.

1 Introduction

The Victorian Government has directed the Victorian Competition and Efficiency Commission (the Commission) to inquire into regulatory and other impediments to the growth in the Victorian financial services sector. This request is part of a broader government strategy to position Victoria as an internationally recognised and competitive financial services hub.

To inform its review, the Commission conducted a public inquiry, which consulted widely with relevant stakeholders, and also drew heavily on other recent reviews and the submissions to those reviews.

This chapter describes, in more detail, the background to the inquiry and the inquiry process. It also outlines the structure of the report.

1.1 Background to the inquiry

The financial sector is at the core of the Victorian and Australian economic system, providing a range of services necessary for other industries to function efficiently, and enabling consumers to effectively manage their consumption-savings requirements over time (AFCF 2009, p. 5). In a recent submission to a Joint Parliamentary Committee, the Commonwealth Treasury noted that:

> The stability, integrity and efficiency of the financial system are critical to the performance of the entire economy. Well functioning and credible financial markets are necessary to attract domestic and foreign investment which contributes to the broader objective of creating employment and delivering sustained economic growth. (Commonwealth Treasury 2009, p. 3)

In terms of the sectors contribution to Victorian economy, the terms of reference for the inquiry note that 'Victoria's financial services sector is large and diverse, employing some 100,000 people' but in addition, 'a stable and vibrant financial services sector underpins economic performance and provides the confidence and stability necessary to attract financial capital and overseas investment'.

The terms of reference also note the Victorian Government's strategy of 'supporting the growth of a financial services sector through positioning Victoria as providing an internationally competitive business location with particular strengths and capabilities'.

The Government's statement *A great place to do business: Growing Victoria's financial services sector* sets the strategic direction to achieve this policy objective and outlines a number of specific initiatives (box 1.1).

Box 1.1 A great place to do business

A great place to do business: Growing Victoria's financial services sector is the Victorian Government's financial services statement. Launched in August 2009, it discusses the financial services sector in Victoria and considers Victoria's strengths and opportunities for government action.

The statement outlines elements that can attract people to live, work and do business in Victoria, including:

- Victoria's strong economy
- a competitive and innovative business environment
- modern, efficient infrastructure
- a prime location, close to Asia's growing markets
- a high quality lifestyle
- a host of major global events.

There are several reasons why Victoria is a great location for financial services, such as:

- the Docklands Financial Services Precinct
- a competitive, affordable and innovative business environment
- leadership in skills, education and research
- strong government support.

The statement outlines future government actions in the following areas:

- positioning Melbourne as a global centre of excellence in pension and funds management
- establishing Melbourne as a Carbon Market Hub for the Asia Pacific
- training the workforce
- building on Victoria's strengths
- moving forward from the Global Financial Crisis.

Source: Victorian Government 2009a.

As part of its commitment to 'build a financial sector that is globally connected, highly capable and robustly competitive' (Victorian Government 2009a, p. 23), the Victorian Government established this inquiry to 'inquire into regulatory impediments in the financial services sector … and make recommendations about how government can further reduce red tape for the sector and boost competitiveness' (Victorian Government 2009a, p. 27).

A key thrust of Commonwealth, state and some local governments is to ensure there are no unnecessary barriers to the growth of financial services because of the direct contribution the sector makes to the Victorian economy and its contribution to business growth more broadly. The City of Melbourne in its submission to the Victorian Parliament's Economic Development and Infrastructure Committee, noted that:

> The size and strength of the financial services industry in Melbourne does not only have a positive influence on direct employment within the sector, but also contributes positively to employment levels across a number of industries, including, but not limited to, accounting, legal, information technology, human resources, recruitment, consulting and education/training industries. (City of Melbourne 2007, p. 1)

This view is supported by data that indicate that financial services are among the industries that other businesses rely on most heavily as an input to their activities.

1.2 Approach to the inquiry

The Commission is undertaking this inquiry into the financial services sector in accordance with the terms of reference for the inquiry. A key aspect of the terms of reference outlines the purpose and scope of the inquiry.

The terms of reference do not define what constitutes the financial services sector in Victoria, but note that the sector includes banking, superannuation and insurance. The Commission has, therefore, developed its own definition of the sector for the purposes of this inquiry, drawing on published material, information received during consultations and feedback on the inquiry's issues paper.

1.2.1 Purpose and scope of the inquiry

The terms of reference require the Commission to inquire into regulatory and other impediments in the financial services sector. Broadly, the Commission is directed to:

- report on the significance and diversity of the financial services sector in Victoria
- identify Commonwealth and State regulations that impact the development of Victoria's financial services sector
- report on any regulatory or other impediments to ensuring sufficient supplies of skilled labour in the sector
- report on options for regulatory and/or operational changes that the Victorian Government can undertake to support the sector in Victoria
- identify the economic impact of any options identified during the inquiry.

In addition, the terms of reference direct the Commission to take account of any other substantive studies or developments in Victoria or in other jurisdictions. The Commission is also to have regard to the strategic directions set out in Victoria's Financial Services Strategic Statement (box 1.1).

1.2.2 Recent reviews of financial services

Recent relevant studies or reviews include:

- the Victorian Government's statement *A great place to do business: Growing Victoria's financial services sector*
- the study undertaken by Deloitte Touche Tohmatsu (2007) for the Victorian Department of Innovation, Industry and Regional Development (DIIRD) entitled *Victorian Financial Services Industry: Strategic Opportunities*
- the Australian Financial Centre Forum's (AFCF) report into *Australia as a financial centre: building on our strengths* (AFCF 2009)
- the Commonwealth's Review into the Governance, Efficiency, Structure and Operation of Australia's Superannuation System (the Cooper review)
- the Commonwealth's review of Australia's Future Tax System (AFTS) (the Henry review).

1.2.3 Defining financial services

There is no single definition of what constitutes a financial service. As a result of its research and feedback received from industry participants, the Commission includes the following services in its definition of financial services:

- banking
- insurance
- funds management, including superannuation
- services offered by finance companies
- trading in new markets (such as water or carbon markets)
- venture capital
- financial advice
- the provision of leasing arrangements
- investment services
- custodial services
- innovative and specialist financial products and services, for example, Islamic and any other culturally-specific finance
- micro-credit (including pay-day and short-term loans)
- stockbroking services
- the creation of and trading in financial instruments.

This definition is consistent with the definition adopted by other recent inquiries into the financial services sector. DIIRD also includes the following types of services as finance and insurance:

- the provision of finance
- investing money in predominantly financial assets
- services to lenders, borrowers and investors
- insurance cover of all types
- services to insurance underwriters and to people or organisations seeking insurance (DIIRD 2008).

The Australian Bureau of Statistics (ABS) defines financial and insurance services as:

- finance (central banking; depository financial intermediation; non-depository financing; financial asset investing)
- insurance and superannuation funds (life insurance; health and general insurance; superannuation funds)
- auxiliary finance and insurance services (auxiliary finance and investment services; auxiliary insurance services) (ABS & SNZ 2006b, p. 48).

Similarly, the coverage of the Victorian Government's financial services strategy indicates the areas that it believes are important: pension and funds management, investment services, insurance and banking, venture capital, and innovative and emerging markets. The strategy also notes the potential for further development of Islamic financial instruments in Victoria (Victorian Government 2009).

1.3 Focus and process of the inquiry

1.3.1 Focus of the report

The Commission's analysis is focused mainly on those sub-sectors that have the greatest potential for growth, and where there are regulatory issues, operational practices or other impediments to growth that:

- government has the capacity to influence (at least to some extent)
- a national agreement between governments does not exist, or has not been recently made and implemented (for example, consumer credit has been excluded because it is the subject of a recent national agreement)
- are not subject to current or recent review (for example, the Commission has not duplicated the work being undertaken by the AFCF). The Commission may, where appropriate, provide a state-based perspective to complement these other reviews.

As well as regulatory impediments, the terms of reference also require the Commission to identify 'other' impediments and barriers to the development of the financial sector. Possible impediments that the Victorian Government can

influence include state taxes and the Government's operational activities as a provider and purchaser of financial services.

The report does not cover government interventions that apply to all or most sectors of the economy. Building and planning regulations, occupational health and safety, and the Fair Trading Act are out of scope of the inquiry.

1.3.2 A national industry

The Commission considers that Victoria and New South Wales, and to a lesser extent other states and territories, are part of a national financial services sector that competes in a global market. This national focus is reinforced by essentially national financial services regulation and Australia's involvement in international negotiations on regulatory standards. The Commission has set this inquiry in that larger context, including by focusing on how actions to remove impediments in Victoria might complement changes in national regulation and other national policies affecting the sector. This perspective, in the Commission's view, would best allow the Victorian industry to build on its strengths and take maximum advantage of new opportunities as they arise.

1.3.3 Inquiry process

The Commission advertised the inquiry in the press and by circular to those who, according to a preliminary analysis, were likely to be interested. In November 2009, the Commission released an issues paper and invited any interested party to make a submission to the inquiry. The terms of reference and inquiry particulars were listed on the Commission's website (www.vcec.vic.gov.au).

In the course of the inquiry, the Commission met with many individuals and organisations (in some cases multiple times to meet different people within the organisation) to identify and assess the issues relevant to this inquiry. The Commission has so far received 13 submissions from interested parties, including businesses and private individuals. In addition, it has reviewed the public submissions made to other inquiries including:

- the Victorian Parliament's Economic Development and Infrastructure Committee's inquiry into key competitive advantages in Victoria's financial services sector (the terms of reference for this inquiry were rescinded by Motion of the Legislative Assembly on 31 July 2008 and no report was published)
- the AFCF's inquiry leading to the report *Australia as a Financial Centre: Building on our Strengths*.

As part of the consultation process, the Commission held two roundtables on skills issues and leveraging opportunities for Victoria's financial services market involving 15 participants.

During the inquiry, the Commission also undertook extensive desk-based research, drawing on published reports and papers, academic studies and web-based information sources. The Commission took account of the *Charter of Human Rights and Responsibilities Act 2006* (Vic.) and considers that this report is consistent with the human rights set out in the Charter.

1.4 Structure of the report

The draft report is structured as follows:

- introduction (chapter 1)
- the financial services sector (chapter 2)
- drivers of investment and location (chapter 3)
- regulation and taxation (chapter 4)
- government operations and other matters (chapter 5)
- skilled labour (chapter 6).

The draft report is drawn together in chapter 7, which assembles the Commission's recommendations and discusses their implications for the sector.

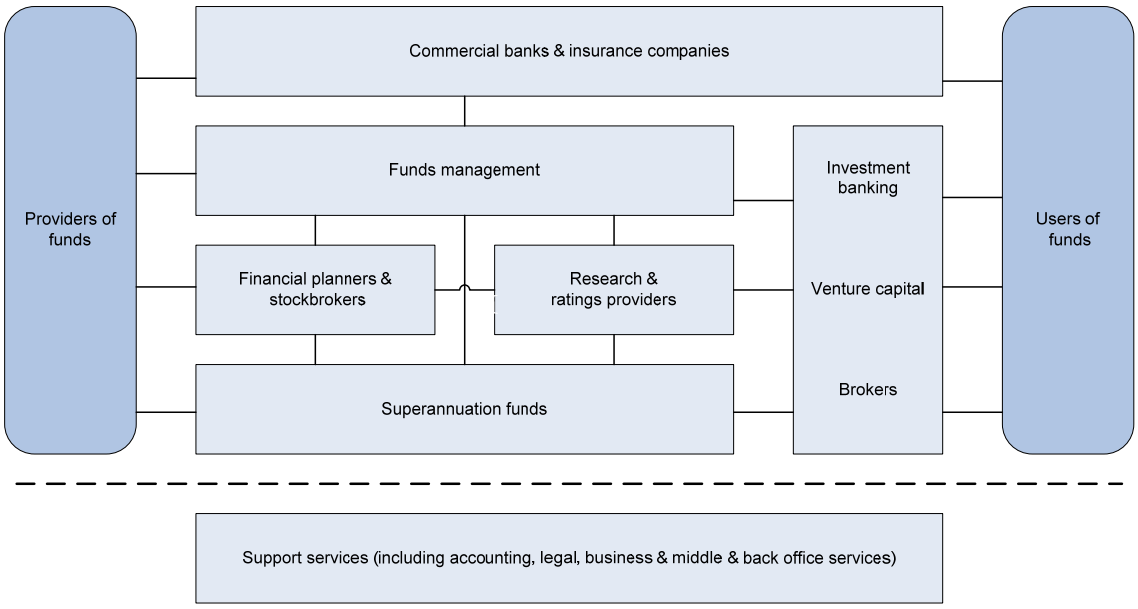
A supporting appendix provides information on parties consulted during the course of the inquiry through meetings, roundtable discussions and submissions (appendix A). Appendix B provides additional data on the financial services workforce in Victoria.

2 The financial services sector in Victoria

2.1 Introduction

The terms of reference ask the Victorian Competition and Efficiency Commission to report on the significance and diversity of the financial services sector in Victoria. As noted in chapter 1, financial services comprise a wide range of products and services such as banking, insurance, funds management and financial advice. These services are important for ensuring an efficient 'flow of funds' from the suppliers of funds — through intermediaries — to the users of funds (figure 2.1). This underpins the efficient functioning of the economy.

Figure 2.1 **Financial services 'value chain'**



Source: Adapted from Brimble et al. 2009.

This chapter highlights the key features of the financial services sector in Victoria. It outlines:

- the economic contribution of the sector (section 2.2)
- the characteristics of major industry segments (section 2.3)
- trends in the sector (section 2.4).

Because the chapter focuses on Victoria's financial services sector, it presents Victorian data wherever possible. In some cases, Australian data are used because equivalent Victorian data are not available. (For a recent overview of Australia's

financial services sector, see for example, the Australian Financial Centre Forum's report *Australia as a Financial Centre: Building on Our Strengths* (AFCF 2009).)

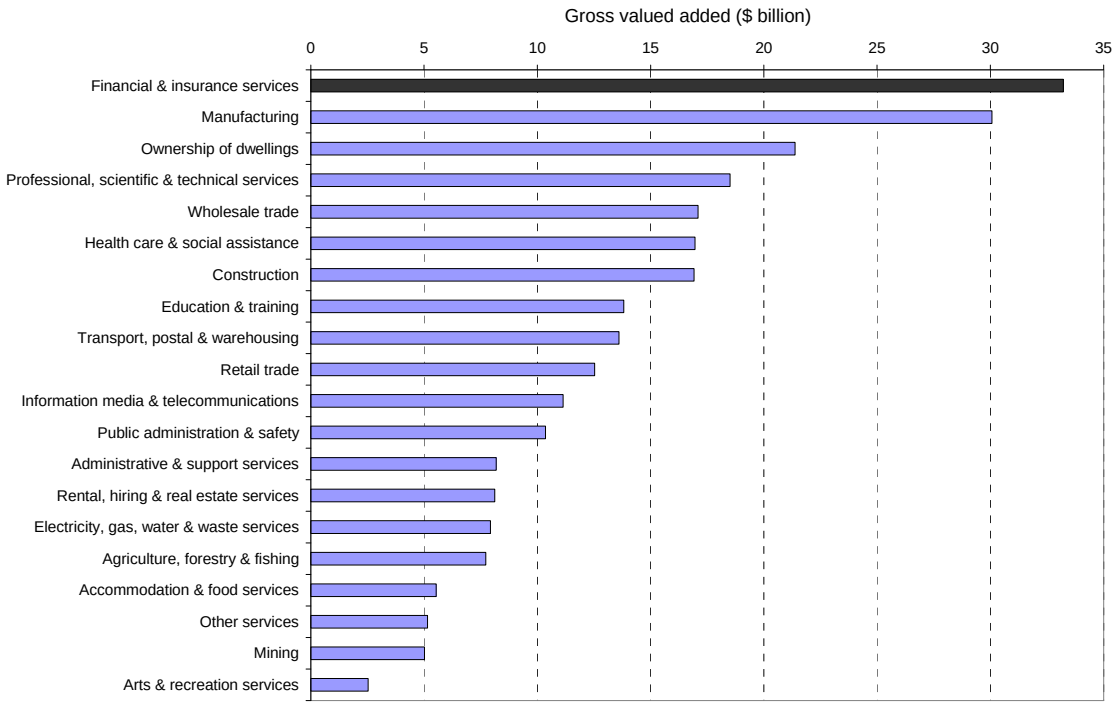
2.2 Economic contribution

The significance of the financial services sector to Victoria's and the national economy can be measured by its contribution to economic activity and employment. Another measure of the sector's significance is the assets managed by financial services businesses that are headquartered in Victoria. However, data on assets under management in Victoria are often not readily available.

2.2.1 Gross value added

The financial services sector was the largest industry sector in Victoria in 2008-09 measured in terms of gross value added (GVA) (figure 2.2).

Figure 2.2 **Gross value added, by industry sector, Victoria, 2008-09[a]**

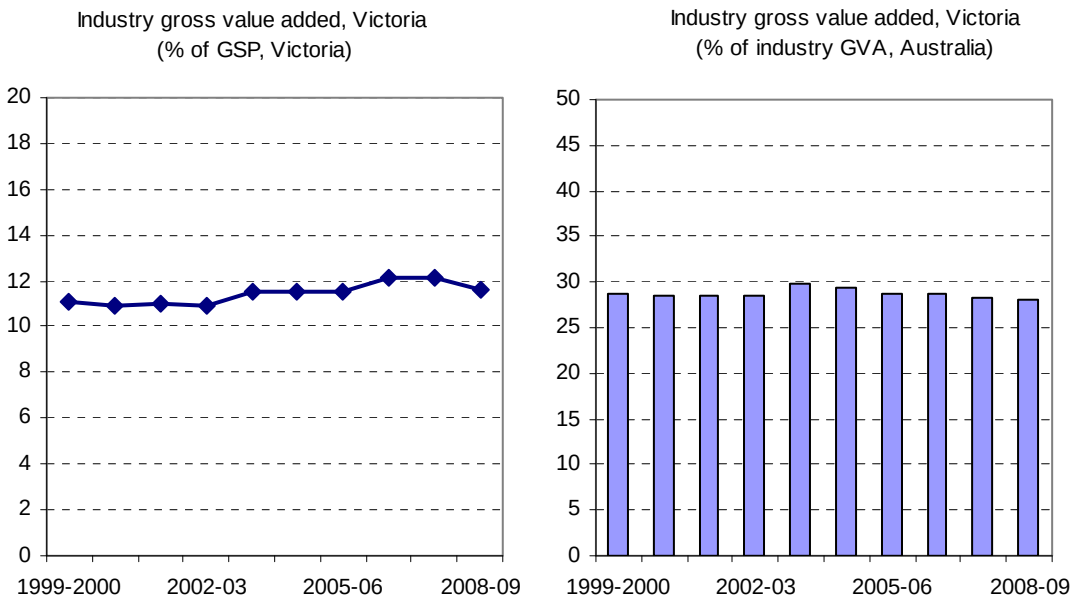


[a] Financial and insurance services under the Australian and New Zealand Standard Industry Classification (ANZSIC) (ABS & SNZ 2006b). Gross value added is the ABS's preferred national accounts measure of industry production (ABS 2005, p. 562). Current price financial year data.

Source: ABS 2009c.

The financial services sector is a significant contributor to the Victorian economy, generating around $33 billion or about 11 per cent of gross state product (GSP) in 2008-09. The sector has increased slightly as a share of GSP over the past decade (figure 2.3, left panel).

Figure 2.3 **Gross value added, financial services, Victoria[a]**



[a] Chain volume financial year data.

Source: ABS 2009c.

Victoria represented about 28 per cent of the GVA generated by Australia's financial services sector in 2008-09 (figure 2.3, right panel).

2.2.2 Employment

Employment in Victoria's financial services sector has averaged around 100 000 in recent years, representing about 4 per cent of the state's workforce and about one-quarter of financial services employment nationally. These shares have remained relatively stable over the past decade. In 2008-09, the sector was the twelfth largest industry by employment in Victoria (appendix B).

A change in the sector's output in Victoria may not necessarily translate into a proportionate change in employment. This is because the demand for labour is also influenced by factors such as labour costs, work practices, technology and the extent of outsourcing (interstate or overseas) and offshoring (moving work to overseas locations).

Remuneration in Victoria's financial services sector is above the average for all industries. The characteristics of workers in the sector (such as their age, gender, educational attainment and earnings) are outlined in appendix B.

2.2.3 Industry segments

More than 35 000 businesses operated in the financial services sector in Victoria in 2007 (table 2.1).[1] There were large numbers of superannuation funds, financial asset investors, and businesses providing support services to finance, investment and insurance businesses but comparatively fewer numbers of deposit-taking and insurance businesses.

Table 2.1 Businesses by industry segment, financial services, Victoria, 30 June 2007

Industry segment	*Businesses*[a]	
	no.	%
Banks	42	0.1
Building societies	3	0.0
Credit unions	48	0.1
Money market dealers	24	0.1
Deposit taking & other financiers	510	1.4
Financial asset investors[b]	11 142	31.4
Life insurance	63	0.2
General insurance	408	1.2
Health insurance	27	0.1
Superannuation funds	10 629	30.0
Financial asset broking services[c]	1341	3.8
Support services[d]	11 223	31.6
Total	35 460	100.0

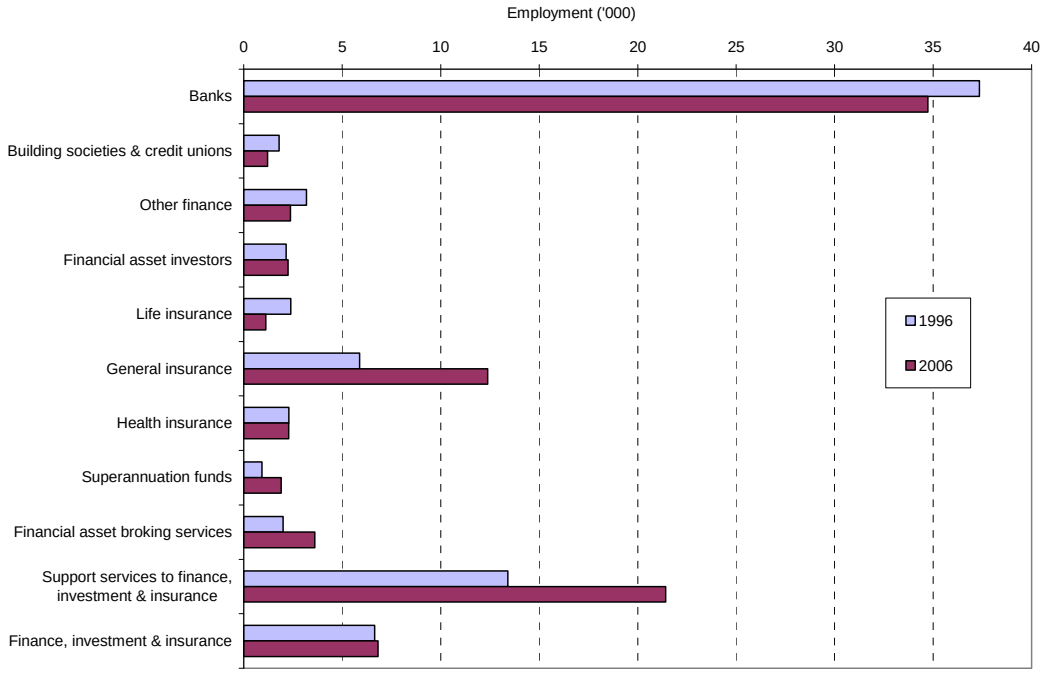
[a] Employing and non-employing businesses. [b] Businesses mainly engaged in investing money on their own account primarily in financial assets (excluding superannuation funds). [c] Businesses mainly engaged in trading financial assets (such as stocks and shares) on behalf of others or in underwriting financial asset issues. [d] This segment includes services to finance, investment and insurance. Businesses in this segment are mainly engaged in providing nominee, trustee, investment management or advisory services, and insurance broking or agency services.

Sources: ABS 2007; ABS & NZDS 1993.

[1] Excluding non-employing businesses, there were more than 9 000 businesses in the sector.

There is considerable diversity in the types of businesses operating in different segments of Victoria's financial services sector. The segments with large numbers of businesses were not necessarily those that employ the most people. Banks, for example, accounted for 0.1 per cent of businesses (table 2.1) but were the largest employers, accounting for nearly 40 per cent of employment in 2006 (figure 2.4).

Figure 2.4 Employment by industry segment, financial services, Victoria[a]



a 'Other finance' includes money market dealers, deposit-taking financiers and other financiers. 'Finance, investment & insurance' includes employment that could not be allocated to more specific categories. August data.

Source: ABS 2009d.

Insurance businesses were also significant employers, with around 16 000 employees in 2006. Auxiliary or support services accounted for more than 21 000 employees.

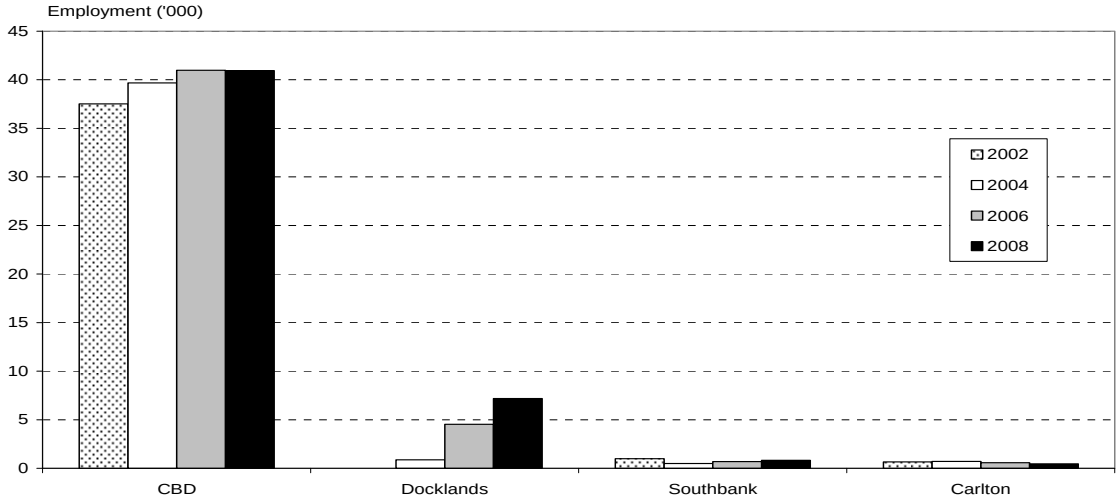
Support services and general insurance were the largest contributors to employment growth in the sector over the ten years to 2006. This may be due, in part, to back office functions in financial institutions being outsourced. Over the same period, the number of people employed by banks, credit unions and building societies fell. There have also been significant changes in the insurance industry, with growth in the general insurance segment and a decline in the life insurance segment.

2.2.4 Business and employment location

More than 80 per cent of financial services businesses in Victoria were located in Melbourne in 2007, with the highest concentration being in inner Melbourne. Most (nearly 90 per cent) of Victoria's financial services workforce was located in metropolitan Melbourne in 2006. Melbourne is the second largest financial centre in Australia when measured by business and employment numbers (ABS 2007, 2009b).

The financial services sector is also a major occupier of office space in the City of Melbourne. While the central business district is the main location for financial services businesses, Docklands has become home to a number of large financial institutions and is emerging as a financial precinct outside the city centre (City of Melbourne 2009a). Financial services employment in Docklands has increased significantly in recent years (figure 2.5).

Figure 2.5 **Employment, financial services, City of Melbourne[a]**



[a] Data from the City of Melbourne's Census of Land Use and Employment (CLUE). The data relates only to the municipality of the City of Melbourne. Although the financial services employment in the City of Melbourne has recorded absolute growth in recent years, its share of total employment in the municipality has been relatively stable.

Source: City of Melbourne 2009b.

According to the Melbourne Financial Services Symposium (MFSS) survey, there has been growth in the percentage of organisations operating as fund managers and as consultants or vendors to the sector. At the same time, the survey reported that there has been a decline in the percentage of organisations operating as banks and non-bank financial institutions (such as credit unions) and as stockbrokers or investment banks (MFSS 2007, p. 7).

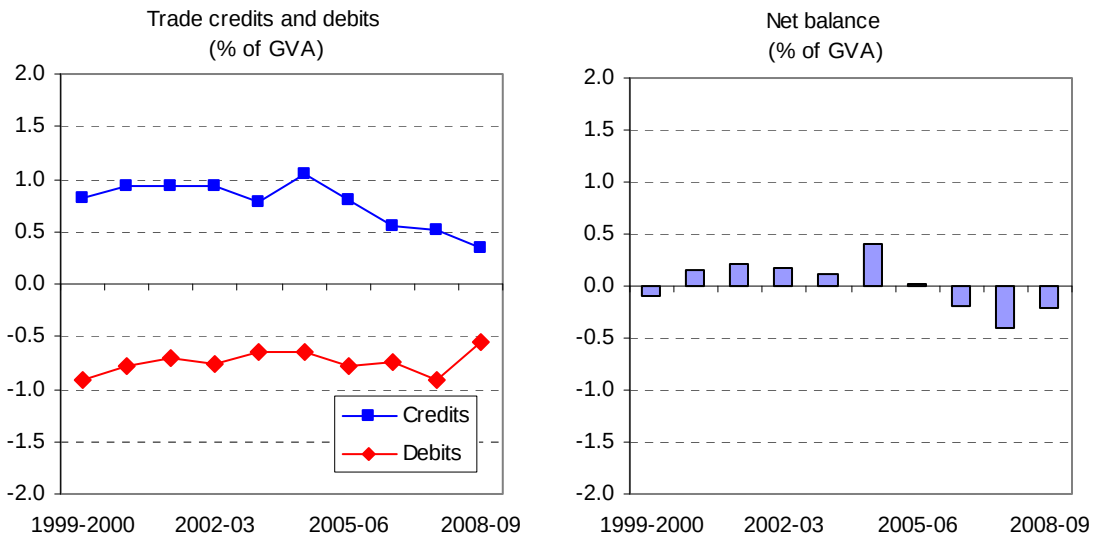
Moreover, a number of clusters[2] of financial services activities have developed in Melbourne. The MFSS survey pointed to clusters in funds management, management of financial institutions, and research and education services (MFSS 2007, p. 3). The role of clusters is discussed in chapter 5.

2.2.5 Trade in financial services

The report *Australia as a Financial Centre: Building on Our Strengths* found that Australia's exports and imports of financial services relative to the size of the financial sector are low by international standards (AFCF 2009, p. 11). The AFCF identified boosting Australia's trade in financial services as a major opportunity, and has made a number of recommendations aimed at removing regulatory and taxation impediments.

The trade performance of Victoria's financial services sector is consistent with the national picture. Exports of financial services from Victoria to overseas destinations represented a minor share of industry output in 2008-09 (less than half a per cent) and this share has declined in recent years (figure 2.6).

Figure 2.6 **International trade in financial services, Victoria and overseas[a]**



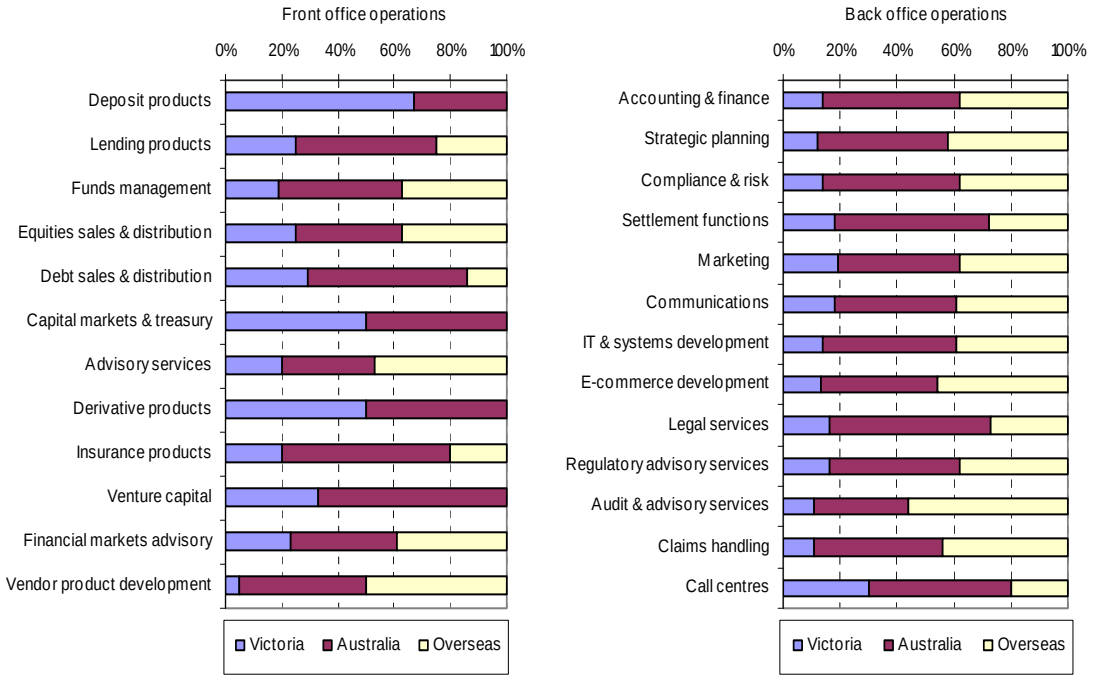
[a] Financial services in this figure includes the balance of payment categories of 'financial services' and 'insurance and pension services'. The ABS classifies credits by the state of provision and debits by the state of consumption. Current price data.

Sources: ABS 2009c, 2009e.

[2] A cluster is a geographically proximate group of interconnected companies and associated institutions in a particular field, linked by commonalities and complementarities (Porter 2000, p. 15).

While overseas exports are generally low, many Victorian financial services businesses sell services interstate. This is most common among back office functions but some businesses also sell front office functions interstate (figure 2.7).

Figure 2.7 **Geographic scope of operations, Melbourne offices, financial services businesses, 2007[a]**



[a] Respondents to the MFSS survey reported that the Melbourne offices of financial services businesses have an Australian focus across a range of front and back office operations.

Source: MFSS 2007.

2.3 Characteristics of major segments of the industry

Key industry segments of the financial services sector in Victoria include:

- banking and finance
- insurance
- funds management
- financial planning and stockbroking
- venture capital
- support services

- financial education and research.[3]

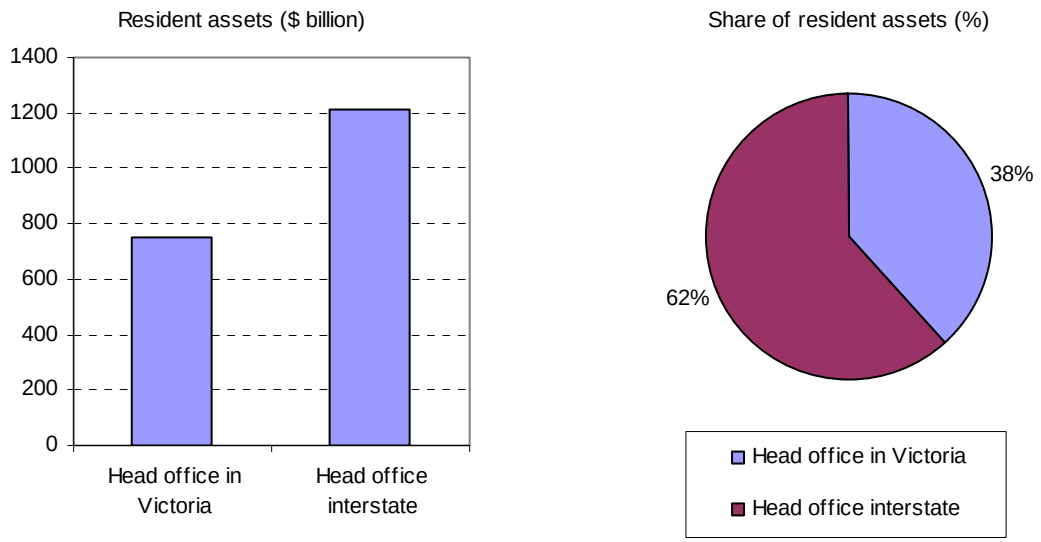
Another feature of Victoria's financial services sector is that a number of state-owned entities are involved in areas such as financing, insurance and funds management. The Victorian Government is also a significant purchaser of financial services, directly and indirectly (where financial services are one element of a larger service).

2.3.1 Banking and finance

Banks, building societies, credit unions and other financiers accounted for more than 40 per cent of total employment in Victoria's financial services sector in 2006 (figure 2.4).

Banks provide a wide range of deposit-taking, lending, wealth management and business banking services. There were around 40 banks in Victoria in 2007 (table 2.1). The head offices of the National Australia Bank and the Australia and New Zealand Banking Group are located in Victoria. The Bendigo and Adelaide Bank has its headquarters in regional Victoria. Banks with head offices in Victoria accounted for about 38 per cent of the resident assets held by the top ten banks in Australia (figure 2.8).

Figure 2.8 **Top ten banks by assets, location of head office, Australia, 30 June 2009[a]**



[a] The top ten banks (by assets) account for 84 per cent of total resident assets of banks in Australia.

Source: VCEC analysis based on APRA 2009a.

[3] While these are the key industry segments, they do not necessarily encompass the entire sector under the inquiry's terms of reference.

There were around 1400 bank branches at 30 June 2009 (table 2.2). Banks operating in Victoria also had about 25 000 electronic points of presence, reflecting the impact of advances in information and communication technology.

Table 2.2 Points of presence: Banks, credit unions and building societies, Victoria, 30 June 2009

Industry	*Face-to-face*		*Non face-to-face*		*Total*
	Branch	*Other*[a]	*Electronic*[b]	*Other*	
Banks	1374	512	24 939	613	27 438
Credit unions	143	690	123	5	961
Building societies	8	2	16	..	26

[a] Includes Bank@Post outlets. [b] Comprises ATMs, EFTPOS and RediPOS, Credit Authorised Transfer (CAT), CAT with Merchant Data CAPture (CAT/CAP).

Source: APRA 2009b.

There were about 50 credit unions and several building societies in Victoria in 2007 (table 2.1). They employed around 1200 people in 2006. These intermediaries offer products or services such as deposit-taking, residential mortgages, credit cards, savings accounts and cash management trusts. Credit unions have a much greater presence than building societies in Victoria (table 2.2).

There is a large number of other deposit-taking and finance businesses in Victoria. Non-bank mortgage lenders (which, unlike banks, fund loans from the capital market rather than depositors) experienced rapid growth in recent years until the global financial crisis. Some of these businesses have been purchased by larger banks (section 2.4).

State-owned finance entities

Treasury Corporation of Victoria (TCV) (box 2.1) and Rural Finance Corporation (box 2.2) are state-owned finance entities.

Box 2.1 Treasury Corporation of Victoria

Treasury Corporation of Victoria (TCV) was established in 1993 under the *Treasury Corporation of Victoria Act 1992* as the central funding authority and financing adviser for the state, statutory authorities, government business enterprises and agencies. At 30 June 2009 TCV served 86 participating authorities in addition to the budget sector (government departments and agencies). The services provided include:

- loan facilities
- deposit facilities
- interest rate, foreign exchange and commodity risk management tools
- treasury management
- general treasury advice and outsourcing
- economic advice.

TCV's borrowings and derivative transactions and its loans to participating authorities are guaranteed by the State of Victoria.

TCV is managed by a Board, with the Treasurer as sole shareholder. Its activities are monitored, supervised and reported through the Department of Treasury and Finance, the Prudential Supervisor, the Prudential Auditor, the Auditor-General and the Minister for Finance.

Source: TCV 2009.

Box 2.2 Rural Finance Corporation

Rural Finance Corporation, based in Bendigo, is a specialist rural lender to primary producers and rural businesses. It has operated since 1958. Its objectives under the *Rural Finance Act 1988* (Vic) are to:

- promote the establishment, growth and stability of, and increased opportunities in, rural industries in Victoria
- promote economic growth in regional Victoria
- provide financial and other services for rural industries in accordance with the Act in a profitable, efficient and competitive manner and, if appropriate, in cooperation with other financial institutions.

Rural Finance Corporation has built a loan portfolio in excess of $1.4 billion, lent to farmers and rural businesses in Victoria, southern New South Wales and eastern South Australia.

It also administers schemes on behalf of the Commonwealth and Victorian Governments: including 2009 Bushfire assistance, exceptional circumstances interest subsidy support and industry restructuring or support programs.

Source: RFC 2009.

2.3.2 Insurance

There were around 500 insurance businesses in Victoria in 2007 (table 2.1). For example, the Asia Pacific headquarters of AXA is based in Melbourne. General insurers comprise the bulk of businesses and are the major employers in the insurance industry in Victoria. These businesses insure, for instance, motor vehicles, home and contents, and business and professional risks.

In addition, there were about 60 life insurers (which offer insurance and investment policies)[4] and around 30 health insurers in Victoria. Victoria is home to Australia's largest private health insurer, Medibank Private.

State-owned insurance entities

There are several state-owned insurance entities — including WorkSafe Victoria, the Transport Accident Commission (TAC) and the Victorian Managed Insurance Authority (VMIA) — which comprise a small proportion of employment in the insurance industry in Victoria.

- WorkSafe Victoria provides workplace injury insurance to companies, partnerships and sole traders that employ workers or contractors that meet certain criteria.
- TAC funds medical treatment for transport accident-related injuries. The *Transport Accident Act 1986* (Vic) sets out what can be funded and any conditions that may apply. TAC's investment portfolio is managed by the Victorian Funds Management Corporation (VFMC).
- VMIA provides insurance and risk services to groups in the 'general government and public health care sectors, including departments, statutory authorities, agencies, infrastructure, rail operations, hospitals, health centres, community service organisations, medical research bodies, tertiary institutions, cemetery trusts, national parks, galleries, museums and event bodies' (VMIA nd).

2.3.3 Funds management

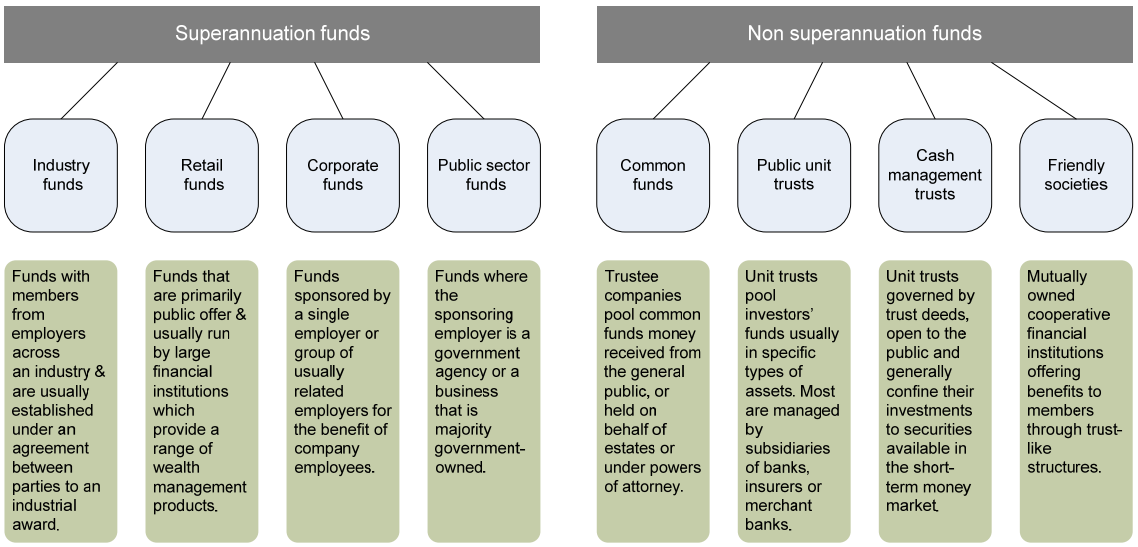
Fund managers invest, manage and monitor client assets. Victoria has become a significant location for the funds management industry in Australia, particularly for industry superannuation funds.

Recent surveys have reported strong growth in Melbourne's funds management sector over the past decade or so. According to the Osborne Group, there were at least 120 national and international funds management players with Melbourne

[4] Insurance policies include payment of a sum of money on the death of the insured or on the insured receiving a permanent disability. Investment products include, for example, annuities and superannuation plans.

operations in 2007 — a doubling of their presence since 1990 (MFSS 2007, p. 16).[5] Managed funds operate within and outside the superannuation environment (figure 2.9).

Figure 2.9 **Types of managed funds**[a]



[a] Definitions abbreviated from Australian Prudential Regulation Authority (APRA) and Reserve Bank of Australia (RBA) sources. The figure does not show small funds such as small APRA funds, single-member approved deposit funds and self-managed funds.

Sources: VCEC analysis based on APRA 2005 and RBA 2010.

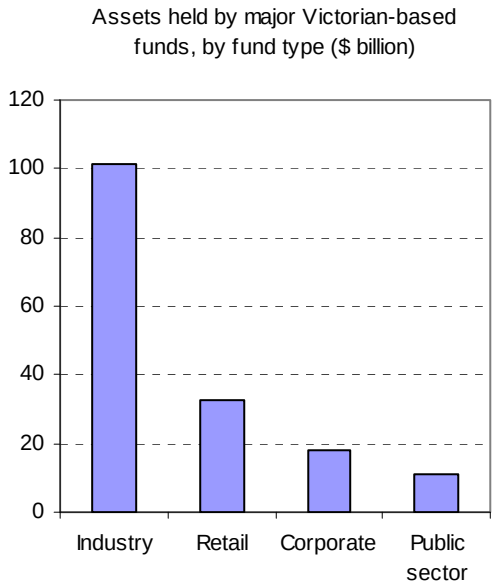
Superannuation funds

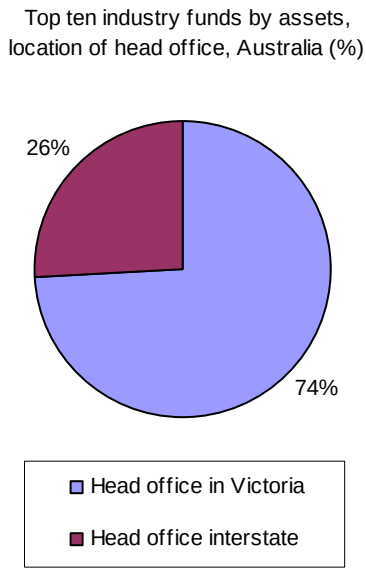
Victoria is a key centre for industry funds in Australia. Seven of Australia's top ten industry funds by assets are based in the state. These Victorian-based funds managed around $100 billion in 2008, representing around three-quarters of the total assets managed by the top ten industry funds in Australia (figure 2.10). These funds include, for example, Australian Super, Construction and Building Unions Superannuation (CBUS) and Health Employees Superannuation Trust Australia (HESTA).

The concentration of industry funds in Victoria stems from the location of labour, employer and industry organisations in the state. The concept of industry funds was developed in the mid 1980s, reportedly driven by union organisations to establish broad based multi-employer funds to cater for the needs of Australian workers, and linked to industrial awards and agreements. A range of agreements with employer associations formed a series of trustee boards for the governance of the funds (ISF nd, p. 1).

[5] National and international fund managers with a presence in Victoria include, for example, AXA Asia Pacific, BlackRock Investment Management, Goldman Sachs JB Were Asset Management, Invesco, IOOF & Perennial Funds Management, Legg Mason, and Vanguard (MFSS 2007, p. 16).

Figure 2.10 **Superannuation funds, Victoria, 30 June 2008[a]**





[a] Major Victorian-based funds are those ranked in the top ten funds by assets for each fund type in Australia.

Source: VCEC analysis based on APRA 2009f.

Initial estimates indicate that major Victorian-based public sector and retail funds manage relatively small proportions of total assets in those fund types nationally (table 2.3).

Table 2.3 **Superannuation funds, Australia, 30 June 2009**

Fund type	*Entities*	*Assets*
	no.	$ billion
Industry	68	191.1
Retail	165	306.0
Corporate	190	54.8
Public sector	40	151.6
Self-managed	411 688	336.1
Other[a]	4471	72.4
Total	416 622	1112.0[b]

[a] Pooled superannuation trusts, small APRA funds and single-member approved deposit funds. [b] Sum of components in this table. In Commonwealth of Australia (2009d), the total reported ($1080.5 billion) is based on the APRA definition.

Source: Commonwealth of Australia 2009d.

Victoria's major public sector superannuation schemes — including the Emergency Services Superannuation Scheme and the former State Superannuation Fund — are managed by ESSSuper.

Non-superannuation funds

Many fund managers with operations in Victoria also offer managed investment products outside of the superannuation environment. For example, firms such as AXA Asia Pacific and Invesco offer a range of wholesale and retail funds. In addition, the MFSS survey reported the presence of specialised and boutique fund managers in Melbourne (MFSS 2007, p. 18).

Victoria is also home to some common funds, such as those managed by State Trustees Limited and the Senior Master's (Funds in Court) Office (SMO).

- State Trustees Limited provides financial services to clients who are unable to manage their affairs themselves, under a community service obligation (CSO) agreement (manages $735 million for 9000 people with a CSO worth $15.4 million) (State Trustees Limited 2009, p. 43). It also provides commercial services (box 2.3).
- The SMO administers funds paid into the court as a result of a court order, or under legislation providing for the receipt of such funds (box 2.4). The SMO held around $1 billion on behalf of beneficiaries at 30 June 2009.

Box 2.3 State Trustees Limited

State Trustees Limited has operated since 1939 and became a State owned company in 1994 under the *State Trustees (State Owned Company) Act 1994* (Vic). The State Trustee's Board is responsible for managing its affairs, and reports to the Treasurer.

State Trustees Limited provides financial services to clients who, due to mental illness, injury, disability or other circumstances, are unable to manage their affairs themselves. This can include preparing and reviewing financial plans and budgets, managing real estate and other assets, collecting income and entitlements, managing liabilities, attending to taxation matters, investing funds and managing legal and associated matters. The Government pays State Trustees Limited to provide these services conditional on achieving certain performance standards stipulated in a five year community service obligation agreement.

State Trustees Limited also provides commercial services including:

- trustee services for government and individuals
- specialised legal, financial and tax services (including will making, financial planning and managing compensation funds)
- funds management services and investment products.

At 30 June 2009, total assets under management and trusteeship were $1.6 billion.

Source: State Trustees Limited 2009.

Box 2.4 Senior Master's (Funds in Court) Office

The Senior Master's (Funds in Court) Office (SMO) is an administrative division of the Supreme Court that administers funds paid into the court as a result of a court order, or under legislation providing for the receipt of such funds.

Sections 113, 113A and 113B of the *Supreme Court Act 1986* (Vic) and Orders 15, 77 and 79 of the Supreme Court (General Civil Procedure) Rules 2005 provide the framework for the Senior Master. Funds are pooled in Common Funds:

- Common Fund No. 1 (CF-1) holds funds for beneficiaries who are not entitled currently to those funds: money held in dispute matters, money held as security for costs and other payments made under legislation.
- Common Fund No. 2 (CF-2) and Common Fund No. 3 (CF-3) hold funds on behalf of beneficiaries who are entitled to those funds, but are under a 'legal' disability: damages and payments awarded to people deemed incapable of managing their own affairs due to disability, dependent minors and minors having sustained personal injury with entitlement to payment out at age 18 (SMO 2009b).

In addition, the Common Funds Guarantee and Reserve Account (CF-GR) acts as a prudential safeguard for the investments of the Common Funds (being the statutory reserve of 1 per cent of their combined value) and is also used for the SMO's operational expenses.

Interest from investments in CF-2 is paid on 1 June each year, according to a rate of return set by the Senior Master (with approval of the Chief Justice).

Income from investments on CF-3, if made, is distributed each month, and net capital gains are distributed at the end of the year.

The Rules of Court provide that money held cannot be paid out except by order of the Court (Order 79.02 (2)): such orders are usually made by the Senior Master.

The SMO held around $1 billion on behalf of beneficiaries at 30 June 2009.

Sources: SMO 2009a, 2009b, nd(a), nd(b).

Sovereign funds

Victoria is the base for the Commonwealth Government's Future Fund (box 2.5) and the VFMC. The VFMC provides investment and funds management services to Victorian public authorities (box 2.6). These funds managed more than $100 billion in 2009.

Box 2.5 The Future Fund and Nation-building Funds

The Future Fund Board of Guardians, supported by the Future Fund Management Agency, invests the assets of the Future Fund and three Nation-building Funds (the Building Australia Fund, the Education Investment Fund and the Health and Hospitals Fund).

The Future Fund is a financial asset fund established by the *Future Fund Act 2006* (Cth). Its purpose is to meet unfunded superannuation liabilities that will become payable during a period when an ageing population is likely to place significant pressure on Commonwealth finances.

The Nation-building Funds were established in 2009 to meet the Commonwealth Government's commitment to investment in critical areas of infrastructure such as transport, communications, energy, water, education, research and health.

The Future Fund's assets were about $61 billion and the balance in the Nation-building Funds was about $21 billion at 30 June 2009.

Source: Future Fund 2009.

Box 2.6 Victorian Funds Management Corporation

The Victorian Funds Management Corporation (VFMC) was established under the *Victorian Funds Management Corporation Act 1994* (Vic). It manages the majority of the state's assets available to it under the Act and is subject to the general direction and control of the Treasurer of Victoria.

At 31 December 2009, VFMC managed investments of $35 billion for 14 Victorian public sector and related organisations:

- $17 billion for insurance funds (Victorian WorkCover Authority, Transport Accident Commission, Victorian Managed Insurance Authority)
- $16.2 billion for superannuation funds (ESSSuper Emergency Services and State Superannuation Scheme and Parliamentary Trustee)
- $1.8 billion for other public sector and not-for-profit institutions including hospitals and universities.

The VFMC operates under a 'centralised model' where its clients set investment objectives and the VFMC manages the rest of the investment process.

The VFMC has sought to take a 'leadership role' in environmental, social and corporate governance. In June 2007, it signed and implemented initiatives under the UN Principles for Responsible Investment.

Sources: VFMC 2009, nd(a), nd(b), nd(c).

2.3.4 Financial planning and stockbroking

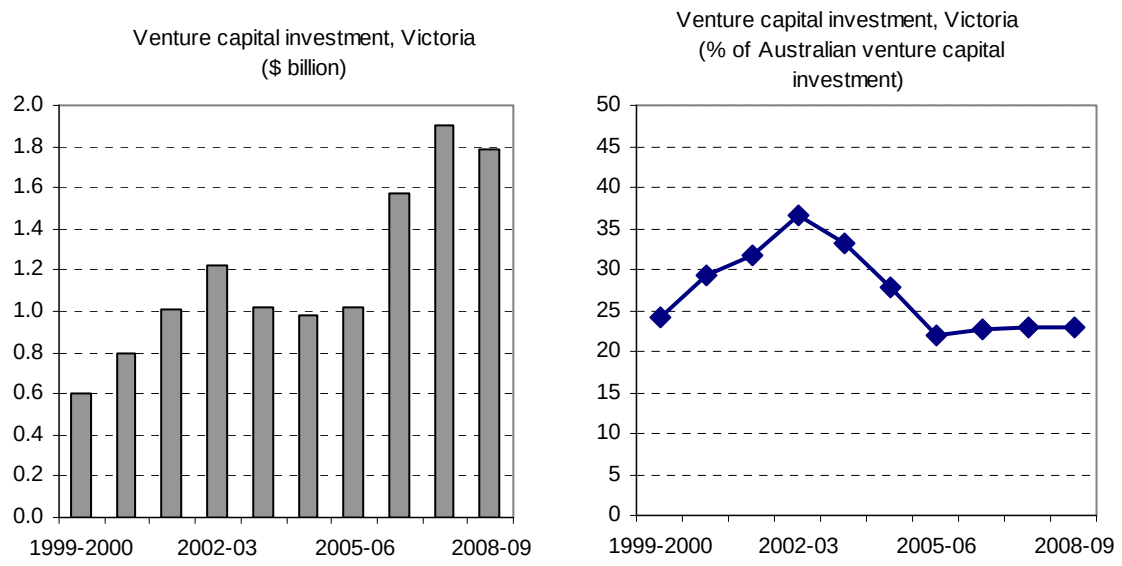
Employment in support services to the financial services sector (which includes financial planners and consultants) increased significantly in the ten years to 2006 (figure 2.4). Financial planning services can be offered through banks, building societies, credit unions, life insurance companies, stockbrokers, dealer groups, trustee companies, independent financial planning firms, fund managers, accountants and solicitors (Finsia 2009a).

There were around 1300 financial asset broking businesses in Victoria in 2007, which includes stockbroking firms and mortgage brokers (table 2.1). Victoria is home to a number of major stockbroking firms. Stockbrokers provide advice and transactional services for people buying and selling securities in listed markets such as the Australian Securities Exchange (ASX) (Finsia 2009a). The headquarters of Australia's stock and futures exchanges are located interstate.

2.3.5 Venture capital

The venture capital sector finances new innovative businesses. Victoria is one of Australia's major destinations for venture capital, with the stock of investments estimated at around $1.8 billion in 2008-09 or 23 per cent of Australia's total (figure 2.11).

Figure 2.11 **Venture capital investment, Victoria[a]**



[a] Investments in investee companies with head offices in Victoria.

Source: ABS 2010.

Venture capital firms located in Victoria include, for example, Starfish Ventures and GBS Venture Partners (Victorian Government 2009, p. 15).

2.3.6 Support services

There are also firms located in Victoria that supply support services. Some examples include Aviva, Computershare, Equity Trustees, Frontier Investment Consulting, Industry Fund Services, Mercer, NAB Custodians, Northern Trust, RiskMetrics Group and Standard & Poors (Victorian Government 2009, p. 12).

The significant growth in support services employment (figure 2.4) may reflect in part a trend to outsourcing services. Industry superannuation funds, for instance, have unbundled components of superannuation services such as administration, investment advice, funds management and insurance (IFS nd, p. 1). The MFSS survey reported that, between 1999 and 2007, there had been marked changes in outsourcing and innovative services which could be driving an increasing role for consultants and vendors to the financial services sector (MFSS 2007, p. 8).

2.3.7 Financial education and research

A significant number of vocational education and training (VET) and higher education institutions in Victoria provide courses for the financial services industry. These institutions train new entrants to the industry and existing financial services workers.

Business and finance courses are offered by VET institutions such as Box Hill, Chisholm and Homesglen Tertiary and Further Education (TAFE) institutes. Victorian universities that provide courses in banking and finance include Deakin University, La Trobe University, Monash University, RMIT University, Swinburne University of Technology, University of Ballarat, University of Melbourne and Victoria University.

The state is also home to the Melbourne Centre for Financial Studies and the Melbourne APEC Finance Centre:

- The Melbourne Centre for Financial Studies was launched in 2005 with seed funding from the Victorian Government. Members of the consortium are Melbourne, Monash and RMIT universities, and the Financial Services Institute of Australasia (Finsia). Its mission is to build linkages among academics, practitioners and government to enhance finance research, practice and education and the reputation of Melbourne's financial institutions and universities and of Melbourne as a financial centre (MCFS 2008).
- The Melbourne APEC Finance Centre's mission is to harness the knowledge and skills vested in Victoria's human capital to provide training programs,

convene symposiums and undertake research to position Victoria as a regional centre of excellence in financial services and education (MAFC 2009a).

The role of educational institutions is discussed further in chapters 5 and 6.

2.4 Trends in the sector

The scope and structure of the financial services sector evolves as there are changes in economic activity, developments in financial products and changes in community needs and expectations. Financial services activities are affected by state, national and international influences. Some of the factors that are expected to affect service provision and the structure of the industry nationally are:

- population shifts and the ageing population
- changes in business activity due to factors such as possible policy responses to climate change
- national and international developments in financial services regulation
- changes in the approach to risk and cost management, including as a result of the global financial crisis.

These influences are already seeing changes in the financial services sector. They are leading to shifts in the mix of products and service providers, such as increases in funds management and retirement products, and the emergence of different types of financial institutions relying on securitised products. According to De Belle (2009), the growth of securitisation, in large part, reflected the change in the composition of lenders in the mortgage market following the entry of mortgage originators, who relied predominantly on securitisation for funding.

In addition, other trends, such as consolidation and convergence have arisen due to influences such as the focus on cost reduction. Convergence has been a longer-term trend, with the traditional boundaries between financial institutions breaking down. For example, banks have expanded into providing insurance, financial advice and asset management services. And insurance companies have been providing superannuation products.

Several inquiry participants reported that some segments of the financial services sector have been consolidating. Key indicators of this trend are the number and the average size of financial enterprises. For example, in 2008, in the banking sector, two of Australia's major banks absorbed two smaller banks, and major banks have purchased securitisation businesses.

The offshoring of financial services jobs was also raised in consultations. Some banks have offshored selected activities, highlighting the importance of cost competitiveness to a range of back office operations. In a recent Senate inquiry

into bank mergers, it was reported that the offshoring by Victorian-based banks has mainly been in back office activities such as accounts processing, information technology and software development (SERC 2009, pp. 66–67).

Information request: What is the extent of offshoring in the financial services sector in Victoria? Which parts of the sector and which activities have been affected by offshoring?

Although the number of self-managed superannuation funds has been increasing since the mid 1990s, there has been significant consolidation in other major fund types (that is, corporate, industry, public sector and retail funds) (APRA 2010). The number of these funds has declined significantly and the average fund size has increased markedly (table 2.4). Analysis until 2025 by Commonwealth Treasury — for the *Review into the Governance, Efficiency, Structure and Operation of Australia's superannuation system* (the Cooper review) — projects continued consolidation.

Table 2.4 Consolidation trends in the superannuation industry, Australia

	1996	*2009*	*2025*[a]
Overall industry scale ($ billion)[b]	245	1100	3200
Funds (number)[c]	4734	447	119
Average fund size ($ billion)[b]	0.04	1.5	17.2
Superannuation assets (% of GDP)[b]	47	90	120

[a] Projection. [b] Nominal terms. [c] Fund types include corporate, industry, public sector and retail funds.

Source: Commonwealth of Australia 2009c.

The global financial crisis has had a significant impact on these trends — reinforcing some, as financial pressure has lead to further consolidation, and counteracting others, for example there has been a collapse in the securitisation market.

2.5 Summing up

There is potentially a strong base on which to grow Victoria's financial services industry. There are already some major segments such as banking, insurance, funds management, and support services. Many financial services businesses are located in close proximity to each other in metropolitan Melbourne. In particular, there is a significant cluster of businesses in the funds management industry.

In addition, the financial education sector is large and there are research bodies charged with raising the sector's profile.

An understanding of the existing industry structure and the dynamics of change is an essential starting point for considering recommendations that would enhance the development of Victoria's financial services sector, as growth is often best built by combining existing strengths with new opportunities, while providing a policy environment that does not inhibit 'blue sky' opportunities.

The limited involvement in offshore financial transactions — a point emphasised in the AFCF review and in its recommendations in relation to the Australian financial sector as a whole — is also evident.

Such growth can also be accompanied by increases in high value employment — not only directly — but also in supplying the services that support a growing industry or in new businesses attracted by growing clusters and new opportunities.

3 Drivers of investment and location

3.1 Introduction

Chapter 2 outlines the current scope and structure of Victoria's financial services sector. The next question for this inquiry is, given the current scope of the industry, what are the areas in which there is potential for growth and which factors might influence that growth.

This chapter, therefore, provides an overview of potential growth opportunities for financial services in Australia, as a whole, and for Victoria, in particular, identified by submissions, discussions with interested parties and other inquiries. It then examines the factors, affecting the investment and location decisions of firms (including foreign firms) in the financial services sector. The chapter considers the drivers of investment and location which can be influenced by state government policy, and relates them to the areas of strength in Victoria's financial services sector.

3.2 Growth prospects and opportunities

During the course of the inquiry, and other related inquires and research, many industry participants have expressed views on the likely growth areas of the financial services sector in Victoria and on potential opportunities for the sector. This section summarises those views, and provides the Victorian Competition and Efficiency Commission's (the Commission's) preliminary conclusions on the matter.

3.2.1 Industry perceptions of growth prospects

As part of the Melbourne Financial Services Survey (MFSS) of executives in the Melbourne financial sector conducted in 2007, respondents were asked to indicate their perceptions of the growth prospects for the industry segment they were in and for other segments about which they felt able to express an opinion. Table 3.1 reports, for each industry segment, the proportions of respondents who considered growth prospects were weak or strong in five years from 2007.

Table 3.1 **Growth prospects, financial services, Melbourne**

Industry segment	*Weak*	*Strong*	*Difference*
	(%)	(%)	(%)
Banking retail	62	38	-24
Banking commercial	8	92	84
Banking wholesale	20	80	60
Investment banks — capital markets & treasury	46	54	12
Investment banks — corporate finance & advisory	0	100	100
Stockbroking	63	37	-26
Life insurance	69	31	-38
General insurance	67	33	-34
Wholesale funds management	0	100	100
Retail funds management & superannuation funds, friendly & building societies & credit unions	8	92	84
Venture capital firms	38	62	24
Financial planning & advisory firms	10	90	80
Industry associations & tertiary education	67	33	-34

a A positive number indicates that a majority of respondents considered the industry segment's growth prospects are strong. A negative number indicates that a majority of respondents considered the industry segment's growth prospects are weak.

Source: MFSS 2007.

The industry segments that a majority of respondents considered had strong growth prospects for Melbourne include:

- funds management
- financial planning and advisory firms
- commercial banking
- investment banks.

On the other hand, respondents saw few, if any, growth prospects in Melbourne for:

- retail banking
- stockbroking
- general and life insurance.

3.2.2 Inquiry participant's views on potential opportunities

In submissions and consultations, inquiry participants raised a number of potential opportunities to grow the financial services sector in Victoria. These suggestions are summarised in table 3.2.

Table 3.2 **Potential opportunities raised by participants**

Potential opportunity	*Participant comment*
Islamic finance products & services	Large potential markets in Asia Pacific region and beyond.
Public private partnerships (PPPs)	Significant expertise in PPPs in Victoria. Potential to grow the industry in Victoria and export services to Asia Pacific.
Environmental markets & trading	Victoria is a leader in developing environmental markets (e.g. water, native vegetation). Carbon Pollution Reduction Scheme being considered in Australia. Significant expertise in electricity trading in Victoria.
Hedging & forward markets	Victoria has a significant manufacturing industry, which exports overseas. Possible need for hedging expertise and services.
Retirement finance & income products	Victoria/Australia has expertise in developing retirement finance and income products such as annuities, reverse mortgages etc. Increasing demand for such products due to an ageing population.
Data warehousing & back up facilities	Victoria has a reliable electricity system. Expertise in ICT. Pool of skilled labour.
E-payment systems and online markets	Low cost transaction systems. Burgeoning take-up of such systems (e.g. PayPal, Prosper etc.).
Reduce barriers to exports & investment	Address barriers to exports and investment in other countries. Scope for mutual recognition agreements and trade agreements.
Focus on 'middle' office operations	Build up expertise in middle office operations (accountants, lawyers, valuation analysts). This emphasis on professional skills has implications for the type of education services being demanded by those in the financial services sector.
Centre of excellence	Research centre with high calibre staff and reputation to attract students and researchers. Develop closer links between academics and industry.
Investment in infrastructure	Potential to grow the proportion of superannuation funds invested in infrastructure projects.
Commonwealth taxation reform	Scope to reform Commonwealth taxes, particularly withholding tax.
State taxation reform	Scope to reduce or remove state-based specific transactions taxes on insurance products.

Source: Submissions and consultations.

3.2.3 Other views on potential opportunities

A number of parties who recently made submissions to other inquiries, including to the inquiry conducted by the Australian Financial Centre Forum (AFCF) Reference Group (2009), suggested potential opportunities in the sector. A cross-section of the views received by the AFCF are presented in box 3.1. The AFCF received many similar suggestions to those put by participants in the Commission's inquiry. But, given the AFCF's national focus, many of the opportunities identified by review participants focused on increasing exports of financial services to Asia, in particular, but also more widely.

Box 3.1 Examples of opportunities identified by participants in the AFCF inquiry

The Financial Planning Association of Australia:

> Financial planning in many markets is newly emerging and there is significant capacity to increase exports. There is significant demand for Intellectual Property in the relevant markets, and in particular Asia Pacific, that require assistance to develop. (FPA 2008, p. 1)

The Institute of Chartered Accountants in Australia noted that:

> The introduction of a Carbon Emissions Trading Scheme provides Australia with the opportunity to establish itself as the carbon trading hub of the Asia region. (ICAA 2008, p. 2)

The Insurance Council of Australia noted the scope to exploit insurance opportunities around the world:

> While the developing economies of Asia are a natural focus of attention because of their proximity to Australia, general insurers are interested in exploring opportunities around the globe. (ICA 2009, pp. 1–2)

The Responsible Investment Association of Australia suggested that Australia is uniquely positioned to benefit from global interest in responsible investment:

> Building Australia's skill base around responsible investment competencies has the capacity to create significant opportunities for Australian investment managers in coming years. … Australia's growing expertise in responsible investment will also create an opportunity for Australia to be a gateway through which European and US pension funds invest into Asia. (RIAA 2008, p. 1)

Sources: FPA 2008; ICAA 2008; ICA 2009; RIAA 2008.

In short, participants in this inquiry and other recent relevant inquiries appear to have a positive outlook for the growth of the financial services sector in Australia and have identified a range of potential opportunities.

3.2.4 The Commission's view

While the Commission has not yet reached its final conclusions regarding the areas of comparative advantage of the financial services sector in Victoria, the Commission considers they may include:

- The industry superannuation funds that provide services to their members around Australia. The bulk (measured both by number and by total funds under administration) of these funds are based in Melbourne. Collectively, they may be a critical and growing mass of capital. This depends on several factors, including the response to the Review into the Governance, Efficiency, Structure and Operation of Australia's Superannuation System (Cooper review).
- Some large scale public sector funds managers domiciled in Melbourne, in particular the Future Fund and the Victorian Funds Management Corporation. A key challenge is whether there are economies of scale in these operations that, without compromising their fundamental objectives, may foster growth in locally domiciled financial services. This is a matter for both the Commonwealth and Victorian Governments.
- The capacity to define, manage and deliver major infrastructure projects, especially PPP projects. This stream of projects has fostered a cluster of project partners comprising construction companies, financiers and ongoing managers, together with an acknowledged capability within the Victorian Government to define and deliver PPP projects. The main implications for the Victorian Government may be in its operations, as discussed in chapter 5.
- Intermediaries whose business has identified specific segments of consumers not adequately served by existing intermediaries. Examples include the ME Bank and the Bendigo and Adelaide Bank, which has developed a network of franchised local banks. Other banks are also moving into the provision of Islamic banking products.

The Commission also considers there may be a number of areas of the financial services sector currently domiciled in Victoria that may be under competitive threat:

- Businesses that compete on cost alone. These businesses, typically those that provide transactional services to the financial sector, are vulnerable to low cost competitors overseas, major fluctuations in exchange rates and to major shifts in enabling technology. For example, some financial intermediaries have outsourced some back office functions to sophisticated offshore locations such as India
- Businesses that do not have a strong customer base in Victoria, including Victorian customers with a domestic and/or overseas focus.

3.3 Drivers of investment and location decisions in the financial services sector

The terms of reference for the inquiry direct the Commission to examine factors affecting the 'attraction of foreign business'. However, attraction and retention matters affect domestic and foreign businesses and will affect the extent to which any financial centre in Victoria attracts and retains service providers. Consequently, the Commission has taken a broad view of the factors affecting location and investment decisions of firms in the financial services sector.

The Commission's discussions with stakeholders have highlighted four factors that are likely to increase the opportunities for businesses nationally to invest further in providing financial services:

(1) economic growth and a growing population
(2) demographic change and changes in government policy
(3) Australia being used as a base for exporting services to other countries
(4) changes in the approach to risk and cost management, including as a result of the global financial crisis.

Financial services are an integral part of the supply of so many other goods and services that general economic growth will generate financial sector growth and affect the location decisions of businesses.

Economic growth and population growth lead to an increase in the number of transactions and, hence, directly to an increased demand for financial services. While demographic change — such as the ageing of the population — and changes in government policy lead to a change in the types of services demanded. For example, an ageing population may increase demand for funds management and superannuation services.

Whether businesses that are expanding or moving into Australia to take advantage of these opportunities choose Melbourne as their primary location depends on a range of factors.

In a study for Invest Victoria, consultants IBM Business Consulting — Plant Location International examined the cost and quality of a number of locations (including Melbourne and Victoria) from the perspective of businesses seeking to set up operations in new markets. The study identified broad factors, not specific to the finance sector, pertaining to the quality of a location and the cost of doing business in a location (table 3.3).

Table 3.3 **Broad factors influencing business location**

Quality of a location	*Cost of doing business in a location*
• general business environment	• investment costs
• local potential to recruit staff	• labour costs
• presence of industry	• property costs
• language skills	• utility costs
• human resource regulations	• transport costs
• quality of infrastructure	
• availability of real estate	
• living environment	

Source: Invest Victoria 2004.

In terms of the general factors affecting the location and decision choices of financial services firms, the Melbourne Centre for Financial Studies (MCFS), summarising studies examining factors affecting the location decisions of financial firms, noted that:

> Those studies identified access to sophisticated technology and labor and a 'critical mass' of expertise as crucial. Competitive costs, a well trained labor force, good telecommunications, sensible regulators and tax policies were all relevant, but the 'critical mass of expertise' dominated. (MCFS 2007, p. 10)

The MFSS survey of the financial services sector in Melbourne provides insights into the relative importance of the various factors for different types of firms. For firms with an existing presence in Melbourne the survey indicates that:

> … clustering factors were given the strongest ranking and were seen to be the most important factors influencing the growth and development of Melbourne's financial services sector. …
>
> In addition to a consistently strong recognition for Victoria's tertiary sector, respondents have now acknowledged that financial services training facilities should also be acknowledged. (MFSS 2007, pp. 26–27)

This suggests that firms with current operations in Victoria look to grow and develop areas for which Victoria already has an advantage because of an existing cluster of activities supported by appropriate training and skills availability.

MCFS noted that one implication of the importance of clusters in Victoria is that:

> For Melbourne, this suggests one point of focus should be on further developing a reputation as a centre of excellence and knowledge for the funds management industry (with particular focus on pension fund management). (MCFS 2007, p. 10)

MCFS also noted the importance of being able to access specialist knowledge and skills:

> Increasingly, ability to access specialist knowledge is going to drive the location decisions of financial firms and the growth and development of financial centres. (MCFS 2007, p. 9)

The report of the AFCF Reference Group similarly noted that in attracting foreign firms to Australia:

> Access to a high quality workforce was cited by industry in discussions with the Forum as one of the principal reasons offshore companies base their regional operations in Australia. (AFCF 2009, p. 101)

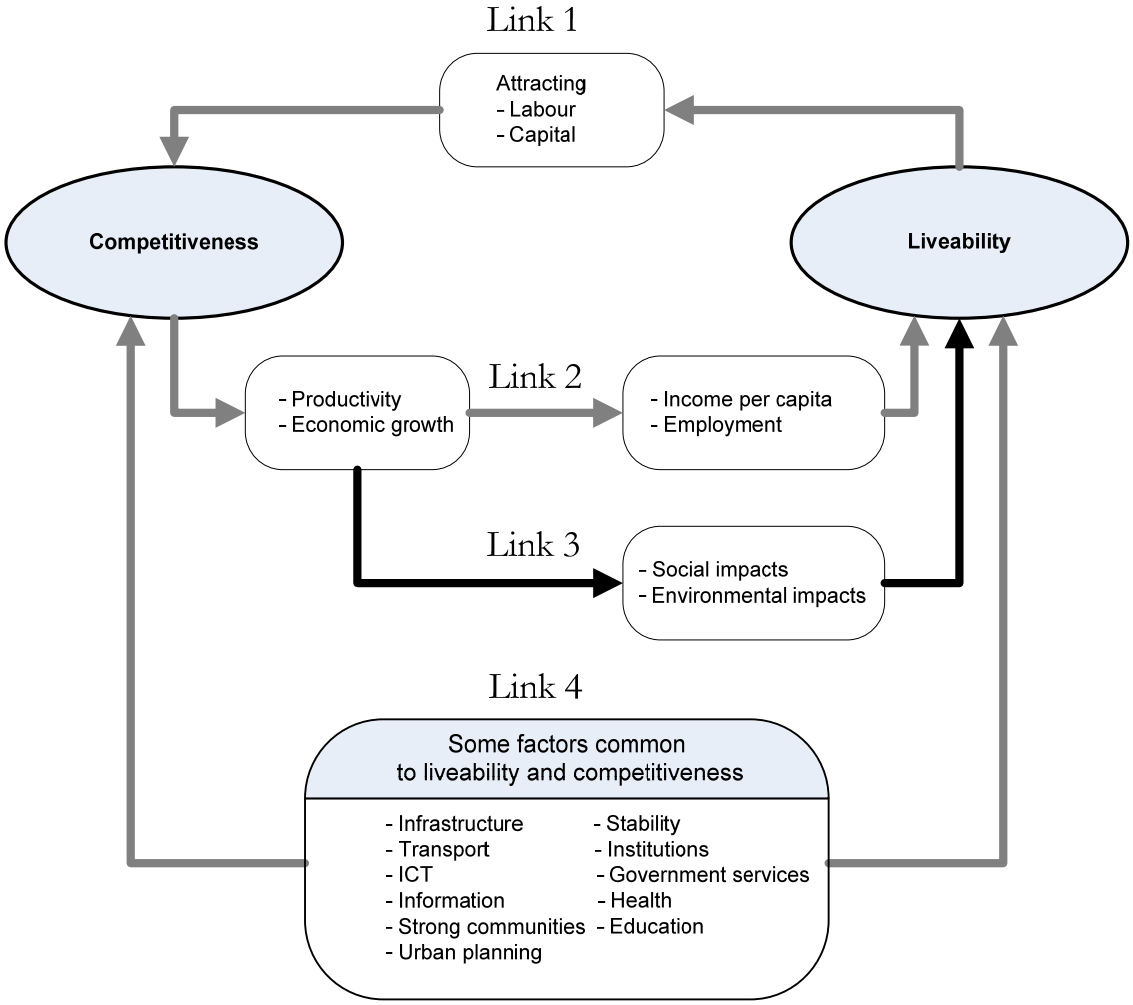
According to the MFSS survey, the other key factor affecting decisions to establish in Melbourne was:

> At a broader level, Melbourne's cost efficiency is now recognised as a major encouragement for interstate and overseas players to establish operations in the City. (MFSS 2007, p. 25)

Liveability and lifestyle factors are often promoted as a way of attracting firms and skilled, innovative people to particular locations. Some recent studies (Florida 2002, 2003) contend that a particular type of innovative worker is important for driving innovation and long-run economic growth and their location decisions are influenced by the liveability of different locations. The implication of this research is that communities might attract this class of labour by, amongst other things, improving liveability.

The Commission has previously examined the links between liveability and industry competitiveness, illustrated in figure 3.1. This analysis is particularly applicable to the financial services sector given the international mobility of its highly skilled workforce.

Figure 3.1 **Thinking about links between liveability and competitiveness**



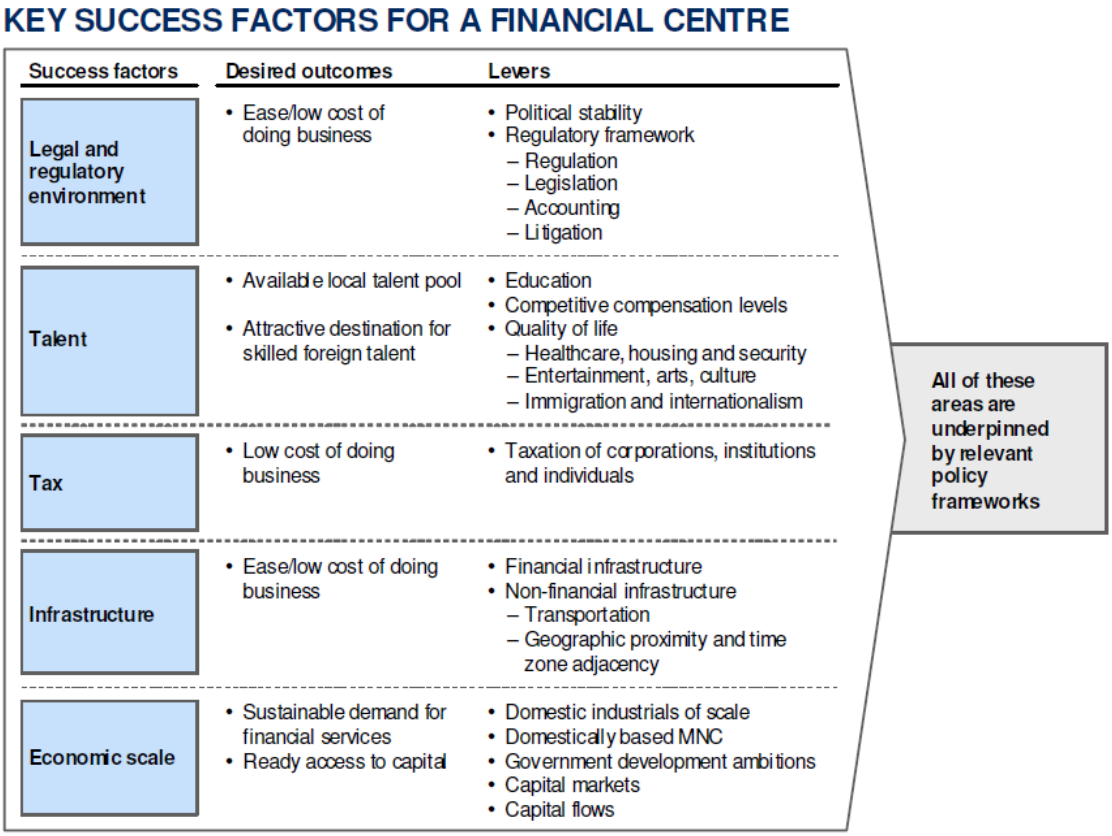
Source: VCEC 2008.

The Commission concluded that:

> It is clear that there are multiple linkages between liveability and competitiveness. A key implication is that policies or actions that improve liveability can have beneficial impacts on competitiveness — a 'win-win' situation for Victorian residents and businesses. (VCEC 2008, p. xxv)

The Australian Bankers' Association (ABA) in its submission to the inquiry (sub. 9) presented the results of analysis undertaken by consultants on the key success factors for a financial centre (figure 3.2). This analysis provides suggestions as to the factors likely to attract and retain financial services firms:

Figure 3.2 **ABA analysis of success factors**



Source: sub. 9, p. 2.

The ABA then applied this model to Australia. The framework has obvious application to locations within Australia (figure 3.3).

Figure 3.3 **Success factors in Australia**

Overview

- The Australia financial services sector's strengths lie in Australia's high quality of life, lower operating costs, strong legal and regulatory system and uncomplicated tax regime. It is undermined by the poor retention of local talent, high level of absolute corporate tax and its isolated geographic position

Background

- Banking and insurance sector revenues are 7.1% of GDP
- In 2007 City of London Corporation's Global Financial Centres Index ranked Sydney 8th globally and Melbourne 18th globally

Business areas

- Australian dollar the sixth most traded currency in the world
- Eighth largest stock exchange in the world (Australian Stock Exchange)
- Fourth largest securities market in Asia behind China, Korea and Japan
- Regional centre for asset management

Success factors

- **Legal and regulatory**
  - Strong legal and regulatory system but certain weaknesses:
    - Overlap between state and federal regulatory regimes
    - Complex system; large number of regulators and government bodies
    - Limited cost-benefit analysis before reforms introduced
  - High political stability
- **Talent**
  - Poor retention of local talent significantly weakens local talent pool
  - Overseas talent attracted by high quality of life with Melbourne and Sydney ranking 2nd and 11th respectively in Economist Intelligence Unit's Liveability Index, but discouraged but geographic isolation and top personal tax rate of 45%
- **Tax**
  - Uncomplicated tax regime (12 tax payments per year / 27th in the world) and relatively low time compliance component (107 hours per year / 23rd in the world)
  - High level of absolute tax rate (50.6% World Bank total tax rate / 122nd in the world) with 30% corporate tax rate
  - Low risk of double taxation with tax treaties with over 50 countries
- **Infrastructure**
  - Efficient and effective clearing and settlement system after introduction of the real time gross settlement system in 1990s
  - Isolated from major global finance centres of New York, London and Tokyo but advantage in being first major centre to open each day
- **Economic scale**
  - 8 Australian companies in Fortune 500 in 2006, another 8 with international headquarters in Australia
  - Reasonable equities markets with low-moderate liquidity
  - 15th largest economy in the world
- **International marketing**
  - Invest Australia has offices in major global cities

Source: Invest Australia; Global Fortune 500 Rankings 2006; City of London Corporation's Global Financial Centres Index; World Bank Paying Taxes 2008; Economist Intelligence Unit's Liveability Index; McKinsey analysis

Source: sub. 9, p. 3.

The Australian Financial Markets Association submission to the AFCF Reference Group suggested that factors similar to those suggested by the ABA were important for a successful financial centre:

> The key elements in a competitive financial centre are:
>
> - A strong economy that offers business opportunities;
> - Effective regulation that inspires investor confidence;
> - Competition in products, services and pricing from a wide range of financial service providers, both Australian and international;
> - Efficient and reliable information technology and other business and social infrastructure;
> - Costs including staff, infrastructure, regulatory compliance and taxation. (AFMA 2008, p. 2)

The Insurance Council of Australia, in its submission to the AFCF Reference Group, identified that, for a successful industry that attracts new investment and activity, the:

> … first priority is a strong, efficient, and well managed Australian economy. If our members can operate their businesses profitably, this puts them in a strong position to compete for offshore business. (ICA 2009, p. 2)

Finally, a survey conducted by the MFSS (MFSS 2007, p. 24) also noted the importance of historical factors — such as the firm being originally established in Victoria — in influencing location decisions.

The preceding discussion indicates that there is a great deal of similarity in the suggested factors affecting the location of financial services businesses, including:

- the general competitiveness of business and regulatory conditions — including regulatory and tax polices
- access to a critical mass of skilled employees
- the presence of related businesses and clients (clusters of activity)
- local demand for services and access to local customers
- access to appropriate infrastructure
- the overall liveability of the location.

The relative importance of these factors to the location and investment choices of individual firms is likely to vary according to the type of firm — for example, whether it is an existing firm, greenfield or blue sky.

3.4 Drivers of investment and location: which can be influenced by the State Government?

The Government states that it wants to build on strengths in financial services 'while searching for innovative ways of doing business, attracting new firms and functions to the state, and creating more jobs in our financial services sector' (Victorian Government 2009a, p. 23). Removing barriers that would otherwise inhibit growth has the potential to increase employment opportunities in Victoria and create opportunities for businesses that supply services to the financial sector.

The State Government directly influences few of the factors that impact on the location decision of a financial services business. Some factors — such as taxation — are the responsibility of the Commonwealth, while for others — such as many of the factors affecting liveability — the State Government has limited influence.

Areas identified in the preceding discussion where the State Government can potentially remove barriers and improve Victoria's attractiveness as a business location are discussed further in this report. They include:

- the general competitiveness of business and regulatory conditions, including regulatory and tax policies (chapters 4 and 5)
- access to a critical mass of skilled employees (chapter 6)
- a range of operations and other actions currently undertaken by the Victorian Government, including overseas promotion, expertise in Public Private Partnerships and a number of other areas (chapter 5)
- removing impediments to clusters of activity (chapter 5).

3.5 Summary

Inquiry participants and others have noted the strong growth potential for parts of the financial services sector in Australia and in Victoria. This growth is likely to result in opportunities for the future development of the sector.

Victoria appears to have some important locational strengths for growing existing businesses and for attracting new businesses, including from overseas. Future growth opportunities would enable Victoria to build on areas where it already has a strong financial services sector presence.

As noted above, while the Commission has not reached a conclusion on Victoria's areas of competitive strengths, they may include:

- industry superannuation funds
- public sector funds management
- the capacity to deliver major infrastructure projects, especially PPPs
- intermediaries that expand their activities to serve specific client groups, such as regional banks and Islamic banking.

The State Government has some scope to influence some of the factors affecting business location decisions, as noted in previous sections, and these matters are considered in the remainder of the report.

4 Regulation and taxation

4.1 Introduction

Victorian financial services businesses are subject to multiple layers of regulation: Commonwealth regulation, Victorian regulation and, as the financial services market becomes increasingly globally interconnected, the sector is also subject to evolving international regulation and standards. Recent international developments have been given particular impetus by the global financial crisis, and include changes to the Basel global capital framework, and changes to accounting practices, among others, through the G20 process (FSB 2009). Australia contributes to these processes, which ultimately may lead to changes in Australia's national regulatory regime. Victoria's role is essentially that of a regulation taker, albeit one that has a large interest in the national regulations.

Both Commonwealth and Victorian legislation affect the Victorian financial services sector. Some of this legislation is directly aimed at financial services, while some has a broader impact across sectors, such as the *Corporations Act 2001* at the Commonwealth level, or the *Fair Trading Act 1999* (Vic) at the state level.

This inquiry focuses on regulation specific to the financial services sector. This chapter addresses the second item in the terms of reference by identifying the main regulators in the financial services industry and their key responsibilities. Some temporary regulation was introduced as a response to the global financial crisis, but will not be discussed in this chapter.[1]

Most of the key prudential and behavioural legislation that impacts on the financial services sector is administered by the Commonwealth and much of this regulation has been reviewed as part of the recent Australian Financial Centre Forum (AFCF) report, *Australia as a Financial Centre: Building on our Strengths*. A range of recommendations have come out of this report. The Victorian Competition and Efficiency Commission (the Commission) supports the thrust of the AFCF report in encouraging the removal of regulatory barriers to overseas opportunities (section 4.2.1).

Recently, there has also been a move to transfer remaining state financial services regulation to the Commonwealth, and increase harmonisation among state governments. As many of these changes are recent, it is too early to assess their effectiveness. This report will therefore not review any of these changes.

[1] For example, the Australian Government Guarantee Scheme for Large Deposits and Wholesale Funding was introduced on 28 November 2008 to promote Australia's financial system stability, and the scheme will close to new liabilities on 31 March 2010 (AGGSLDWF 2008).

Taxation is another significant area that impacts on the financial services sector. Financial services are subject to a range of taxes — some broad taxes that apply economy-wide (such as the GST or payroll tax), and some that only apply to certain types of financial services (such as stamp duty on insurance products). As with regulation, taxes are administered by both the Commonwealth and states.

Section 4.2 provides an overview of other recent reports impacting on the financial services sector. Section 4.3 covers Commonwealth regulation in the financial services sector, outlining the current regulators, and considers some of the Commonwealth regulations that impact on Victoria. Section 4.4 highlights the main Victorian legislation in the sector, mainly focusing on the legislation underpinning numerous state-owned financial entities. Section 4.5 considers the impact of Commonwealth taxation, and section 4.6 focuses on Victorian taxation, particularly on the effect of state stamp duty on insurance. Section 4.7 provides a summary of the chapter.

4.2 Current reviews

The inquiry terms of reference ask the Commission to identify any Commonwealth regulations that impact the financial services sector in Victoria. A number of relevant Commonwealth reviews have recently been completed, or are being undertaken. These reviews are outlined below.

4.2.1 Australian Financial Centre Forum report

The AFCF recently released the report *Australia as a Financial Centre: Building on our Strengths*. This report largely focused on Commonwealth legislation, but does have implications for the states and territories, including Victoria. Its focus was on proposals that would '… develop Australia as a leading financial centre' (AFCF 2009, p. 8). These recommendations cover regulation, taxation and the best way to boost trade in financial services and improving the competitiveness and efficiency of the sector (AFCF 2009, p. 1). A number of the recommendations were aimed at reducing impediments to expanding opportunities for overseas entry and exports. Table 4.1 summarises the AFCF's recommendations. The Commission has not duplicated this work, but comments on the recommendations relevant to Victoria's financial services sector.

Table 4.1 **AFCF recommendations**

Policy initiatives	*Recommendation reference*	*Benefits*
Increasing the size of the market		
Investment manager regime — settle tax scope and uncertainty issues for non-resident investors	3.1	Increased business in Australia and more opportunities offshore
Offshore banking units — adjustments to give full effect to policy intentions	3.2	
Funds management vehicles — review the scope for providing a broader range of tax flow-through collective investment vehicles	3.3	
Regional funds passport: managing offshore funds — introduce bilateral mutual recognition agreements and a multilateral Passport regime	4.3	
Improving access to capital		
Remove withholding tax on offshore borrowing and remove LIBOR cap	3.4, 3.5	More diversified funding sources and lower borrowing costs for consumers and business
Remove impediments to Islamic finance — assess products' parity of treatment and remove regulatory barriers	3.6, 4.8	
Enhancing competition and efficiency		
Remove state insurance taxes and rationalise regulations	3.7, 4.7	Lower costs and wider choice for consumers and business
Increase competition in exchange-traded markets — early consideration of licences	4.5	
Simplify retail debt issuance — reduce regulatory requirements on corporate debt issuance to retail investors	4.6	
Regulatory online gateway — information for potential foreign entrants	4.4	
Regional funds passport: domestic competition	4.3	
Maintaining best practice regulation		
Avoid unnecessary regulation — fully test and evaluate significant regulatory proposals	4.1	Maintenance of an efficient and effective regulatory system that protects consumers
Regulatory reviews — periodic reviews of the regulatory rules and framework	4.2	
Deepening regional engagement		
Government declaration of intent — to maintain and improve openness, competitiveness and regional engagement	6.1	Promotion of Australia as a financial centre
Financial missions — greater Ministerial and agency involvement	6.2	
Strengthening government/business partnership		
Financial Centre Task Force — establish the Task Force, including to monitor and advise on tax issues	3.8, 6.3	Support for effective and ongoing policy reform

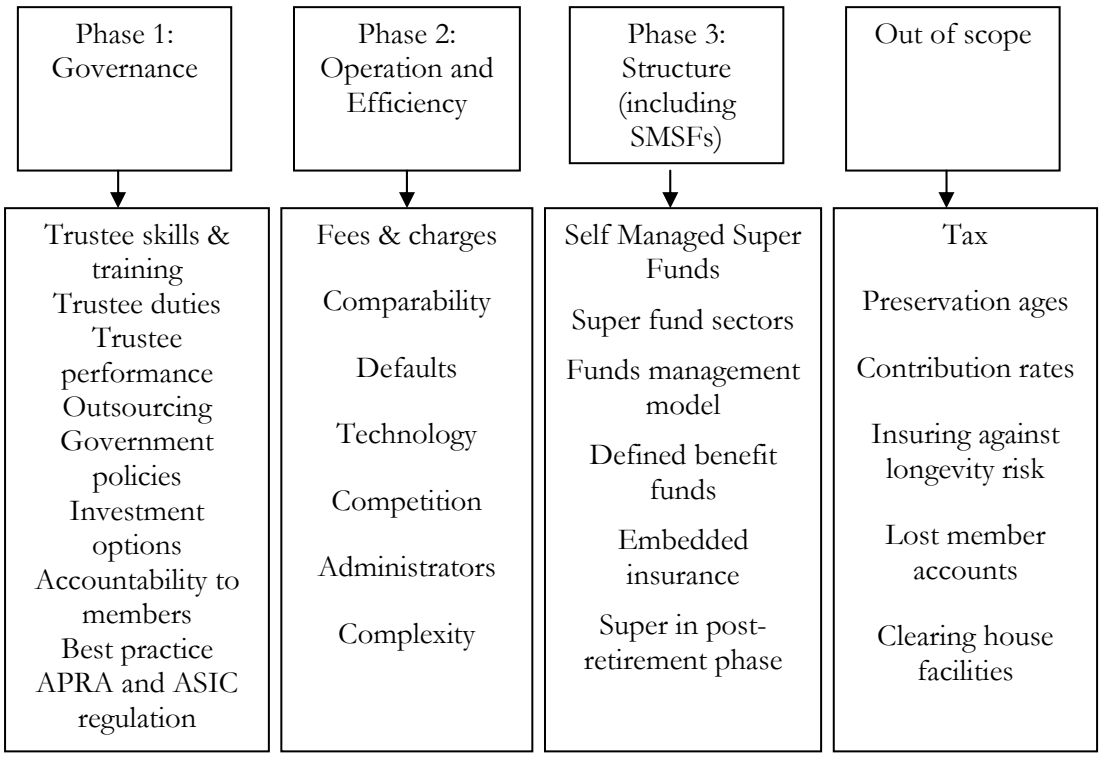
Source: adapted from AFCF 2009, p. 3, pp. 117–124.

4.2.2 Review into the Governance, Efficiency, Structure and Operation of Australia's Superannuation System

In May 2009, the Commonwealth Government announced a *Review into the Governance, Efficiency, Structure and Operation of Australia's Superannuation System* (the Cooper review). The Cooper review has been divided into a three-phased consultation process. Each phase of the process addresses different issues relevant to the review.

The first phase examines 'Governance', the legal and regulatory framework of the superannuation system (Commonwealth of Australia 2009b, p. 10). The second phase looks at the 'Operation and Efficiency' of the system. This phase is concerned with maximising returns for all members by removing unnecessary complexities and ensuring that the system operates in the most cost effective manner (Commonwealth of Australia 2009b, p. 10). Phase three examines the 'Structure' of the system, examining effective competition (Commonwealth of Australia 2009b, p. 10). The specific issues addressed by each phase are outlined in figure 4.1.

Figure 4.1 **Cooper review phases**



Source: adapted from Commonwealth of Australia 2009b, p. 7.

The review is to be conducted in the best interests of superannuation members, with a view to maximising retirement incomes for Australians, improving regulation and reducing business costs (Commonwealth of Australia 2009b, p. 10). The review must present recommendations around options for reform. Preliminary recommendations around phase one were released in December 2009. The review is currently analysing submissions received for phases two and three, ahead of releasing preliminary recommendations in March–April and April–May 2010 respectively. The final report will be delivered to the Commonwealth Government by 30 June 2010.

4.2.3 Australia's future tax system review

The *Australia's future tax system review* (the Henry review) was established in 2008 to review Commonwealth and State government taxes and interactions with the transfer system. The Henry review panel has submitted its final report to the Commonwealth Government. This report is not publicly available, but the Commonwealth Government is expected to release the report, along with a response, in early 2010 (AFTS nd(a)). The terms of reference for this tax review include taxation collected by the states (AFTS nd(b)), and the Commonwealth Government's response on these matters can be expected to have implications for state taxation, including specific transactions taxes.

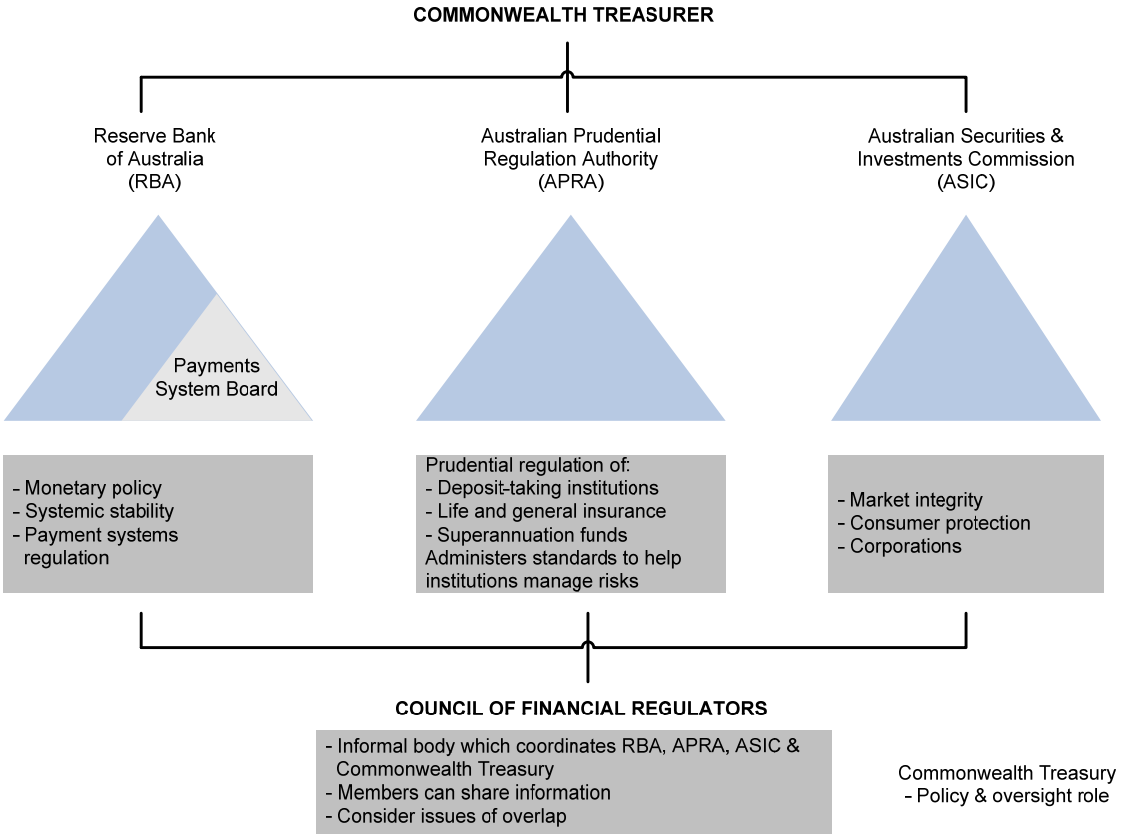
4.3 Commonwealth regulation

As noted above, most of the legislation and regulators that impact on the financial services sector are Commonwealth and much of the remaining state regulation is being moved to the Commonwealth to help create seamless national financial markets. An example of this is the 2008 agreement by the Council of Australian Governments (COAG) that the Commonwealth Government take over the regulation of consumer credit from the states (ASIC 2009). The regulation of trustee companies is also in the process of transferring to the Commonwealth.

4.3.1 Commonwealth regulatory framework

Responsibility for national regulation specific to the financial services sector lies with the Reserve Bank of Australia (RBA), the Australian Prudential Regulation Authority (APRA), and the Australian Securities and Investments Commission (ASIC). These agencies, along with the Commonwealth Treasury, are members of the Council of Financial Regulators (figure 4.2), which assists in coordinating the various regulators. While different regulators may oversee different parts of the operations of some financial institutions, there is clear coordinated regulatory oversight overall.

Figure 4.2 **Commonwealth regulatory framework**



Source: adapted from KPMG 1998 quoted in Austrade 2009b.

The Australian Transaction Reports and Analysis Centre (AUSTRAC) monitors compliance with anti-money laundering and counter-terrorism legislation of businesses classed as reporting entities under the acts (AUSTRAC 2009a) and performs a financial intelligence role. It 'collects financial transaction reports from a range of businesses in the financial, money service, gambling and bullion sectors' (AUSTRAC 2009b, p. 5).

Australia's regulation of its financial markets compares favourably worldwide, with many other jurisdictions viewing Australia's regulatory framework as a model (Australian Trade Commission 2009, p. 21). In the *Global Competitiveness Report 2009-2010*, released by the World Economic Forum (WEF), Australia was ranked six (out of 133 countries) in regulation of securities exchanges (WEF 2009a, p. 75), and was previously ranked third in the 2008-09 report (WEF 2008, p. 93).

4.3.2 Impact of Commonwealth legislation on Victoria

A number of general opportunities as well as strengths for Victoria in the financial services sector were identified in chapter 3. These general opportunities stem from economic growth and growing population, demographic and policy change, taking advantage of export opportunities and changes in approaches to risk and cost management (section 3.3). Chapter 3 also outlines a number of potential growth prospects for Victoria, including funds management. Islamic finance has also been noted by participants as an opportunity.

With the market for financial services largely being national in character, the development of Victoria's financial services sector is inextricably linked with changes at the national level.

Australian Financial Centre Forum report

The AFCF report highlights a number of regulatory changes that could be made, primarily by the Commonwealth, to help grow Australia's financial services sector, through improving efficiency, competitiveness and access to overseas markets (AFCF 2009, p. 77). All of these recommendations are of interest to Victoria and have the potential to remove barriers to growth in Victorian financial services. The Commission considers, however, that the recommendations on funds management and Islamic finance should be a priority for the Victorian Government in its dealings with the Commonwealth on implementation of the AFCF review outcomes.

As outlined in chapters 2 and 3, funds management is a current strength of the Victorian financial sector and has been identified by many, including participants in this inquiry, as a source of potential growth. In this area, the AFCF considered that greater international mutual recognition of regulation of funds managers had the potential to reduce some of the barriers to Victorian, and other Australian, fund managers providing services in Asia. Benefits to consumers from mutual recognition could arise from greater investment choice and more competition. The AFCF also concluded that difficulties can arise from differences in regulatory requirements and inconsistencies across different mutual recognition agreements (AFCF 2009, pp. 85–86).

The AFCF recommended developing an Asia Region Funds Passport through a two-stage process, involving negotiating a series of bilateral mutual recognition agreements, and then governments working to develop these into a multilateral Passport regime. The Passport aims to 'streamline the process of offering a managed fund in any country within the Passport group' (AFCF 2009, p. 86). The full recommendation is replicated in box 4.1.

Box 4.1 AFCF recommendation 4.3: The Asia Region Funds Passport

The Forum recommends that the Asia Region Funds Passport be developed as set out in Appendix 8 [of the AFCF report]. Broadly, this would involve a two-stage process:

- Stage one: ASIC negotiates bilateral mutual recognition agreements with key jurisdictions in the region. In doing this, the Forum recommends that ASIC attempt to ensure that investment restrictions allow a relatively broad range of funds to be offered across borders, and that licensing requirements are as streamlined as possible.
- Stage two: once bilateral agreements are in place, regional governments and agencies work together in the appropriate forums to develop these into a multilateral Passport regime. This would involve:
  - developing a commonly agreed set of licensing arrangements, investment restrictions and, where possible, offer conditions that would allow complying funds registered in one Passport country to be offered in each of the other passport countries; and
  - putting in place mechanisms for the continued administration of the Passport regime at national and regional levels.

Source: AFCF 2009, p. 87.

As noted previously, however, the extent to which such reforms would translate into growth in the Victorian financial services sector depends critically on whether businesses in Victoria take advantage of new international opportunities that emerge from any reforms.

Another area in which the AFCF made recommendations was Islamic finance (recommendation 4.8). The increasing interest in Islamic finance products was noted by a number of inquiry participants as one opportunity for growth in Victoria's financial services sector. In the education sector, Victoria's La Trobe University now offers a Master of Islamic Banking and Finance. It is the first course in Australia dedicated to Islamic banking and finance (Invest Victoria 2009, p. 2).

Victoria has already reformed its stamp duties to remove impediments to the development and sale of Islamic finance products (box 4.2). The AFCF identified a need to remove any wider regulatory impediments to the development and sale of these products. Its report noted possible regulatory issues with the classification of forms of Islamic finance products, and the relationship between Islamic banks and Sharia scholars (AFCF 2009, pp. 97–98). Given Victoria's past reforms in this area, it should be well placed to take advantage of any opportunities that arise from future Commonwealth reforms that recognise the distinct characteristics of Islamic finance products.

Draft recommendation 4.1

That the Victorian Government should support and encourage the Commonwealth to implement recommendations 4.3 and 4.8 from the Australian Financial Centre Forum report. This would involve support for:

- **Recommendation 4.3: The Asia Region Funds Passport**
- **Recommendation 4.8: Removal of regulatory barriers to Islamic finance.**

Cooper review

Chapter 2 noted the Victorian financial sector's relative concentration in superannuation, with seven of the top ten industry funds by assets in Australia based in Victoria, managing around $100 billion (section 2.3.3). Victoria is, therefore, well placed to capitalise on new opportunities for growth in the superannuation sector. The Cooper review (section 4.2.2) intends to make recommendations about the governance, operation and efficiency, and structure of the superannuation system in Australia. While the Cooper review is still in progress, submissions to the review and its preliminary papers highlight a wide range of issues for consideration. Two of the issues relevant to the impact of Commonwealth regulation include the flexibility of the *Superannuation Industry (Supervision) Act 1993* (Cth) (SIS Act) and the 30-day portability requirement.

Some submissions to the Cooper review suggested that the SIS Act should be reviewed. The submission from AMP, for example, noted that changes to legislation and the superannuation market meant that the SIS Act may need to be reviewed (AMP 2009, p. 5). The Association of Superannuation Funds of Australia (ASFA) also questioned the flexibility of the SIS Act in catering for sub-trusts and different categories of members (ASFA 2009, p. 4). In its preliminary report for phase one, the Cooper review acknowledged some issues arising from the SIS Act and noted its support or consideration of recommending changes (Commonwealth of Australia 2009c). The Cooper review has not reviewed the SIS Act as a whole, but its issues papers have posed questions about specific parts of the Act.

Several participants to this inquiry have questioned why investment in infrastructure does not appear to be attractive to superannuation funds. This issue is also being considered by the Cooper review. A relevant issue raised in the context of that review is the impact of the 30-day portability requirement. APRA describes this requirement:

> The portability provisions of the SIS Regulations require RSE [Registrable Superannuation Entity] licensees generally to transfer benefits to another fund within 30 days of receiving a member request. (APRA 2009d, p. 8)

In certain circumstances, APRA can provide relief from this requirement, but ASFA argued that this does not cater for funds with longer term investment horizons (ASFA 2009, p. 3). The issues paper for phase two of the Cooper review questioned the impact of the 30-day portability obligations on investment in infrastructure (Commonwealth of Australia 2009a, p. 10) (but a position has not yet been taken).

The Commission notes that the Victorian Government recently made a submission to the Cooper review.

Information request: The Commission has identified some areas from both the Australian Financial Centre Forum report and Cooper review as areas of particular significance for Victoria — does this list cover the main issues, or are there other additional (or fewer) areas the Victorian Government should focus on?

4.4 Victorian regulation

While much of the legislation (and regulation) that impacts on the financial services sector is administered by the Commonwealth, there is still some legislation administered by Victoria. The Commission has identified the major pieces of Victorian legislation that impact on the financial services sector, particularly those that are not the subject of agreed and imminent transfer to the Commonwealth.

4.4.1 Public financial corporations

Victoria has seven public financial corporations (PFCs), which are public entities with responsibility for delivering financial services. Some of these entities deliver services to the Victorian public. Others service areas of the Victorian Government sector. The background and operations of these entities are discussed in chapter 2.

The main Victorian legislation affecting financial services pertains to the acts underpinning the operations of these PFCs. These acts and their relevant organisations include:

- *Rural Finance Act 1988* (Vic) — Rural Finance Corporation (box 2.2)
- *State Trustees (State Owned Company) Act 1994* (Vic) — State Trustees Limited (box 2.3)
- *Victorian Funds Management Act 1994* (Vic) — Victorian Funds Management Corporation (VFMC) (box 2.6)
- *Treasury Corporation of Victoria Act 1992* (Vic) — Treasury Corporation of Victoria (TCV) (box 2.1)
- *Victorian Managed Insurance Authority Act 1996* (Vic) — Victorian Managed Insurance Authority (VMIA) (section 2.3.2)

- *Transport Accident Act 1986* (Vic) — Transport Accident Commission (TAC) (section 2.3.2)
- *Accident Compensation (WorkCover Insurance) Act 1993* (Vic) — WorkSafe Victoria (section 2.3.2) (with other statutory obligations outlined in a number of other acts).

The Commission has not reviewed the detailed operations of these PFCs, as this is outside its terms of reference. However, issues relating to two of these PFCs have been raised during the Commission's public consultation and are discussed below, in the context of two case studies.

Overall, given the scope and volume of financial services provided by PFCs, there is a significant amount of financial services activity reserved to the Government. There can be good reasons why government may be the most appropriate body to provide certain financial services, for example, to achieve social or equity objectives. But in the absence of clear reasons for government provision of particular services, there is a risk that government service providers could reduce competition or crowd out private services.

None of the participants in this inquiry has raised concerns with the Commission about the scope of direct government provision of financial services. The Commission notes that a number of these bodies, such as the Rural Finance Corporation, operate subject to constraints on their activities that could be reasonably expected to have some impact on the financial services sector. However, in the absence of any strong evidence from participants to the contrary, the Commission's working conclusion is that the current operational constraints on the scope of the clients served by PFCs are not limiting the development of the Victorian financial services sector to any significant degree.

The ways in which different approaches to service delivery can affect the efficiency of government financial services and the broader market are discussed below using Rural Finance and the VFMC as case studies. The Commission notes that its terms of reference relate to regulatory impediments and operations, and do not extend to policy issues. Its areas of interest, therefore, cover the operation of the service providers but do not extend to government policy on issues like compulsory insurance.

Case study: Rural Finance Corporation

Rural Finance is 'a specialist rural lender to primary producers and rural businesses' (RFC 2009, p. 6). Rural Finance increased both profits and total assets each year between 2005 and 2009 (RFC 2009, p. 8). The success of its commercial operations points to it having a strong understanding of rural lending. The Commission is not aware of equivalent bodies in other Australian jurisdictions.

The principal restriction on the operations of Rural Finance is that currently, the Rural Finance Act (the Act) only allows Rural Finance to lend (and provide other financial services outlined under s 18 of the Act) to rural industries. Section 3 of the Act defines rural industries to be primary or secondary industry carried on, wholly or partly, in Victoria. While the definition is not entirely clear, the Commission understands that Rural Finance is unable to provide its services to parties wholly outside of Victoria.

The Commission has not received any public comment on whether this matter is an issue for the financial services sector or if it is constraining rural lending or other rural financial services. The Commission is also aware that there are other institutions focusing on lending in rural areas, such as Rural Bank.

The Treasurer has appointed KPMG as Rural Finance's Prudential Supervisor (RFC 2009, p. 25). This prudential supervision essentially mirrors the APRA framework (RFC 2010). However, there are some differences between the APRA supervision of banks, compared with the framework applied to Rural Finance. One of these differences relates to its capital ratio. APRA assesses the capital adequacy of authorised deposit-taking institutions (ADIs) through the risk-based capital adequacy framework (expressed as a percentage). The risk-based capital adequacy ratio for an ADI is determined by dividing the capital base by the total risk-weighted assets (APRA 2008, p. 12). Generally, a lower ratio indicates greater risk is involved. The minimum ratio applied to Rural Finance is higher than banks regulated by APRA (RFC 2010). This ratio may be higher for Rural Finance due to increased concentration of risk resulting from the restricted location of clients and the industry it operates in, relative to ADIs. The need for a higher ratio may be somewhat offset by Rural Finance's limited bad debt history (RFC 2010).

Information request: Are there any issues associated with the scope of operation, and legislative restrictions on that scope, and the methods of prudential regulation applied to public financial corporations in Victoria?

Case study: the Victorian Funds Management Corporation

One area that has been brought to the Commission's attention is the role of the VFMC in managing funds on behalf of certain government agencies. At 30 June 2009, the VFMC had 14 clients in the categories of insurance, superannuation and other, ranging from some government departments to universities and hospitals (VFMC 2009, p. 9). To invest with the VFMC, clients must be a public authority, which is defined under the *Victorian Funds Management Corporation Act 1994* (Vic) (VFMC nd(a)).

In 2004, the Department of Treasury and Finance engaged Access Economics to review the model for managing the State's financial assets and to recommend a

business model that will achieve the Government's policy objectives and operate efficiently in an evolving investment environment (DTF 2009d). The review report, released in 2005, evaluated three different business models for the VFMC; a decentralised model, the status quo and a centralised model. Access Economics recommended that the VFMC operate under the centralised model[2] (Access Economics 2005, p. xiv).

The VFMC noted that the key outcome of the review was 'to expand VFMC's responsibilities and in particular, to centralise within VFMC the responsibility for setting investment strategy and asset allocation on behalf of its clients' (VFMC 2005, p. 2).

The VFMC provides a good illustration of how decisions on the delivery of financial services by government agencies can impact on the financial services sector more broadly. Two key characteristics of the current service delivery model are:

(1) the VFMC is responsible for delivering services on behalf of a number, but not all, government agencies (clients are listed in the VFMC's annual report (VFMC 2009, p. 9))
(2) the VFMC provides a range of services to meet clients' investment objectives by working with them to advise and agree on asset mix, risk and timeframes (VFMC 2009, p. 8).

Decisions on the scope of clients and whether clients can choose to use VFMC services and the scope of services provided by the VFMC need to take account of:

- the efficiency of managing larger pools of funds
- the benefits to organisations of having greater control of funds management
- whether there are any barriers, such as inertia, to organisations voluntarily choosing the most efficient approach to funds management.

Such decisions can, however, also affect the broader financial services industry. A single, large government fund manager with significant funds to invest may raise the industry's profile, including internationally, but it can also limit the areas in which local private sector providers can access government work.

Given the review by Access Economics and subsequent actions are relatively recent, then in the absence of significant changes in circumstances or new information, the Commission will not consider VFMC's operations further.

[2] The criteria used to evaluate these models reflected the broad objectives of the VFMC and managing public sector funds. The impact on the rest of the financial services sector in Victoria was not directly included among the criteria.

4.4.2 Other areas

The Commission has discussed two PFCs in the above case studies — Rural Finance Corporation and the VFMC. PFCs that have not been discussed in detail are State Trustees Limited, TCV, VMIA, TAC and WorkSafe Victoria. Another body providing financial services is the Senior Master's (Funds in Court) Office. Chapter 2 describes the Senior Master's role in managing funds on behalf of beneficiaries (box 2.4), and also outlines the roles of the other PFCs. The Commission is seeking comment on whether there are any other issues, within the scope of its terms of reference, in the operations of these organisations that are impacting on growth in the financial services sector in Victoria.

Information request: Are there any other impediments or operations issues relating to the operation of bodies providing financial services on behalf of the Victorian Government that the Commission should consider in meeting its terms of reference?

4.4.3 Insurance regulation

The AFCF report also discusses some state regulation, focusing on insurance. The specific issues cited relate to the states applying different regulatory approaches to some insurance areas, specifically home builders warranty insurance, motor vehicle licensing and work cover regulations (AFCF 2009, pp. 96–97). The AFCF recommendation on non-prudential regulation of the insurance sector states that 'the Forum recommends that state regulations relating to the insurance sector be standardised, wherever possible' (AFCF 2009, p. 97). In addition to issues with insurance regulation, participants to the AFCF review also noted concerns with taxation. Tax is discussed later in this chapter. The AFCF report suggested that:

> … resolving these tax and regulatory issues will provide the basis for a more competitive and efficient domestic insurance industry, by providing growth opportunities, economies of scale, lower costs (through less administrative and compliance complexity) and, potentially, more competition. (AFCF 2009, p. 96)

The Commission agrees that standardisation of state insurance regulations can reduce costs to businesses operating across states and can potentially result in cost savings being passed on to consumers.

In its submission to the Commission's inquiry, the Insurance Council of Australia also mentions that there are differences in the treatment of compulsory third party (CTP) insurance as well as workers' compensation among states, and claims that:

> The need to comply with different regulations in each jurisdiction, and also the requirement in practical terms often to have individual State/Territory operations (for example separate personnel and IT systems), makes it difficult

> for insurers to achieve economies of scale and manage risks efficiently. (sub. 10, p. 2)

The Insurance Council of Australia did, however, acknowledge the complexities of the harmonisation process:

> … there are significant issues involved in determining an appropriate basis for the harmonisation of these State-based schemes. Such issues go to the heart of the policy reasons why a government mandates a particular insurance requirement, such as CTP. (sub. 10, p. 2)

As a result of these complexities, this harmonisation process would require significant resources at the feasibility and negotiation stages to ensure that all states, including Victoria, were supportive of the harmonised system. Costs would also arise as a result of implementing a new system. In addition, care is needed to ensure that the harmonisation process does not compromise the regulation's effectiveness.

The AFCF report suggested that these insurance issues could be brought to COAG. COAG seems the most appropriate forum to pursue these issues, particularly given the recent work from COAG with harmonisation of occupational health and safety (OH&S) regulations and the establishment of Safe Work Australia in 2009, which is 'the new national body to develop model OH&S laws and to drive and implement national policy development of OH&S workers' compensation matters' (COAG BRCWG nd, p. 1). Safe Work Australia is engaging government and workplace representatives to progress nationally consistent workers' compensation arrangements (Safe Work Australia 2009).

Draft recommendation 4.2

That when future Council of Australian Governments (COAG) priorities are being identified, the Victorian Government should encourage the inclusion of harmonisation of regulation covering mandatory insurance requirements on the national COAG agenda.

4.5 Commonwealth taxation

Taxation has the ability to impact on the financial services market and improving the efficiency of taxation can aid the development of the financial services sector. The AFCF report noted the importance of tax, stating:

> … [the tax system] is one of the central determinants of the competitiveness of the financial sector; of its capacity to attract and retain talented people; and of the willingness of domestic and offshore participants to engage in cross-border transactions through that financial centre. (AFCF 2009, p. 51)

As taxes can have such a pervasive impact on the sector, minimising the distortive effects of taxes can benefit the sector and the wider economy. A tax can increase the relative price of one product compared with another and reduce the demand for the tax-affected product or service. Some parties may reduce their use of the product or substituting into other products, while others may decide not to use it at all if use becomes unaffordable.

Different sorts of taxes can have different impacts on the market, and lead to different changes in the behaviour of consumers. For example, a tax on a specific type of transaction may discourage the buying and selling of the product or service, and reduce activity in the market. Alternatively, a consumption tax with a wide tax base may have a smaller impact on behaviour, as relative prices are not as affected by the tax (and it is harder to avoid the tax).

As previously noted, Victoria has strength in funds management (including superannuation industry funds). Opportunities may also exist in the area of Islamic finance. The AFCF report and Cooper review have, or will, consider issues that impact on these two areas including tax issues.

4.5.1 Australian Financial Centre Forum report

The AFCF made two relevant recommendations (3.1 and 3.3) on the tax treatment of funds management. Recommendation 3.1 suggests changes to the taxation liability for investments made by non-residents through an Investment Manager Regime (AFCF 2009, pp. 59–60). The AFCF outlined stakeholders' uncertainties over the tax treatment of certain offshore transactions, particularly in relation to the activities of offshore banking units.

The AFCF recommended clarification of when investments on behalf of non-residents would and would not attract a tax liability in Australia, giving 'greater clarity and certainty regarding the tax treatment of offshore transactions undertaken through Australia' (AFCF 2009, p. 58).

The greater clarity in the treatment of taxation relating to funds management activities could reduce the risk perceived by foreign investors, and encourage greater investment through Australia, including Victoria. The Commission believes that this could deliver benefits through growth in funds management activities.

Recommendation 3.3 suggested a further review to consider providing a wider range of tax flow-through collective investment vehicles (AFCF 2009, p. 64). The report highlights that a lack of availability of alternative funds management vehicles that allow tax to flow to the end investor has, in some cases, meant that Australian companies are going offshore to establish and administer alternative vehicles (AFCF 2009, p. 62). The Commission considers that the Victorian

Government should support a Commonwealth review in this area. Availability of more vehicles may lead to fund managers in Victoria and Australia being better equipped to manage funds locally.

Recommendation 3.6 of the AFCF report suggested the Board of Taxation question whether any Commonwealth taxation provisions need to be amended, so that Islamic finance products have parity of treatment with conventional products, having regard to their economic substance (AFCF 2009, p. 71). The AFCF identified the problem that adverse tax treatment of Islamic finance products can occur, as these products are often structured differently to non-Islamic financial products (AFCF 2009, p. 70). The Victorian Government should support investigation into this matter, given the interest and potential for growth in Islamic finance products. In regard to state taxation, the Victorian Government has already made some progress in removing unequal tax treatment of Islamic finance products (box 4.2).

Box 4.2 **Islamic finance**

Islamic finance is based on the principles of Islamic law, the Sharia. Islamic banking is different from other forms of banking in that it does not allow for interest. Islamic banks also share risk with customers, channel profits into ethical investments and transact in real assets. Islamic finance is growing rapidly, with expected annual growth rates of 15 per cent (Sawlani 2009).

Under common Islamic finance arrangements, the legal title in the purchase of real estate is first transferred to the financial institution, and then transferred to the customer. Under previous laws, both these transfers attracted stamp duty. In 2004, an amendment was made to Victoria's *Duties Act 2000* (Vic) with the insertion of sections 57A–57F allowing for the removal of double stamp duty on property purchases. Removing stamp duty on the second title transfer has allowed Islamic property purchase arrangements to be more commercially viable and put them on an equal footing with other mortgages (Aly 2004).

This change to Victorian legislation has removed a significant barrier for Islamic financial institutions and interested customers in providing and accessing Islamic finance products.

Sources: Aly 2004; Invest Victoria 2009a; Sawlani 2009.

In determining its response to the AFCF report, the Victorian Government should give particular attention to these recommendations, as these are likely to have the most significant consequences for Victoria.

Draft recommendation 4.3

That the Victorian Government should support and encourage the Commonwealth to implement recommendations 3.1, 3.3 and 3.6 from the Australian Financial Centre Forum report. This would involve support for:

- **Recommendation 3.1: Investment Manager Regime**
- **Recommendation 3.3: Funds management vehicles**
- **Recommendation 3.6: Islamic finance products.**

4.5.2 Cooper review

As noted in section 4.3.2, given the importance of superannuation fund managers in Victoria, the outcomes of the Cooper review are also likely to be important to the Victorian Government.

One issue that the Cooper review may consider is increasing the scale of funds, including consolidation. The structure of the sector is addressed in the issues paper for phase three. The extent to which the Cooper review will consider tax impediments to consolidation is, however, not clear. Some issues have been raised in the context of that review. For example, submissions have suggested that the current capital gains treatment of amalgamating funds is discouraging consolidation. ASFA argued that:

> In order to facilitate the cost effective merger of funds, and protect the interests of fund members, capital gains tax and loss relief on all mergers of funds should be made permanent. (ASFA 2009, p. 3)

The review has already stated in its scoping paper that 'taxation arrangements and preservation ages applying to superannuation are outside the scope of the Review' (Commonwealth of Australia 2009b, p. 5). These issues may, however, be picked up in the Henry review. The Henry review mentions capital gains tax in its 2008 consultation paper and acknowledges that some submissions have raised this in the context of mergers of superannuation funds (AFTS 2008b, p. 147).

Information request: As with the regulatory issues, the Commission has identified some areas from the Australian Financial Centre Forum report, Cooper review and Henry review as areas of particular significance for Victoria — are these issues being sufficiently covered by these reviews, and does this list cover the main issues, or are there other additional (or fewer) areas the Victorian Government should focus on?

4.6 Victorian taxation

A range of Victorian taxes affect financial services, some of which are specific to parts of the financial services sector. Taxes on insurance received considerable attention throughout the Commission's consultation. Numerous inquiry participants highlighted concerns about taxes on insurance. These taxes were also raised in the AFCF report. Budget Paper 4 from the Victorian Government's 2009-10 Budget lists four types of insurance that are currently subject to state taxes:

- non-life insurance, which includes 'any sort of insurance that is applicable to property in Victoria, a risk, contingency or event that may occur within, or partly in Victoria, or both' (Victorian Government 2009d, p. 202). Common examples include motor vehicle, home and contents insurance.
- life insurance covering people domiciled in Victoria (Victorian Government 2009d, p. 202).
- Compulsory third party premiums — the transport accident charge — which covers Victorian motor vehicle owners for the injury or death caused by their vehicle to another person (TAC 2006).
- Fire brigades are funded by a fire services levy imposed on insurance companies. Insurance companies generally recover this levy through insurance premiums. Non-residential property owners, who choose to either self-insure or insure offshore, generally pay a contribution to the property's local fire service (Victorian Government 2009d, pp. 202–203).

Table 4.2 outlines the tax rates and government revenue from state insurance taxes in Victoria.

As the fire services levy is currently being reviewed by the 2009 Victorian Bushfires Royal Commission (The Fire Services Levy and Insurance Discussion Paper) and the Victorian Government (Fire Services and the Non-insured Green Paper) it will not be covered in this report.

Table 4.2 Taxes on insurance in Victoria

Tax	*Rate*	*State government revenue ($ m) (2008-09 revised estimate)*
Non-life insurance	10% on gross value of premiums	645.3
Life insurance	Of the sum insured: Up to $200 — nil $201–$2000 — $0.12 for every $200 or part thereof Over $2000 — $1.20 + $0.24 per $200 or part thereof above $2000 Temporary or term insurance — 5% of first year's premium	8.8

(continued next page)

Table 4.2 **Taxes on insurance in Victoria** (continued)

Tax	*Rate*	*State government revenue ($ m) (2008-09 revised estimate)*
Duty on compulsory third party premiums	10% on premium	131.6
Insurance contributions to fire brigades	Insurance companies, local councils and the state government all contribute to funding. For metropolitan areas: 75.0% from insurance industry 12.5% from local government 12.5% from state government For country areas: 77.5% from insurance industry 22.5% from state government	435.3

Sources: Victorian Government 2009d; SROV 2009a; AFTS 2008a.

4.6.1 Comparison with other states

There is no requirement for consistency in tax rates and tax bases across state insurance taxes. Some states apply a standard tax rate across all types of general insurance, while others levy different rates on subcategories. For example, New South Wales has three different subcategories and rates, and Queensland has two. States may also have different exemptions to stamp duty on insurance.

For stamp duty on motor vehicle insurance, several states or territories apply a rate of 10 per cent, including Victoria. New South Wales and Queensland apply five per cent, Tasmania applies eight per cent, and South Australia applies $11 for every $100 or part $100 (AFTS 2008a, pp. 90–91). As a result of the different rates of tax on insurance, relative rankings of states may change when a different insurance product is considered. For car insurance, the difference among states is not as pronounced as the difference in home and contents insurance. In the case of car insurance, Victoria's stamp duty rates are similar to many other states, but it is far from the lowest taxing position.

Table 4.3 compares the differences among states for stamp duties on home and contents insurance. The examples presented are indicative only as the absolute and relative amounts of stamp duty can change, depending on the selected premium and product.

Table 4.3 Comparison of home and contents insurance stamp duty among states and territories

State or Territory	*Tax rate on the premium*	*Stamp duty payable on a $1000 home and contents insurance premium* [a]
Victoria	10%	Basic premium = $1000 + 20%[b] fire service levy = $1200 + 10% GST = $1320 + 10% stamp duty = $1452
Australian Capital Territory	10%	Basic premium = $1000 + 10% GST = $1100 + 10% stamp duty = $1210
New South Wales	9%	Basic premium = $1000 + 21%[b] fire service levy = $1210 + 10% GST = $1331 + 9% stamp duty = $1450.79
Northern Territory	10%	Basic premium = $1000 + 10% GST = $1100 + 10% stamp duty = $1210
Queensland	7.5%	Basic premium = $1000 + 10% GST = $1100 + 7.5% stamp duty = $1182.50
South Australia	$11 for every $100 or part $100	Basic premium = $1000 + 10% GST = $1100 + stamp duty = $1221
Tasmania	8%	Basic premium = $1000 + 10% GST = $1100 + 8% stamp duty = $1188
Western Australia	10%	Basic premium = $1000 + 10% GST = $1100 + 10% stamp duty = $1210

[a] This example is for an insurance premium for a metropolitan residential property. Due to the impact of the differing rates of the fire services levy, figures for Victoria, New South Wales and Tasmania may change for a different property type. [b] The fire services levy rates used for Victoria and New South Wales are notional rates only. It is left to the discretion of the individual insurer to set the exact rate for the levy. In Victoria, the fire services levy is often different for home and commercial insurance policies, and metropolitan or rural. In New South Wales, different rates may apply to residential and commercial property insurance. Tasmania also applies a set fire services levy on commercial property insurance.

Sources: SROV 2009a; ACT Revenue Office 2010; OSRNSW 2009; Territory Revenue Office 2006; OSRQ 2009; RevenueSA 2009; SROT 2009; State Revenue nd.

Table 4.3 compares the taxes applied to home and contents insurance among states (for a metropolitan residential property). Most states and territories apply the same rate of stamp duty to all general insurance products. Under this example, Victoria has the highest level of taxes, with New South Wales a close second. One of the sources of this higher final insurance premium is the fire services levy, which the Commission has noted it will not be evaluating, but the inflating effect of Victoria's stamp duty rates is still highlighted. If the fire services levy was not charged on insurance in Victoria and New South Wales, the total impact of the stamp duty would be much closer to that in other states and territories.

4.6.2 The impact of taxes on insurance

The following section outlines the views of various groups on taxes on insurance, as well as outlining the recommendations that a number of reports have made.

The National Insurance Brokers Association (NIBA) claims that 'Victoria has the world's highest level of insurance taxes' (NIBA 2009b, p. 9). In its submission to the AFCF, NIBA also indicated that Victoria is the highest taxing state in Australia pertaining to insurance, especially non-metropolitan business insurance (NIBA 2009a, p. 2). In the example used in table 4.3, Victoria does have the highest taxes among states.

The Insurance Council of Australia noted the distorting effect of taxes on insurance, stating that 'taxing insurance distorts the take up of insurance and therefore the ability of economic agents to share and spread risk' (ICA 2006, p. 5). In its submission to this inquiry, the Insurance Council of Australia stated that it '… is a strong advocate of … the elimination of inefficient State taxes on insurance i.e. stamp duty on insurance contracts and the current fire services levy' (sub. 10, p. 1).

Other reports and publications

The consultation paper for the Henry review noted the potential effect of underinsurance or non-insurance as a result of state taxes on insurance:

> Submissions note that stamp duty on insurance may encourage people to either under insure or to not insure at all by increasing the cost of insurance products relative to other goods. While this in itself is inefficient, it may also lead to an increase in government expenditure if assistance is provided to the uninsured in the event of a disaster. (AFTS 2008b, p. 191)

In a 2002 paper, Professor John Freebairn highlighted that:

> In the absence of market failure reasons for restricting the supply and consumption of insurance, the present GST and stamp duties generate large deadweight costs. (Freebairn 2002, p. 411)

The AFCF report noted that insurance taxes (as well as other non-prudential regulations) act as a barrier to entry in the insurance market and one of its recommendations suggested 'that all state taxes and levies on the insurance sector be removed' (AFCF 2009, p. 73).

Other reports have also suggested the need to consider reform of state taxes on transactions:

- *Review of State Business Taxes* (State Business Tax Review Committee 2001) — this review evaluated the appropriateness of Victorian taxes and charges that affect business. It recommended reform of the Victorian tax system, including the removal of stamp duties affecting business, which it identified as the least efficient taxes (SBTRC 2001, p. 55). This included recommending the abolition of general and life insurance duties (SBTRC 2001, p. 95).
- *Review of State Taxation* — the Independent Pricing and Regulatory Tribunal provided a report for the New South Wales Treasurer in 2008, which acknowledged that 'Stamp duties on insurance and asset transactions are among the State's most inefficient taxes' (IPART 2008, p. 9). It recommended that, in the long term, New South Wales should 'aim to either reduce its reliance on revenue from these taxes, or eliminate these taxes by placing more weight on other more efficient taxes' (IPART 2008, p. 9).

This is not an exhaustive list of completed reviews that have discussed taxes on insurance, but the strong theme from these is that taxes on insurance, particularly stamp duties, should be removed.

There are also current reviews being undertaken involving state taxation. The Victorian *Inquiry into State Government Taxation and Debt* by the Economic Development and Infrastructure Committee has been asked to consider the impact of various state government taxes on a range of factors, including development and competitiveness.

4.6.3 Recommendations

Many of the arguments against taxes on insurance are strongly based on efficiency grounds. Removing stamp duties on insurance would reduce the distortion that these taxes have on the market by lowering the artificially increased prices. This would improve the affordability of insurance, with the expectation that those parties interested in taking out insurance would be more able and more likely to do so. This could lead to growth in the insurance sector, as well as other sectors that rely on insurance as an input.

When evaluating taxes, efficiency is an important, but not the sole, consideration. While other objectives, such as equity or simplicity must be evaluated, the impact

on government revenue is also an important acknowledgement. Revenue from stamp duties on insurance constitutes a large part of Victorian tax revenue. The only practical means of removing this is likely to include a restructuring of state and Commonwealth taxation and a review of intergovernmental financial relations, which is outside the terms of reference. However, the Commission suggests that a better approach to stamp duty on insurance is worth pursuing.

With the forthcoming Henry review expected to make recommendations impacting on all Australian jurisdictions, this provides an opportunity for Victoria to review its state tax system. From the perspective of the financial services sector, the Commission suggests that taxes on insurance, particularly stamp duty, be given due consideration as part of a wider review of Victoria's taxes and the role of state taxes in the national tax framework.

Draft recommendation 4.4

That, in light of the findings of the review of *Australia's future tax system* (Henry review), the Victorian Government should take a lead role in negotiating national harmonisation of stamp duty on insurance and reducing the reliance on such taxes.

The Commission notes that there would be a significant reduction in revenue from reducing stamp duties on general insurance to a lower rate. For example, if stamp duty were to be reduced from 10 per cent to 7.5 per cent (the current lowest rate in table 4.3), stamp duty revenue from general insurance premiums might fall by the order of $150 million, which would be significant in the overall revenues of the state.

This is a highly indicative estimate, as a number of factors would influence this figure. For example, as a tax reduction is expected to flow through to reduce insurance premiums, it is likely to encourage new customers to take up insurance or existing customers to extend their coverage.[3] This would lead to an increase in general insurance premiums and, in turn, a corresponding increase in stamp duty. This would somewhat offset the reduction in stamp duty revenue.

The Victorian Government cannot, however, mandate the timing and priorities of any national negotiations. It may, therefore, wish to consider unilateral action if the national processes are unlikely to deliver reform within a reasonable timeframe.

[3] In a submission to the Victorian Bushfires Royal Commission, Professor Deborah Ralston referred to research (by Drs Tooth and Barker) that found households to be quite price-sensitive to insurance products (Ralston 2009, p. 2), and notes the potential gains from tax reform.

Draft recommendation 4.5

That, in the absence of the conditions necessary for achieving national harmonisation of stamp duty on insurance, the Victorian Government consider reducing the distorting impact of the state tax on insurance by reducing stamp duty to the lowest rate among state jurisdictions as circumstances permit.

There is a significant amount of revenue that Victoria sources through taxes on insurance (table 4.2). If the rate of duty were to be reduced, without an offsetting increase in revenue from other sources, the Government would need to take regard of the revenue impact.

4.6.4 Land rich duty

Finally, in its submission to this inquiry, the National Stock Exchange Limited (NSX) raised concerns about an exemption in Victoria's *Duties Act 2000* that, the NSX argued, put it at a competitive disadvantage to the Australian Securities Exchange (ASX) (sub. 12, p. 1).

Land transfer duty is incurred when certain interests in land rich landholders are acquired (SROV 2009b). The State Revenue Office (Victoria) describes a land rich landholder as:

> … either a private company, a private unit trust scheme or a wholesale unit trust scheme that has land holdings in Victoria with an unencumbered value of $1,000,000 or more, and its land holdings in all places, whether within or outside Australia, comprise 60% or more of the unencumbered value of all its property. (SROV 2009b)

Section 71 of the Duties Act defines the meaning of 'landholder' and the Act excludes ASX and the World Federation of Exchanges (WFE) listed companies from being private company landholders. As a result, ASX and WFE listed companies are exempt from land rich duty.

In its submission to the inquiry, the NSX argued that:

> … the issues raised leave NSX markets (National Stock Exchange of Australia and Bendigo Stock Exchange) at a disadvantage those markets specifically excluded from the land rich provisions. I can see no policy reason for the difference of treatment in this regard between NSXA and BSX listed entities as compared to entities listed on ASX or members of the World Federation of Exchanges.
>
> … reform is required to promote competitive neutrality between exchanges and regulatory neutrality between the entities listed on the various exchanges. (sub. 12, p. 1)

Imposing an exemption for certain exchanges makes listing with other (non-exempt) exchanges relatively more costly. This creates a distortion in the market

by changing the relative costs of listing with certain exchanges, and may be negatively impacting on competition between exchanges.

While the NSX did provide arguments for extending the exemption, there are also arguments for keeping the current exemption only available to the ASX (and other WFE stock exchanges).

Different stock exchanges have different requirements that companies must meet before being able to list with an exchange, for example, different levels of market capitalisation and minimum number of shareholders. Comparatively speaking, the requirements for listing on the ASX are more difficult to meet than listing on, for example, the NSX.

An unintended consequence of extending the exemption may also lead to a potential increase in tax avoidance. For example, companies with large land holdings may list on an exchange (with an exemption on land rich duty) with the intention of avoiding a tax liability. If the barriers to listing were sufficiently low, this could provide an opportunity for companies to avoid stamp duty on conveyances, and lead to reduced revenue to the state government.

Information request: If an exemption to land rich duty were to be extended to all licensed stock exchanges, what would be the likely economic impact?

4.7 Summing up

This chapter considered the impact of regulation and taxation on the financial services sector in Victoria. At the state level, there appears to be little regulation that impedes the sector.

Information request: Are there any other state-imposed regulatory impediments that are restricting the growth of the financial services sector in Victoria?

However, there has been some concern about inconsistency across jurisdictions. Submissions raised inconsistency in insurance regulation as a potential area for harmonisation among states.

Also, state regulation appears to reserve a lot of service provision to state agencies. While it is recognised that how the state government chooses to provide some services can have a significant impact on their efficiency and the opportunities available to the private sector, the Commission has not received evidence that this is either significantly impacting on the financial services sector in Victoria or a controversial issue.

Finally, concerns have been raised with the Commission about state taxes, particularly stamp duties on insurance. The Commission considers that concerns about the efficiency of these taxes are valid and should be addressed, ideally in the context of a national response to the Henry review.

5 Government operations and other matters

5.1 Introduction

This chapter addresses that part of the terms of reference that requires the Victorian Competition and Efficiency Commission (the Commission) to inquire into options for 'operational changes that the Victorian Government can undertake to support development of the Victorian financial services sector'.

The essential underpinning of a robust, growing financial services sector is a group of competitive, profitable and entrepreneurial firms, which exploit opportunities that meet their business purposes. While governments cannot create sustained wealth in this (or any other) sector in the absence of comparative advantage, they can make two key contributions to the environment in which these firms operate: by setting a stable framework for appropriately regulated competition; and by removing or minimising unnecessary regulatory impediments to their operations. Regulatory matters were addressed in chapter 4.

The other areas of the Victorian Government's current operations, outside directly regulating the Victorian financial services sector, that may also affect the sector include:

- providing an internationally competitive regulatory environment for business in general, encouraging growth in the Victorian economy (section 5.2)
- removing, or advocating the removal, of impediments that adversely impact on the competitiveness of those areas of the sector that have comparative advantage. By so doing, the Victorian Government may contribute to the further development of sub-sectoral clusters within the Victorian financial services sector (section 5.3).
- improving access to information by potential new businesses and customers outside Victoria about the strength, quality and sophistication of the Australian financial system, including that part operating in Victoria, through promotion activities, including overseas missions (section 5.4)
- deepening, and capitalising on, the expertise of its own operations in financial activities to deepen the sophistication and capability of the sector (section 5.5).

That said, the Commission notes that the financial services sector is one where change — in demographics, economic circumstances, and in technology — will continue to provide new opportunities and challenges.

5.2 Competitive business and regulatory conditions

During the course of the inquiry, participants have stressed the importance of the impact the general economic environment has on activities in the financial services market, in particular in terms of the global financial crisis and ensuing economic slowdown and recovery.

The Commission considers that ongoing regulatory reform, including attention to reducing unnecessary regulation, makes a material difference to the state's economic growth and competitiveness, including the pace and robustness of economic recovery (VCEC 2009a). Better quality and less burdensome regulation means that businesses are better placed to adapt to changing circumstances and take advantage of opportunities that emerge when the economy starts to recover. Such a regime also provides a competitive advantage to Victoria in attracting and retaining business generally.

The Commission considers that a well designed strategic approach to regulation for economic performance includes:

- rigorously identifying priorities for reform
- instilling discipline in regulatory development and design and implementation processes — by maintaining, and preferably strengthening, efforts to review existing regulation to look for more efficient means of achieving intended policy outcomes and ensure that regulatory interventions are justified
- improving the performance of regulators — by monitoring and improving implementation, compliance and enforcement approaches, including increasing the use of risk-based enforcement.

The Commission notes Victoria's longstanding commitment to regulatory reform. State-based initiatives include introducing specific reforms in particular policy areas and undertaking broader systemic reforms, such as greater scrutiny of new regulation and the Reducing the Regulatory Burden initiative (including establishing a revised cost reduction target, encompassing a broader range of regulatory costs (DTF 2009a)). In addition, the Victorian Government has sought to work collaboratively with the Commonwealth and other state and territory governments to pursue national reforms.

The Commission considers that past and current approaches to reducing regulatory costs have produced substantial benefits for the Victorian community (VCEC 2009a). Adopting strategies that build on the successes of these initiatives would underpin improved future outcomes.

5.3 Clusters and networks

Chapter 3 noted, among the factors affecting location choices by financial services firms, the importance of clustering factors to firms considering locating in a financial centre and to established firms considering expanding their activities. A number of participants in the inquiry emphasised the value of developing 'face-to-face' relationships, networks of ancillary services and having access to a labour force equipped with specific skills that are valued by (and transferable among) businesses located near each other.

The Commission was also advised that, for a number of financial services, having a critical mass of demand from a primary financial corporation (or corporations) was a highly relevant factor in deciding whether to establish a presence in a financial centre like Melbourne.

In a study of financial services clustering in the United Kingdom, Pandit and Cook conclude that the benefits of clustering in financial services are:

> In particular, access to specialised inputs and knowledge spillovers on the supply side and a clusters reputation and close proximity to sophisticated customers on the demand side are important benefits in financial services clusters. (Pandit and Cook 2003, p. 242)

The Commission considers that many of the benefits from financial services clusters accrue to the businesses within the cluster. For example, firms may have better access to customers as clusters tend to reduce customer search costs, particularly for related and ancillary products. The existence of clusters can also attract specialist skilled labour, to the extent that employees locate in areas with high concentrations of potential employers. In addition, clusters that promote effective networks and strong connections between businesses can reduce business costs by improving information flows and knowledge spillovers.

As such, there are strong commercial incentives for financial services businesses (and relevant industry organisations) to establish and develop industry groupings and networks that best reflect their particular business needs.

Having regard to these considerations, the Commission concludes that the underpinnings of natural clusters are the existence of significant economies of scale and scope in areas of the financial services sector. In that context, the Commission notes the view of the Melbourne Centre for Financial Studies (MCFS), cautioning against the use by government of 'special deals and concessions' to '"buy" financial services' (MCFS 2007, p. 5).

Further, based on their research in the United Kingdom, Pandit and Cook caution that:

> … since dynamic clusters are unique and complex they are impossible to create or replicate. Indeed this is the very source of their sustainability. … [clusters] created through government inducements are of doubtful longevity and may exist only until another region offers a bigger enticement. (Pandit and Cook 2003, p. 243)

Having regard to these considerations — especially the strong and privately appropriable benefits — the Commission concludes the role of government in relation to the development of natural clusters seems limited to:

- removing specific regulatory impediments and fostering an appropriately regulated competitive environment (now almost entirely the preserve of the Commonwealth Government). Beyond the matters identified and discussed in chapter 4, the Commission is not aware of any specific regulatory barriers that impede the growth of natural clusters within the financial services sector.
- setting the general economic policies and general regulatory conditions for a competitive Victorian economy (section 5.2)
- addressing some operational matters of the Victorian Government that may improve access to information and increase the depth of, and access to, specific capabilities (sections 5.4 and 5.5)
- providing a policy and institutional framework to encourage deep and flexible supplies of the relevantly skilled labour for the sector (chapter 6)
- in conjunction with local government, using planning and other processes to reduce impediments to businesses locating close to each other, and to ensure the availability of internationally competitive infrastructure.

There is also potentially a role for government in highlighting the scope and strengths of Melbourne's financial clusters in overseas promotion.

The Victorian Government's statement *A great place to do business: Growing Victoria's financial services sector* indicates the Government's intention to:

> … target its actions towards attracting new firms in markets and areas where Melbourne offers clear advantages of critical mass and business depth. (Victorian Government 2009a, p. 26)

Specific initiatives include supporting the development of Docklands as a financial services precinct through planning policies, investment in infrastructure and by actively recruiting businesses to the precinct (Victorian Government 2009a, p. 18). The Government has also supported the creation and development of institutions such as the MCFS and the Melbourne APEC Finance Centre (MAFC) which, among other things, provides opportunities to bring together finance practitioners, academics and government. At the roundtable into leveraging opportunities for Victoria's financial services market, participants

indicated the important benefits from seeking to develop centres of academic excellence (section 5.4.1).

Ensuring that existing programs and initiatives remain relevant, and targeted to where they can have the most effect, requires ongoing evidence-based evaluation and review. On this, the MCFS note that in the Victorian context:

> The importance of information availability and agglomeration economies which influence financial sector development suggest that some government policies designed to further develop a local financial sector can pass a social cost-benefit test. (MCFS 2007, p. 5)

5.3.1 Case study: Superannuation funds

The Commission was advised that Melbourne has a strong and growing cluster based around superannuation funds management: with many corporate, industry and public sector funds already headquartered in the state (chapter 2). The growth of this cluster is underpinned by national policies to increase private provision for retirement incomes and superannuation.

Participants suggested a key benefit for firms within the cluster (and, in particular the 'subcluster' of not-for-profit superannuation funds) is having the capacity to exploit the competitive advantages and other group synergies in locating near each other. For example, the Commission understands firms have achieved cost savings by sharing or jointly outsourcing back office and other support services, as well as secured benefits from more coordinated and collaborative promotion activities to find, and attract, customers.

In addition, the Commission heard that a strong superannuation cluster has assisted in the development of innovative approaches and the delivery of innovative products. For example, Carol O'Donnell noted that:

> The strength of the superannuation funds and insurance industries in Victoria ideally should positively affect innovation and development not only in the financial services sector but also in all other sectors that must be supported effectively by finance. (sub. 3, p. 1)

An example of such innovation includes the Melbourne Mercer Global Pension Index (a new initiative that compares and ranks pension systems from around the world) which emerged as a result of strong industry presence and existing academic interest in the area: along with financial support from the Victorian Government (box 5.1).

Box 5.1 Melbourne Mercer Global Pension Funds Index

The Melbourne Mercer Global Pension Index (the Index) was created through a partnership between Mercer and the Melbourne Centre for Financial Studies (MCFS), funded by the Victorian Government. The first report, published in October 2009, draws on the results of a pilot study that included 11 countries, including Australia.

The Index aims to objectively compare pension systems across different countries by evaluating the public and private retirement income systems.

The index value is determined by calculating a weighted average of three sub-indices: adequacy, sustainability and integrity. These sub-indices are also made up of different indicators. The country is then assigned a letter grade from A to E, depending on its numerical index value; for example, an A grade is assigned to scores over 80 (Mercer 2009a).

The Index allows for comparison across countries, but it also highlights strengths and areas for improvement within each country's system. The MCFS has acknowledged that no single pension system would be suitable for all countries, and that different systems are the result of different economic, social, cultural, political and historic factors (MCFS 2009).

To date, the retirement income systems of 11 countries have been evaluated. None of these countries has received an A-grade rating, but the Netherlands has received the highest rating with 76.1. Australia has scored the second highest value with 74.0 (Mercer 2009b).

Sources: MCFS 2009; Mercer 2009a; Mercer 2009b.

The Commission has identified a number of factors that may currently hinder opportunities for superannuation funds, and in particular industry superannuation funds to expand their business. In particular, the Commission has heard that while it may be desirable for superannuation funds to be involved in long term investments in infrastructure projects, superannuation funds have been slow to take up these opportunities.

Participants suggested a number of reasons why superannuation funds are unlikely to increase infrastructure investment while projects are offered in their current form, including:

- the industry is made up of a wide range of funds (including a large growing number of self-managed funds) each with different ownership structures, investment strategies and approaches, appetites for risk and subsequent allocation to infrastructure assets
- difficulties in smaller funds reaching the size and scale required (through consolidation, or otherwise collaborating) to bid on larger scale, longer term investments

- problems with liquidity particularly for funds with low net cash flows and more 'active' memberships (those with a high proportion of members closer to retirement or in retirement products)
- a mismatch between funds' short-term objectives (including reporting requirements) and the timing of returns from longer term investment strategies
- the tendency for funds to take an 'ultraconservative' investment approach and the perception that infrastructure is a volatile, high risk asset
- the tendency for funds to 'stick to what they know', particularly for funds that lack the specialist expertise required to properly assess new or innovative infrastructure asset classes.

Some factors fall beyond the influence of government: such as the design of individual investment strategies or firms having a pessimistic perception of infrastructure value and volatility (Ernst and Young 2009). On this, the Australian Institute of Superannuation Trustees suggests that a key issue is that infrastructure is 'still considered by some as an alternative investment' (AIST 2009, p. 20).

Of those matters that might be more amenable to government action, most appear to be related to the existing Commonwealth legal and regulatory framework. Accordingly, these are likely to be, or have already been, considered as part of recent and current national reviews impacting on the financial services sector (chapter 4). In particular the *Review into the Governance, Efficiency, Structure and Operation of Australia's Superannuation System* (the Cooper review) is considering barriers preventing trustees investing in long-term investments as well as the nature of impediments to the further consolidation of super funds — and the role for governments to reduce them.

The Commission notes that the Victorian Government has made a submission to the Cooper review.

Commonwealth regulatory and tax impediments are discussed in chapter 4. The Commission anticipates that actions by the Commonwealth that reduce barriers and facilitate access to large scale infrastructure investment would provide opportunities for Victorian superannuation funds to expand their business — and so reinforce the superannuation funds cluster in the state's financial market.

Participants identified a role for Commonwealth and Victorian governments in contributing to a predictable and well-managed pipeline of infrastructure projects. These participants noted that such long-term assets were (or should be) attractive to financial firms, such as superannuation funds, that have long-term liabilities.

Both the timing and nature of projects is important. In its submission to the Cooper review, the Association of Superannuation Funds of Australia (ASFA) suggested that:

> … good long-term investments will stand on their own merits and attract investment from trustees as part of their funds' overall investment portfolios. The issue is that there is currently a shortage of attractive long-term investment products in which funds can invest. (ASFA 2009, p. 15)

Participants also linked the opportunities for more investment in infrastructure to Victoria's perceived expertise in managing Public Private Partnerships (PPPs) in procuring major infrastructure and more broadly in developing a larger, more predictable flow of infrastructure assets. This is considered further in section 5.5.2. The Commission sees this as an opportunity to increase the nature, number and value of transactions.

Finally, participants identified that the bureaucracy involved with planning and local and state government regulations can reduce the attractiveness of projects because these processes can 'absorb a disproportionate share of the projects' costs, and increase the at-risk bid costs' (AIST 2009, p. 20). Streamlining processes and reducing costs are an important element of the Victorian Government's overall strategy to seek to ensure a robust economy. The Commission has made recommendations in a number of its inquiries on these matters, most recently in its inquiry into environmental regulation.

5.4 Increasing access to information about Victoria's financial services sector

A number of participants considered that government and industry could do more to raise the awareness, especially overseas, of Victoria's, and particularly Melbourne's, financial services sector.

Participants considered Victoria's reputation as having a sophisticated and stable market for financial services is one of Victoria's more valuable assets, and activities designed to build and communicate that reputation may influence locational decisions by financial sector firms not currently operating in Victoria or not currently doing business in Victoria. Reflecting this, the Melbourne Financial Services Symposium concluded that:

> A strategy of nurturing emerging centres of excellence and articulating their competencies to the global financial community provides the best prospect for sustained employment growth for Melbourne. (MFSS 2007, p. 14)

The Australian Bankers' Association suggested that the Victorian Government has an important role in facilitating and encouraging growth of the financial

services sector, including through reputation building (sub. 9, p. 1). On this, the MCFS suggested that:

> … the correct approach is one which focuses upon fostering and developing a reputation as a place where financial expertise abounds, where specialist knowledge can be readily accessed and where strong networks of contacts can be accessed. (MCFS 2007, p. 11)

The Commission's view is that businesses in the financial services sector have some responsibility for enhancing the sector's reputation and promoting the strengths of the sector in Victoria, including through their industry associations.

However, there are a number of factors that, taken together, suggest that the financial services sector is unlikely to undertake an efficient level of reputation building activities.

- For small businesses (such as investment advisors and support services) there are likely to be high, possibly prohibitive transaction costs, affecting the ability of a large number of small firms to coordinate otherwise desirable promotion activities.
- Some activities that improve individual firms' reputations (such as basic research and development) can also benefit other related financial services providers, or the Victorian economy more broadly. If these broader benefits are not taken into account in individual firms' decisions, there may be an under provision of such activities.
- There may be free rider problems in relation to industry promotion. Not all firms may wish to participate in such activity but they will capture some of the industry-wide benefits — hence there may be an under provision of such activities by the sector alone.

This suggests that government action to complement (or supplement) industry initiatives may improve outcomes, in particular to ensure that sector (and economy) wide benefits are captured. Here, a key question, is whether government action is warranted — and in particular whether it is the best option — which will depend, among other things, on how government initiatives are developed, designed and implemented.

The Victorian Government is already active in fostering the state's strengths and reputation in financial services both domestically and internationally. In its statement *A great place to do business: Growing Victoria's financial services sector* the Victorian Government states that it aims:

> … to build a financial sector that is globally connected, highly capable and robustly competitive … by building Victoria's international reputation as a world class location for financial services; by boosting the quality of financial services

research, education and training; and by enhancing this business environment for the sector. (Victorian Government 2009a, p. 23)

During the course of the inquiry, the Commission heard that reputation is strongly influenced by many of the factors that also encourage the development of clusters and industry growth. Issues, not addressed elsewhere in this report that related to building and communicating Victoria's reputation as a financial services centre, are discussed in the following sections.

5.4.1 A stable sophisticated market

Victoria's reputation as a financial services centre is enhanced by it having a stable and sophisticated financial services market. A stable and sophisticated market also means that the State Government and the financial services sector are able to:

- respond quickly to changing circumstances and take advantage of opportunities as they arise
- quickly identify and remove impediments to new markets
- take a forward looking strategic approach to identify innovative markets.

Participants identified a number of instances in which the Victorian financial services sector produced innovative approaches to opportunities, including some regulatory changes to facilitate these opportunities. Box 5.2 provides further details.

Box 5.2 Victorian experience with emerging markets

Victoria has a well-earned reputation as a leader in innovative market reforms and developing emerging markets.

- In 2006, the Victorian Government engaged the Bendigo Stock Exchange (BSX) to establish the world's first market for taxi licence trading to provide a centralised, orderly and transparent trading system for the sale and lease of Victorian taxi licences. The BSX taxi market operates through an internet-based bid/offer market, with trading undertaken in accordance with BSX taxi market business rules including being restricted to accredited BSX approved taxi licence brokers (BSX nd(a), nd(b)). The system has now been transposed to a national platform, the National Licence Exchange (NSX nd).
- Victoria's BushTender program uses auctioned conservation contracts to conserve native vegetation. Under this system, landholders competitively tender for contracts to better protect and improve their native vegetation. Successful bidders receive periodic payments for their management actions under agreements signed with the Department of Sustainability and Environment (DSE). This approach was first piloted in 2000 and is now part of the core DSE approach to native vegetation management (DSE 2008).

(continued next page)

Box 5.2 Victorian experience with emerging markets (continued)

- Victoria is at the forefront in the development of Islamic banking and finance in Australia. In 2004 the Victorian Government amended the *Duties Act 2000* (Vic) to recognise the distinct characteristics of common Islamic finance arrangements (and in particular that the legal title in the purchase of real estate is first transferred to the financial institution, and then transferred to the customer). Removing double stamp duty charges on residential property has opened up the market for local Islamic financial institutions (Invest Victoria 2009a).

  Private sector banking institutions and education institutions have become involved in this developing market. This includes the growth of Islamic financial institutions, like the Melbourne-based Muslim Community (Co-operative) Australia Ltd. In addition, NAB and ANZ both offer Islamic finance products, and NAB offers a US$20 000 PhD scholarship in Islamic Finance (Invest Victoria 2009a). In 2010 La Trobe University offered a Master of Islamic Banking and Finance — the first course in Australia dedicated to Islamic banking and finance (La Trobe 2010).

Sources: Aly 2004; BSX nd(a), nd(b); DSE 2008; Invest Victoria 2009a; LaTrobe 2010; NSX nd; VCEC 2009b; Victorian Government 2009a.

Centres of academic excellence

The Commission accepts the view expressed by several participants that having a well recognised capacity for financial sector research can contribute significantly to the reputation of Melbourne's financial institutions and of Melbourne as a financial centre.

There are several existing Victorian Government initiatives and programs that seek to enhance (and showcase) Victoria's research strengths and so support Victoria's reputation as a centre of academic excellence.

- MCFS was established in 2005 with seed funding from the Victorian Government as a consortium of Melbourne-based universities and the Financial Services Institute of Australasia (Finsia) that seeks to:

  > … build links between academics, practitioners and government in the finance community, to enhance research, practice, education and the reputation of Melbourne's financial institutions and universities, and of Australia as a financial centre. (MCFS 2009, p. 2)

  The MCFS provides competitive research grants to its research associates at consortium universities, undertakes in-house research and brings together industry and academic research partners (MCFS 2009). Since its creation, MCFS has distributed $1.4 million in research funding to Australian finance academics (sub. 13, p. 2), funding 78 research projects (MCFS 2009, p. 6).

MCFS has also delivered more than 40 research-related conferences, workshops and events (sub. 13, p. 2).

The MCFS anticipates that it will broaden its role and functions (including by seeking to draw from a wider university network, undertake an expanded research program and attract broader national corporate sponsorship) as the renamed Australian Centre for Financial Studies (box 5.3).

- MAFC is sponsored by the Victorian Government's Department of Innovation, Industry and Regional Development to develop a range of activities in financial services education, research and training. It aims to:

  > … harness the knowledge and skills vested in Victoria's human capital to provide training programs, convene symposiums and undertake research to position Victoria as a regional centre of excellence in financial services and education. (MAFC 2009a)

  A key focus of MAFC's research is emerging regulatory regimes for the supervision of superannuation and pension systems — which it then uses to develop training programs for regulators from emerging markets in the Asia-Pacific Economic Cooperation region (MAFC 2009b).

Box 5.3 The Australian Centre for Financial Studies

The Australian Centre for Financial Studies (ACFS) will draw on expertise from academia, industry and government, to promote excellence in financial services.

ACFS activities are expected to draw from, and extend on, activities currently undertaken by MCFS and include:

- increasing its in-house capacity to undertake research and consulting projects, particularly in areas that inform the public interest
- expanding the university network involved, to include other Victorian universities and universities from for other states
- extending the existing research grants scheme to increase the amounts of research funding and access to finance academics and post graduate research students
- maintaining 'research reference groups' to inform a national research agenda
- pursuing industry partnerships with nationally based organisations
- attracting the commitment of larger nationally based sponsors
- establishing links with similar centres internationally
- highlighting the strengths of the Australian financial services sector and the complementary attributes of financial sectors in Melbourne and Sydney.

Source: MCFS, sub. 13.

High quality research and development underpins market developments and innovation, particularly in new processes, products or services. It may also contribute to the development of networks and reinforce and support clusters of financial services in Victoria (section 5.3).

This means the amount of research undertaken locally and its usefulness and relevance to firms in Australia and abroad has an important influence on Melbourne's reputation as a centre of academic excellence — especially given the global nature of the industry. This is underpinned by a continual input of new ideas and robust academic debate and research.

The Commission has heard that although Melbourne has a number of well regarded universities, there are likely to be limits on incentives for industry and academia to collaborate, and accordingly on the amount of research undertaken and its direct relevance to industry.

- The public good nature of basic or 'pre-competitive' research means that individual financial services businesses are less likely to initiate such research. Pre-competitive research and development activities are those that would benefit the sector as a whole, but lack, in the absence of application to specific business services, an appropriable private value that directly benefits the shareholders of the business. The lack of incentives to initiate such research leads to an under provision of basic research.
- Even when there are strong commercial incentives to undertake (or otherwise sponsor) 'competitive' research, sophisticated financial services businesses often have access to an international academic talent pool. As a result, work is less likely to be carried out locally when local universities have little appetite for undertaking that type of research or when their research capabilities and focus do not align with business's priorities or are not consistent with business's activities and practice.

It is clear that forging stronger links (across institutions and between institutions and industry) will provide a way to identify and assess issues and priorities, and take action to get things done — which in turn leads to better research outcomes. One key issue appears to be the complexity of bringing industry and academic institutions and academics together, given their different objectives and operating constraints. This complexity does not, however, in itself, provide a rationale for government involvement.

In relation to lifting the capacity for universities and financial services businesses to undertake 'competitive' research, the Commission considers this is fundamentally a matter for those businesses, universities and the sector as a whole. The Commission notes the efforts of the mining industry and individual companies in building the strength of university departments specialising in mining profession disciplines, providing endowments to fund recruitment of

specific expertise and in supporting centres of excellence. This model may hold relevant and practical insights for the financial services sector.

However, the Commission considers that there appears to be a role for government in 'pre-competitive' or basic research — for example to act as a catalyst to focus fundamental research efforts. On this, the Commission notes MCFS initiatives to establish 'research reference groups' made up of academic leaders, industry experts and regulators in banking, funds management and insurance to provide direction for research by identifying and developing research issues that are most relevant to industry (MCFS 2009).

In addition, government may become involved in research in the broader public interest including research that supports the further development of public policy and regulatory issues. It is important to ensure that, over time, government involvement of this nature is still required and still remains relevant and targeted to where it has the most effect. This reinforces the importance of ongoing evidence-based evaluation and review.

Information request: In what way could the Victorian Government support Victoria's capacity for financial sector research and its reputation as a centre of academic excellence, in particular in relation to 'pre-competitive' or basic research?

5.4.2 Promotional activities

Participants identified the value of promoting Victoria's financial services sector, especially overseas.

Increasing access to information about the Victorian financial sector, including its products and services, may assist Victorian businesses to harness opportunities interstate and overseas. It can also influence location decisions for overseas businesses wishing to establish a presence in the region. For example, effective promotion can enable better decision making by potential overseas businesses by reducing their search costs (to gather market information and make contacts) and facilitating the due diligence process.

The Commission notes that the Commonwealth and Victorian governments already actively promote the strengths of Australia and Victoria as a financial services centre. In addition, the City of Melbourne promotes Melbourne's role as a financial centre and other organisations such as MCFS and MAFC are involved with international training and events that contribute to promotion.

Given that current activities and initiatives are undertaken by multiple levels of government, academia, industry and firms, maintaining an effective focus can be complex.

At the Commonwealth level, the Australian Trade Commission (Austrade) has a prominent role in promoting trade and investment with Australia (box 5.4).

Box 5.4 **Austrade**

Austrade is a statutory agency under the Commonwealth Foreign Affairs and Trade portfolio with a number of onshore and offshore activities. Globally, Austrade has representatives in over 55 countries. Locally, it has a series of offices and Export Hubs across Australia in partnership with public and private sector organisations (Austrade 2010).

Among its roles, Austrade 'promotes Australia as an inward investment destination and, with the States and Territories, supports the inflow of productive foreign direct investment' and 'undertakes initiatives designed to improve community awareness of, and commitment to, international trade and investment' (Austrade 2010).

Focusing on financial services, Austrade is taking a lead role in trade and investment promotion. It has a dedicated financial services team which:

- raises the profile of the sector internationally
- develops strategies to grow business opportunities for Australian companies in markets where Australia has a world reputation or strong competitiveness
- works directly with individual financial services firms to assist their entry or expansion into the Australian market
- works with industry associations and other government agencies to develop and deliver specialised initiatives and activities to promote the industry and its members (Austrade 2009a, p. 1).

Austrade's promotion activities include supporting local and international trade missions, sponsorship and participation for government and industry, as well as marketing the sector through highlighting its depth, sophistication, liquidity and innovative nature (Austrade 2009a, p. 1).

Austrade also releases a number of reports, which can aid in building awareness and branding (Austrade 2009a, p. 3).

Sources: Austrade 2009a, 2010.

The Commission notes that there have been some calls for promotion activities undertaken at a national level to be strengthened. On this, the Australian Financial Centre Forum (AFCF) concluded:

> Australia needs to more actively and effectively promote the strengths of its financial sector and the advantages to overseas investors of recent and prospective policy changes. … Austrade is doing a good deal of valuable promotional work in the region with respect to financial services. … it needs to be fully supported by a significant effort at the official level — through regional initiatives, financial service missions and capacity building — and at the industry level. (AFCF 2009, p. 110)

For example, recommendation 4.4 of the AFCF report suggests that state agencies and regulators should aid Austrade to develop an online gateway to help foreign entities find information about investing in Australia. The Commission supports this idea in principle, noting that making information more easily accessible can reduce the search costs for interested groups. This could reduce barriers to foreign entities investing in Australia, potentially leading to more funds invested in Victoria. The recommendation also suggests making formal arrangements for a contact person within the regulators and other entities, including state agencies. A Victorian agency that would be in a good position to aid this process is Invest Victoria, the investment promotion agency of the Victorian Government.

Participants in the Commission's inquiry have expressed some concerns about the 'balance' in promotional activities by the Commonwealth and state governments. In particular, participants considered the efforts should be reinforcing and complementary. Promotion by the Commonwealth aims to enhance Australia's reputation as a whole, while promotional activity by state and local government should promote the relevant specific strengths and opportunities at the state and local level. Some concerns were expressed that Commonwealth promotional activities may have a bias towards Sydney as a financial centre.

Initiatives with a national focus, that seek to enhance Australia's reputation, can also influence Victoria's (and Melbourne's) reputation. Participants considered Victoria should continue to collaborate and communicate at a national level to ensure that appropriate weight is placed on Victoria's interests and help ensure Victoria has a clear profile in national promotions. The Commission notes, and broadly agrees with these views.

In its statement *A great place to do business: Growing Victoria's financial services sector,* the Victorian Government states that it will:

> … partner with industry to boost Victoria's global connections and to identify and promote trade and investment opportunities in financial services. (Victorian Government 2009a, p. 26)

Invest Victoria provides information and services to businesses seeking to establish new businesses or grow an existing business in Melbourne and Victoria. This includes providing information about:

- the state — the business, political and economic environment, infrastructure, global access and living environment — which serves to highlight Victoria's broad competitive strengths and liveability advantages
- Victoria's financial services industries — existing operations and companies, market potential, research and development capabilities, available skills and

costs — which serves to highlight Victoria's strengths and market potential (Invest Victoria 2010a, 2009b).

Invest Victoria also provides investor support services and professional advice, which, among other things, seeks to connect investors with existing networks, local suppliers, service providers and partners. For example, Invest Victoria has partnered with Advance to develop an expatriate network, to keep Victoria's expatriate network connected, informed and better able to promote the state (Advance nd).

Enterprise Melbourne, an economic development initiative of the City of Melbourne, undertakes similar activities — but with a focus on promoting Melbourne as a business and investment location and helping Melbourne businesses consider new markets, including overseas (Enterprise Melbourne nd).

The challenge is to ensure that ongoing promotion activities by the Victorian Government remain focused on the parts of the financial services sector where they can have the most effect. This is particularly important now, given the market has changed substantially (including in response to the global financial crisis and economic slowdown) and will continue to do so as ongoing national reforms are developed and implemented (chapter 4).

The Commission considers the Victorian Government might ensure that ongoing state-based efforts focus on priorities and contribute to a consistent message about Victoria's strengths as a key part of a robust national financial services sector. It notes the importance of government effectively consulting with industry with a view of informing itself of key priorities and opportunities, particularly identifying areas in which business has sufficient interest in international links or opportunities to take advantage of prospects that open up as a result of government's promotional activity.

Draft recommendation 5.1

That to promote the strengths of Victoria's financial sector in a changing global environment, the Department of Innovation, Industry and Regional Development work with Austrade to ensure that appropriate weighting is given to the financial services sector based in Victoria in national promotional activities.

5.5 Exploiting public sector expertise

5.5.1 Government engagement with industry

The Victorian Government engages with the financial services market as a buyer and supplier of financial services (chapter 2). Accordingly it may, through its supplying and purchasing decisions, influence the structure and development of

the financial services market, including the nature of financial products developed and used.

Government procurement of financial services

The Victorian Government is a significant purchaser of financial services, directly and indirectly (where financial services are one element of a larger service). The terms of reference of this inquiry do not extend to making recommendations on state government purchasing. However, the Commission notes that procurement policies and practices can affect the financial services sector in three ways:

- their efficiency impacts on industry generally, which flows on to the demand for many financial services (since the strength and growth in financial services is closely linked to overall performance)
- the basis on which financial services purchased by government (including transactions and cash, insurance and leasing) are transacted directly affects the businesses bidding for this work
- indirect effects that arise when goods and services are procured in ways that stimulate 'enabling' innovations by the financial services sector, to support the provision and financing of those goods and services.

The Commission understands that considerable work is going on to improve government purchasing policy, including through the Public Finance and Accountability Bill (PFAB) (box 5.5). Going forward, the Commission considers the Victorian Government should aim to remain a 'sophisticated customer' of financial goods and services that:

- is open to more innovative and cost effective ways of meeting its financial services needs
- requires providers to deliver high quality services at a competitive price
- establishes effective links with suppliers so that opportunities to improve service can be identified and acted upon.

Box 5.5 Public Finance and Accountability Bill

On 8 December 2009 the Victorian Government introduced the Public Finance and Accountability Bill (PFAB) into Parliament. It is expected the Bill will be considered when Parliament resumes in early 2010.

PFAB seeks to 'modernise the framework for public finance, accountability and resource management in Victoria' to ensure best practice public financial management continues. The Bill replaces the *Financial Management Act 1994* (Vic) and a number of related acts, to provide a cohesive legislative framework that covers all key elements of public finance.

(continued next page)

Box 5.5 Public Finance and Accountability Bill (continued)

PFAB sets out the procurement principles that will apply to all public procurement arrangements (Clause 9). These are:

- achieve value for money outcomes (based on a balanced judgement of relevant financial and non-financial factors)
- align accountability with appropriate levels of authority and responsibility
- ensure probity through ethical behaviour
- scale governance, policies and processes and capability to the complexity and significance of the procurement.

All government departments and public bodies must comply with the procurement principles.

PFAB also provides for the continuation of the Victorian Government Purchasing Board as the State Procurement Board (Clause 15), and sets out its functions and powers (Clause 16), which include supporting departments and public bodies with their procurement activities, and developing procurement capability across government.

Extensive consultation and research was undertaken during the development of the Bill, both within Australia and internationally.

Sources: DTF 2009b, 2010a; Victorian Government 2009b.

5.5.2 Other matters

In addition, there may be opportunities for the Victorian Government to leverage its expertise in the provision of particular financial services, or broader products and services that include an embedded financial services component.

Public private partnerships

In Victoria, PPP projects are procured under the Partnerships Victoria Framework (box 5.6) and have been used for a large number of projects across a broad range of industry sectors and infrastructure assets. Twenty projects have been undertaken under the Partnerships Victoria Framework worth around $10.25 billion capital investment. These include social infrastructure, such as correctional facilities, the new Royal Children's Hospital and the Partnerships Victoria in Schools Project; environmental infrastructure such as water treatment plants; and economic infrastructure such as the EastLink and Peninsula Link road projects. There are two further projects worth over $1.25 billion in the market: the Parkville Comprehensive Cancer Centre and Ararat prison (DTF 2010b).

Box 5.6 Partnerships Victoria

The Partnerships Victoria policy provides a whole-of-government approach for integrating private investment into public infrastructure and related ancillary services.

The Partnerships Victoria policy was first introduced in 2000. Now the Partnerships Victoria Framework comprises the National Public Private Partnership (PPP) Policy and Guidelines agreed by the Council of Australian Governments (COAG) in November 2008 (IA 2008) and the state specific requirements outlined in the Partnerships Victoria Requirements document and annexures (DTF 2009c; IA 2010a).

The National PPP Policy objectives (contained in the National Policy Framework document) are to:

- encourage private sector investment in public infrastructure and related services where value for money for government can be clearly demonstrated
- encourage innovation in the provision of infrastructure and related service delivery
- ensure rigorous governance over the selection of projects for PPPs and the competition for and awarding of contracts
- provide a framework and streamlined procedures for applying PPPs across Australia
- clearly articulate accountability for outcomes (IA 2008).

There are also state-specific objectives to:

- maximise the social and economic returns from government expenditure
- promote growth and employment opportunities for the whole of Victoria
- manage Partnerships Victoria contracts in a proactive, practical and constructive manner to achieve project objectives incorporating balance long-term value for money outcomes (DTF 2010d).

The Partnerships Victoria unit (part of the Commercial Division in the Department of Treasury and Finance) develops policy and guidelines for the implementation of best practice in public-private partnerships at a state and national level. It also advises departments and agencies on the scoping, contracting and ongoing management of PPP projects.

Sources: DTF 2009c, 2010b, 2010c, 2010d; IA 2008, 2010a.

During the course of the inquiry the Commission was advised that there was further scope for PPPs to benefit government by improving services and value for money, encouraging innovation, improving asset utilisation and integrating whole-of-life management. For example Duffield et al. (2008) found that in Australia PPP projects are delivered for a price 'far closer' to the expected cost and with far greater cost certainty after the contract is signed when compared with projects procured in traditional ways. Allen Consulting Group et al. found that PPPs provide superior cost and time performance — and that these

advantages increase (in absolute terms) with the size and complexity of projects (Allen Consulting Group et al. 2007). The UK National Audit Office found that private finance projects 'normally deliver what is asked of them' — between 2003 and 2008, 69 per cent of projects were delivered on time, 65 per cent were delivered at the contracted price and public bodies are usually satisfied with the services provided (NAO UK 2009, p. 7).[1]

On this, Infrastructure Partnerships Australia argued:

> The case to retain and sustain Australia's PPP infrastructure market is clear and compelling. … It is not in Australia's interests to return to a limited public works model with its inherent constraints or inefficiencies for infrastructure development. Over the next five years, Australia needs the large desalination plants, hospitals, transport facilities and social infrastructure that PPPs can most effectively deliver. (Infrastructure Partnerships Australia 2009, pp. 4–5)

While the Commission recognises the benefits of using PPPs under the right circumstances, it is also mindful that the PPP approach is one of many procurement approaches.

The finance industry and PPPs

The Commission notes that PPP arrangements are underpinned by private financing. Such projects can be funded by a mix of private debt and equity funding, thereby removing the need for governments to borrow or fund the project from the budget. There is also a range of institutional arrangements that can be used to access private funding and allow a range of private sector partners to contribute to a project while ensuring they are comfortable with the risks and potential returns. For example, a single firm may be unwilling to 'put all its eggs in one basket' by fully funding a large, long lived infrastructure asset, but may be willing to contribute as part of a consortium of firms.

One consequence of this flexibility is that PPPs can also create additional secondary benefits: including supporting both new and traditional financing methodologies and approaches. That is, project delivery benefits (the primary purpose of PPPs) may be accompanied by increasing growth in ancillary services.

The Commission heard that while Victoria is considered a leading proponent of PPPs, PPPs are not currently used in Australia to the same extent as other national jurisdictions. The Commission considers that a greater use of PPPs, all

[1] As of September 2009, there were over 500 operational Private Finance Initiatives projects in England, with a capital value in excess of £28 billion. Under this approach public authorities establish a detailed output specification at the outset of the tendering process and a private sector consortium (usually a special purpose vehicle) is appointed to deliver the project. Payments are made once services are available (NAO UK 2009).

other things being equal, is likely to have positive flow-on effects in Victoria's financial services market. For example, as the nature, complexity and application of PPPs develops, so does the level and types of financing used in those contracts. This, in turn, can encourage new players into the market, facilitate the development of skills within the consortium and also underlie the development of new financial instruments and approaches.

Further, the extent of any benefit to Victoria's financial services market from harnessing these opportunities will be increased if arrangements allow government and private parties to respond flexibly to changing circumstances; and in particular providing 'room' for the private partner to be innovative in its financing options.

The Commission sees merit in the Government seeking to understand what additional opportunities may exist to expand its use of PPPs. It understands that Infrastructure Australia (IA) is reviewing barriers to competition and efficiency in the procurement of PPPs with a view to improving PPP outcomes across Australia.

Participants in this inquiry identified two key priorities: developing a project 'pipeline' and 'unlocking' Victoria's expertise. Improving the way that government engages with industry is also important (section 5.5.1): this could include reducing bureaucracy and streamlining processes.

Developing Victoria's PPP project pipeline

During its consultation and at the roundtable into leveraging opportunities for Victoria's financial services market, the Commission heard that there may be opportunities to broaden the application of PPPs (to increase the scope and size of PPP projects) and the share of public sector capital investment undertaken using a PPP approach. For example, the Commission heard that Victoria delivers around 10 per cent of annual public sector asset commitments through PPPs (DTF 2010c) — compared to Canada (in the order of 10–20 per cent) and the United Kingdom (10–14 per cent) (as reported in Iacobacci 2010).

One possibility includes the Government committing to a forward 'pipeline' of PPP projects. This type of commitment helps to increase certainty and demonstrate that government considers the PPP approach as a valuable and legitimate way of funding infrastructure. This, in turn, can enable existing and new market players (including superannuation funds) to make better informed choices about potential opportunities.

Several options have been suggested by participants:

- At the roundtable into leveraging opportunities for Victoria's financial services market, participants suggested that the infrastructure pipeline would

be substantially improved if the PPP model was used as a default approach for major capital projects (unless specific factors favour another approach).[2]

- The Commission also heard of the importance of having publicly available information on planned and upcoming infrastructure projects and large infrastructure plans that are likely to include a PPP component. On this, the Commission notes that IA publishes information on projects that are being delivered, are in the process of being procured or that governments have identified as potential candidates for PPPs (IA 2010b).
- The Commission also understands that governments overseas have identified a proportion of infrastructure projects that are likely to be delivered through PPP mechanisms (subject to satisfactory review of business cases).

The Commission accepts each would send a strong signal of the Government's commitment to PPPs where they are a fit for purpose mechanism for building and financing infrastructure — but notes none is without cost.

Unlocking Victorian expertise

Victoria has had considerable experience with successfully undertaking PPP projects in a wide range of areas. However, much of this experience is internal to the Victorian public service, that is, it rests with those who have been involved in initiating and seeing the projects through to completion.

This may limit the ability of these skills to be used more widely and outside traditional departmental boundaries. Locking up skills may limit the number of potential PPP projects and hence impact on the development of the financial services sector in Victoria.

There are a number of options that might be explored, or further expanded, to exploit further this expertise for the benefits of Victoria, or more broadly. At a fundamental level, Victoria could continue to seek to take a leading role in PPP policy and practice by contributing to the national PPP agenda. Beyond this, Victoria might consider removing departmental and jurisdictional boundaries (with appropriate checks and balances) to create a stand alone PPP unit that draws on the skills already in the public service. Once established, such a unit might contribute to a PPP cluster, attracting other skilled staff from outside the public sector. This unit could also act as a 'consultant' to the Victorian

[2] Under the National PPP policy, Commonwealth, state and territory governments are required to consider PPP delivery for any project with a capital cost in excess of $50 million when conducting a procurement options analysis. Projects of less than $50 million may also be suitable for PPP delivery if they exhibit sufficient value for money drivers (IA 2008). In Victoria, the procurement options analysis is undertaken in accordance with the National PPP guidelines and Victorian guidelines such as the Victorian Gateway Initiative Project Lifecycle guidelines (DTF 2010d).

Government, other jurisdictions and also to private sector companies with an interest in participating in PPP projects in Victoria, interstate or overseas.

Information request: How can Victoria best exploit its expertise in PPPs? How would this affect Victoria's financial services sector? What are the benefits? What are the risks? How could the risks be mitigated?

5.6 Summing up

The Commission considers that governments make two key contributions to the environment in which financial services businesses operate: by setting a stable framework for appropriately regulated competition; and by removing or minimising unnecessary regulatory impediments to their operations. This is largely a Commonwealth issue (chapter 4) — so a key role for the Victorian Government is to advocate the removal of regulatory impediments that have a disproportionately adverse impact on the competitiveness of Victorian businesses.

In addition to continuing its efforts to improve general competitiveness of Victoria's business and regulatory conditions, encouraging growth in the Victorian economy, and continuing to support Victoria's capacity for financial sector research and its reputation as a centre of academic excellence, in particular in relation to 'pre-competitive' or basic research, the Victorian Government might consider:

- addressing operational matters that may improve access to information about the strength, quality and sophistication of Victorian financial services businesses having regard to activities and initiatives undertaken on a national level
- capitalising on its own expertise in financial activities to deepen the sophistication and capability of the sector, and contribute to the supply of long-term assets with characteristics that are a good fit for retirement income provision.

The Victorian Government also has an important role in providing a policy and institutional framework that encourages deep and flexible supplies of relevantly skilled labour (chapter 6).

6 Skilled labour

6.1 Introduction

As noted in chapter 3, access to a critical mass of skilled employees is one of the key locational factors for financial services businesses. This is recognised in the terms of reference for this inquiry, which ask the Victorian Competition and Efficiency Commission (the Commission) to inquire into any regulatory or other impediments to ensuring sufficient supplies of skilled labour in Victoria's financial services sector, including consideration of the need for accreditation to facilitate labour mobility within the sector. The quantity and quality of labour is significantly shaped by the education and training system.

The financial services sector is highly labour-intensive and provides sophisticated services. The sector's success therefore depends in part on the availability of skilled workers. As outlined below, the financial services workforce in Victoria is aged mainly between 25–49, well educated and receives above average earnings.

This chapter provides an overview of the financial services labour market in Victoria (section 6.2), examines national and Victorian evidence on skill shortages in the financial services sector (section 6.3) and explores a number of elements of the skills formation system (section 6.4). The Commission has not found any significant regulatory impediments to the supply of skilled labour to the financial services sector, although there may be scope to fine-tune particular aspects of current arrangements.

6.2 Overview of the financial services labour market

Financial services businesses such as banks, credit unions, insurance companies, and managed funds all require skilled labour to provide a wide range of financial services.[1] This labour can be sourced from the education and training system in Victoria (box 6.1). There can also be a demand for, and supply of, skilled labour from other industry sectors, interstate and overseas (figure 6.1).

A range of vocational education and training (VET) and higher education institutions in Victoria provide courses for the financial services industry. These include Tertiary and Further Education (TAFE) institutes, universities and private providers. Many financial services businesses also provide training. These institutions and organisations train new entrants to the industry and existing financial services workers.

[1] The key industry segments in Victoria's financial services sector are described in chapter 2.

Box 6.1 Education and training in Victoria

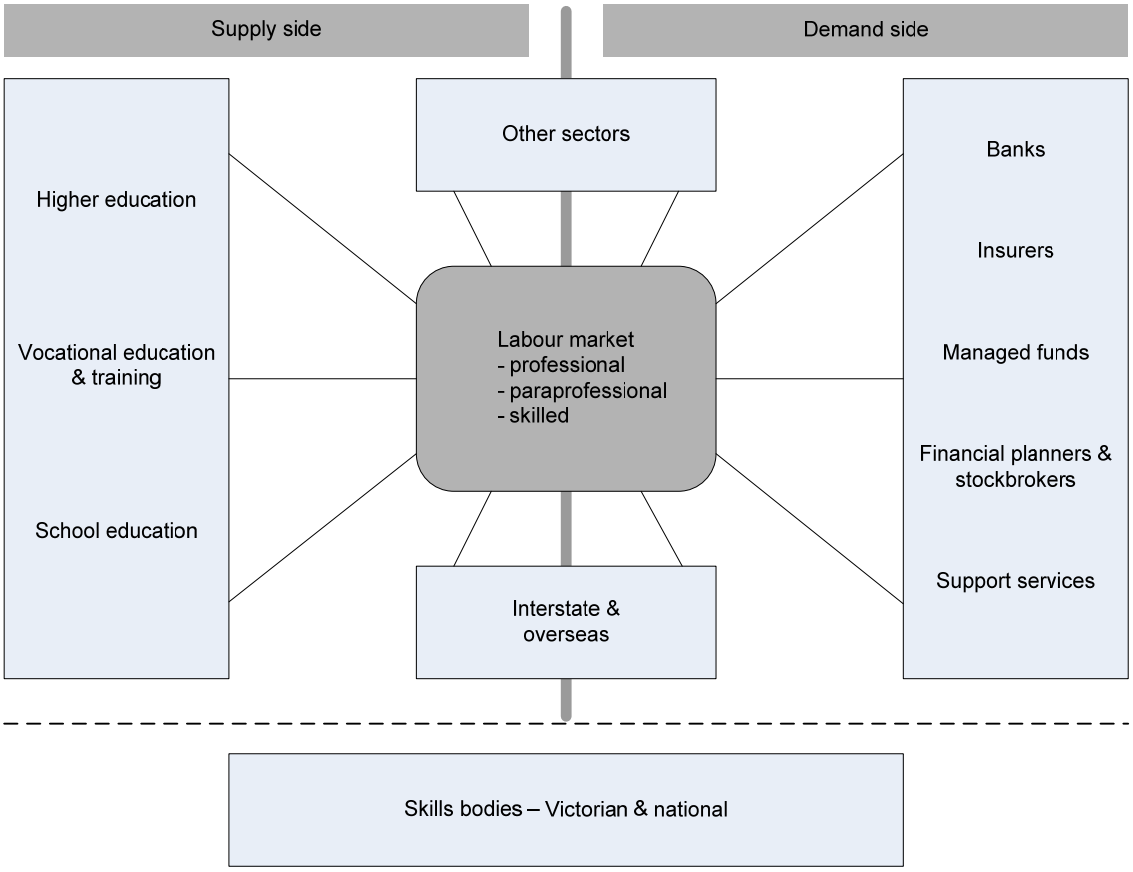
In addition to the school system, there are vocational education and training (VET) and higher education institutions.

More than 1300 providers are registered to deliver VET in Victoria. They are a mix of universities (dual sector), Tertiary and Further Education (TAFE) institutes, Adult Community Education (ACE) providers and private for-profit organisations. These organisations are funded from government and private sources. In 2008, 577 providers reported VET activity.

The higher education sector in Victoria, at 30 June 2009, had nine public universities and one self-accrediting higher education institution, 54 non self-accrediting providers approved to deliver accredited higher education qualifications, and four interstate universities approved to deliver higher education courses to overseas students in Victoria.

Sources: DIIRD 2009a, p. 73; 2009b, p. 5.

Figure 6.1 The financial services labour market



Source: VCEC.

VET providers in Victoria offer courses that lead to qualifications in business administration, commerce, management, accounting, human resource management, project management, marketing, advertising, property services and information technology. In 2008, around 19 660 students enrolled in VET courses leading to financial services industry qualifications mainly at the Diploma level. In addition, nearly 18 500 students enrolled in VET courses leading to more general business services industry qualifications (appendix B).

Undergraduate and postgraduate courses at Victorian universities include, for example, principles of finance, derivative securities, risk management and regulation, international finance, finance law, financial planning and advising, treasury management, financial econometrics, options and futures, and portfolio management. In 2008, about 97 000 students were studying commerce and management with Victorian universities (appendix B).

6.2.1 Government and industry skills bodies

There is significant government involvement in the funding and provision of education and training relevant to the financial services sector. The Victorian Government provides nearly half of the funding for the VET sector in Victoria. The Commonwealth Government provides about 17 per cent (DIIRD 2009b, p. 23). The Commonwealth Government has primary responsibility for funding higher education.

A number of state-based advisory, funding and regulatory bodies operate in the skills formation system.

- Skills Victoria analyses and advises on Victoria's skill needs, and acts as the system managers for the VET sector (Skills Victoria 2009a).
- The Victorian Skills Commission advises the State Government on post compulsory education and training, funds training and further education, and regulates the apprenticeship and traineeship system (VSC 2008).
- Industry Training Advisory Boards (ITABs) identify and advise on vocational training needs for industries in Victoria. Business Skills Victoria is the ITAB for the business, finance and property services industries (BSV 2009).
- The Victorian Registration and Qualifications Authority (VRQA) registers education and training providers in Victoria and accredits courses offered by these providers (VRQA 2010).

Nationally, there are policy, advisory and regulatory bodies that participate in the skills formation system.

- The Department of Education, Employment and Workplace Relations (DEEWR) is the Commonwealth body providing national leadership in

education and workplace training, transition to work, and conditions and values in the workplace (DEEWR 2010).

- Skills Australia advises the Commonwealth Government on current, emerging and future workforce development needs and workforce skills needs (Skills Australia 2009b).
- Industry Skills Councils (ISCs) work to involve industry in the development of nationally applicable education and training. Innovation and Business Skills Australia (IBSA) is the ISC covering the financial services sector (IBSA 2009c, p. 4).

There are also national quality assurance arrangements. The National Quality Council (NQC) oversees quality assurance and ensures national consistency in the application of the Australian Quality Training Framework standards for the audit and registration of training providers. The NQC also endorses training packages (SCRGSP 2010, p. 5.8). In addition, the Council of Australian Governments (COAG) recently agreed to establish a new national regulator for the VET sector (section 6.4.7).

6.2.2 The financial services workforce

The financial services workforce in Victoria has averaged around 100 000 in recent years (chapter 2). Key characteristics of the workforce include:

- most workers are aged between 25–49 years
- employment is broadly even by gender
- most workers are employed on a full-time basis
- the proportion of employees with higher level qualifications is greater than that for all industries
- average earnings are significantly above that for all industries.

Further detail on Victoria's financial services workforce is contained in appendix B.

6.2.3 Regulatory environment

The regulation of education and training providers in Victoria involves registration and accreditation (section 6.4.7) while financial services providers may be required to comply with licensing and training requirements.

The Australian Securities and Investments Commission (ASIC) administers a national licensing regime for providers of financial services. Under this system, people who carry on a business of providing financial services[2] are required to

[2] Financial services encompass, for example, providing financial product advice, dealing in financial products, or providing depository services.

hold an Australian financial services licence, unless certain exemptions apply. Licensees can appoint or 'authorise' representatives to provide financial services on their behalf (ASIC 2010a). Licensees and their authorised representatives, who provide financial product advice to retail clients, must meet minimum training standards.

As a result of the Commonwealth Government taking over responsibility for the regulation of consumer credit, ASIC is preparing to introduce a national licensing regime for credit providers (such as finance brokers and mortgage managers). Under this regime, people who engage in credit activities will have to register with ASIC and apply for an Australian credit licence, unless certain exemptions apply. Representatives who engage in credit activities on behalf of a registered person or licensee are exempt from registering or applying for a licence (ASIC 2010b).

6.3 Identifying skill shortages and gaps

In submissions and consultations, a number of inquiry participants expressed concern about skill shortages and gaps, which are defined as follows.

- Skill shortages exist when employers are unable to fill or have considerable difficulty filling vacancies for an occupation, or significant specialised skill needs within that occupation, at current levels of remuneration and conditions of employment, and in reasonably accessible locations (DEEWR 2008, p. 5).
- Skill gaps exist where existing employees lack the required qualifications, experience and/or specialised skills to meet the firm's skill needs for an occupation (DEWR & NCVER 2002, p. 3). Skill gaps are discussed in box 6.2.

Box 6.2 Skill gaps in the financial services sector

Some inquiry participants in consultations and roundtables reported skill gaps in a number of areas, including: interpersonal and communication skills (also known as 'soft' skills); risk management and compliance skills; sustainable and ethical investment skills; project management skills; insolvency management skills; and finance skills for non-finance managers.

A survey of 350 senior professionals working in the Australian financial services industry reported that 55 per cent of respondents believe that, since the global financial crisis began, a notable capability or skills gap has emerged within their organisations. Around one-third of respondents believe that the greatest skills gap in financial services will exist among professionals and industry specialists (Finsia & Chandler Macleod Group 2009, pp. 10, 16).

Sources: Consultations; roundtable 1; Finsia & Chandler Macleod Group 2009.

This section primarily examines the available evidence on skill shortages in the financial sector nationally and in Victoria. The Commission has drawn on a range of sources to gain an overall picture of the sector's skill needs in recent years.

6.3.1 National evidence

The Australian Bankers' Association (ABA) conducted research in 2007 that examined labour supply and demand until 2012. At that time, the research identified significant shortages in financial planning, business banking and customer service roles (sub. 9, p. 6).

More recent national surveys also point to skill shortages in particular areas of the financial services labour market. In a survey of more than 400 Australian financial and human resource managers in 2009, nearly two-thirds of companies believed there is a shortage of high quality finance and accounting professionals in Australia, despite the global financial crisis (Robert Half 2009, p. 1).

IBSA's environmental scan in 2009 reported a small number of occupations that were in demand in the financial services sector including:

- financial planners
- superannuation funds managers
- credit/audit compliance managers
- financial services managers
- insolvency officers (IBSA 2009a, pp. 80–81).

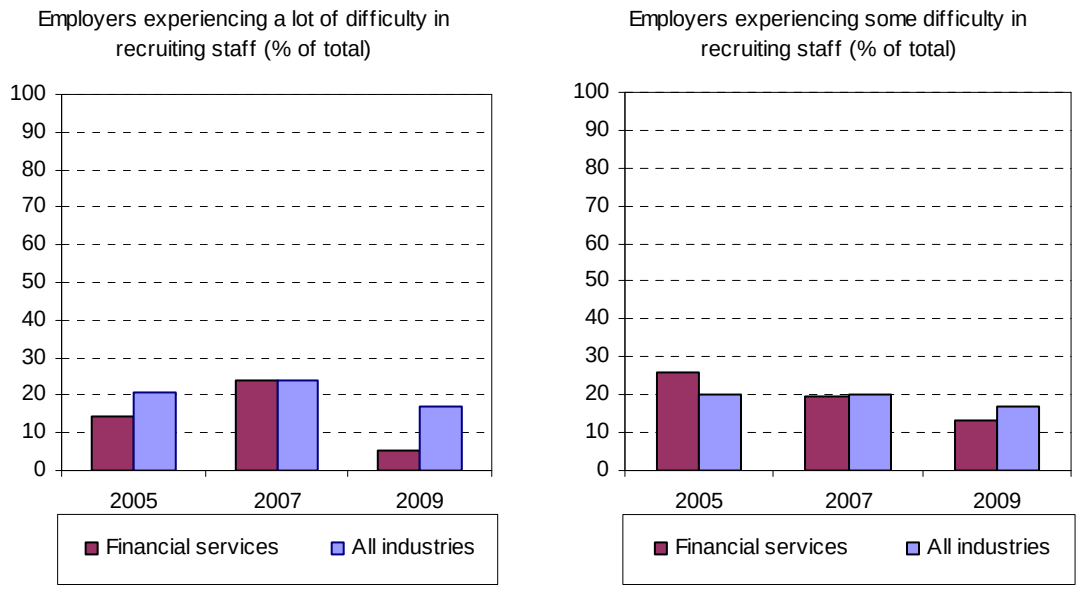
The National Centre of Vocational Education Research (NCVER) surveys employers using the VET system biennially. It found that, in 2009, only 5 per cent of employers in the financial services sector in Australia reported great difficulty in recruiting staff and about 13 per cent reported some difficulty in recruiting staff. This is less than the national average (figure 6.2). Moreover, the difficulty in recruiting staff eased between 2007 and 2009. A key reason for this easing is the impact of the global financial crisis.

Another way of identifying areas of skill shortages in financial services is by examining the occupations on the Critical Skills List maintained by the Commonwealth Department of Immigration and Citizenship (DIC) (DIC 2009).[3] There are only a couple of occupations on the list that seem relevant to the financial services industry. These include accountants and computer professionals (various specialities). The National Institute of Accountants (NIA) noted that, despite the global financial crisis, there is, at least

[3] These occupations are considered by DIC as being in critical shortage and eligible for priority processing for general skilled migration. The Critical Skills List was adopted as an interim measure while the Migration Occupations in Demand List was being reviewed (DIC 2010b).

for the foreseeable future, a skills shortage in the accounting and audit professions (NIA 2009, p. 5).

Figure 6.2 **Employers experiencing difficulty in recruiting staff, financial services, Australia[a]**



[a] Some of the estimates have a relative standard error greater than 25%.

Sources: NCVER 2009a, 2009b.

While the national evidence points to a small number of occupations that are in high demand, it does not shed much light on the magnitude or depth of these skill shortages. That said, the NCVER survey suggests that the extent of any shortages being experienced by employers is not particularly widespread. Moreover, it is likely that the global financial crisis has moderated the sector's demand for skilled labour.

6.3.2 Victorian evidence

There are several sources of information on skill shortages in the financial services sector in Victoria, though some are dated. The Victorian Employers' Chamber of Commerce and Industry (VECCI) conducted a skills survey in 2006 covering industries that included the financial services sector. It reported skilled vacancies for financial investment advisers and accountants (VECCI 2007, p. 33). In the 2006 *Regional Skill Shortages Survey*, of the 297 vacancies reported, 191 were considered difficult to fill including positions for financial investment advisors, accountants and accounting clerks (DVC 2006, p. 15).

More recently, the *Melbourne Metropolitan Skills and Labour Needs Survey 2008*, provides evidence of skill shortfalls in the financial services sector. About 160 businesses in this sector were surveyed and the results were weighted to represent the 6861 employing financial services businesses in the Melbourne metropolitan area.[4] Table 6.1 shows the top ten occupations that employers reported difficulty filling.

Table 6.1 Occupations most difficult to fill, financial services, metropolitan Melbourne, 2008[a]

Occupation	*Responses*	
	(no.)	(%)
General clerks	459	6.7
Accountants	354	5.2
Credit & loans officers	301	4.4
Sales representatives	232	3.4
Financial investment advisers & managers	221	3.2
Sales assistants (general)	124	1.8
Advertising & sales managers	108	1.6
Financial brokers	105	1.5
Manager NFI[b]	95	1.4
Insurance agents	94	1.4

[a] All data are weighted. The data can be interpreted as follows: in the case of general clerks, 459 employers (6.7 per cent of employers in the sector) reported difficulty in filling vacancies for this occupation. [b] No further information.

Source: Workforce Victoria 2008.

Based on these survey results, it appears that skill shortages in the financial services sector in Victoria are not particularly widespread among businesses. For each occupation listed in table 6.1, only a small percentage of businesses in the sector reported difficulties in filling those positions. Business Skills Victoria also reported an acute shortage of accountants, particularly auditors (BSV 2008, p. 8).

In a recent assessment, Skills Victoria (2010b) identified shortages in tax, risk and compliance professionals, and financial and management accountants. It also noted that demand is likely to remain high for wealth management advisers, financial planners and superannuation planners.

[4] The sample represents about 2 per cent of the business population in the sector.

A further source of information on the skills situation in the financial services sector in Victoria is the Government's list of occupations sought from overseas. The Victorian Government offers visa sponsorship to a small number of occupations that are relevant to the financial services field; that is, accountants, external auditors, and computing professionals (Victorian Government 2009c, pp. 3–4).

Although the data sources have limitations, the most recent Victorian evidence, like the national evidence, indicates that skill shortages in the financial services sector affect only a small number of occupations and are not particularly widespread among businesses. 'Financial services' also was not identified as an area of skill shortage in the Victorian Government's *Securing Jobs for Your Future — Skills for Victoria* (Victorian Government 2008b, p. 5).

While some of the Victorian evidence examined above is no longer current, the Commission's recent consultations and roundtable (appendix A) with a range of industry participants suggest that the conclusion still holds. Furthermore, it is likely that the global financial crisis, which began in 2008, would have dampened the demand for a range of financial services, with flow-on effects for labour demand in the sector.

Given that immediate skill shortages appear to be limited, this chapter now considers the systems that allow the education sector, employers and employees to predict and respond to future changes in the demand for, and supply of, different groups of skilled people.

6.4 Ensuring sufficient supplies of skilled labour

While skill shortages are not currently a major problem for Victoria's financial services sector, some inquiry participants noted that shortages could emerge as the economy gathers strength in coming years. It is important to ensure that the skill formation system remains responsive to industry and student needs into the future.

The financial services sector is a major investor in education and training of employees, and many occupations employed in the sector generally require high levels of entry-level training and skills. While a significant amount of this education and training is accredited, much of the in-house training that occurs after employees have entered the industry is not accredited.

Based on information gathered from submissions, consultations and roundtables together with additional research, the Commission has focused its attention on the following areas:

- recent funding reforms
- information on current and future skill needs

- financial literacy and career information in schools
- the range and type of qualifications available
- recognition of prior learning and credit transfer
- consultation between industry and education and training providers
- accreditation, quality assurance and labour mobility
- skilled migration.

6.4.1 Recent funding reforms

The Victorian Government recently initiated major reforms in the Victorian training system through *Securing Jobs for Your Future — Skills for Victoria*. This initiative will deliver $316 million in extra funding and provide for an additional 172 000 training places over four years. The reforms also introduce the Victorian Training Guarantee which makes government subsidised training places available to all eligible Victorians at all levels of skills development, subject to eligibility requirements (Victorian Government 2008b, p. 15; 2008c, p. 1).

Commenting on these reforms, the Department of Innovation, Industry and Regional Development (DIIRD) stated that:

> The aim is to encourage more people into VET for the first time, and for Victorians to upgrade their qualifications. The reform has a strong focus on lifting the qualifications profile of Victoria's working-age population. (DIIRD 2009a, p. 64)

A key feature of the new skills system is that it will be demand driven; that is, the number of training places available will be determined by the number of people seeking them, not by government or training providers (Victorian Government 2008b, p. 18). This is a major departure from the former funding approach which focused on the supply of education and training rather than meeting the demand.[5]

Implementation of the new system commenced in July 2009 and will be phased in over the next four years (2009–2012), starting with Diploma and Advanced Diploma level qualifications. The Victorian Skills Commission will monitor the changes, and the Government has indicated that there will be a mid-term review of the new system to check that Victoria is getting the intended outcomes (Victorian Government 2008c, p. 2).

The Commission supports the scheduling of a mid-term review. The monitoring and reporting of reform outcomes is good practice, and is an integral part of the process of continuous improvement. The Commission anticipates that the mid-

[5] Some other problems with previous arrangements included the lack of alignment between the allocation of government subsidies and individual need for training or retraining and between the benefits and costs of training, and the lack of incentives to support up-skilling (Victorian Government 2008a, pp. 9–10).

term review will examine the early outcomes of the reforms and ascertain whether there is a need for further adjustments to improve the operation of the system. To enable proper evaluation, it is important that a comprehensive set of performance indicators is developed and that data for these indicators are collected.

To ensure transparency and accountability, the Commission considers that the results of the mid-term review should be published. The system should also be evaluated after the reforms are fully implemented and the results published.

6.4.2 Skill needs information

There are many participants in the financial services labour market and the skills system (section 6.2). For the market and system to operate efficiently, participants need to be well-informed about skill needs, training options and employment opportunities. It is therefore important to have high quality and timely information about skill needs in the financial services sector. This typically involves the analysis of the demand and supply of skilled labour.

Information on current skill needs

Considerable market information is available about current skill needs in the financial services sector. For example, general and specialist websites (including those maintained by labour hire companies) list job vacancies in the sector. There is also private sector analysis of skill trends, such as the *Clarius Skills Index* and *The Hudson Report* (Clarius Group 2010; Hudson 2010). These sources of information can give an indication to students and workers of what occupations are currently in demand.

In addition, information on, and analysis of, skill needs is compiled or undertaken by a number of government and industry skills bodies at the national and state levels. For example, Workforce Victoria conducts skill and labour needs surveys to map the current and emerging skill needs of the state. Its survey program is broken into metropolitan and regional research:

- the *Melbourne Metropolitan Skills and Labour Needs Survey* was conducted in 2008 (Workforce Victoria 2008)
- the *Regional Skills Shortage Survey* was conducted in 2006. In a national first, the Victorian Government and the then Commonwealth Department of Employment and Workplace Relations joined together to develop and implement this survey (DVC 2006, p. 1).

These surveys provide a snapshot of skill needs at a point in time. Thus their value will tend to diminish as circumstances change. The Commission understands that, going forward, these respective surveys will be conducted biennially.

Given Victoria's move to demand-driven training provision, it could be argued that such surveys will become less relevant. However, reasons for continuing some form of research and monitoring of skill shortages include:

- having the ability to objectively assess calls for changes in skilled migration
- helping decision makers to (a) plan long-term investments and (b) assess whether the demand-driven model actually meets industry needs
- helping potential students to identify employment opportunities.

The Commission supports a cost-effective assessment process which uses sample surveys, supplemented by information from labour hire companies and industry consultations to compile a picture of skill needs.

The Commission considers that, in a practical sense, drawing on the current information held by practitioners is likely to provide a robust global picture on current shortages. While adequate for decision making on current gaps, these estimates would not be sufficient to project future shortages with enough confidence to support decision making. For forecasts, more rigorous estimates are likely to be needed.

Information request: What is the appropriate frequency of the metropolitan and regional skills and labour needs surveys, given the changes under the new skills system?

Information on future skill needs

Because completion of education and training generally takes a number of years, the supply of skilled labour is somewhat constrained in the short run — unless supply is augmented by attracting 'job ready' skilled labour from other sectors or overseas. In other words, there can be long lags (typically between 1–5 years) for the education and training system to produce skilled labour whilst demand can change quite rapidly.

The VET and higher education sectors seek to provide courses that will meet future demands of individuals and businesses. If the changes in quantity and types of skills needed can be anticipated, this may avoid the development of redundant capacity; that is, excess capacity of skilled labour and excess capacity in education and training institutions (Richardson & Tan 2007, p. 8). This appears to be one rationale for preparing skill forecasts or projections.

In addition to providing strategic advice and analysis of the state's skill needs, Skills Victoria prepares labour and training forecasts for Victoria which are published on its website. To date, it has published employment forecasts for a

number of industry sectors.[6] The Commission understands that Skills Victoria intends to progressively publish forecasts for other industry sectors.

DEEWR prepares and publishes five-year employment projections for the financial services sector in Australia. The projections are updated annually. The department noted that a 'certain degree of uncertainty' is attached to these projections (DEEWR 2009a, p. 6).

Although skills projections are prepared at the state and national levels, there has been vigorous debate about the use of skills forecasts or employment projections (Lewis 2008, p. 7). The OECD Review of VET in Australia questioned the reliability of skills forecasts, and considered that information from forecasts should inform user choice rather than government planning:

> … despite their methodological problems …, skills forecasts can provide some useful information to labour market actors who remain free to make their own decisions. (Hoeckel et al. 2008, p. 27)

The accuracy of skills forecasts in Victoria is now less critical because they are no longer being used to allocate training places. These forecasts, however, have some value in pointing to the likely future direction of labour demand — based on the latest available information — which may assist participants in the labour market and skills system in making decisions.

The quality of any forecasts depends on the information used, assumptions adopted and the inherent volatility of the business environment. It is important that, to produce forecasts, a rigorous modelling methodology, the latest available information and soundly-based assumptions are used. The Commission considers that Skills Victoria could prepare and publish employment forecasts for the financial services sector at least annually. It is also important that these forecasts reach their intended users (including industry, employers and students).

Draft recommendation 6.1

That the Department of Innovation, Industry and Regional Development prepare and publish, as soon as is practicable, employment and training forecasts for the financial services sector in Victoria. These forecasts should be updated and published at least annually using the latest available information.

[6] The industries include: accommodation, cafes and restaurants; agriculture, forestry and fishing; building and construction; electricity, gas and water; government administration and defence; health and community services; and transport and storage (Victorian Government 2009e, p. 1).

Occupational codes

The Australian Financial Markets Association (AFMA) argued that a significant structural impediment that makes it very difficult to identify skill shortages in the financial services sector is the Australian and New Zealand Standard Classification of Occupations (ANZSCO) — the primary instrument used to measure labour shortages in Australia. AFMA argued that the codes are out of date and do not include most of the operations and 'middle office' job roles in the banking sector (which account for over 60 per cent of all jobs in the banking sector) (sub. 8, p. 2).

ANZSCO was developed jointly by the Australian Bureau of Statistics (ABS), Statistics New Zealand (SNZ), and the Commonwealth Department of Employment and Workplace Relations (now DEEWR) for use in the collection, analysis and dissemination of occupation statistics in Australia and New Zealand. It was intended to improve the comparability of occupation statistics between the two countries and with the rest of the world (ABS & SNZ 2006a, p. v).

Analysis by AMFA identified a number of banking sector job roles that are not included in the ANZSCO codes (table 6.2).

Table 6.2 Banking sector job roles not in ANZSCO[a]

Operations roles	*Middle office roles*	*Customer service & advising*
Settlements officer (treasury & commodities)	Operational risk manager	Financial product sales
Settlements officer (equities)	Treasury risk manager	Retail banking sales
Reconciliation officer	Credit analyst	Retail relationship manager
Investigation officer	Treasury credit controller	Telephone banker
Operational risk and control officer	Treasury compliance manager	Paraplanner
Custody operations officer	Treasury market risk officer	
Custody unit registry administrator	Retail product risk manager	
Custody settlements officer		

[a] AFMA analysis.

Source: AFMA, sub. 8, pp. 2–3.

The issue of occupational codes has been raised by industry skills councils in discussion forums convened by Skills Australia:

> Each forum commented [that] the codes were problematic. This stems from the fact [that] not all occupations are represented or that the occupations do not adequately reflect the nature of the jobs at the enterprise level. The absence of

> such alignment has had a number of consequences for the availability of training funding when this is confined to ASCO-listed occupations.[7] (The Nous Group 2008, p. 27).

The forums pointed out that the codes were developed for a particular ABS purpose and that problems arose when the codes were used for other purposes, such as the identification of skill shortages or the allocation of training funds (The Nous Group 2008, p. 27). At the *Futures in Finance Skills Forum*, concerns were expressed that future skill needs were often based on past occupational categories and did not address new and emerging skill groupings (FSU 2008, p. 20).

The concerns regarding ANZSCO codes have been recognised by Skills Australia. One of its key priorities in 2008-09 was to conduct a pilot project to review occupations within the civil construction industry to inform a broader review of ANZSCO. Skills Australia has been working with relevant stakeholders to inform advice to be provided to the Deputy Prime Minister in early 2010 (Skills Australia 2009, pp. 10, 13).

The emergence of new occupations in the financial services sector (and other industry sectors) in recent years suggests that a broader review of ANZSCO may be warranted. The Commission considers that the Victorian Government could usefully raise this issue with the Commonwealth Government through its representatives on national advisory bodies such as the Australian Statistics Advisory Council. One issue that needs to be considered when updating classifications is the impact on the compatibility of the statistics over time and with international standards.

As part of a broader review, there would appear to be a need for a process of identifying new and emerging occupations as well as occupations that have become obsolete in the financial services sector. This process would require the involvement of industry, possibly through joint government-industry working groups.

Draft recommendation 6.2

That the Victorian Government, through its representatives on national advisory bodies such as the Australian Statistics Advisory Council, report the limitations of the Australian and New Zealand Standard Classification of Occupations in the financial services sector, and advocate that the classifications in that sector be updated to reflect current occupations.

[7] ASCO refers the Australian Standard Classification of Occupations which was superseded by ANZSCO.

6.4.3 Financial literacy and career information in schools

In consultations, some inquiry participants commented on secondary school students' (1) financial and consumer literacy and (2) knowledge of career options in the financial services sector.

Some inquiry participants expressed concern about school students' understanding of financial matters such as managing mobile phone contracts. The Commission was also told that a lack of financial literacy makes school leavers less 'job ready' for the financial services sector. This issue has been recognised nationally. In 2005, the Ministerial Council on Education, Employment, Training and Youth Affairs directed the development of the National Consumer and Financial Literacy Framework. The framework outlines the key knowledge, understandings, skills and values in consumer and financial literary that students can acquire through their studies in English, Mathematics, Science, Humanities and other subjects. The intention is that, by the end of compulsory schooling, students will have been exposed to concepts such as income and expenses, savings, credit and interest, financial records, consumer contracts, and consumer rights and responsibilities (AGNPDRG 2007, pp. 1–2).

In addition, the Commission's consultations with education and training providers indicated that secondary school students (and their parents) are often not aware of the full range of employment and training possibilities in the financial services sector. There appears to be a number of misconceptions which may be distorting students' career choices. For example, there is a perception among students that the primary path to a career in financial services is by attaining an honours or postgraduate degree in business or finance from a higher education institution — when many occupations in the sector require a vocational qualification from a VET provider. There are also misperceptions about the jobs available in the industry; for instance, many students have a narrow view about what constitutes the industry (for example, that investment banks are a major source of employment).

While considerable career information is available (from government and market sources), such misconceptions suggests that this information is not reaching, or not being accessed by, its intended audience. Some inquiry participants suggested that the employers could do more to promote or market career opportunities in the sector. For example, employer or industry associations could emphasise the breadth of employment opportunities and pathways in information packages provided to careers advisers or directly to students and their parents within school settings, such as careers seminars.

6.4.4 Qualifications and unaccredited training

Skill acquisition can typically occur in two key ways (1) through education and training (often leading to qualifications) and (2) on-the-job training and experience. As noted by Lowry et al. (2008, p. 10), qualifications are not skills in themselves but are a proxy for skills. Qualifications can assist employers to identify appropriate workers and provide individuals with portable credentials. Courses leading to accredited qualifications are offered by VET and higher education institutions in Victoria.

VET qualifications

At the national level, IBSA prepares the Financial Services Training Package.[8] The package contains skills standards that apply to enterprises and individuals and to people working in the financial services sector. There are 32 qualifications in the current training package ranging from Certificate I in Financial Services to Advanced Diplomas in a range of specialisations (IBSA 2009d). The current package was endorsed by the NQC.

IBSA described the training package as:

> … a mix of generic qualifications providing flexible entry and progression pathways into the industry through training and certification, and specialist outcomes that reflect an occupational stream or, in some cases, professional body requirements. (IBSA 2009b, p. 18)

A key benefit of the qualifications in the package is that all are fully transferable and portable across Australia, no matter who the provider of the course is or where in Australia the course is delivered (FSU 2008, p. 37). The national training package is recognised by industry, training and financial regulators.

Table 6.3 shows the take-up of the Financial Services Training Package qualifications in Victoria. Two key observations can be drawn from the table. First, a small number of accounting-related qualifications represented about three-quarters of total enrolments in financial services package qualifications in Victoria. Second, there were no or few enrolments for more than half of the qualifications listed. While the take-up of many qualifications in the package appears to be low, there are some limitations to the dataset; it does not include all training delivered with government support nor does it include non-publicly funded delivery (IBSA 2009b, p. 16).

[8] IBSA also prepares the Business Services Training Package which may be another pathway to employment in the financial services sector.

Table 6.3 **Take-up of Financial Services Training Package qualifications, Victoria, 2007[a]**

Qualification	*Number enrolled*	*Per cent*
Certificate II in Financial Services	16	0.1
Certificate III in Financial Services (FNS30104)	356	2.6
Certificate III in Financial Services (FNS30107)	3	0.0
Certificate III in Insurance Services	..	..
Certificate III in Financial Services (Accounts Clerical)	3642	26.3
Certificate III in Financial Services (Mercantile Agents)	..	..
Certificate IV in Financial Services (FNS40104)	2131	15.4
Certificate IV in Financial Services (FNS40107)	..	..
Certificate IV in Financial Services (Credit Management)	55	0.4
Certificate IV in Insurance Services	..	..
Certificate IV in Financial Services (Accounting)	2732	19.7
Certificate IV in Financial Services (Financial Practice Support)	..	..
Certificate IV in Financial Services (Finance/Mortgage Broking)	..	..
Diploma of Financial Services (FNS50104)	361	2.6
Diploma of Financial Services (FNS50107)	17	0.1
Diploma of Accounting	2799	20.2
Diploma of Financial Services (Finance/Mortgage Broking Management)	..	..
Diploma of Financial Services (Conveyancing)	156	1.1
Diploma of Financial Services (Financial Planning)	63	0.5
Diploma of Financial Services (Superannuation)	..	..
Diploma of Financial Services (Banking)	92	0.7
Advanced Diploma of Financial Services	11	0.1
Advanced Diploma of Accounting	1406	10.1
Advanced Diploma of Financial Services (Conveyancing)	..	..
Advanced Diploma of Financial Services (Financial Planning)	13	0.1
Total	13853	100.0

[a] Publicly funded training.

Source: IBSA 2009b.

That said, at the *Futures in Finance Skills Forum* in 2008, it was reported that use of the training package has been low among some in the industry:

> The Financial Services Training Package attempts to set a benchmark for the competencies required for roles in the industry, but awareness and usage of the Training Package is relatively low amongst some participating in the Forum. (FSU 2008, p. 25)

Moreover, it was reported that people working in learning roles in finance organisations have often experienced difficulty in convincing those in more senior positions of the value of the package as part of their workforce development strategies and programs (FSU 2008, p. 22).

IBSA, with input from industry, has developed a new draft package containing 47 qualifications. There has been an 'unbundling' of insurance industry qualifications from the previous financial services generic qualifications. The banking, credit/lending and financial markets sectors have also defined new qualifications (IBSA nd, p. 3).

Higher education qualifications

Higher education qualifications are generally undergraduate degrees or post graduate diplomas or degrees in business, accounting, commerce, management and finance. These qualifications can provide the skills platform for a wide range of jobs in the financial services sector. Some new qualifications have been developed specifically for the sector, such as La Trobe University's Master of Islamic Banking and Finance, and Victoria University's Graduate Certificate in Superannuation Management.

Several suggestions from inquiry participants and other sources regarding higher education courses and qualifications are aimed at addressing skill shortages or particular skill gaps:

- 'Bridge' diplomas: The Financial Services Institute of Australasia (Finsia) has argued that government and industry should give consideration to additional methods of sourcing talent, such as encouraging 'bridge' diplomas for non-business degree holders which would increase the number of finance job-ready graduates (Finsia 2009b, p. 5; Finsia & Roy Morgan Research 2008, p. 18).
- Internships, industry placements, and cooperative education programs: At the *Futures in Finance Skills Forum,* it was reported that university graduates often lack 'soft skills' such as sales and customer service skills (FSU 2008, p. 16). In the Commission's consultations, inquiry participants also pointed to skill gaps in areas such as interpersonal and communication skills (box 6.2). One way to address these skill gaps might be through internships with financial services businesses and cooperative education programs (FSU 2008, p. 16).
- University provision of specialised courses: One inquiry participant suggested that there may be scope for universities to provide short courses to financial institutions such as superannuation and sovereign funds to address their specialised skill needs.

Some inquiry participants told the Commission that the Chartered Financial Analyst (CFA) qualification is highly valued in the industry and is seen as a global standard (box 6.3). The CFA Institute does not have an office in Australia. It was suggested that Melbourne could become a centre for the CFA Institute in Australia, which may raise Melbourne's profile as a centre for financial education and possibly attract students to Melbourne.

Box 6.3 Chartered Financial Analyst Program

The Chartered Financial Analyst (CFA) Program is a graduate-level, self-study curriculum and examination program for investment specialists administered by the CFA Institute. The CFA Program sets a global standard for investment knowledge, standards and ethics. Earning the credential can serve as a 'passport' to entry or advancement within the investment profession or to work in other countries. It tells clients, employers and colleagues that the charterholder has mastered a rigorous curriculum covering a broad range of investment topics and that he or she is committed to the highest ethical standards in the profession.

Source: CFA Institute 2010.

Although there is some evidence of innovation in course development, some professional associations have argued for curriculum renewal. For instance, CPA Australia (2009, p. 2) argued for an increase in the capacity of higher education institutions to engage in curriculum renewal that better reflects the contemporary demand of business in a rapidly changing globally competitive world. CPA Australia also argued for greater emphasis on soft skills in curriculum development. The Institute of Chartered Accountants in Australia (ICAA) noted that its members had expressed concern about the lack of 'work ready' graduates being produced by Australian universities (ICAA 2008, p. 1).

Information request: The Commission seeks further information from industry, employers and higher education providers on the advantages and disadvantages of 'bridge' diplomas, internships, industry placements, cooperative education programs, and provision of specialised courses.

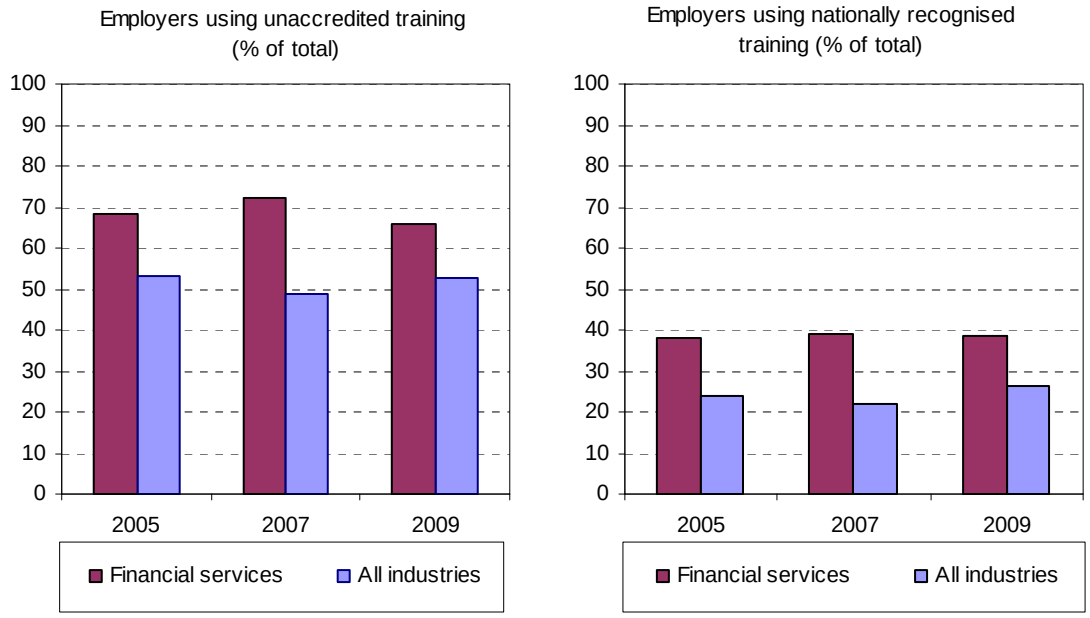
Unaccredited training

At the VECCI Victoria Summit in 2009, concerns were raised by some employers about the value and accessibility of accredited training and qualifications, including in the financial services sector. Apparently, these employers have stopped using Certificate III level qualifications, and returned to an in-house, non-accredited training model (Workplace Futures Task Group 2009, p. 11).

Survey evidence indicates that the proportion of financial services employers using unaccredited training is higher than the proportion using nationally

recognised training (figure 6.3).[9] That said, the proportions of employers in the sector using accredited and unaccredited training significantly exceed those for all industries.

Figure 6.3 **Employers' use of nationally recognised and unaccredited training, Australia[a]**



[a] Nationally recognised training is defined as nationally recognised training other than as part of an apprenticeship or traineeship.

Source: NCVER 2009b.

In choosing between accredited and unaccredited training, businesses are likely to consider factors such as the appropriateness of courses (and the likely benefits to the business), duration and cost (including tuition fees[10] and lost productivity associated with the time employees spend away from the workplace) and implications for staff retention.

According to the Workplace Futures Task Group (2009, p. 11), the key reason cited by business for the comparatively high level of unaccredited training was that government-supported training requires the completion of a full qualification, whereas the workplace need is only for specific competencies to meet key job or project requirements.

[9] The data in figure 6.3 does not include nationally recognised training that is part of traineeships.

[10] Tuition fees and other charges are generally paid by the student unless the employer pays the fees under an award or voluntarily (Skills Victoria 2009b, p. 8).

Business use of training appears to place priority on meeting workplace needs rather than achieving qualifications for their workers. IBSA stated that:

> Enterprise training is, naturally, focussed on workplace needs so although in-house training may relate to FNS04 [Financial Services Training Package] competencies and qualifications and in some cases lead to formal recognition for individuals, it is not the primary driver for the training … (IBSA 2009b, p. 17)

IBSA (2009b, p. 17) also noted that private training organisations offer short courses that relate to aspects of financial services but are not based on competencies or qualifications from the training package.

However, the use of unaccredited training has implications for labour mobility. While this training may benefit individual businesses by meeting specific workplace needs, workers do not gain a recognised qualification — an outcome which may reduce their mobility within the industry. This point was also made in the roundtable discussion (appendix A). Consequently, if labour mobility is impeded, businesses have a longer period over which to obtain a return on their investment in training. The incentives for using accredited training for businesses and employees do not necessarily align closely.

Considerable resources and consultation have gone into developing the Financial Services Training Package to provide generic skill sets for the financial services sector. But, as noted above, the take-up of the package has been relatively low for a number of qualifications. This appears to be a broader issue; the OECD Review of the VET sector reported that many training packages in Australia are little used (Hoeckel et al. 2008, p. 36). This, it should be noted, is occurring in a sector that invests substantially in training and suggests an underlying problem may be in the value perceived by businesses.

The Commission sees scope for more flexible use of the Financial Services Training Package. In particular, the package offers the flexibility for businesses to select only those courses that will deliver specific competencies needed in their workplaces, although selective use of these courses would generally be on a fee-for-service basis. A further advantage is that many registered training organisations (RTOs) are already 'geared up' to offer these courses. In many cases, RTOs can customise courses whilst retaining the integrity of courses. Where businesses use these courses, workers will at least obtain some credit towards a nationally recognised qualification, which they may wish to complete at a later stage.

Moreover, the Commission's consultations revealed that students and workers are often not aware of the full range of training options offered by education and training institutions in Victoria. There appears to be a need for awareness-raising that points businesses, workers and students to relevant information sources about education and training options.

In this regard, it should be noted that businesses commonly would regard significant expenditures on skill formation and development as investments in their employees, and typically would expect a business case to support the commitment. In communicating with business, the Commission considers Business Skills Victoria could develop representative business cases for the training packages, including expected benefits, costs and returns and comparison with other training. This would help to ensure that business decisions about whether to use accredited or unaccredited training are fully informed and are not affected by misconceptions about the flexibility of accredited training or the benefits to business of such training. The take-up of accredited training would be helped by having more, and transparent, information about the performance of RTOs.

Draft recommendation 6.3

That the Victorian Government request Business Skills Victoria to develop representative business cases for the Financial Services Training Package and Business Services Training Package, including expected benefits, costs and returns and comparison with other training.

Victoria's skills reforms seek to address the need for information and awareness-raising through various initiatives, including the development of a qualifications navigator, a strengthened role for ITABs and a public information campaign. Additional funding will be provided to ITABs to work with the Victorian Skills Commission on a consolidated industry information service available to students, careers advisors and employers to facilitate the take up of training in areas of shortage (Victorian Government 2008b, pp. 18–21).

The Commission considers that the advantages of nationally recognised qualifications in the Financial Services Training Package and Business Services Training Package (which are most relevant to the financial services industry) should be highlighted in the consolidated industry information service and the public information campaign.

Draft recommendation 6.4

Information about nationally recognised qualifications — such as those in the Financial Services Training Package and Business Services Training Package — should be included in:

- **the consolidated industry information service being developed by the Victorian Skills Commission and Industry Training Advisory Bodies**
- **the Victorian Government's public information campaign about the new skills system.**

6.4.5 Recognition of prior learning and credit transfer

The issues of recognition of prior learning and credit transfer between VET and higher education institutions were raised in consultations.

Recognition of prior learning

In consultations, the Commission was told that some financial institutions did not recognise prior learning, which resulted in new staff (who were already compliant with ASIC Regulatory Guide 146) repeating training. Apparently this was done to manage compliance risks and meet licence conditions. It was also contended that ASIC policy recognises previous experience and skills but there are high thresholds to meet.

Recognition of Prior Learning (RPL) is granted when a provider gives recognition to a person for part of a course, or the whole course, without having to complete the study for that course. This is because the person is able to demonstrate that they have already undertaken the learning, through previous experience, or have developed the competencies in the workplace (Skills Victoria 2010a). RPL is granted after a formal assessment by teachers or assessors. Some Victorian universities have been seeking to improve their RPL services (box 6.4).

Box 6.4 Recognition of Prior Learning (RPL): Swinburne University of Technology

Swinburne University of Technology is a dual sector (VET and higher education), multi-campus educational institution offering students the opportunity to undertake studies from Certificate I through to PhD. The university has been providing professional and vocational teaching and learning for over 100 years.

Since the introduction of the Victorian Government's Maintaining the Advantage strategy in 2006, Swinburne's Financial Services team has been working to build its capacity to provide customer-focused quality recognition services. Key activities to achieve this have included:

- employing an RPL convenor for the School of Business to drive the recognition process, in particular in terms of industry engagement
- increasing RPL awareness among staff and prospective students
- employing an online convenor, who actively promotes and supports RPL among students using this mode of delivery
- building relationships with Swinburne's newly established Recognition Access Point, and through that, with local Skills Stores.

As a result of these activities, there was a substantial increase in RPL Financial Services student contact hour completions between 2006 and 2008.

Source: Swinburne University of Technology nd.

The major benefits of recognition of prior learning to the economy are avoiding unnecessary duplication of training, encouraging upgrading of skills and knowledge, improving employment outcomes, accelerating progression through learning programs, and saving time and money (Smith & Clayton 2009, p. 12).

At a seminar on skills formation in Australia, it was claimed that recognition by VET institutions of prior skills is limited, with RPL often failing to include all the skills that people have attained on the job with an employer (Lewis 2008, p. 13). Moreover, one of the issues raised consistently in discussion forums of industry skills councils was the need to simplify the processes for recognising prior learning. It was also contended that current processes were expensive (The Nous Group 2008, p. 23).

Information request: What scope is there to improve existing Recognition of Prior Learning (RPL) processes? Is there a need for additional measures to raise awareness about RPL among registered training organisations in relation to financial services skills? If so, what measures are needed?

Credit transfer between the VET and higher education sectors

Credit transfer is a process that gives credit for a unit of competency previously achieved. Some inquiry participants indicated that there may be scope for better integration between the VET and higher education sectors. In consultations, the Commission was told that universities sometimes do not recognise or give credit for subjects, courses or qualifications completed in the VET sector. One reason for such outcomes may be that universities are seeking to achieve or maintain a certain standard and reputation.

The Review of Australian Higher Education (2008) reported that there has been gradual improvement in pathways between VET and higher education:

> The proportion of domestic commencing undergraduate students admitted on the basis of prior TAFE study increased from 5.8 per cent in 1994 to 10.1 per cent in 2006. The proportion of students gaining credit (or exemption) for previous TAFE study increased from 2.4 per cent to 4.3 per cent over the same period. There are large differences between universities in the proportion of students admitted on the basis of TAFE qualifications or receiving credit for TAFE studies. (Review of Australian Higher Education 2008, p. 192)

While noting significant debate about the extent of the problem in this area, the review concluded that the VET and higher education sectors should continue to enhance pathways for students through the development and implementation of common terminology and graded assessment in the upper levels of VET (Review of Australian Higher Education 2008, p. 193).

There are Victorian initiatives aimed at improving credit transfer. For example, the VRQA has been developing a credit matrix which is a system for describing and comparing learning across all courses and qualifications (VRQA 2009a).

Information request: Are there any impediments to credit transfer for completed units or subjects in finance, business and commerce between vocational education and training institutions and higher education institutions in Victoria?

6.4.6 Consultation mechanisms

The quality of information collected through industry consultation, at the state and national levels, has been emphasised by various inquiry participants. As noted in section 6.2, industry skills bodies — such as Business Skills Victoria and IBSA — advise training authorities about skill shortages, qualifications and training packages. However, most of these bodies focus largely on VET sector skills rather than broad tertiary skill needs (Review of Australian Higher Education 2008, p. 189).

While some higher education institutions consult directly with financial services employers on curriculum development, it appears that consultation on matters such as skill needs is piecemeal and irregular. In the *Futures in Finance Skills Forum*, it was reported that a lot of companies do not have direct relationships with universities and that the relationships between universities and industry could be better (FSU 2008, p. 16).

In the roundtable discussions, it was noted that peak bodies play an important role in communicating industry needs to education providers. For example, in the accounting profession, organisations such as the NIA, CPA Australia and ICAA act as a conduit between the industry and education providers, feeding a coordinated view about what the industry needs from undergraduate level accountants. However, it appears that industry bodies in some other sectors of the financial services industry are often not as effective as the accounting bodies in their engagement with the education sector.

There seems to be scope to strengthen links and communication between higher education providers and financial services employers. This could be achieved by establishing an industry advisory panel to provide input to a national higher education committee, such as the Australian Business Deans Council (ABDC).[11] The industry panel could advise on industry needs, at least annually, with a focus on skill needs, qualifications and associated curriculum development. Panel

[11] The ABDC, which represents Australia's higher education business faculties and schools, is particularly concerned to improve business education through curriculum development, and forging strong relationships with the business community and government (ABDC 2010).

members would comprise senior managers from the human resource areas of financial services businesses.

The information and advice provided by such a panel would be useful for higher education institutions in reviewing and/or updating their curricula, qualifications and entry requirements. The Commission therefore considers that the Victorian Government should propose, in the Ministerial Council for Tertiary Education and Employment, the establishment of an industry panel to advise a national higher education committee such as the ABDC. In the absence of national agreement on this proposal, the Victorian Government should implement an equivalent arrangement in Victoria.

Draft recommendation 6.5

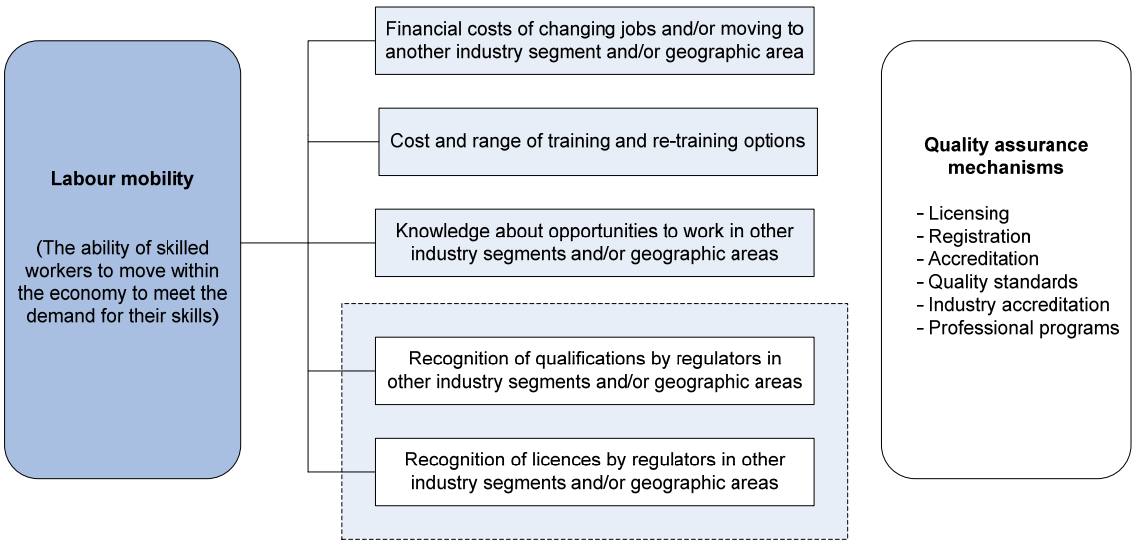
That the Victorian Government propose, in the Ministerial Council for Tertiary Education and Employment, the establishment of an industry panel to advise a national higher education committee such as the Australian Business Deans Council on industry needs regarding skill needs, qualifications and associated curriculum development. In the absence of national agreement, the Victorian Government should implement an equivalent arrangement in Victoria.

6.4.7 Accreditation, quality assurance and labour mobility

While there are market incentives to maintain the quality of services provided in the financial services sector, there are also government and industry mechanisms to assure quality such as accreditation and licensing. (Licensing of financial services providers was outlined in section 6.2.3.) The terms of reference for this inquiry require the Commission to consider the need for accreditation to facilitate labour mobility within the financial services sector.

Accreditation of education and training courses is one way of ensuring the quality and consistency of courses. Although accreditation is primarily about quality assurance, it can also affect labour mobility in that courses and qualifications are recognised and portable (figure 6.4), allowing people to move to the jobs, sectors or locations in which their skills are needed most. Labour mobility can help meet changing patterns of demand for financial services.

Figure 6.4 **Factors influencing labour mobility**



Source: Adapted from ACG 2008.

Accreditation and registration

The VRQA regulates all education and training providers in Victoria. It accredits courses and qualifications and maintains registers of providers and the accredited qualifications they offer. The VRQA aims to ensure that providers meet quality standards and that information is readily available to support informed choice (VRQA 2010; 2009c, p. 5).

New arrangements are being established nationally which affect the VET sector. COAG agreed to establish a new national regulator for the VET sector, with responsibility for the registration and auditing of training providers and accreditation of courses. The regulator will be established under Commonwealth legislation and become operational from 2011 (COAG 2009, p. 5). Victoria will enact legislation to mirror the Commonwealth legislation and the VRQA will continue to regulate providers operating in Victoria.

In submissions, consultations and the roundtable (appendix A), inquiry participants did not identify any significant issues with existing accreditation arrangements — or any need to extend or contract the coverage of accreditation in Victoria.

Information request: Based on submissions, consultations and roundtable discussions for this inquiry, there do not appear to be significant concerns with existing accreditation arrangements. Are there any reasons why this is not a valid conclusion?

Industry accreditation

There are some industry-based accreditation programs. For example, AFMA provides two national accreditation programs for individuals working in the Australian over-the-counter and exchange-traded markets; namely:

- the AFMA Financial Markets Accreditation Program
- the AFMA Operations Accreditation program.

The programs assist AFMA members in ensuring that their staff, when operating in Australian financial markets, have had their general knowledge of these markets and their legal, regulatory and compliance components objectively assessed against an agreed industry standard. The adoption and implementation of the AFMA accreditation programs is at the discretion of AFMA member organisations (sub. 8, p. 3).

Professional programs

Professional bodies (such as CPA Australia) and industry associations offer training and professional programs. For instance, the Securities and Derivatives Industry Association (SDIA) Professional Program sets the industry benchmark in the securities and derivatives industry, earning its participants the SDIA Professional Diploma in Securities and Derivatives. The content includes the role, characteristics and professional standards of the sector, along with the operation of markets and technical details of financial product types commonly used by securities and derivatives professionals (SDIA 2008, p. 3).

In addition, the Investment and Financial Services Association offers a range of industry training programs and professional development initiatives relating to managed investments, superannuation, retirement income streams and life insurance. These programs are designed to meet the training needs of industry participants whose roles encompass the administration, support or management of financial services products (IFSA 2005).

Quality indicators

Under the Australian Quality Training Framework, all RTOs are required to collect, use and report data on three quality indicators:

- competency completion
- learner engagement
- employer satisfaction.

Victorian RTOs are required to submit reports to the VRQA. The NQC has agreed that the quality indicator data will be used by RTOs to undertake continuous improvement processes and by state registering bodies to inform each RTO's risk assessment. Registering bodies are bound by legislation in their

capacity to share data and will not release to other parties any quality indicator data provided by RTOs (VRQA 2009b). A key question is whether there would be a net benefit from publishing this data.

Information request: The Commission seeks further information on the advantages and disadvantages of publishing the quality indicators collected under the Australian Quality Training Framework.

6.4.8 Skilled labour from overseas

While the education and training system and domestic labour market are the primary sources of skilled labour, skilled migration can be used to meet skill shortages in the financial services sector as they arise. DIC administers the General Skilled Migration program, which is for people who are not sponsored by an employer and who have skills in particular occupations required in Australia (DIC 2010a). In addition, the Victorian Government maintains lists of occupations that are eligible for visa sponsorship by the state (Victorian Government 2010).

The Commonwealth Government recently announced reforms to the skilled migration program to make it more responsive to the needs of industry and employers and to better address future skill needs. The reforms will involve, among other things, revoking the Migration Occupations in Demand List and phasing out the Critical Skills List. A new and more targeted Skilled Occupations List will be developed and reviewed annually by Skills Australia (Evans 2010a).

As part of the reforms, the Commonwealth Government has invited state and territory governments to prepare State Migration Plans to address regional variations in skills demand. These plans will form bilateral agreements to frame the level and type of state sponsored skilled migration sought over a rolling four-year period. States and territories will be able to nominate occupations including those that are not on the new Skilled Occupations List, where this is supported by labour market evidence (Evans 2010b).[12] The Commission understands that the Victorian Government is preparing its State Migration Plan.

6.5 Summing up

There are many participants in the financial services labour market and the skills formation system (which caters for the financial services sector — and other sectors in the economy). The skills formation system involves state and national education and training providers, and government and industry skills bodies.

[12] Under new priority processing arrangements, migrants nominated by a state or territory government under their State Migration Plan will be processed ahead of applications for independent skilled migration (Evans 2010a).

In response to concerns about skill shortages, the Commission examined national and Victorian evidence on skill shortages. The latest available evidence, whilst subject to limitations, indicates skill shortages in Victoria's financial services sector are confined to a small number of occupations and are not particularly widespread among businesses. This is supported by the Commission's recent consultations with businesses and other participants in the sector.

Major reform to the skills system in Victoria is being phased in over the next four years. Given the significant nature of this reform, good practice dictates that the outcomes of the reform be monitored, evaluated and reported.

The Commission has not found any significant regulatory impediments to the supply of skilled labour to the financial services sector. Nonetheless, there appears to be scope to improve aspects of current arrangements by enhancing skill needs information, updating occupational codes, developing representative business cases for training packages, providing information on nationally recognised courses and qualifications, and establishing a consultation mechanism between industry and the higher education sector.

In relation to accreditation and licensing, the Commission has not found sufficient evidence that suggests major changes are needed.

As this is a draft report, the Commission encourages interested parties to comment on the analysis and draft recommendations, and to provide further information and evidence where they believe there is a case for improvement or change.

7 Implications of the Commission's recommendations

7.1 Introduction

The terms of reference require the Victorian Competition and Efficiency Commission (the Commission) to, amongst other things, inquire into and report on the 'identification of the economic impacts (including reductions in the regulatory burden on business) of any options identified in this inquiry'.

The financial services sector makes a significant contribution to the Victorian economy and Victoria has particular strengths in some areas (chapter 2). Participants and others have identified a number of potential opportunities for further development of the sector (chapter 3). These opportunities stem from:

- a growing national and state economy and population growth
- demographic, structural and policy changes causing shifts in the demand for financial services
- taking advantage of global opportunities to grow the industry beyond the domestic market
- changes in the approach to risk and cost management, including as a result of the global financial crisis.

In applying its analysis to the issues raised during the inquiry, the Commission found it useful to link a number of the elements of the report around some high level themes. The Commission took the view that the benefits to Victoria from a competitive financial services sector would come in the first instance from increased levels of transactions and assets, and second from leveraging that growing activity into sustained, well paid employment. Many of the Commission's conclusions and recommendations relate directly to those two themes.

The third linking theme is raising the level of awareness of, and knowledge about, the strengths of Victoria's financial services sector as part of a competitive, robust and efficient Australian financial services sector.

These three linking themes are considered in the rest of this chapter.

In its draft report, the Commission has made a number of requests for further information. The Commission is therefore not in a position to fully evaluate its package of proposed reforms. The full package and its implications for that part of the financial services sector located in Victoria will be presented in the

Commission's final report. Below are some preliminary comments and the Commission invites comments on the likely impact of its recommendations.

Information request: The Commission invites feedback on all the recommendations and other requests for information made in this draft report. In particular, the Commission invites comment on the economic impact of its recommendations and potential impacts in areas where it has made specific information requests.

7.2 Increased levels of transactions and assets

Increasing the number of transactions and proportion of assets under management in Victoria has the potential to grow the sector in Victoria and generate opportunities for Victorian-based businesses. The increasing amount of financial service business undertaken from and within Victoria will increase the level of economic activity in Victoria and expand employment opportunities. This can happen in a number of ways — taking a share of increases in international and national transactions and increasing the value of transactions undertaken, and assets managed, in Victoria.

International and national regulation of the financial services sector was recently examined by a number of Commonwealth reviews — notably the work of the Australian Financial Centre Forum (AFCF), the yet to be completed Review into the Governance, Efficiency, Structure and Operation of Australia's Superannuation System (Cooper review) and the Australia's future tax system review (Henry review). The Commonwealth Government has yet to respond to these reviews, which limits the Commission's ability to comment on how the Commonwealth's actions would affect Victoria.

The Commission has not sought to duplicate the work of these reviews. However, the Commission supports the intent of the AFCF's recommendations on Commonwealth taxation and regulatory reforms, aimed at increasing the international opportunities for the financial services sector in Australia. The Commission has also identified a number of specific recommendations which will particularly affect the financial services sector in Victoria. It suggests the Victorian Government takes an advocacy position with the Commonwealth in relation to those recommendations in particular.

In the Victorian context, the Commission has identified specific transactions taxes imposed on insurance products as being an impediment to the further development of the financial services sector in Victoria. Victoria has amongst the highest rates of duties on these products among Australian jurisdictions. The Commission considers that while concerns about the efficiency of these taxes are valid, they are best addressed in the context of a national response to the Henry review.

The Commission expects that reform of these taxes would:

- enhance the financial services sector in Victoria by increasing demand for insurance products — there is evidence that demand for insurance products is sensitive to changes in price
- have budgetary implications that will need to be considered in the context of the state's total revenue raising system.

Regulatory arrangements also impact on the scope to increase the volume of transactions and assets nationally and in Victoria. The vast majority of regulation impacting on the financial services sector is the domain of the Commonwealth Government and has been the subject of recent Commonwealth reviews, including the AFCF.

There has been some concern about inconsistency of regulation across jurisdictions. Submissions raised inconsistency in insurance regulation as a potential area for harmonisation among states. The Commission has recommended that COAG consider harmonising state insurance regulation.

However, during the inquiry, the Commission identified a number of major pieces of Victorian legislation that impact on the financial services sector. This legislation pertains to the acts underpinning the operations of seven public financial corporations (PFCs), some of which provide services to the Victorian public and others who provide services to other areas of government. The seven PFCs are: Rural Finance Corporation; State Trustees Limited; Victorian Funds Management Corporation; Treasury Corporation of Victoria; Victorian Managed Insurance Authority; Transport Accident Commission; and WorkSafe Victoria (chapter 2).

The Commission did not review the operations of these organisations in detail and no participants to the inquiry raised concerns regarding the scope of government provision of financial services. However, the Commission notes that, for longstanding policy and operational reasons, a significant amount of financial services activity is reserved to the Government and that a number of these bodies, such as the Rural Finance Corporation, operate subject to constraints on their activities that would have some impact on the financial services sector.

The Commission has requested further information on the operation of these bodies and whether there are any factors in their operation that impede the development of the financial services sector in Victoria (chapter 4).

7.3 Leverage employment opportunities

Growing the number of transactions and demand for financial services by developing the state economy and taking advantage of national and international opportunities will generate employment growth. However, the Commission considers that the resulting (well renumerated) employment opportunities will be enhanced if the state has a responsive education and training system and is able to attract skilled labour.

The financial services sector is highly labour intensive and provides sophisticated services. The sector's success therefore depends in part on the availability of skilled workers. Victoria is fortunate to have a strong education system at all levels — including at TAFE and university level, which is involved in providing the types of skills required by those in the financial services sector.

The Commission notes that recent changes to the education system have been directed towards, among other things, increasing flexibility. Given the significant nature of this reform, good practice dictates that the outcomes of the reform be monitored, evaluated and reported.

The Commission has not identified any significant regulatory impediments to the supply of labour to the financial services sector, nor has it been made aware of any systematic and significant shortage of skilled labour except in some limited areas, such as accountants. Nonetheless, there appears to be scope to improve aspects of current arrangements by enhancing skill needs information, updating occupational codes, developing representative business cases for training packages, providing information on nationally recognised courses and qualifications, and establishing a consultation mechanism between industry and the higher education sector.

The Commission expects the outcome of accepting these recommendations will be a flexible, responsive system that is able to adapt more quickly to industry needs while supplying a highly skilled workforce to the financial services sector.

7.4 Increase awareness of the state's strengths

The Commission has identified a number of strengths in the Victorian financial services sector, including:

- industry superannuation funds
- public sector funds management
- the capacity to deliver major infrastructure projects, especially Public Private Partnerships
- intermediaries that expand their activities to serve specific client groups, such as regional banks and Islamic banking.

The state already has significant clusters of activity in these areas.

It is important to build on the state's strengths, but without inhibiting the development of new markets or areas of comparative advantage in the future. One way to do this is to promote the strengths of the Victorian financial sector and raise the profile of Victorian financial products (chapter 5). Such promotion can assist Victorian businesses to harness opportunities interstate and overseas. It can also influence location decisions for overseas businesses wishing to establish a presence in the region.

The challenge is to seek to ensure that Victorian initiatives remain relevant and focussed where they can have the most effect. This is particularly important now given the market has changed substantially (including in response to the global financial crisis and economic slowdown) and will continue to do so as ongoing reform at a national level is developed and implemented (chapter 4).

In this context, the Commission has recommended that the Victorian Government work with Austrade to ensure that an appropriate weighting is given to Victoria's strengths when promoting the sector more widely (chapter 5). The Commission expects that this cooperation between state and national activities will ensure that Victoria's interests are represented in a way that complements the broader national promotional activities.

7.5 The recommendations as a package

Taken together the Commission's recommendations will help remove impediments to Victoria's financial services sector taking advantage of growth opportunities and ensure it has the flexibility to respond to opportunities as they arise.

However, the Commission also notes that:

- where recommendations have significant budgetary implications, such as the harmonisation of stamp duties on insurance products, they should be considered as part of wider reforms to taxation affecting the Commonwealth and states
- there were few regulatory impediments to the sector as a result of state-based regulation and so has not undertaken an analysis of the reductions in regulatory burdens affecting businesses.

In developing its recommendations the Commission has, and will, focus on ideas that would facilitate sustainable growth. Such growth will result when the market is strongly competitive and barriers are removed so that the industry can take advantage of new ideas, opportunities and innovations, in areas in which it has a comparative advantage.

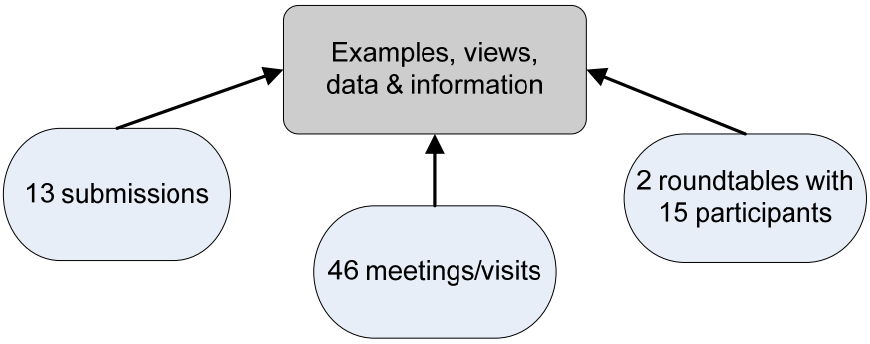
The types of activities the Commission is seeking to reinforce through its recommendations, for example, the development of clusters, have proven in the past to stimulate innovation and growth — the development of the Mercer Global Pension Index is an example.

Appendix A: Consultation

A.1 Introduction

This appendix describes the consultations undertaken by the Victorian Competition and Efficiency Commission (the Commission) during the inquiry (figure A.1).

Figure A.1 **Consultation during the inquiry**



Source: VCEC.

The Commission received the terms of reference on 18 September 2009. In keeping with its charter to conduct public inquiries, the Commission advertised the inquiry into the financial services sector in Victoria in major metropolitan newspapers in November 2009. It also published an issues paper in November 2009, which outlined:

- the inquiry timetable
- the scope of the inquiry
- background information and issues
- how to make a submission.

The issues paper invited interested parties to make submissions. The Commission received 13 submissions before the release of the draft report (section A.2).

The Commission also held two roundtable meetings in February 2010 involving 15 participants from business, government, Tertiary and Further Education (TAFE) and higher education organisations (section A.3).

In addition, the Commission consulted with 31 organisations or individuals during the inquiry (section A.4).

A.2 Submissions

The Commission received 13 submissions (table A.1). The submissions can be viewed on the Commission's website.

Table A.1 Submissions received

Participant	*Submission no.*
Carol O'Donnell	1
Carol O'Donnell	2
Carol O'Donnell	3
Carol O'Donnell	4
Carol O'Donnell	5
Confidential	6
Confidential	7
Australian Financial Markets Association	8
Australian Bankers' Association	9
Insurance Council of Australia	10
Carol O'Donnell	11
National Stock Exchange Limited	12
Melbourne Centre for Financial Studies	13

A.3 Roundtables

The Commission held two roundtable meetings in February 2010 with a range of participants from business, government, TAFE and higher education organisations (tables A.2 and A.3). Summaries of the roundtable discussions can be viewed on the Commission's website.

Table A.2 Ensuring sufficient supplies of skilled labour in Victoria's financial services sector

Name	*Position*	*Representing*
Andree Butler	Director of Policy, Skills Victoria	Department of Innovation, Industry and Regional Development
Dr Matthew Butlin	Chair	Victorian Competition and Efficiency Commission
Deborah Cope	Commissioner	Victorian Competition and Efficiency Commission
Dr Mary Dunkley	Deputy Head of Group (Assurance of Learning) — Accounting, Economics, Finance & Law, Senior Lecturer, Accounting	Swinburne University of Technology
Lynn Glover	Director	Victorian Registration and Qualifications Authority
Anna Henderson	Executive Director, Business Finance and Property Industry Training Board	Victorian Business Services
Max Newton	Associate Director of the Business Services Centre	Holmesglen Institute of TAFE
Shrimal Perera	Course Director, Masters of Banking and Finance	Monash University
John Stapleton	Manager Industry Relations, Skills Victoria	Department of Innovation, Industry and Regional Development
Heidi Tarjani	Manager Labour Market Analysis, Skills Victoria	Department of Innovation, Industry and Regional Development

Table A.3 Leveraging opportunities for Victoria's financial services market

Name	*Position*	*Representing*
Dr Matthew Butlin	Chair	Victorian Competition and Efficiency Commission
Deborah Cope	Commissioner	Victorian Competition and Efficiency Commission
Xavier Csar	Executive Director, Economic Projects	Department of Innovation, Industry and Regional Development
Ian Ferres	Former Chairman	Treasury Corporation of Victoria
Dugald Graham	Chief Executive Officer	Rural Finance Corporation
Megan Jones	Public Affairs Manager	Members Equity Bank
Diana Joslin	Senior Manager, Commercial Division	Department of Treasury and Finance
Rod Maddock	Executive General Manager	Commonwealth Bank of Australia
Bill Whitford	Managing Director	Treasury Corporation of Victoria

A.4 Stakeholder consultations

The terms of reference required the Commission to consult with key interest groups and to draw on the knowledge and expertise of relevant Victorian Government departments and agencies. Stakeholder consultations (table A.4) may include organisations that also attended one of the roundtables.

Table A.4 Stakeholder consultations

Organisation (or individual)	*Organisation (or individual)*
Asia-Pacific Emissions Trading Forum	Melbourne Centre for Financial Studies (MCFS)
Australian Bankers' Association (ABA)	Melbourne City Council
Australian Institute of Superannuation Trustees	Members Equity Bank
Australian National University	Mercer
Australian Prudential Regulation Authority (APRA)	National Australia Bank (NAB)
Australian Securities and Investments Commission (ASIC)	National Stock Exchange (NSX)
Commonwealth Bank of Australia	Plenary Group
Commonwealth Treasury	Productivity Commission
Department of Innovation, Industry and Regional Development (DIIRD)	Reserve Bank of Australia (RBA)
Department of Justice	Rural Finance Corporation
Department of Treasury and Finance	State Trustees Limited
Finance Sector Union	The Australian APEC Study Centre
Financial Services Institute of Australasia (Finsia)	Treasury Corporation of Victoria (TCV)
Health Employees Superannuation Trust Australia (HESTA)	Victorian Funds Management Corporation (VFMC)
Innovation and Business Skills Australia (IBSA)	Victorian Registration and Qualifications Authority (VRQA)
Investment and Financial Services Association	

Appendix B: The financial services workforce in Victoria

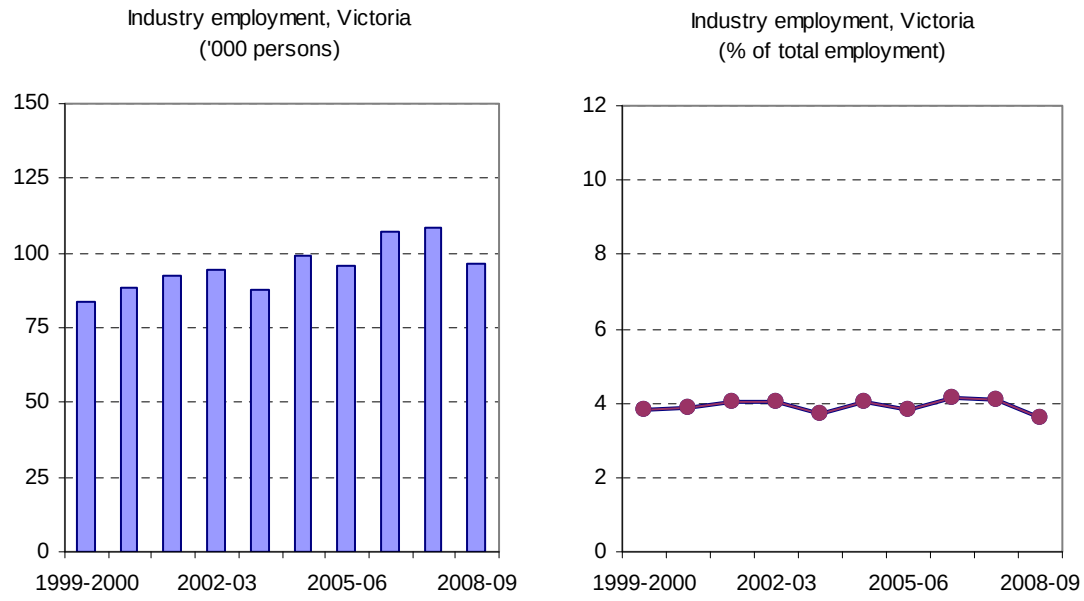
B.1 Introduction

This appendix outlines key characteristics of the financial services workforce in Victoria. It relies substantially on information and analysis supplied by Skills Victoria and data collected by the Australian Bureau of Statistics, the Commonwealth Department of Employment, Education and Workplace Relations and the National Centre for Vocational Education Research.

B.2 Employment profile

Employment in Victoria's financial services industry increased from around 83 500 employees in 1999-2000 to about 108 000 in 2007-08 — an increase of 30 per cent (figure B.1). Employment in the industry decreased to about 96 100 in 2008-09. In the past five years, employment in the industry has averaged about 100 000, representing about 4 per cent of total employment in Victoria.

Figure B.1 **Employment, financial services, Victoria[a]**

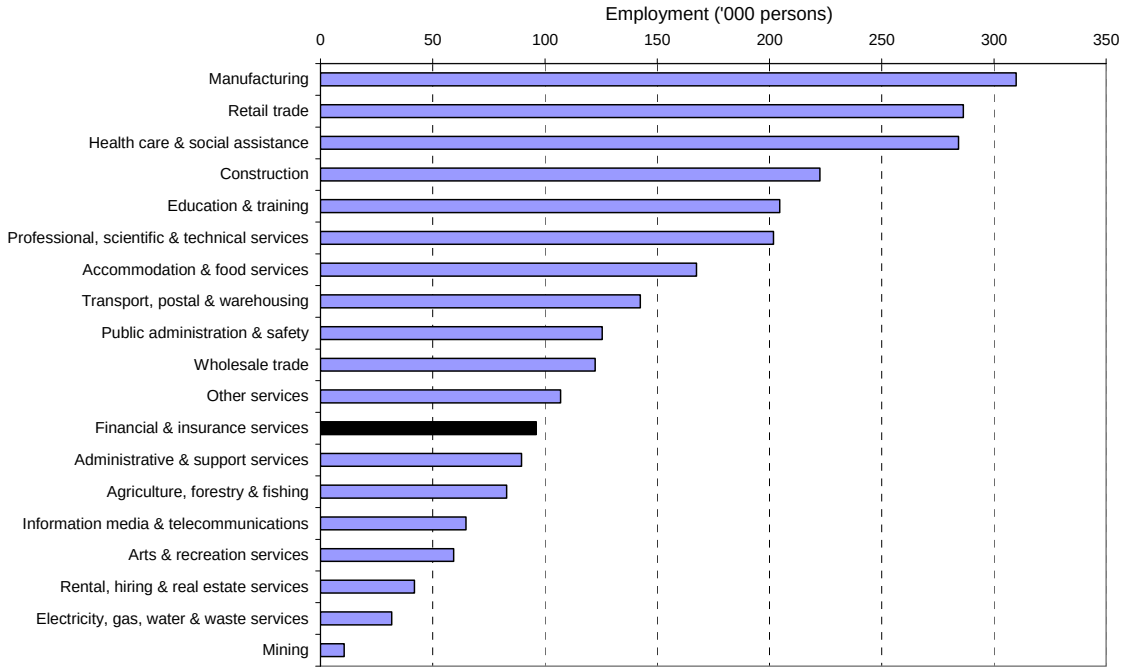


[a] Financial year estimates for employment were derived by averaging quarterly employment data.

Source: ABS 2009b.

In 2008-09, the sector was the twelfth largest industry by employment in Victoria (figure B.2).

Figure B.2 **Employment, by industry sector, Victoria, 2008-09[a]**



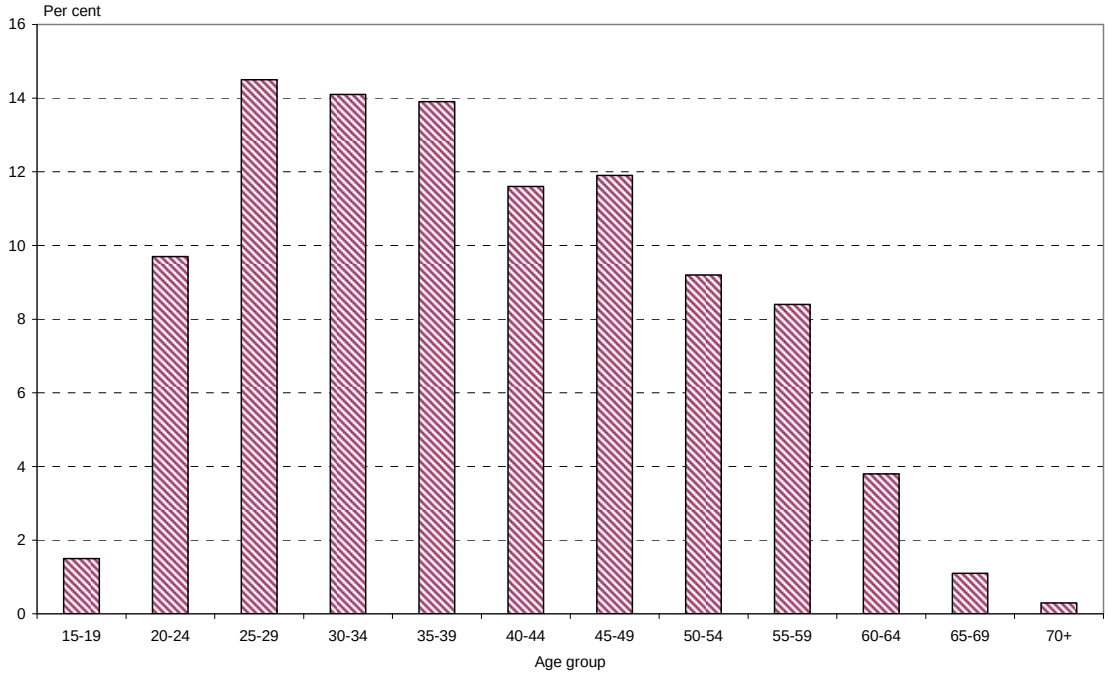
a ANZSIC industry classification. Financial year estimates derived by averaging quarterly employment data.

Source: ABS 2009b.

The industry is characterised by a high proportion of full-time positions. In 2008-09, only 16 per cent of workers were employed on a part-time basis (ABS 2009b).

In 2008, most employees in the industry (about two-thirds) were aged between 25–49 (figure B.3). The proportion of young employees (15–24) was relatively low at 11 per cent, as most occupations in the industry require formal qualifications after completing Year 12. The percentage of older employees (over 60) in the industry is also relatively low (Skills Victoria 2010b, 2010c).

Figure B.3 **Employment, by age group, financial services, Victoria, 2008**



Source: Skills Victoria 2010c.

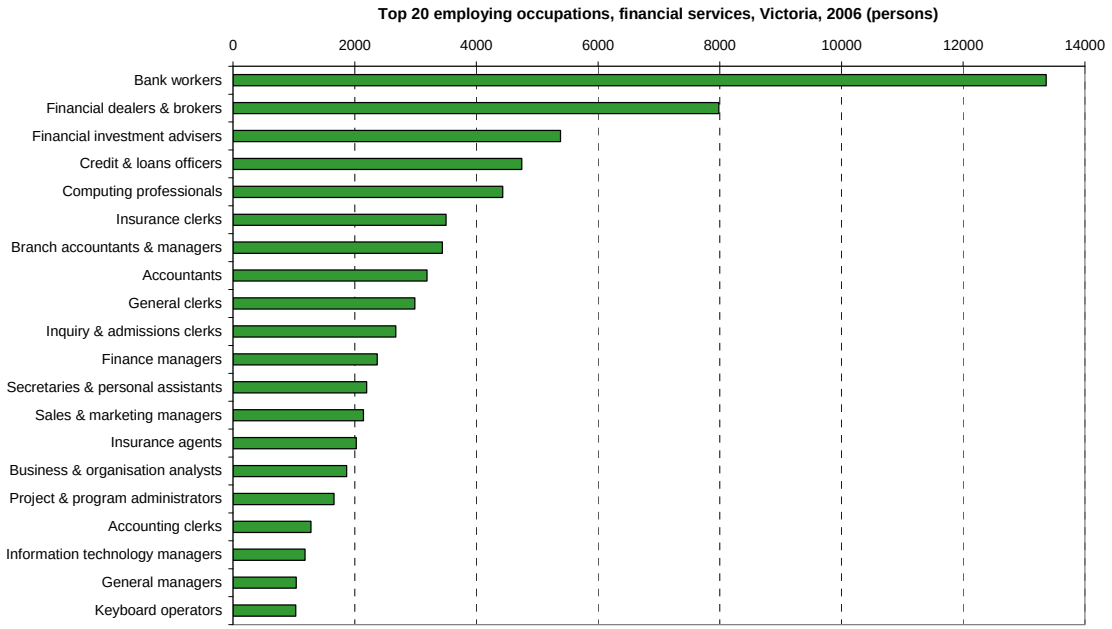
Around half of the employees in Victoria's financial services industry were female in 2008-09 (ABS 2009b). The Australian Bankers' Association (ABA) noted that the banking industry is a key industry in providing employment opportunities for women, including working mothers (sub. 9, p. 16).

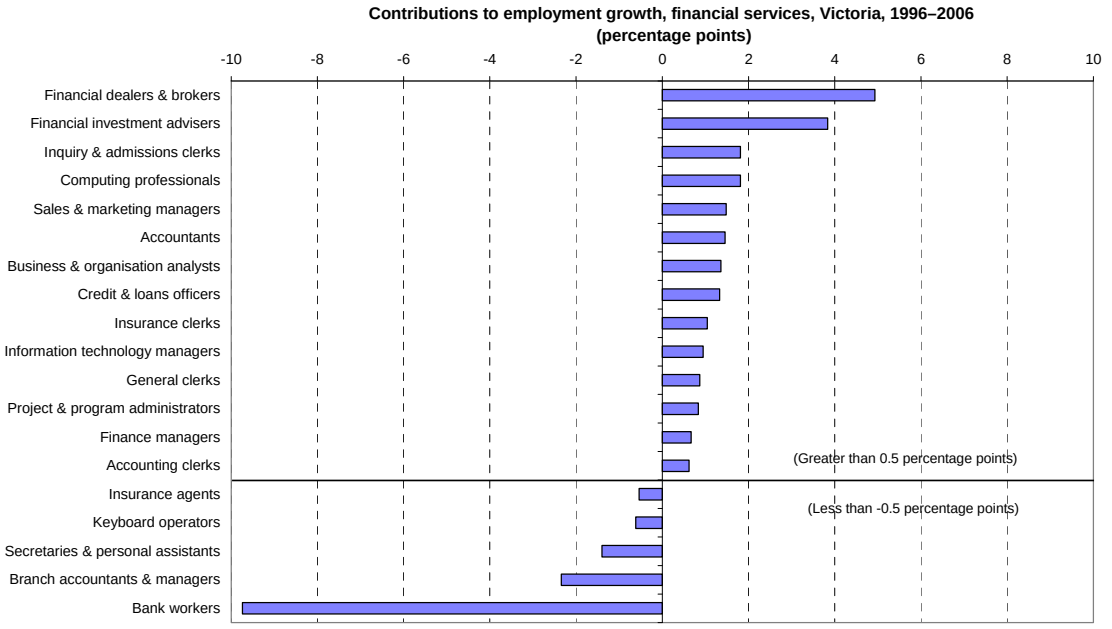
B.3 Occupational profile

The financial services sector employs a wide range of skilled workers. Figure B.4 (upper panel) shows the top 20 occupations by employment in the financial services sector in Victoria in 2006. These occupations accounted for around three-quarters of total employment in the sector. The largest numbers of employees worked as bank workers, financial dealers and brokers, financial investment advisers, credit and loans officers, and computing professionals.

The occupations that contributed most to employment growth in the ten years to 2006 included financial dealers and brokers, financial investment advisers, inquiry and admissions clerks, and computing professionals (figure B.4, lower panel).

Figure B.4 Employment, by occupation, financial services, Victoria, 2006[a]





a Census Classification and Classified List of Occupations. August data.

Source: ABS 2009d.

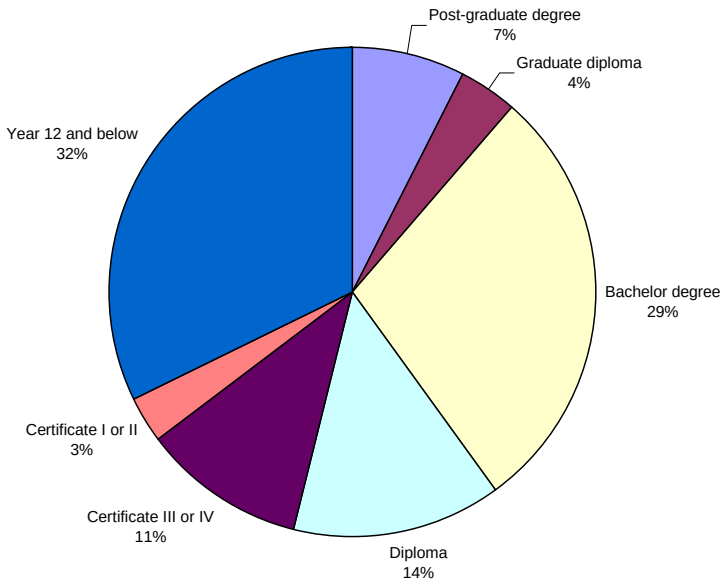
In the ten years to 2006, the occupations that detracted most from employment growth in the sector included bank workers, branch accountants and managers, and secretaries and personal assistants (figure B.4, lower panel).

B.4 Educational profile

The level of educational attainment is one measure of skill acquisition but it is a partial measure because it may not reflect the skills acquired through on-the-job experience.

As most occupations in the industry require formal qualifications on top of Year 12, the proportion of employees with higher level qualifications is high. The proportion of employees with higher level (Diploma and above) qualifications was more than 50 per cent (figure B.5). While about 14 per cent of employees held Certificate I–IV level qualifications, about one-third of the workforce did not have formal qualifications above Year 12.

Figure B.5 **Educational attainment, financial services, Victoria, 2008**



Source: Skills Victoria 2010c.

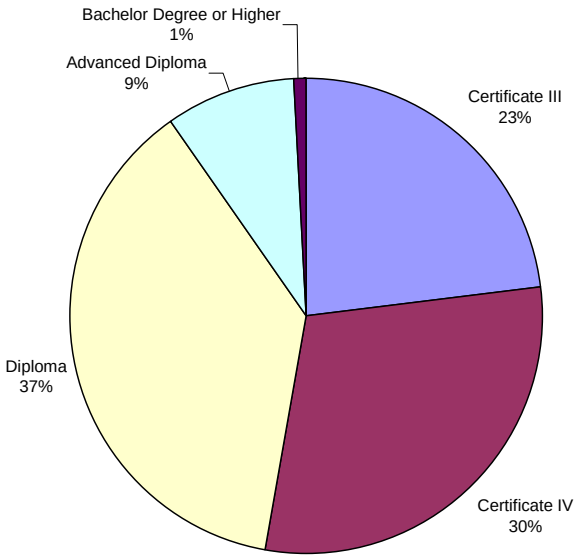
Financial services workers in Victoria are highly qualified, with about 68 per cent of the industry workforce having completed a non-school qualification compared with about 62 per cent for all industries (Skills Victoria 2010d).

B.5 Student profile

In 2008, around 19 660 students enrolled in vocational education and training (VET) courses leading to qualifications that may lead to employment in the financial services industry. In addition, nearly 18 500 students enrolled in VET courses leading to more general qualifications that could be applied across the business services industry (Skills Victoria 2010b).

Of the students studying VET finance courses, more than half were enrolled in Certificate III and IV level courses (figure B.6), including courses such as Certificate III in Financial Services (Accounts Clerical) and Certificate IV in Financial Services (Accounting and Bookkeeping). Over one-third of enrolments were at the Diploma level, including courses such as the Diploma of Accounting and the Diploma of Financial Services. About 10 per cent of enrolments were in higher level courses.

Figure B.6 **Student enrolments, by qualification, VET finance courses, Victoria, 2008[a]**



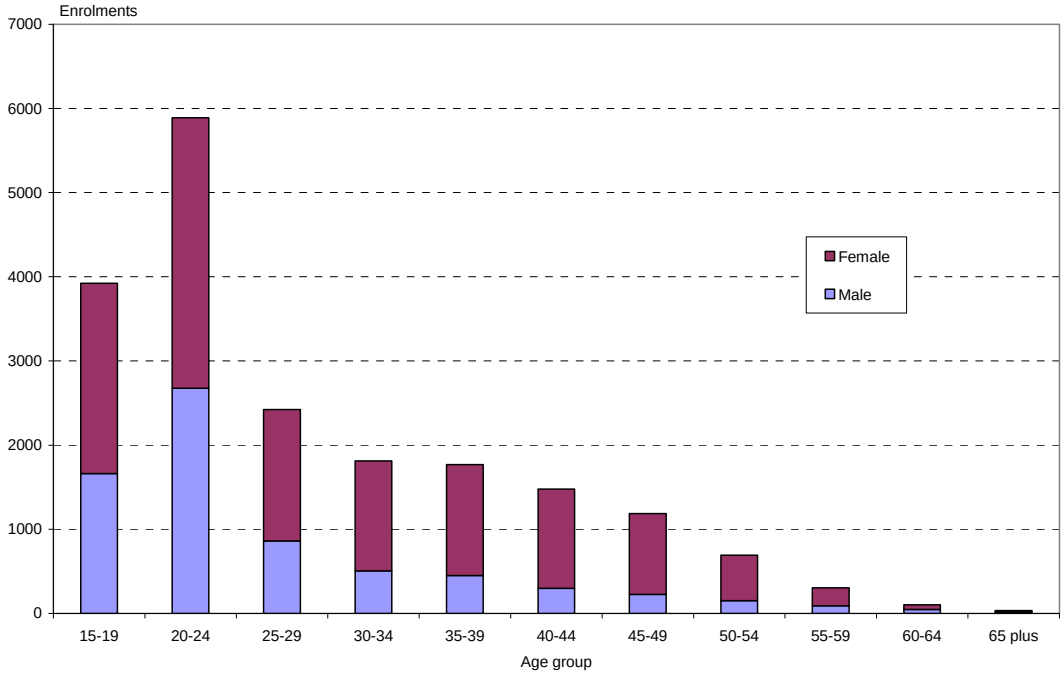
[a] Includes some higher education qualifications delivered by TAFE institutes but excludes non-qualification courses.

Source: Skills Victoria 2010c.

The share of enrolments in non-qualification courses was modest, amounting to 7.5 per cent of total course enrolments. This included courses such as the Computerised Accounting, MYOB, Quickbooks and Basic Book-keeping courses (Skills Victoria 2010b).

Around two-thirds of students were female and about half of students were younger than 25 (figure B.7).

Figure B.7 **Student enrolments, by gender and age, VET finance courses, Victoria, 2008[a]**



a Includes enrolments in non-qualification courses.

Source: Skills Victoria 2010c.

In 2008, it is estimated that about 1500 trainees commenced training in finance and accounting.[1] In the same year, around 1000 finance and accounting trainees completed their training (NCVER 2009c).

In the higher education sector, there were about 97 000 students studying commerce and management with Victorian universities and about 25 500 course completions within these fields in 2008 (DEEWR 2009b, 2009c).

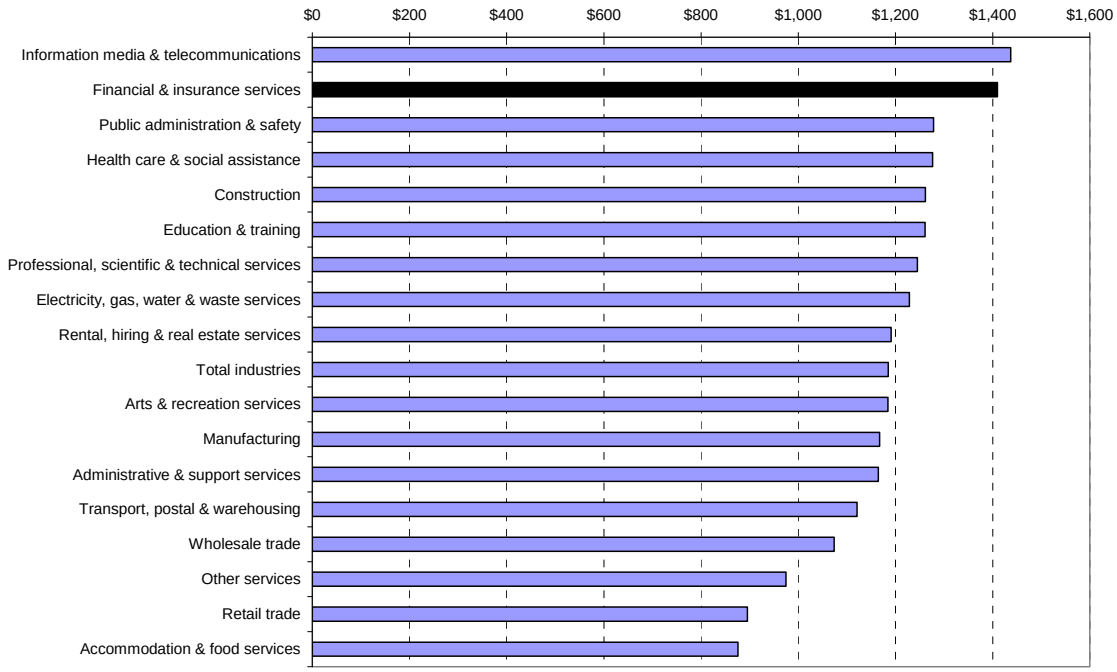
[1] Traineeships in finance and accounting would fall into occupation sub-major groups 'Business, Human Resource and Marketing Professionals' and 'Numerical Clerks' (NCVER 2009c).

B.6 Earnings profile

The ABA noted that average weekly ordinary time earnings in the financial services sector in Australia have, on average, been about 26 per cent higher than the national average for all industries (sub. 9, p. 17).

In Victoria, average weekly ordinary time earnings in the sector were $1410 in 2009, almost 20 per cent above the all industries average of $1185 (figure B.8).

Figure B.8 **Average weekly earnings, by industry, Victoria, 2009[a]**



[a] Full time adult persons ordinary time earnings. November data.

Source: Skills Victoria 2010d.

B.7 Summing up

The financial services workforce in Victoria has averaged around 100 000 people in recent years. Key characteristics of the workforce include:

- most workers are aged between 25–49 years
- employment is broadly even by gender
- most workers are employed on a full-time basis
- the proportion of employees with higher level qualifications is greater than that for all industries

- average earnings are significantly above that for all industries.

In 2008, there were about 20 000 students enrolled in VET finance courses and a further 100 000 enrolled in higher education courses in commerce and management in Victoria.

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