Australian Finance Industry Association Limited
ABN 13 000 493 907
L11, 130 Pitt Street Sydney NSW 2000
T: 02 9231 5877

6 July 2017

Ms Ruth Moore
Manager – Financial Services Unit
Financial Systems Division
Treasury
CANBERRA ACT

By email: Ruth.Moore@treasury.gov.au

Dear Ms Moore

ASIC REVIEW OF MORTGAGE BROKER REMUNERATION

The Australian Finance Industry Association (**AFIA**) is the industry advocate for Australia's finance sector. AFIA represents more than 100 leading providers of consumer, commercial and wholesale credit, including ASX-listed and customer owned banks, captive financiers and credit reporting bureaus. A membership list accompanies. AFIA's bank and customer owned bank members together with a number of non-bank members actively participate in the home loan market utilising the services of finance brokers and were included in ASIC's industry survey. AFIA members provide billions to fund the future of Australian families and businesses and employ thousands to do so. AFIA provides specialist policy expertise to represent the interests of its members to federal and state governments, and Australia's financial and corporate regulators.

AFIA welcomes the opportunity to comment on *ASIC's Report No 516 – Review of Mortgage Broker Remuneration* [the **Report**]. AFIA supports the review, but notes that each holder of an Australian Credit License [ACL]- whether the introducer, facilitator or lender - is responsible for compliance with their own obligations as licensees under the National Consumer Credit Protection Act and Regulations (NCCPA) and are accountable to ASIC as the regulator. AFIA has limited its comments to the following broader implications of broker remuneration in the context of improving customer outcomes including:

- more appropriate commission models
- more effective disclosures and conflict management;
- stronger governance frameworks for brokers, aggregators and lenders to support a customer focused culture; and,
- compliance and oversight of mortgage brokers.

Role of Brokers in the Home Lending/Mortgage Market

Both ASIC in its 2017 Report[1], and Ernst & Young its May 2015 Report[2], recognise the role that brokers have played in recent years as a distribution channel for mortgage lenders by in facilitating more than 50% of home loans in FY 2105 and promoting competition in the market for home loans.

---

[1] Australian Securities & Investments Commission Report 516 Review of mortgage broker administration dated March 2017 at page 9

[2] Ernst & Young *Observations on the value of mortgage broking* prepared for the Mortgage & Finance Association of Australia (MFAA) dated May 2015 at page2

Mortgage brokers (and aggregators) are recognised as providing an efficient conduit for the delivery of residential housing loans relieving in part the need for home mortgage lenders to maintain with the attendant costs a comprehensive network of mobile lenders and on site staff to deal with the increasing demands for home mortgage finance. Indeed, a number of major banks have interests in listed and unlisted mortgage broker entities which actively support their own or other lender products.

> ***AFIA Recommendation**: Based on clear evidence that the mortgage broker distribution channel appears critical to a competitive and efficient home lending market, Government should ensure that in taking forward any of the six key proposals in the ASIC Report that it does so in a way that ensures it remains a viable channel.*

Commission Structures

ASIC has highlighted the need to change standard commission models to reduce the risk of poor customer outcomes. AFIA's members acknowledge ASIC's concerns, as noted in the Sedgwick Report, there was no compelling evidence of systemic harm in either the ASIC Report or its report that warrant the banning of such payments.[3]

In the case of mortgage brokers, commission plans need to fairly and commercially reward brokers for the level of credit assistance provided to borrowers of differing credit and financial standing having regard to the range and suitability of mortgage products and, credit and lending policies to determine those products (or their design) which meet the requirements of existing and prospective customers.

Price controls in the form of capping of remuneration would simply encourage the introduction of, or an increase in, application fees by brokers to preserve their income, thereby potentially increasing the costs incurred by consumers.

> ***AFIA Recommendation**: AFIA supports the Report, but notes that the NCCPA already includes an obligation on brokers, aggregators and lenders to ensure transparency of commissions for the introduction of mortgage loans, and to manage and monitor the risks of non-compliance with the pre-contractual disclosure requirements of the NCCPA. Compliance with these disclosure obligations and with product suitability requirements of the NCCPA mitigates the risk of disadvantage to customers. Active compliance oversight of ASIC as regulator assists this process. We acknowledge this requires adequate resourcing of ASIC and also note the passage of legislation to implement the Government's proposal for industry to fund ASIC's oversight including of its credit activities. This may be adequate to address shortcomings in the current marketplace removing the need for additional regulation.*

Conflicts of interest

Submissions to the Sedgwick Report and to ASIC's Report continue to arouse concern that current broker remuneration models give rise to conflicts of interest and, by implication, disadvantage to customers.

[3] Retail Banking Remuneration Review , Report Stephen Sedgwick, 19 April, 2017 at page34

While ASIC in its Report has referenced the payment of significant upfront, trailing and soft commissions as being of concern, the payment of such commissions is not *prima facie* unfair or unlawful.

AFIA and it members acknowledge the potential for conflict where a mortgage broker puts their interests ahead of the consumer to derive an unjust benefit and in so doing fail to meet their NCCPA obligations - whether in relation to the effective management of conflict of interest, compliance with their pre-contractual disclosure obligations, failing to fulfil their responsible lending obligations or their general licensing obligation to act efficiently, honestly and fairly under the NCCPA.

To the extent that there are perceived operational shortcomings in relation to broker remuneration including the need for cultural change (as evidenced in the Sedgwick Report[4] in relation to the remuneration of staff by lenders), it is important that all ACLs review the efficacy of their internal controls including compliance and risk management programs to identify opportunities to redress those perceived shortcomings arising out of their remuneration arrangements with mortgage brokers. This could be as simple as the review of their sales processes; and, where appropriate, enhanced disclosures and production of customer guides, supplementary broker training and compliance monitoring including the review of customer feedback and complaints.

> ***AFIA recommendation***: *AFIA believes that the NCCPA in its current form mandates that ACLs have in place a comprehensive framework for the risk management and compliance including the management conflict of interest. Notwithstanding the cultural issues identified in the Sedgwick Report, the current regulatory framework is adequate to address disadvantage to customers where the interest of mortgage brokers are put before those of their customers causing disadvantage. As such further regulatory intervention is arguably not required. AFIA does not discount the obligations of ACLs to continuously review and improve this framework and in particular to monitor compliance by its representatives and address cultural issues. AFIA supports the ongoing activities of ASIC as the industry regulator to monitor compliance and in particular identify and address areas of potential disadvantage including due to such conflict and/or irresponsible lending.*

Compliance & Governance Framework
NCCP section 47(1) requires that each credit licensee (whether a lender aggregator or broker) must *inter alia*:

- do all things necessary to ensure that the credit activities authorised by the licence are engaged in efficiently, honestly and fairly;
- have in place adequate arrangements to ensure that clients of the licensee are not disadvantaged by any conflict of interest that may arise wholly or partly in relation to those credit activities engaged in by the licensee or its representatives;
- take reasonable steps to ensure that its representatives comply with the credit legislation
- to ensure that its officers and its representatives are competent and trained.; and,
- to comply with the credit legislation;

[4] Op cit

These obligations, together with responsible lending requirements, apply to all ACLs.

As the licensing authority it is the responsibility of ASIC to ensure that ACLs have in place a compliance and governance framework that fulfils the requirements of NCCPA section 47 and all other relevant provisions of the NCCPA and to supervise the conduct of licensees and monitor compliance.

Without discounting an ACL's obligations to implement and maintain that framework and in particular to monitor compliance with the NCCPA by credit representatives and the licensee itself, AFIA believes that it is ASIC's primary responsibility to proactively monitor licensee compliance with the NCCPA. AFIA acknowledges that while it is not generally an ACL's role to monitor other licensees, where there are clear breaches by that licensee, such as a representative/licensed broker providing to it fraudulent information in support of a loan application, then it is appropriate for the receiving licensee on becoming aware of that information to inform ASIC accordingly. It is expected that the ASIC Supervisor Levy on licence holders referred to above will be applied *inter alia* for the monitoring, supervision and guidance of ACLs.

In its Report ASIC has identified from the data provided, potential shortcomings in the standards of compliance and governance. AFIA and its members accept the need to ensure that any perceived shortcomings are addressed and that their risk management and compliance programs are updated to ensure that they meet the acceptable standards of governance under the NCCPA and ASIC Act.

AFIA and its members also recognise that risk management and compliance programs continue to evolve over time and that it is incumbent on members that hold ACLs to constantly monitor and review compliance and to respond to changes designed to ensure market integrity. Where opportunities exist for improvement of the delivery of their credit services or credit assistance, AFIA members also recognise the need to respond appropriately and responsibly. Members also acknowledge the value of social media, customer satisfaction surveys and complaints to identify events of non-compliance and/or poor service standards as drivers for cultural and procedural change to ensure that their compliance and governance frameworks continue to relevant and that they continue to meet their NCCPA obligations.

> ***AFIA recommendation***: *AFIA and its members support ASIC's continued focus on regulatory compliance and sound governance. Members appreciate ASIC's observations and guidance and requests that in the event of any proposed changes to the NCCPA or regulatory instruments designed to facilitate enhanced risk management and compliance and governance generally, ACLs be afforded a reasonable period to review and implement any such proposals.*

Conclusion

AFIA is keen to work with ASIC on any proposals emanating from the Report designed to mitigate concerns relating to the potential for disadvantage to mortgage borrowers by inappropriate broker remuneration structures or practices.

As noted in both the ASIC and Sedgwick Reports, mortgage brokers play a significant role in and provide an efficient conduit for retail customers to access mortgage finance. It is important that any proposals for change to existing broker remuneration plans continue to reward brokers in a fair and transparent manner without disadvantage to consumers and in accordance with the underlying principles of the NCCPA.

AFIA believes that the current regulatory NCCPA framework continues to be relevant and support compliant outcomes. Coupled with the ASIC Supervisory Levy this should see a well-resourced and active regulator working to ensure an appropriate level of behavior of participants in the mortgage lending market.

The Review provides an opportunity for all ACLs to review and, where necessary, enhance their risk, compliance and governance frameworks to mitigate the risk of non-compliance, to address issues of potential disadvantage arising from the payment of commissions while assisting consumers to fulfil their aspirations of home ownership.

AFIA and it members look forward to ongoing discussions with the Government and ASIC on any proposed reforms or initiatives designed to ensure equity between all participants in the home lending market.

Kind regards,

Helen Gordon
Chief Executive Officer

Australian Finance Industry Association Limited
ABN 13 000 493 907
L11 130 Pitt Street Sydney NSW 2000
T: 02 9231 5877

AFIA MEMBERS

255 Finance

Alleasing Group

Allied Credit

American Express

ANZ Banking Corporation/Esanda

Australian Structured Finance

Automotive Financial Services

Avis Budget Group

Bank of China

Bank of Queensland

Bendigo & Adelaide Bank

BMW Australia Finance / Alphabet Australia

Branded Financial Services

Cashflow Funding Limited

Caterpillar Financial Australia

Cisco Systems Capital (Australia)

Classic Funding Group

CNH Industrial Capital Australia

Commonwealth Bank of Australia

Credit Corp Group

Custom Fleet

Dun & Bradstreet

East Coast Car Rentals

Eclipx Group / FleetPartners

Elantis Premium Funding

Europcar Australia & NZ

Experian Asia Pacific

Equifax (Veda)

Finance One

Fleetcare

FlexFleet

FlexiGroup

Fuji Xerox (Finance) Australia

Genworth

Hertz Australia

HP Enterprise Financial Services

Hunter Premium Funding

HSBC Bank Australia

IBM Global Financing

Indigenous Business Australia

John Deere Financial

Komatsu Corporate Finance

Kubota Australia Finance

Latitude Financial Services

LeasePlan Australia

Leasewise Australia

Liberty Financial

Macquarie Leasing

Macquarie Premium Funding

Marubeni Finance (Oceania)

Max Recovery Australia

McMillian Shakespeare Group

ME Bank

Mercedes-Benz Financial Services

MetroFinance

Moneytech

National Australia Bank

Nissan Financial Services

On Deck Capital

ORIX Australia

PACCAR Financial

Pepper Money

Premium Funding Limited

Principal Finance

QFleet

QPR Premium Funding

Qudos Bank

RABO Equipment Finance / De Lage Landen

RAC Finance

RACV Finance

Ricoh Finance

Scottish Pacific Business Finance

Selfco Leasing

Service Finance Corporation

sgfleet / nlc Pty Ltd

Sharp Finance

SmartGroup

Summit Fleet Leasing & Management

Suttons Motors

Thorn Group

Thrifty Australia & NZ

Australian Finance Industry Association Limited
ABN 13 000 493 907
L11 130 Pitt Street Sydney NSW 2000
T: 02 9231 5877

TL Rentals

Toyota Finance Australia

Volkswagen Financial Services

Volvo Finance

Walker Stores

Wells Fargo International

Westlawn Finance/ North State Finance

Westpac Banking Corporation/St George Bank / Bank of Melbourne / Capital Finance Australia

WEX Australia

Wingate Consumer Finance

Yamaha Finance

ASSOCIATE MEMBERS

Ashurst Australia

Alfa

Bynx Australia

CAFG Australease

ClarkeKann Lawyers

Clayton Utz

Colin Biggers & Paisley

Commercil & Asset Finance Brokers Association

Cornwall Stodart Lawyers

Credit Sense Australia

Dibbs Barker

DLA Piper Australia

Element Fleet Services Australia

FIS Systems Pty Ltd

FTI Consulting

Genpact

Group and General Finance

Hall Chadwick

Henry Davis York

Herbert Smith Freehills

Hermes Data Systems

Holman Webb Lawyers

HPD Software Asia Pacific

Insyston

International Decision Systems

Kemp Strang

King & Wood Mallesons

KPMG

Lock Finance NZ

Lowe Lippmann Trakman FS

Macpherson + Kelley Lawyers

Norton Rose Fulbright Australia

Pacific Invoice Finance NZ

Polczynski Lawyers

Realtime Computing

Red Planet Software

Scottish Pacific Debtor Finance NZ

Sofico Services Australia

Sword Apak

Trace Personnel

Traction Group

Xeberg

White Clarke Asia Pacific