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ASIC Enforcement Review
Financial System Division
The Treasury
Langton Crescent
PARKES ACT 2600

Email: ASICenforcementreview@TREASURY.GOV.AU

Dear Sir or Madam

MFAA Response to the Treasury on ASIC's Directions Powers

On behalf of the Mortgage & Finance Association of Australia (MFAA), we welcome the opportunity to respond to the ASIC Enforcement Review Taskforce Position and Consultation Paper 8, released on the 8th November 2017 on ASIC's Directions Powers. In addition, we thank Treasury and the Enforcement Review team for extending the submission date.

Originally established in 1982, the MFAA is Australia's leading professional association for mortgage and finance brokers. The aim of the MFAA is to help MFAA members to be recognised as trusted professionals and to be their client's first choice. To achieve this aim, the MFAA promotes and advances the broker proposition to consumers as well as external stakeholders including governments and regulators, and continues to demonstrate the commitment of MFAA professionals to the maintenance of the highest standards of education and development.

Its membership profile also includes ADI and non-ADI lending institutions that distribute their products via intermediaries and businesses that provide support services to the mortgage and finance sector. The MFAA's current membership is in excess of 13,000 individual and business members.

Executive Summary

The MFAA's submission focuses on Australian Credit Licences and Licensees and does not generally refer to the Australian Financial Services Licensing regime.

The proposed changes to powers relates only to licensees. It can be argued that ASIC already has sufficient powers to monitor and control licensees. A more useful power would be a product intervention power when schemes are used by non-licensed entities to avoid the operation of credit and financial services law. This power would be valuable in cases

where ASIC forms the view, acting reasonably, that there is avoidance and/or material consumer detriment.

The Association has been advised that it is of concern to credit industry participants, in particular, credit licensees, that the paper proposes a significant expansion of ASIC's power to give enforceable directions to licensees (including ACL holders). The MFAA believes the proposed regulatory powers are extremely broad and may exceed an appropriate regulatory response to normal business decision making.

The MFAA, as a major representative of industry more broadly, supports high standards of conduct, but its members are suffering from 'regulation and change overload'. We are not aware of poor conduct that warrants an expansion of ASIC's current powers. Our observation is that the regulator's existing powers are achieving ASIC's objectives without unduly fettering businesses or exposing industry to mistaken extreme or arbitrary conduct by ASIC.

We have reviewed the case studies in the paper put forward to support the need for change. These studies relate to financial services. We maintain that the financial services sector is quite different from credit, and has the potential for far greater consumer harm. The proposed enhancement to ASIC's powers may be appropriate for the AFSL regime, but it is not appropriate for credit. There is a fundamental difference between the two industries – a lender risks its money whereas in financial services consumers risk their money. It is appropriate for the latter to be subject to closer scrutiny and controls.

The concern to be addressed

The primary reason for the new power is to enable ASIC to act promptly to prevent serious or systemic non-compliance. Under the proposal, ASIC effectively becomes sole arbiter of decisions about what action is required to minimise consumer detriment subject to a licensee's right of appeal. A lender's right to recover their money may be jeopardised by this action. The possibility of this power being exercised may constrict lender's capacity to raise money, thereby increasing costs to consumers. In our view, such a market-wide consequence is not justified by concerns about the rare cases of extreme conduct in the credit sphere warranting immediate action.

Scope of proposals

The proposals for reform should be limited to the issues identified by the 2014 Financial Services Inquiry¹ which referred to the need for ASIC to have more capacity to impose conditions requiring licensees to address concerns about serious or systemic non-compliance with licence obligations (including expert reviews). As currently formulated, we have significant concerns that the proposed ASIC powers could result in ASIC issuing directions that may undermine the effectiveness and usefulness of normal business decision making. This could have unintended effects on the productivity, efficiency and competitiveness of affected licensees.

Interaction with other current law reform proposals

We note that the Taskforce has recognised the overlap of these proposals with the proposed ASIC Product Intervention Power.

On 8 May 2017, the Treasurer requested that the Productivity Commission undertake a review of "competition in Australia's financial system with a view to improving consumer

¹ Financial System Inquiry, Final Report, Recommendation 29, 'Strengthening Australian Securities and Investments Commission's funding and powers', 7 December 2014, <http://fsi.gov.au/publications/final-report/chapter-5/strengthening-asic/>.

outcomes, the productivity and international competitiveness of the financial system and economy more broadly, and supporting ongoing financial system innovation, while balancing financial stability objectives.”²

The Treasurer specified that the Productivity Commission should consider the following matters in undertaking the review.

Without limiting related matters on which the Commission may report, its report to the Government should:

1. consider the level of contestability and concentration in key segments of the financial system (including the degree of vertical and horizontal integration, and the related business models of major firms), and its implications for competition and consumer outcomes
2. examine the degree and nature of competition in the provision of personal deposit accounts and mortgages for households and of credit and financial services for small and medium sized enterprises
3. compare the competitiveness and productivity of Australia's financial system, and consequent consumer outcomes, with that of comparable countries
4. examine barriers to and enablers of innovation and competition in the system, including policy and regulation
5. prioritise any potential policy changes with reference to existing pro-competition policies to which the Government is already committed or considering in light of other inquiries

The Commission should have regard to the Government's existing wide-ranging financial system reform agenda and its aims to:

- strengthen the resilience of the financial system
- improve the efficiency of the superannuation system
- stimulate innovation in the financial system
- support consumers of financial products being treated fairly
- strengthen regulator capabilities and accountability.

Consistent with the Treasurer’s directions to the Productivity Commission, these proposals should be revised to balance the goal of accountability with the goal of strengthening regulator capabilities. Unfortunately, the need for appropriate limits on regulatory discretion and the external accountability for regulatory decisions seems to have been largely dismissed in the development of these proposals in favour of regulatory expediency.

In addition, these new proposals should be included in the matters currently being considered by the Productivity Commission to ensure that a holistic approach is taken with respect to all current law reform proposals affecting credit licensees.

² See Australian Government, Productivity Commission, ‘Competition in the Australian Financial System, Terms of Reference’, 8 May 2017, <https://www.pc.gov.au/inquiries/current/financial-system/terms-of-reference>.

It is vital that the legislative framework that regulates mortgage brokers and other credit intermediaries delivers a competitive, diverse and sustainable sector, while at the same time providing appropriate and effective safeguards for the consumers of those services. Regulatory change and red tape can have a profound impact on the productivity of small business operators and mortgage brokers often operate within small businesses or are sole traders and, for many operators, on reasonably tight margins.

Response on the three preliminary Positions

In the following material, the words in shaded grey are taken from the Position and Consultation Paper. Our comments are in ordinary text.

Our concerns with the Preliminary Positions outlined in the Consultation Paper are shown below.

Position 1

ASIC should have the power to direct financial services or credit licensees in the conduct of their business where necessary to address or prevent compliance failures.

First, we note that, crucially, these powers can only be exercised after the condition stated in Position 2 is satisfied. The following powers are reviewed in that light. We also consider in Position 1 that the following actions are the **only** additional actions ASIC can take:

1. The legislation should set out the types of directions that ASIC can make. This would include directing an AFS or credit licensee to:
 - a. cease appointing authorised representatives; **Accepted**
 - b. cease accepting new clients; **We believe that this could threaten the viability of a business if it has borrowings and other outgoings to support (including salaries)**
 - c. conduct a review or audit of an authorised representative's records; **Accepted**
 - d. engage properly qualified compliance staff; **Accepted**
 - e. cease transferring business to another licence; **We aren't aware of the reasoning for this (in relation to credit activities)**
 - f. cease making specific representations about financial products or services; **Accepted**
 - g. appoint a person nominated by ASIC to review and report on compliance processes; **Accepted**
 - h. establish a programme to assess claims for restitution or compensation to customers. **In our view, the existing regime does not need change**

Questions

1. Should ASIC be able to give a direction to a financial services or credit licensee requiring them to take or refrain from taking specified action in the conduct of their business where necessary to address or prevent compliance failures? **See our general comments**
2. Should the directions ASIC can make be prescribed in the legislation (with an ability to extend the list by regulation)? If so, is the above list appropriate? **Yes, the powers should be prescribed. See our comments on the list above.**
3. Alternatively, should a directions power be drafted broadly to allow for a wider variety of directions? **No, we don't agree that this is reasonable or necessary.**

In our view, the proposed powers are quite extensive. ASIC's powers must be clearly linked to and limited by the achievement of specific regulatory outcomes and should not extend to what are, in effect, operational business decisions.

The differentiation between powers necessary to limit consumer detriment in a financial services activity is quite different from the powers necessary when dealing with a credit activity where a consumer's funds are extremely unlikely to be accessible by the credit intermediary licensee and the likelihood for consumer detriment is correspondingly diminished.

Position 2

The directions power should be triggered where a licensee has, is or will contravene financial services or credit licensing requirements (including relevant laws)

Questions

4. Should the directions power be triggered if ASIC has reason to believe that a licensee:
 - a. has engaged, is engaging or is proposing to engage in conduct that constituted, constitutes, or would constitute a contravention of a law relevant to the provision of services by the licensee? **See below.**
 - b. has refused or failed, is or is proposing to refuse or fail to do an act or thing that the legislation requires a financial services or credit licensee to do? **Yes (subject to our comment that the initiative should not apply to credit at all).**
5. Alternatively, should broad public interest considerations or objectives provide the basis for ASIC making a direction? If so, are the objectives outlined above appropriate? The considerations are too wide. How will a judgement be properly made about what is in the 'broad public interest'?

It is of significant concern that the proposed power would extend to the prevention of compliance failures that have not yet occurred. This is likely to require an impossible level of regulatory forecasting and is likely to result in a stifling of innovation as a natural outcome of regulatory conservatism. The proposed power should be limited to the regulatory need identified by the 2014 Financial System Inquiry which was for a power to enable ASIC to impose conditions to address existing serious or systemic non-compliance with licence obligations.

Position 3

ASIC should be able to apply to a court to enforce the direction and take administrative action if an AFS or credit licensee does not comply with a direction

Questions

6. Should ASIC be able to apply to a court to seek an order requiring a licensee to comply with the direction? **Yes (subject to our comment that the initiative should not apply to credit at all).**
7. If so, should there be sanctions, in addition to those relating to contempt, for a licensee and/or its directors if the licensee breaches the court order? **Yes (subject to our comment that the initiative should not apply to credit at all).**
8. Should failure to comply with an ASIC direction be a:
 - a. criminal offence? **No.**

- b. civil penalty provision? Yes, but subject to the right to contest the direction.
 - c. breach of a financial services law or credit legislation and therefore a basis for administrative action? Yes, but subject to the right to contest the direction.
9. Should ASIC be required to give written notice to a licensee before making a direction setting out: its intention to make a direction, reasons and a period of time for the licensee to respond that is reasonable in the circumstances? Yes.
10. Alternatively, should ASIC be required to offer the affected licensee an opportunity to appear, or be represented at a hearing and to make submissions on the matter before making a direction? If so, should ASIC also be able to make an interim direction without providing a hearing and be required to provide a hearing within a certain time frame? No.

There are fundamental questions that must be considered before formulating what actions ASIC should be able to take to enforce a direction, in particular, with respect to credit licensees.

The fact that financial services and credit licences are issued in a similar way by the regulator does not mean that consumer harm is equivalent. On the contrary, as discussed above, credit intermediaries have little, if any, opportunity to cause consumer harm other than to recommend an unsuitable loan. Where that occurred, it would still require a credit provider to determine whether or not that recommendation led to the making of that loan.

There is no real reason to align regulatory powers on the two licensing types when the potential for consumer harm is so dramatically different.

Most importantly, the question of regulator accountability must be considered. Processes may necessarily be “slow” or “cumbersome” because of recognition of the need for decisions to be based on evidence and not rumour or supposition. When making decisions affecting a licensee’s ability to provide licensed services, the principles of procedural fairness should apply. In addition, where decisions affecting livelihood are made, as is the case with respect to decisions about the provision of licensed services, there must be a fast and cost effective external review mechanism available, such as the Administrative Appeals Tribunal.

The MFAA would like to thank you again for the opportunity to respond to the Treasury on ASIC’s Directions Powers and should the Treasury have any questions regarding this submission, please do not hesitate to contact me.

Yours sincerely



Mike Felton

CEO