

Mortgage broker best interests duty and remuneration reforms

Submission on draft legislation

Australian Financial Complaints Authority

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Overview

The Australian Financial Complaints Authority¹ (AFCA) is the independent external dispute resolution (EDR) scheme for the financial sector. We welcome the opportunity to provide comments on the proposed mortgage broking reforms in the draft Bill² and regulations³ released by Treasury on 26 August 2019.

This submission⁴ draws on the experience of AFCA and its predecessors – organisations that have handled financial services complaints for more than 25 years.

Key points

- AFCA strongly supports the introduction of a best interests duty for mortgage brokers. The duty will in our view bring the obligations of mortgage brokers into line with expectations of consumers and will assist in addressing issues that give rise to complaints and systemic issues.
- AFCA notes that detailed regulatory guidance will be required to assist in the application of the principle-based standard of conduct reflected in the draft Bill.
- To promote compliance with the new best interests duty, AFCA considers the draft Bill should impose clear record keeping obligations.
- AFCA suggests consideration be given to further extending the best interests duty to apply to all financial products recommended by any financial firm that engages in broking or equivalent activities.

This submission does not comment on the proposed remuneration reforms. Issues relating to fees and remuneration structures are outside our complaint jurisdiction.

Introduction of best interests duty

AFCA strongly supports the introduction of a best interests duty for mortgage brokers. We expect this proposed reform to improve outcomes for consumers by requiring mortgage brokers to act in the best interests of consumers and place the consumers' interests ahead of their own. The reform is an important measure to extend consumer protection and make mortgage brokers subject to obligations that already apply to certain other providers of financial services.

¹ The Appendix provides a brief overview of AFCA. For comprehensive information about AFCA, see our website www.afca.org.au.

² National Consumer Credit Protection Amendment (Mortgage Brokers) Bill 2019.

³ National Consumer Credit Protection Amendment (Mortgage Brokers) Regulations 2019.

⁴ This submission has been prepared by the staff of AFCA and does not necessarily represent the views of individual directors of AFCA.

Consumer expectations

AFCA believes that the best interests duty will bring the obligations of mortgage brokers into line with the expectations of consumers. The research findings set out in ASIC's Report 628⁵ support this view.

Report 628 indicated that consumers expected mortgage brokers to find them the best loan. Often this was based on an understanding that a broker compares a range of lenders and loans. The findings in Report 628 also indicated that:

- Consumers who used brokers:
 - > 'tended to value the knowledge and expertise a broker can provide and preferred the broker to "do the work" for them in finding a home loan'⁶
 - > looked to the broker to 'bridge their knowledge gap and support and advise them through the home lending process'.⁷
- Some first home buyers who used a broker relied almost entirely on the broker's advice.⁸
- In general, consumers compared only a few offers. Few consumers systematically compared loan options and calculated which loan would be the most cost-effective for them in the long run.⁹

Complaints and systemic issues

AFCA resolves complaints about mortgage brokers and systemic issues in mortgage broking. Our predecessors also resolved these complaints and systemic issues.

Complaints

AFCA believes that introducing the proposed best interests duty will assist in addressing issues that give rise to complaints relating to mortgage brokers.

The types of issues raised in these complaints commonly include:

- failure to disclose conflict of interests
- failure to provide relevant product information
- business loan obtained where the funds were to be used for consumer purposes
- failure to assess suitability and/or serviceability
- serious misconduct, including falsifying documents

⁵ [ASIC's Report 628](#) *Looking for a mortgage: Consumer experiences and expectations in getting a home loan*, August 2019.

⁶ Report 628, page 13.

⁷ Report 628, paragraph 29.

⁸ Report 628, paragraph 98.

⁹ Report 628, paragraph 39.

- providing inaccurate or incomplete information to the credit provider or misrepresenting the borrower's financial situation.

Systemic issues

AFCA believes that introducing the proposed best interests duty may also reduce systemic issues relating to mortgage brokers. Our recent systemic issues investigations have concerned broker conduct of the kind identified above in relation to complaints.

Regulatory guidance

The draft Bill states the best interests duty as a broad statement of principle. We note this adopts the approach suggested by the recent Royal Commission.¹⁰ As the duty is stated in very simple terms without elaboration in the legislation, we believe the industry will need detailed regulatory guidance on the duty.

ASIC's Regulatory Guide 175 provides extensive guidance on the best interests duty for financial advisors. Comparable guidance for mortgage brokers would be useful. AFCA would have regard to any relevant guidance issued by ASIC when resolving mortgage broking complaints.

Record keeping

AFCA considers the draft Bill should impose specific record keeping obligations to support compliance with the new best interests duty.

The inclusion of record keeping requirements will provide clarity about what mortgage brokers should do to document compliance with the best interests duty and should assist in resolving complaints. In our experience, there is currently significant variation in the nature and extent of record keeping across the industry.

Extension of best interests duty

AFCA considers the best interests duty to be a fundamental protection for consumers who rely on the services provided by brokers to make decisions about financial products. AFCA notes Recommendation 7.3 of the Royal Commission Final Report states that, as far as possible, exceptions or qualifications to generally applicable norms of conduct in legislation governing financial services entities should be eliminated.

¹⁰ Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry - see Final Report, page 72.

In line with this approach, AFCA suggests consideration should be given to extending the best interest duty:

- to all financial products and services recommended by mortgage brokers (including non-home loan arrangements such as leasing and other unsecured credit)
- to all financial firms that engage in any form of broking or equivalent activity in relation to financial products or services.

Appendix – About AFCA

AFCA is the new independent EDR scheme for the financial sector replacing the Financial Ombudsman Service, the Credit and Investments Ombudsman and the Superannuation Complaints Tribunal.

AFCA sees its purpose as providing fair, independent and effective solutions for financial complaints. It does this not only by providing complaint resolution services free to consumers, but also by working with its members to improve their processes and drive up industry standards of service, thereby minimising complaints.

More broadly, AFCA plays a key role in restoring trust in the financial services sector. In addition to providing solutions for financial complaints, AFCA has responsibilities¹¹ to identify, resolve and report on systemic issues and to notify ASIC, and other regulators, of serious contraventions of the law.

AFCA's service is offered as an alternative to tribunals and courts to resolve complaints consumers and small businesses have with their financial firms. We consider complaints about:

- credit, finance and loans
- insurance
- banking deposits and payments
- investments and financial advice
- superannuation.

AFCA's role is to assist consumers and small businesses to reach agreements with financial firms about how to resolve their complaints. We are impartial and independent.

If a complaint does not resolve between the parties, we will decide an appropriate outcome, including awarding compensation for losses suffered or substituting the trustee's decision in the case of a superannuation complaint.

¹¹ See [ASIC's Regulatory Guide 267](#) *Oversight of the Australian Financial Complaints Authority*.