4 October 2019

Ms Ruth Moore
Manager
Financial Services Reform Taskforce
The Treasury
Langton Crescent
PARKES ACT 2600
Via email only: ConsumerCredit@treasury.gov.au(mailto:ConsumerCredit@treasury.gov.au)

Dear Ms Moore,

Submission by Mortgage Choice Limited in respect of the
Exposure Draft
National Consumer Credit Protection Amendment (Mortgage Brokers) Bill 2019 (Bill) and
National Consumer Credit Protection Amendment (Mortgage Brokers) Regulations 2019
re Mortgage Broker best interests duty and remuneration reforms

Mortgage Choice

Mortgage Choice Limited (ACN 009 161 979) (Mortgage Choice) is a provider of credit assistance services, operating as a franchisor of mortgage broking businesses under Australian Credit Licence 382869 issued by the Australian Securities & Investments Commission (ASIC) pursuant to the National Consumer Credit Protection Act (NCCP Act). As at 30 June 2019, the franchise network comprised 391 franchises, located in all Australian States and Territories, with 562 mortgage brokers registered as Credit Representatives under Mortgage Choice's credit licence.
Mortgage Choice was founded in 1992 and became a public company listed on the Australian Securities Exchange in 2004. It is a member of the Mortgage and Finance Association of Australia (MFAA) and the Combined Industry Forum (CIF). The Company's residential lender panel comprised 28 credit providers as at 30 June 2019, with an additional 4 personal loan providers and 14 commercial lending providers. The Company also provides access to 42 credit providers on our asset finance panel. Mortgage Choice's brokers offer customers a wide choice of home loan products in addition to being able to also assist with personal loans, commercial loans, asset finance, deposit bonds, and risk and general insurances.
Mortgage Choice's wholly owned subsidiary, Mortgage Choice Financial Planning Pty Ltd (ACN 158 645 624) (MCFP), holds an Australian Financial Services Licence (AFSL): AFSL Licence Number 422854 issued by ASIC pursuant to s. 913B of the Corporations Act. As at 30 June 2019, MCFP had 33 financial

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planning franchises with 38 financial planners. The financial planners are registered as AFSL authorised representatives of MCFP.

Proposed Changes to Draft Legislation and Draft Regulations

Mortgage Choice believes that its brokers already put the need of the consumer before their own and is supportive that the duty to the consumer is clarified through Best Interests Duty (BID) being introduced as part of the proposed amendments to the NCCP Act. However, we do believe that the broad scope of the exposure draft legislation and the wording around remuneration in the accompanying regulations would likely result in unintended consequences.
This submission puts forward the following suggested changes to the amendments referred to above:

1. The requirement to act in the consumer's best interests (S.158LA) should be revised to be applicable solely at the time credit assistance was provided. This is the only practical solution as the consumer's situation and the features of the product recommended may change over time (product features change very rapidly) and it is untenable that BID should be judged based on later market changes or a change in the borrower's circumstances that were unknown at the time credit assistance was given.

2. The application of BID and the remuneration reforms should be changed from a Mortgage Broker as proposed to an activity based measure – the provision of credit assistance under the NCCP Act with regard to credit contracts secured by residential property. For the avoidance of doubt BID should not relate to other credit contracts under the NCCP Act that are not secured by residential property The specific exclusion of credit assistance provided by a credit provider should remain. This would ensure that the consumer's expectation of credit assistance with relation to a mortgage that includes a choice of lender is always provided in their best interests regardless of whether the person giving credit assistance technically meets the definition of Mortgage Broker as currently proposed. We believe that this is the intention of these amendments and that the current drafting is too broad. It takes in more of a mortgage broker's activities than required and does not cover the activities of others.

3. The reference to annual reviews of home loans in the Explanatory Memorandum should be changed to periodic to ensure that there is no suggestion of the requirement to provide an annual review.

4. The proposed limitation of the clawback of commissions to two years is current industry practice. This proposal ignores the fact that for two years brokers are under threat of losing remuneration, through no fault of their own, for work performed in the best interests of their clients (100% in year 1 and 50% in year 2). Clawbacks were put in place to help ensure that brokers placed the consumer in a loan that was right for them at the time and did not engage in churn over the short term to the detriment of the consumer and the financial system

Mortgage Choice

overall. The requirement to act in the best interests of the consumer should ensure that a consumer who does move out of a loan in the short term is doing so because of a change in circumstances. This cost should be more fairly borne between the lender and broker. Our proposal is to reduce the clawback evenly over the proposed period in a straight line fashion with 100% being the starting point and 0% being the ending point. Consideration should also be given as to whether 2 years is the appropriate period. One year would be more in keeping with BID.

5. The drafting of drawndown amount in clause 28VB needs to be addressed in two concerns: the 90 day period over which a consumer is assumed to use the loan funds borrowed is unrealistic and the drafting is confusing and may not be achieving the intended result. We understand the overall intention is to ensure consumers only borrow what they need and have clear plans to utilise the funds borrowed and we are supportive of this premise. It is important that the current method of paying upfront commission on drawn funds be more standardised as in its present varied form it introduces conflict. Ninety days, however, underestimates the variety of plans consumers have and the complexity of many of those plans. The most common uses of excess funds (another investment or renovation) rarely come to fruition in 90 days. The most common period of review for use of funds borrowed is one year at the present time. Ideally it should be whenever those funds are used but the minimum should at least be the one year in place with most lenders today.

The drafting of drawndown funds should be clarified on several points:

a. As pertains to upfront commission, payment should be made on funds drawn and utilised (i.e., not in the offset account). The proxy for this calculation should not be the entire offset balance that may have other funds in it unrelated to the loan funds. This is current practice with some lenders and is not in the spirit of the intention to pay brokers commission on funds utilised.

b. The 90 day period (which as above should be extended to at least a year) should relate to a lookback period to determine if funds not utilised in the first few days have subsequently been utilised and then form the basis for a top-up of commission paid at settlement if that is so. The drafting should make this clear.

c. Trail is currently paid based on the monthly loan balance and in the majority of cases net of the offset balance. The current drafting of this section could be interpreted as setting the trail balance at a point in time and I do not believe that is the intention. This would not allow for an increase in the facility limit following a top-up application and may have further unintended consequences.

6. The proposed maximum civil penalty of 5,000 penalty units (which equates to $1,050,000) is unduly harsh and prejudicial and would be significantly in excess of the loss suffered by the

consumer having regard that in approximately the last 25 years AFCA (and its predecessor dispute resolution bodies) have typical settlements in the order of $10,000 - $15,000. This level would be financially debilitating and cause the small business operators that make up the mortgage broking industry to declare bankruptcy. The penalty regime should be commensurate with the detriment caused by the failure to discharge the best interests duty.

What is in the Best Interests of the Consumer?

It should be recognised that the cheapest home loan product on the market may not necessarily be in the best interests of the consumer. The consumer grows consistently more complicated as time progresses as does the loan process. The loan that best meets the consumer's requirements and circumstances may be at a higher rate but be considered by the consumer worth the extra dollars for the desired features (internet banking quality, offset account, consideration of a consumer special case, exit strategy, property type, reputation of institution, length of employment, casual nature of employment,…). The broker should not be put in the position of being liable in these circumstances, especially if a reasonable broker would have made the same recommendation given the fact pattern and the consumer's requirements. Consumers will not always act economically even if a cheaper loan has been brought to their attention.

Similarly, it is unreasonable and unacceptable that the best interest duty should be judged by reference to altered economic circumstances that arise subsequent to the credit assistance having been provided such as falling property prices or a significant change in interest rates or a change in the borrower's circumstances that was not anticipated (divorce, illness, job loss).

It is also unrealistic for a broker to compare loans against options that are not available to brokers or all the options that might be available to brokers. This is an unnecessarily large consideration set that needlessly complicates the process and will not provide a better answer for the consumer. Given that a broker has access to a sufficiently wide selection (which must be disclosed to the consumer through CIF reforms), the best interests duty should be able to be achieved.

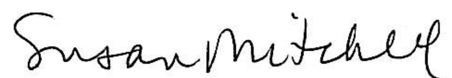
Similarly, it should not automatically follow that mortgage brokers will always suggest or recommend to a consumer a home loan product that will, of its nature, pay the mortgage broker a higher level of commission. Such scenarios may often be explained by consumers incorporating their preference for a credit provider which is prepared to lend the necessary funding to finance the initial acquisition cost of the house as well as the additional loan funds for a renovation. This can be a great consumer outcome as they choose not to go through the credit application process a second time in a relatively short period of time.

Conclusion

The Bill, as presently drafted, goes beyond what is legally necessary for mortgage brokers to act in the best interests of consumers looking for a home loan. Consumer outcomes can best be optimised by incorporating and dealing with the various suggestions for clarification and improvement made in this submission which we commend for the consideration and adoption by the Financial Services Reform Taskforce.

I would be pleased to comment further should this be of assistance to the Taskforce.

Yours sincerely,



Susan Mitchell
Chief Executive Officer
Mortgage Choice Limited