11 March 2016

Australian Securities and Investments Commission
GPO Box 9827
Sydney NSW 2001

By email:

Dear Sir/Madam,

Response to the Review of Mortgage Broker Remuneration Structures Scoping Discussion Paper

The Mortgage and Finance Association of Australia (MFAA) welcomes the opportunity to respond in respect to the subject matter of the Review of Mortgage Broker Remuneration Structures Scoping Discussion Paper (Scope) prepared and circulated in February 2015. Our comments below are made in relation to the MFAA's view, and the views of contributing MFAA members of the Scoping Considerations and Scoping Questions set out in the discussion paper.

Established in 1982, the MFAA is the peak professional body providing service and representation for more than 12,000 professional finance brokers (mortgage and finance brokers and intermediaries, mortgage management businesses, non-bank lenders and aggregators) to assist them to develop, foster and promote the mortgage and finance industry in Australia. Its membership profile also includes ADI lending institutions that distribute their products via intermediaries, and businesses that provide support services to the mortgage and finance sector.

The business of assisting people in securing suitable financing for real estate and providing long-term professional service throughout the life of a customer's loan brings with it professional obligations to act honestly and ethically. The MFAA has a strict code of practice and ethics attached to its membership, which is founded on and entrenched with the standards set by the *National Consumer Credit Protection Act (Cth) (NCCP)* 2009. The MFAA requires a higher standard of education and annual CPD than that set by ASIC. Members must renew their membership with the industry body annually which allows the MFAA to strictly enforce continual compliance to these standards. Our strict adherence is most clearly demonstrated through the published suspension or expulsion of 47 members who have been found by the MFAA Tribunal to have breached that Code of Practice over the past five years.

We thank ASIC for the opportunity to contribute on the subject matter of the Review of Mortgage Broker Remuneration Structures Scoping Discussion Paper. Given the feedback requested by ASIC, our comments are solely focused on the MFAA assessing the suitability of the scope outlined in the discussion paper in relation to the home lending market, remuneration structures and consumer outcomes.

The MFAA is committed to ensuring its members act in accordance with industry regulation and would be pleased to continue working with ASIC and with MFAA members in providing further feedback and analysis as required in the Review of Mortgage Broker Remuneration Structures.

Should you have any queries in relation to this submission, please do not hesitate to contact the MFAA's CEO, Siobhan Hayden on 0405 182 591.

Yours sincerely

Siobhan Hayden

CEO

Introduction

The home lending industry plays a significant role in the Australian Economy. As previously outlined by Peter Kell, Deputy Chairman of ASIC, there are significant differences between the commission structures of financial planners and mortgage brokers. Mortgage broker commissions are structured in a way that ensures the broker provides professional services and assistance for the life of the loan. If a loan goes into default, there are remuneration consequences for the broker such as commission claw-back and cessation of the payment of trail commission components to ensure consumers are offered a long term product that is not unsuitable for their requirements and objectives at the time of application.

Mortgage brokers settled 51.8% of new residential homes in 2015, an increase from 50.4% in 2014.The continued year on year growth (2.5%) in mortgage broker market share indicates consumer's value choice in deciding how to secure finance and see value in partnering with a mortgage broker instead of a traditional lender.

Prior to the de-regulation of the Australian financial system in the 1980's, origination generally occurred directly at branches of the major banks and building societies. Since de-regulation there have been widespread bank branch closures and rationalization and in response the mortgage broking industry has grown significantly.

Mortgage brokers have become an effective method of originating loans for lenders, particularly those smaller lenders without the balance sheet to support a branch network.

At the same time, mortgage brokers have become popular with borrowers by providing a convenient service that assists them to find a mortgage product that meets their needs from the range of products available that they may otherwise not have access to. The adoption of the mortgage broker channel by borrowers has resulted in better consumer outcomes with increased competition resulting in access to more innovative products and pricing.

Within the mortgage broking industry there are a number of different operating models, including;

- Wholesale Mortgage/Broker Model,
- Franchisee Model,
- Licensee Model,
- Sole Trader

The services of mortgage brokers and wholesale mortgage brokers are increasingly important in the Australian mortgage landscape. It is important to note however that some participants operate as a single model, or a combination of more than one and furthermore that industry models vary, such as a Head Groups with credit representatives under their licence compared to groups with independent licence holders operating within their model.

Scoping Considerations - the Home Lending Market

The Home Lending Market value chain in Australia, can be divided into three (3) broad categories;

- Origination
- Servicing
- Funding

As an industry association, the MFAA represents three key pillars; professionalism, ethics and education. This means that any mortgage and/or finance broker who holds MFAA membership adheres to a code of conduct. The MFAA provides resources and guidance to borrowers, helping them make informed choices during their borrowing and home-buying journey.

The MFAA works in partnership with the diverse range of industry participants, as identified by ASIC in their Scope across all three categories to ensure;

- Management of annual member compliance (AML/CTF/CPD),
- Industry advocacy and adherence to a Code of Conduct,
- Provision of Continual Professional Development (CPD) opportunities,
- Access to broader business & skills development opportunities, and
- Member reward & recognition.

Should any MFAA member not conform to this code of conduct and fail to provide a service which is professional or legally compliant, the MFAA will assess that adviser's membership through the MFAA Tribunal. The Tribunal is run independently of the Association. The Tribunal provides the Association with their findings and recommendations and where brokers are found to be guilty of misconduct, they will either be suspended or expelled from the MFAA.

In addition to the MFAA's annual member compliance, certain mortgage brokers head groups have their own internal diplomas, ongoing training and compliance requirements.

The MFAA would like to highlight that the Scope should include all participants that have the opportunity to be financially compensated for their involvement in the Australian home lending market. It notes that currently; credit repair agents, mortgage introducers, new property sales (spruikers) and solicitor funding providers often receive a benefit from their involvement in the market without regulation or declaration of interest.

Distribution Channels

The MFAA believes that ASIC should consider all distribution channels, including referrers, and should consider where there may be remuneration arrangements between brokers, real estate agents and/or property developers.

With regard to gathering information to measure loan performance by distribution channel, there may be natural bias in the type of customers who choose not to be directly to lenders, although the MFAA does not expect this to be significant.

Mortgage brokers settled just under 52% of all new residential homes in Australia, in December 2015. A mortgage is a long-term commitment which can span 20-30 years, and many home buyers prefer to be reassured by a mortgage broker who is independent of any one lender that the mortgage product they choose is not unsuitable for their needs. Mortgage brokers provide a benefit to both lenders and borrowers.

Mortgage brokers benefit lenders by:

- Providing a distribution network without lenders having to invest in branches and other physical infrastructure (particularly important following industry wide branch closures and rationalisation);
- Allowing lenders to differentiate their products to capture a different segment of the mortgage market; and
- In the case of wholesale mortgage brokers, managing a large volume of mortgage brokers on a day to day basis and therefore reducing the Lender's fixed costs. Management of a mortgage broker may encompass compliance, training, and distribution of revised and new product details and also

payment of remuneration for all settled loans.

Mortgage brokers benefit borrowers (consumer) by:

- One point of contact in the loan origination process, with knowledge of and access to products from a variety of lenders, saving time and reducing the administrative burden on the borrower;
- Large mortgage broker networks that provide opportunities to extract competitive loan pricing and terms from Lenders;
- A customised approach to each individual borrower's needs;
- Flexibility and convenience in being able to talk to or meet a mortgage broker outside bank opening hours and at locations of the consumer's choice, and;
- Advice on a wide range of lending products that may otherwise be difficult to source.

Lenders usually pay upfront and/or trail commissions in respect of the loans originated through mortgage brokers. The upfront remuneration offered by lenders is (mostly) uniform at 0.65%, and trail remuneration (mostly) uniform at 0.15% for the life of the loan. Lenders vary in their application of claw-back, ranging from 12-24 month terms as well as their introduction of trail payments (delayed until the 13mth).

The MFAA would like to note that broker remuneration provided by lenders has reduced over the past ten (10) years from a (mostly) uniform offering of 0.70% and 0.25% for upfront and trail commissions respectively. In parallel, broker costs, compliance requirements and client engagement per file have all increased. The MFAA also notes that residential mortgage brokers generally do not charge borrowers an upfront service fee.

The MFAA is aware of a few key lender products that require additional accreditation and/or offer dissimilar commission structures, such as Reverse Mortgages, Self-Managed Super Funds (SMSF) and Commercial Lending. Due to the different remuneration models, the MFAA advocates that these products be excluded from the Scope. The MFAA does not believe that remuneration from these products has a material impact on remuneration in respect to residential mortgage products.

Ownership Structures
The MFAA is aware of the following ownership structures within our membership.

- AFG (publicly listed)
- Aussie (80% owned by CBA)
- National Mortgage Brokers (wholly owned by Aussie)
- Choice/FAST/PLAN (wholly owned by NAB)
- Connective (18% owned by Macquarie Bank)
- Mortgage Choice (publicly listed entity)
- VOW/YBR (17% owned by Macquarie Bank)

The MFAA supports the need for transparency when dealing with consumers and therefore supports provision of guidance on disclosure of vertical ownership structures, where they exist. The MFAA notes that some organisation already make some disclosure in this regard.

<u>Scoping Considerations- Remuneration Structures</u>
ASIC appears to have identified the main remuneration structures in their Scope and it is noted that ASIC are interested in correlating all remuneration structures with the services provided by participants within the value chain.

MFAA members are keen to ensure that reasonable parity exists with all remuneration structures and/or controls for all participants, regardless of channel. Parity will ensure clearer outcomes for all consumers (regardless of channel) as well as ensuring a uniform market in which all participants can operate and flourish.

Payments
The MFAA supports all the remuneration categories identified by ASIC in their Scope.

To ensure broader industry success and ongoing benefits to consumers, the MFAA advocates that all monetary rewards be fully disclosed to consumers, as they currently are on a broker's credit proposal. The credit proposal currently outlines the range of commissions offered by the broker and furthermore, the upfront and trail remuneration following settlement of the customer loan based on the actual loan size.

The MFAA would like access to non-monetary rewards to be clear and measurable, and that a willingness to participate does not create a bias towards any one industry participant over another.

MFAA members are mostly small to medium entities (SME's) and are therefore heavily reliant on business cash-flow to continue to develop their businesses. The MFAA would like to encourage lenders to work with the industry to ensure that brokers are remunerated in a timely fashion. Current timing of up-front payments (currently range 7 to 30 days) within the value chain and we look for opportunities to make these payments standardized, where possible.

The MFAA requests that when conducting its review, ASIC objectively looks at the flawed assumptions that drives the incorrect assertion that mortgage brokers deliberately inflate loan amounts in order to maximize their commissions.

Scoping Considerations- Consumer Outcomes
The MFAA supports the scoping consideration categories set out under the Consumer Outcomes section within the Scope. The MFAA also strongly agrees with the state that "consumer outcomes are multifaceted". The MFAA further notes that its members currently offer and support customers with these requirements. The goal, and challenge for ASIC's Review rests with defining a good customer outcome and then accurately measuring industry performance.

The MFAA recommends that brokers assess their customer's satisfaction with the performance of their settled loan on three (3) key areas including; loan product (features), lender (process) and broker (performance). MFAA members are encouraged to conduct customer reviews 45 days following settlement, which ensures that customers have had adequate time to complete their first mortgage repayment. Due to the range of industry participants, customer satisfaction is not measured or captured in a uniform manner.

Conclusion

The MFAA broadly supports the ASIC Scoping Document into Broker Remuneration Review and would like to ensure the Inquiry focuses on consumer outcomes for residential mortgage lending within this review due to the detailed Scope and tight timeframes.

Successful outcomes from the Inquiry will need to be data-driven where possible. MFAA encourages ASIC to consider the timing of the data requests, and the response times provided to industry participants. Data gathering is likely to be onerous and time consuming for many MFAA members.